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E-ALERT | Anti-Corruption

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TYCO INTERNATIONAL, LTD. PAYS MORE THAN $26 MILLION TO SETTLE FCPA ALLEGATIONS

Improper Payments Made to Foreign Officials in Over a Dozen Countries, Including China

On September 24, 2012, Tyco International Ltd. ("Tyco") agreed to pay more than $26 million to settle allegations that its subsidiaries violated the Foreign Corrupt Practices Act ("FCPA") by making improper payments to government officials in over a dozen countries across the globe. According to a complaint filed by the US Securities and Exchange Commission ("SEC") (the "SEC Complaint") and a non-prosecution agreement issued by the US Department of Justice ("DOJ"), Tyco subsidiaries made improper payments either directly or through third-party agents to government officials and employees of state-owned or controlled enterprises, and then improperly recorded the payments in its books and records.

To settle the SEC Complaint, Tyco agreed to pay more than $13 million in disgorgement and prejudgment interest. To settle the parallel criminal prosecution brought by DOJ, Tyco and a subsidiary pleaded guilty to conspiring to violate the anti-bribery provisions of the FCPA, agreed to pay a penalty of approximately $13.68 million, and entered into a non-prosecution agreement with the DOJ. In total, Tyco will pay more than $26 million to settle the claims brought by DOJ and SEC.

Alleged Misconduct

Tyco, a Swiss conglomerate in the security, fire protection, and energy sectors, is listed on the New York Stock Exchange. In 2006, the SEC brought an action against Tyco alleging accounting fraud and FCPA violations. Tyco consented to enter into a final judgment enjoining it from further violations of U.S. securities laws. At the time of that judgment, Tyco had commenced a comprehensive FCPA compliance review and an internal investigation of its activities worldwide. The allegations found in the SEC Complaint are a result of this review and investigation; some of the conduct occurred after the 2006 injunction.

The SEC Complaint alleges improper payments through Tyco's wholly owned subsidiaries operating in China, Turkey, Croatia, Libya, Saudi Arabia, Serbia, the United Arab Emirates, Mauritania, Congo, Niger, Madagascar, Thailand, Malaysia, and Egypt. The DOJ charges relate to improper payments to employees of government-owned or -controlled companies in China, India, Thailand, Laos, Indonesia, Bosnia, Croatia, Serbia, Slovenia, Slovakia, Iran, Saudi Arabia, Libya, Syria, the United Arab Emirates, Mauritania, Congo, Nigeria, Madagascar, and Turkey.

China-Related Misconduct

According to the SEC Complaint, Tyco made improper payments in China through several local wholly owned subsidiaries, as described below:

- According to the SEC Complaint, a Tyco subsidiary -- Tyco Thermal Controls ("TTC China") -- made a $3700 payment to the "site project team" of a state-owned corporation in order to secure a $770,000 contract with China's Ministry of Public Security. The SEC alleges that part of that amount was passed on to Ministry personnel, and that the payment was later improperly recorded in TTC China's books as a "commission." TTC China also authorized more than 100 payments totaling $196,267 to designers at state-owned or -controlled design institutes, and improperly recorded these payments as "technical consultation" or "marketing promotion" expenses.

- According to the SEC Complaint, a Hong Kong-based Tyco subsidiary, Tyco Flow Control Hong Kong Limited ("TFC HK"), collaborated with another Tyco subsidiary, Beijing Valve Co. Ltd. ("Keystone"), to pay approximately $137,000 to local agencies owned by Keystone employees, a portion of which was then transferred as cash or gifts to Chinese government officials, including employees of design institutes. Keystone further made payments to one of its sales agent in connection with sales to Sinopec, and improperly recorded those payments as "commissions." Subsequently, Tyco was unable to identify what legitimate services, if any, were provided by the agent.

- The SEC Complaint alleges that employees of Tyco Healthcare International Trading (Shanghai) Co., Ltd. ("THC China")[1] submitted numerous fictitious expense claims related to entertainment of Chinese publicly employed healthcare officials, some of which involved fictitious receipts or the "seal" of a fictitious company. THC China employees also submitted false itineraries and other documentation incurred in connection with medical conferences. In each of these cases, Tyco approved the reimbursements. Employees used fake receipts because Tyco's internal guidelines prohibited the expenditures.

- The SEC Complaint alleges that Tyco's subsidiary in Germany paid third parties to secure contracts or avoid fines or penalties in several countries, including China.

The Tyco subsidiaries recorded the improper payments under such headings as "commissions," "business introduction services," "renovation work," "unanticipated costs for equipment," "technical consultation and marketing promotion expenses," and "conveyance expenses."

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[1] In 2007, the healthcare services branch of Tyco split off and became a unit of Covidien Public Limited Company.

Consequences

As part of a non-prosecution agreement with the DOJ, Tyco agreed to pay a $13.68 million penalty for falsifying its books and records. The DOJ press release noted Tyco's voluntary and complete disclosure, cooperation, and remedial efforts, which included the implementation of an enhanced compliance program, termination of employees responsible, severance of relations with responsible third-party agents, and the closing of subsidiaries for compliance failures.

In a parallel civil action, the SEC charged Tyco with violating the FCPA's anti-bribery, books and records, and internal control provisions. Tyco consented to a proposed final judgment that ordered the company to pay $10,564,922 in disgorgement, $2,566,517 in prejudgment interest, and to continue to implement an enhanced compliance program and internal controls to prevent and detect future FCPA violations.

The SEC Complaint noted that the internal investigation and subsequent remediation ultimately involved 454 business entities in 50 separate countries, "active monitoring and evaluation of all of Tyco's agents and other relevant third-party relationships," quarterly compliance training for 4,000 middle managers, focused site reviews of higher risk entities, creation of segment-specific compliance counsel positions, and exit from several businesses In high-risk areas.

Implications

This is the sixth China-related FCPA enforcement action in 2012, after the Biomet, Carsons (former CCI executives), Garth Peterson (former Morgan Stanley executive), NORDAM, and Pfizer enforcement actions. The Tyco enforcement action reinforces lessons learned from other FCPA and anti-corruption cases, including the need for:

- careful oversight, monitoring, and control of both company employees and third parties that represent the company, including distributors and sales agents;
- importance of accurate recording of transactions in books and records;
- scrutiny from an anti-corruption perspective, and careful control of, payments such as sales commissions and rebates; and
- scrutiny of relationships with design institutes in China.[2]

[2] FCPA enforcement actions against ITT Corp (February 2009), Avery Dennison (July 2009), Rockwell Automation (May 2011), and Watts Water (October 2011) also involved allegations of improper payments to state-owned design institutes in China.

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