

**UNITED STATES OF AMERICA**  
**Before the**  
**SECURITIES AND EXCHANGE COMMISSION**

**SECURITIES EXCHANGE ACT OF 1934**  
**Release No. 78287 / July 11, 2016**

**ADMINISTRATIVE PROCEEDING**  
**File No. 3-17337**

**In the Matter of**

**JOHNSON CONTROLS,  
INC.,**

**Respondent.**

**ORDER INSTITUTING CEASE-AND-  
DESIST PROCEEDINGS PURSUANT TO  
SECTION 21C OF THE SECURITIES  
EXCHANGE ACT OF 1934, MAKING  
FINDINGS, AND IMPOSING A CEASE-  
AND-DESIST ORDER**

**I.**

The Securities and Exchange Commission (“Commission”) deems it appropriate that cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 21C of the Securities Exchange Act of 1934 (“Exchange Act”), against Johnson Controls, Inc. (“JCI” or “Respondent”).

**II.**

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the “Offer”) which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission’s jurisdiction over Respondent and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Cease-and-Desist Proceedings Pursuant to Section 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing a Cease-and-Desist Order (“Order”), as set forth below.

### III.

On the basis of this Order and Respondent's Offer, the Commission finds<sup>1</sup> that:

#### Summary

1. This matter concerns violations of the books and records and internal controls provisions of the Foreign Corrupt Practices Act ("FCPA") [15 U.S.C. § 78m(b)(2)] by Johnson Controls, Inc. through its managers and employees at its wholly-owned Chinese subsidiary referred to herein as "China Marine." From 2007 to 2013, the managing director and approximately eighteen employees of China Marine made payments to sham vendors, some of which were then used to make improper payments of approximately \$4.9 million to employees of Chinese government owned shipyards, and ship-owners and others, to obtain and retain business, as well as to personally enrich China Marine employees. The improper vendor payments were improperly recorded on JCI's books and records, and JCI failed to devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances to detect and prevent such payments.

#### Respondent

2. **Johnson Controls, Inc.**, headquartered in Milwaukee, Wisconsin, is, among other businesses, a global provider of automatic temperature control systems for buildings, industrial facilities, and ships. JCI operates in 150 countries, has approximately 150,000 employees, and in fiscal year 2015, reported revenue of \$37.2 billion. JCI's shares trade on the New York Stock Exchange under the symbol "JCI" and are registered with the Commission pursuant to Section 12(b) of the Exchange Act. In 2005, JCI acquired York International, a global provider of heating, ventilating, air-conditioning and refrigeration equipment and services, while York was subject to an FCPA investigation. In October 2007, the Commission brought a settled civil action against York, pursuant to which York consented to an order enjoining it from future violations of Sections 30A, 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act, disgorgement of \$8,949,132, pre-judgment interest of \$1,083,748, and a civil penalty of \$2,000,000, and the retention of an independent compliance monitor.<sup>2</sup> The monitor provided the Commission and Johnson Controls, as York's parent, periodic reports that reviewed and analyzed the effectiveness of the controls within the legacy York operations. The monitorship ended in 2010.

#### Relevant Entities

3. **China Marine** is part of JCI's Global Marine business within the company's Building Efficiency ("BE") business, which engages in the design and sale of marine HVAC and refrigeration systems as well as aftermarket services and sales. China Marine is comprised of two legal entities: York Refrigeration Marine (China) Ltd. ("YRMC") and JCI Marine

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<sup>1</sup> The findings herein are made pursuant to Respondent's Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

<sup>2</sup> See SEC v. York International Corporation, 07-cv-01750 (D.D.C.).

(Shanghai) Trading Company Ltd. The China Marine entities operate as indirect, wholly-owned subsidiaries of JCI and are consolidated into JCI's financials.

### **Background**

4. The Commission's 2007 action against York alleged that, from 2004 to 2006, YRMC, a subsidiary that sold air conditioning and refrigeration equipment to shipbuilders and shipyards, some of which were owned by the Chinese government, made improper payments to agents and others, including Chinese government personnel at the shipyards, to obtain business. The payments were described in YRMC's books and records as commissions, sales and marketing expenditures, or gifts and entertainment. YRMC became part of China Marine, a business within BE.

5. After acquiring York, JCI devoted additional resources to its compliance program, including hiring compliance personnel, conducting trainings, and implementing risk-based procedures and controls. With respect to China Marine, JCI terminated the individuals involved in the YRMC conduct and hired a new managing director of China Marine to oversee the business. The managing director, a Chinese national and resident, reported to the Marine business management in JCI's Denmark subsidiary, which oversaw the Global Marine business in multiple countries. Because the misconduct identified in the prior civil action involved the improper use of agents, JCI limited the use of agents in its China Marine business model and required that all sales go through its internal sales team based in China. China Marine employees, however, devised another avenue to continue the payments. JCI conducted multiple compliance trainings for the China Marine employees, including trainings on the FCPA. JCI also conducted audits of China Marine, which detected some missing paperwork but failed to detect that the improper payments continued.

