

BUSINESS

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THE OTTAWA CITIZEN

SECTION E

Meet the man who told you so

BY SIMON DOYLE

TORONTO • Five years ago, Al Rosen was seen as the nut job who said Nortel Networks was riddled with sloppy accounting. Watch it plummet to the cellar of the Toronto Stock Exchange, he said.

Few had any reason to believe the investigative accountant, known for his hard-hitting attacks on the way Canada's corporations report their financial figures. At a seemingly invincible \$150-plus per share, analysts promoted Nortel and investors continued to buy, making it the most widely held stock in Canada.

'The politicians are going to look awful when these blowups continue. Do you understand what I'm getting at? They're doing nothing!'

AL ROSEN

manager, Rosen & Associates Ltd.

All that has changed. Nortel, now sitting between \$4 and \$5, late Monday issued a long-delayed restatement of its 2003 financial results, and it wasn't a pretty sight. The report took to task former chief executive Frank Dunn for improperly moving profits from one quarter to another so executives could take advantage of performance bonuses. Five directors announced they would not be standing for re-election to the board. Twelve top executives decided they should repay \$10.4 million in bonuses. It was a house-cleaning seldom seen in the corporate world.

Is Mr. Rosen one to say, "I told you so?"

Probably.

As the force behind one of Canada's leading investigative accounting firms, he is in high demand, some would even say revered. Reporters, investors and finance lawyers take an interest in his analysis, because, as Mr. Rosen would say, understanding investing is really a matter of understanding accounting. But for all his celebratory rise in stature, Mr.

Rosen remains forever fed up.

On the 38th floor of the Toronto Dominion Centre, thousands of financial reports and legal documents are piled on his desk and stacked in boxes in the hallway. Aggressive accounting, or the deceptive art of piecing together pretty financial statements, he says, has not been solved. Canadian securities regulators, and their friends in the political world, are doing nothing to fix lax Canadian accounting.

On Bay Street, Mr. Rosen is known as Dr. Al, or the Enforcer. As the manager of Rosen & Associates Ltd., he has worked on more than 750 litigation cases, often as an expert witness. Now in his late 60s, his many credentials include a PhD (he taught accounting at York University for more than 30 years) and a CFE (Certified Fraud Examiner).

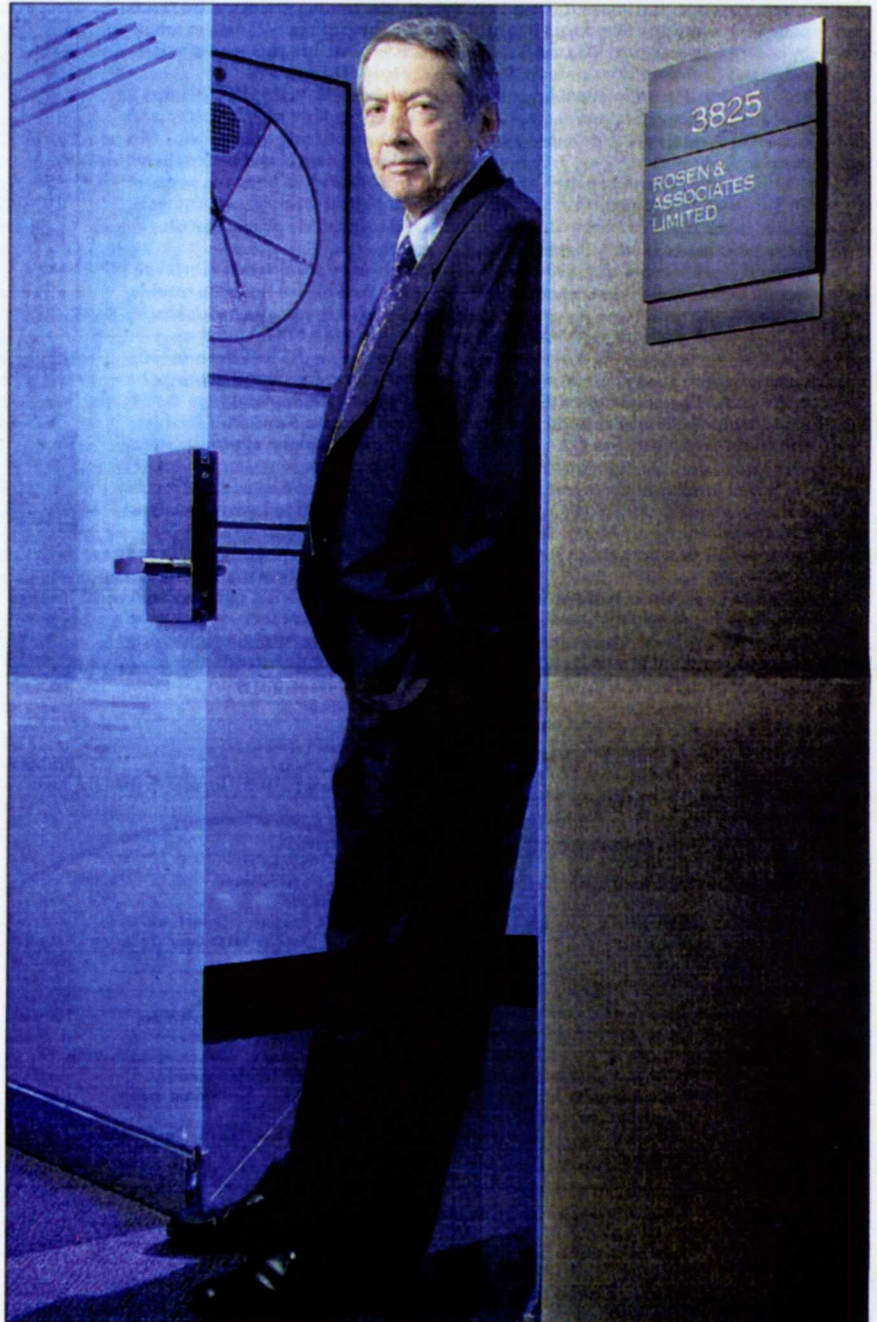
"Dr. Rosen is the undisputed reigning champion of forensic accounting in Canada," said Douglas Hunter in his 2002 book *The Bubble and the Bear*, on Nortel's collapse. He, along with analysts Ross Healey and Paul Sagawa, were the first to recognize Nortel problems.