### **Improper Payment Scheme**

6. Despite the efforts taken by JCI, the bribery and embezzlement schemes at China Marine continued. From 2007 to 2013, the managing director of China Marine, with the aid of approximately eighteen China Marine employees in three China Marine offices, continued the bribery and theft that began under his predecessor by using vendors instead of agents to facilitate the improper payments. The improper payments were made to employees of government-owned shipyards as well as ship-owners and unknown persons, and for the personal enrichment of the China Marine employees.

7. The scheme was a multi-stepped arrangement that required the complicity of nearly the entire China Marine office from the managing director, to the sales managers, the procurement managers and finally to the finance manager. The managing director aided or at times approved requests for the addition of certain vendors to the vendor master file without disclosing that certain sales managers had ownership or beneficial interest in the vendors. After the managing director's approval, sales managers added bogus costs for parts and services to sales reports, which inflated the overall cost of the project, and generated purchase orders for the bogus parts and services. The procurement manager knowingly approved the purchase orders. The vendors, at the direction of China Marine sales managers, created fake order confirmations

for the unnecessary parts and services and submitted invoices for payment. The finance manager authorized payments even when supporting documentation was missing or erroneous. Once the sham vendors were paid, the money was returned to China Marine employees' personal bank accounts, where it was then used in part for foreign and commercial bribery and personal enrichment.

8. The employees knew that JCI limited the use of agents, and thus they used the vendor scheme to create slush funds. The employees fashioned the improper scheme using certain vendors specifically because those vendor transactions were considered low risk by JCI due to the low dollar value of the transactions. Vendors were also considered low risk because they did not interface with government officials. JCI's internal controls over these vendor payments were less rigorous and, as a result, China Marine employees were able to continue generating money to bribe officials and enrich themselves by using vendors instead of agents.

9. China Marine operated with very little oversight by JCI's Denmark office, which oversaw the Global Marine business. JCI gave the newly hired managing director a lot of autonomy and put significant reliance on his ability to self-police his business operations. Because of the Delegation of Authority thresholds in place, and the average low-dollar value of the transactions in China Marine, few business transactions in China Marine required approval by managers in the Denmark office that oversaw China Marine. The average vendor payment was approximately \$3,400. The China Marine employees fashioned the vendor scheme to stay below certain thresholds that would not trigger review by Denmark. Even in the instances where managers in Denmark did a review, they did not understand some of the highly customized transactions at China Marine or the projects involving the sham vendors. The managing director masterminded the scheme to make improper payments to government officials and others to obtain shipbuilding projects and to enrich him and other China Marine employees. Further, the managing director instructed China Marine employees to be cautious about their discussions regarding vendor payments to JCI lawyers, accountants, and auditors, as well as to avoid or delete documentation about vendor payments.

10. From 2007 to 2013, JCI obtained a benefit of \$11.8 million as a result of over \$4.9 million in improper payments made to or through approximately eleven problematic vendors for the purpose of foreign and commercial bribery, and embezzlement.

11. JCI did not learn of the conduct until December 2012, when JCI received the first of two anonymous hotline reports alleging that certain employees in China Marine were making payments to sham vendors that did not provide goods or services in order to personally profit and/or bribe Chinese officials. The reports arrived shortly after China Marine's managing director left the company. JCI self-reported the conduct and began an internal investigation.

### **Failure to Maintain Accurate Books and Records**

12. JCI failed to make and keep books, records, and accounts that accurately and fairly reflected JCI's transactions and the disposition of its assets. Numerous vendor payments were incorrectly recorded as legitimate vendor transactions or design fees when in fact they were payments for goods never received or payments intended for foreign or commercial bribery or embezzlement.

### **Failure to Maintain Adequate Internal Accounting Controls**

13. JCI failed to devise and maintain an adequate system of internal accounting controls. JCI knew that the China Marine subsidiary had a history of FCPA problems and that the China Marine business was high risk. Despite taking steps to address the monitor's recommendation that the company integrate the Marine business more closely into JCI's compliance culture, JCI put almost all of its reliance for oversight of China Marine on a newly hired managing director to self-police his high risk business. On paper, the China Marine business was formally overseen by JCI Denmark. However, no one in Denmark reviewed vendor transactions or reviewed sales reports or projects that were below two million dollars in value or had profit margins above 10%. The average China Marine project was valued between \$3,000 and \$100,000 and therefore was rarely, if ever, scrutinized by the Denmark office. Further, despite conducting some audits of the China Marine business, JCI failed to ensure that its audit and testing procedures would adequately review payments that were routinely below their testing threshold.

14. Denmark managers stated that even if they had performed additional review, they did not have sufficient knowledge and understanding of China Marine's projects to recognize when certain vendor payments were unnecessary, whether goods ordered had actually been delivered, or whether design fees were necessary given JCI had an in-house design service.

15. Because the China Marine employees operated so independently, a culture of impunity existed, and several members of the China Marine staff, including the managing director, colluded with each other and circumvented and manipulated JCI's internal and financial controls for over six years. JCI failed to detect the improper vendor scheme, which did not come to light until an anonymous report came in after the managing director departed the company.

16. As a result of the undetected conduct, over \$4.9 million in vendor payments were paid for goods and services that were either never delivered or were purchased at inflated rates, and JCI obtained \$11.8 million in profits on transactions involving the problematic vendor payments.

### **Legal Standards and Violations**

17. As a result of the conduct described above, JCI violated Section 13(b)(2)(A) of the Exchange Act, which requires issuers to make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and disposition of the assets of the issuer. [15 U.S.C. § 78m(b)(2)(A)].

18. In addition, as a result of the conduct described above, JCI violated Section 13(b)(2)(B) of the Exchange Act, which requires issuers to devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that (i) transactions are executed in accordance with management's general or specific authorization; (ii) transactions are recorded as necessary (I) to permit preparation of financial statements in conformity with generally accepted accounting principles or any other criteria applicable to such statements, and (II) to maintain

accountability for assets; (iii) access to assets is permitted only in accordance with management's general or specific authorization; and (iv) the recorded accountability for assets is compared with the existing assets at reasonable intervals and appropriate action is taken with respect to any differences. [15 U.S.C. § 78m(b)(2)(B)].

### **JCI's Cooperation and Remedial Actions**

19. In determining to accept the Offer, the Commission considered remedial acts promptly undertaken by Respondent and cooperation afforded the Commission staff. JCI self-reported the potential FCPA violations to the SEC staff and DOJ in June 2013, after it retained outside counsel to conduct an internal investigation and approximately one month after it received the second anonymous complaint. The company provided thorough, complete, and timely cooperation throughout the investigation. JCI promptly and routinely provided the staff with the results of its investigation as it progressed, and provided all supporting documentation requested. It also provided factual chronologies, hot document binders, and interview summaries, as well as English translations of numerous documents and emails. JCI made employees available for interviews. JCI provided "real time" downloads of employee interviews and made other foreign employees available for interview. When the company caught a Chinese employee shredding documents, it quickly secured the office to preserve evidence. JCI's cooperation assisted the staff's investigation. JCI's timely self-report as well as the thorough productions allowed the staff to initiate and complete its investigation quickly.

20. JCI has undertaken remedial efforts. JCI terminated or separated sixteen employees implicated in or associated with the illegal scheme and placed all suspect vendors on a do-not-use/do-not-pay list. The managing director resigned from the company before JCI was alerted to the wrongdoing. JCI has closed down its China Marine offices and moved all remaining China Marine employees, none of whom performs a sales or procurement function, into existing BE offices. In addition, JCI enhanced its integrity testing and internal audits to re-evaluate vendor onboarding for all JCI business worldwide. JCI implemented random site audits to ensure the delivery of goods on purchase orders. The random testing of delivery of goods would have tested the transactions at issue here and potentially detected the improper payments.

## **IV.**

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Respondent JCI's Offer.

Accordingly, it is hereby ORDERED that:

A. Pursuant to Section 21C of the Exchange Act, Respondent cease and desist from committing or causing any violations and any future violations of Sections 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act [15 U.S.C. §§ 78m(b)(2)(A) and 78m(b)(2)(B)].

B. Respondent shall, within fourteen days of the entry of this Order, pay disgorgement of \$11,800,000, prejudgment interest of \$1,382,561, and a civil money penalty of \$1,180,000 for a total payment of \$14,362,561 to the Securities and Exchange Commission for transfer to the general fund of the United States Treasury, subject to Exchange Act Section 21F(g)(3). If timely payment of disgorgement and prejudgment interest is not made, additional interest shall accrue pursuant to SEC Rule of Practice 600, and if timely payment of the civil monetary penalty is not made, additional interest shall accrue pursuant to 31 U.S.C. § 3717. Payment must be made in one of the following ways:

- 1) Respondent may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request;
- 2) Respondent may make direct payment from a bank account via Pay.gov through the SEC website at <http://www.sec.gov/about/offices/ofm.htm>; or
- 3) Respondent may pay by certified check, bank cashier's check, or United States postal money order, made payable to the Securities and Exchange Commission and hand-delivered or mailed to:

Enterprise Services Center  
Accounts Receivable Branch  
HQ Bldg., Room 181, AMZ-341  
6500 South MacArthur Boulevard  
Oklahoma City, OK 73169

Payments by check or money order must be accompanied by a cover letter identifying Johnson Controls as a Respondent in these proceedings, and the file number of these proceedings; a copy of the cover letter and check or money order must be sent to Tracy L. Price, Assistant Director, Division of Enforcement, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-5631.