So who should be less impressed with Nortel's attempt at a fresh start than Mr. Rosen, who says the company has not redeemed itself. The bonus repayment scheme involving 12 managers is a mere public relations scheme, he says, and he expects Nortel to go on to use the same accountants and auditors.

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BOARD: THREE RECRUITS ARE HIGHLY ACCOMPLISHED, **PAGE E3**

LEARNING: SOME INVESTORS STILL DON'T GET IT, **PAGE E8**



CHRIS BOLIN, THE NATIONAL POST

Known as 'the undisputed reigning champion of forensic accounting in Canada,' Al Rosen blames — in part — lax Canadian accounting standards for allowing the Nortel debacle to happen.

Rosen: Frustrated by lack of will to tighten standards

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Asked if he feels personally vindicated, he says without pause, "Not at all."

The most interesting thing about Nortel's 2003 restatement, he says, is that it was cleared by the company's auditors, while at the same time the law firm investigating Nortel, Wilmer Cutler Pickering Hale & Dorr LLP, reported there were uncertainties surrounding its 1999 and 2000 financial reports.

"The balance sheet is cumulative," Mr. Rosen says. "Think of it as a glass of water. They're signing off, saying, 'Here's the level in the glass of water, but if there's problems in 1999 and 2000, the water could be higher, it could be lower.'"

Looking forward, Mr. Rosen says, it will take at least a couple of years for the company to rid itself of the suspicions surrounding its financial statements. "Hopefully they'll have the technology after that to try and build. I can see two or three years down the road they may have a fresh start, but to say they have a fresh start today is just ludicrous."

Mr. Rosen's biggest beef with Canadian accounting is that the rules are set by a board within the Canadian Institute of Chartered Accountants. There is no independence, he says, and because the auditors are running the show, Canadians have a serious lack of accounting and auditing rules.

The U.S. accounting body, the Financial Accounting Standards Board, by contrast, is responsible to the Securities and Exchange Commission. In a study by Mr. Rosen in 2003, he compared BCE's Canadian and American financial statements over a five-year period.

The income reported on the Canadian side was five times what was reported in the U.S. That's why Mr. Rosen loves pointing to Nortel. It was under perfectly legal accounting that Nortel turned billion-dollar losses into multi-million-dollar profits.

Mr. Rosen has specific concerns about Canadian accounting. He points to the Generally Accepted Accounting Principles (GAAP), called one of the loosest accounting standards in the industrialized world. Canadian GAAP gives companies room to manoeuvre. They can make losses appear lower by creating questionable assets, report rising income while obscuring the fact that overall cash flow might be on the decline.