C. Amounts ordered to be paid as civil money penalties pursuant to this Order shall be treated as penalties paid to the government for all purposes, including all tax purposes. To preserve the deterrent effect of the civil penalty, Respondent agrees that in any Related Investor Action, it shall not argue that it is entitled to, nor shall it benefit by, offset or reduction of any award of compensatory damages by the amount of any part of Respondent's payment of a civil penalty in this action ("Penalty Offset"). If the court in any Related Investor Action grants such a Penalty Offset, Respondent agrees that it shall, within 30 days after entry of a final order granting the Penalty Offset, notify the Commission's counsel in this action and pay the amount of the Penalty Offset to the Securities and Exchange Commission. Such a payment shall not be deemed an additional civil penalty and shall not be deemed to change the amount of the civil penalty imposed in this proceeding. For purposes of this paragraph, a "Related Investor Action" means a private damages action brought against Respondent by or on behalf of one or more investors based on substantially the same facts as alleged in the Order instituted by the Commission in this proceeding.

D. Respondent acknowledges that the Commission is not imposing a civil penalty in excess of \$1.18 million based upon its cooperation in a Commission investigation and related enforcement action. If at any time following the entry of the Order, the Division of Enforcement (“Division”) obtains information indicating that Respondent knowingly provided materially false or misleading information or materials to the Commission or in a related proceeding, the Division may, at its sole discretion and with prior notice to the Respondent, petition the Commission to reopen this matter and seek an order directing that the Respondent pay an additional civil money penalty. Respondent may contest by way of defense in any resulting administrative proceeding whether it knowingly provided materially false or misleading information, but may not: (1) contest the findings in the Order; or (2) assert any defense to liability or remedy, including, but not limited to any statute of limitations defense.

E. Respondent undertakes to:

1) Report to the Commission periodically, at not less than six-month intervals during a one-year term from the date of the entry of this Order, the status of its FCPA and anti-corruption related remediation and implementation of compliance measures. During this one-year period, should the Respondent discover credible evidence, not already reported to the Commission, that questionable or corrupt payments or questionable or corrupt transfers of property or interests may have been offered, promised, paid, or authorized by any Respondent entity or person, or any entity or person acting on behalf of Respondent, or that related false books and records have been maintained, Respondent shall promptly report such conduct to the Commission staff. During this one-year period, Respondent shall (1) submit an initial report, and (2) conduct and prepare one follow-up review and report, as described below:

a. Respondent shall submit to the Commission staff a written report within one-hundred eighty (180) calendar days of the entry of this Order setting forth a complete description of its remediation efforts to date, its plans for any future enhancements or improvements to its policies and procedures for ensuring compliance with the FCPA and other applicable anti-corruption laws, and the parameters of the subsequent review (the “Initial Report”). The Initial Report shall be transmitted to Tracy L. Price, Assistant Director, Division of Enforcement, Securities and Exchange Commission, 100 F Street, N.E., Washington, DC 20549. Respondent may extend the time period for issuance of the Initial Report with prior written approval of the Commission staff.

b. Respondent shall undertake one follow-up review and submit a written report relating to Respondent’s remedial efforts to devise and maintain policies and procedures reasonably designed to detect and prevent violations of the FCPA and other applicable anti-corruption laws (the “Final Report”). The Final Report should be completed within one-



hundred (180) calendar days after the completion of the Initial Report. Respondent may extend the time period for issuance of the Final Report with prior written approval of the Commission staff.

c. The periodic reviews and reports submitted by Respondent will likely include proprietary, financial, confidential, and competitive business information. Public disclosure of the reports could discourage cooperation, impede pending or potential government investigations or undermine the objectives of the reporting requirement. For these reasons, among others, the reports and the contents thereof are intended to remain and shall remain non-public, except (1) pursuant to court order, (2) as agreed by the parties in writing, (3) to the extent that the Commission staff determines in its sole discretion that disclosure would be in furtherance of the Commission's discharge of its duties and responsibilities, or (4) is otherwise required by law.

2) Certify, in writing, compliance with the undertakings set forth above. The certification and any supporting material shall be submitted to Tracy L. Price, Assistant Director, Division of Enforcement, with a copy to the Office of Chief Counsel of the Enforcement Division, no later than sixty (60) calendar days from the date of the completion of the undertakings.

By the Commission.

Brent J. Fields  
Secretary