In fact, in its Monday report, which wasn't made public until Tuesday, Nortel itself identified adherence to the Canadian accounting standards as having contributed to the company's

problems.

It was in early 2000, after watching Nortel's shares rise to \$170 and seeing its executives redeem a pile of stock options, that Mr. Rosen took a close look at a company that had been under his suspicion since its dramatic growth took hold in 1998.

As part of his research business, he had been writing a newsletter for mutual fund and pension managers, analysing the good and bad of the stock market. His first major warning on Nortel came a full year before the crash began, and about two years before the public would fully grasp Nortel's downfall.

He examined Nortel's current receivables and noticed that some of them were due as far as 12 months into the future. If some receivables became difficult to collect, Nortel would face a cash crunch.

Throughout 2000, and into 2001, Mr. Rosen and his son, Mark, who's been pegged as "Rosen 2.0," continued to warn investors that the company was unsafe. They said its revenue was misleading: Nortel was expanding by trading shares for acquisitions and, of course, adding their revenues to its figures. Through certain accounting methods, the expenses of the acquisitions were also ignored. At the time Mr. Rosen could be heard saying there were three types of accounting: Canadian, American, and Nortel's.

In an interview with *Money Sense* in January 2001, Mr. Rosen estimated that Nortel was trading at a price 880 times its actual earnings. When the magazine asked for his top 2001 torpedo stock? Nortel.

"Everybody thought that this was a new wave, a whole new industry, and that manufacturing was passé," Mr. Rosen says. "Some of our better clients sold and others just hung on, because they thought it was a great euphoria. It's hard to convince people that they're wrong."

By February 2001, when Nortel released its first hint of financial trouble, investors and the media had taken an increasing interest in his analysis.

Where the media had been mostly "cheerleaders" for Nortel, he says, he began writing commentary for the *Financial Post* and *Canadian Business* magazine and making appearances on television. Says a longtime associate, Mike Girard: "There were a number of people who began to take his analysis and his warnings more seriously."

As much as Mr. Rosen has gathered somewhat of a following among investors, for him it's not good enough. He is frustrated that there seems to be little political traction on tightening Canadian accounting standards.

"The politicians are going to look

awful when these blowups continue," he says. "Do you understand what I'm getting at? They're doing nothing."

Canada cannot create independent, national standards, however, without a federal securities regulator. Observers say that to build such an agency, the public would have to apply a tremendous amount of pressure on the government, and the general public — let alone investors — isn't concerned enough.

It's not that something isn't being done; it's simply not enough.

The newly formed Canadian Public Accountability Board has been set up to oversee accounting practices. In October, the CPAB issued its first report and said the Big Four accounting firms, Ernst & Young, Deloitte & Touche, KPMG and PricewaterhouseCoopers, had no major problems, but needed to improve their documentation and accuracy. The CPAB would give the firms 180 days to respond.

When Mr. Rosen thinks about this, he feigns weariness, as though he can't take much more. The CPAB is not independent, he says. It's an illusory oversight committee tasked with creating investor confidence, run and financed by accountants. In fact, four of the board's 11 members are accountants, and it is funded by the accounting firms. The board refused to comment for this story after being told it was about Mr. Rosen.

One factor setting the U.S. apart from

Canada, says Leonard Brooks, a professor of accounting at the Rotman School of Management at the University of Toronto, is that the U.S. already had the national Securities and Exchange Commission in place when the country faced a sequence of financial meltdowns in 2001-2002. It was unlike the Canadian experience.

First, Enron collapsed, which took down with it one of the world's largest accounting firms, Arthur Andersen LLP. Then, the revelation of fraud at WorldCom in 2002 dealt a lasting blow to investor confidence. This prompted U.S. President George W. Bush to address "corporate corruption" and sign the Sarbanes-Oxley Act the same year. The new law created criminal liability for chief executives and chief financial officers, and as a result managers in the United States took a more conservative approach to their accounting.

If it is going to take a similar string of financial catastrophes to create a national regulator in Canada, Mr. Rosen doesn't know what he'll do. For decades he has been saying that Canadians need mechanisms to put managers and accountants in jail, that they need to see "names raked across the coals."

If Canadian investors do suffer a meltdown bigger than anything they've seen before, Mr. Rosen will at least have licence to say, "I told you so."