

Litigation Release No. 8815 (S.E.C. Release No.), 17 S.E.C. Docket 1302, 1979 WL 174272

Securities and Exchange Commission (S.E.C.)

SECURITIES AND EXCHANGE COMMISSION v. INTERNATIONAL SYSTEMS & CONTROLS CORPORATION, et al., (United States District Court for the District of Columbia). Civil Action No. 79-1760.

July 9, 1979

**\*1** The Securities and Exchange Commission announced today the filing of a Complaint for injunctive relief, appointment of a receiver and other equitable relief against International Systems & Controls Corporation ("ISC"), a Houston-based corporation, and five individuals. The individual defendants are J. Thomas Kenneally, currently a director and former Chief Executive Officer and Chairman of the Board of Directors of ISC; Herman M. Frietsch, senior vice-president of ISC; Raymond G. Hofker, formerly vice-president and general counsel of ISC; Albert W. Angulo, formerly treasurer of ISC; and Harlan M. Stein, formerly president of ISC's Engineering Group. The individual defendants reside in the Houston area.

The Complaint, alleges violations of the antifraud, reporting and proxy provisions of the Securities Act of 1933 and the Securities Exchange Act of 1934, as well as the accounting and bookkeeping provisions of the Foreign Corrupt Practices Act. Alleged, among other things, are ISC's false and misleading disclosure and failures to disclose the following: a) its commitments to pay a total of \$33 million and its payment of approximately \$23 million in connection with the securing of or solicitation of business in, among other countries, Iran, Algeria, Saudi Arabia, Nicaragua, Chile and the Ivory Coast, b) ISC's overstatement of its assets, earnings and shareholders' equity, included unbilled receivables which as of ISC's fiscal 1978 year-end totaled \$31 million, and which included cost overruns on fixed-price contracts, sham claims for escalation and kickback arrangements. The Complaint further alleges that ISC failed to disclose in its periodic reports and proxy materials that defendant Kenneally and two of his associates were the prime beneficiaries of the Deferred Compensation Corporation established and funded by ISC for its key personnel; that more than one million dollars of company funds had been used to purchase, furnish and maintain a residence in Ireland principally used as the summer residence of defendant Kenneally. The Complaint also alleges that defendants Kenneally, Angulo, Hofker and Stein resigned their former positions after the time they became aware that the Commission intended to file this action against them.

The Commission simultaneously filed with the Complaint, a motion for a preliminary injunction against ISC and for the appointment of a Special Agent of the Court to take custody and control of all assets of ISC; to oversee the business activities of ISC to assure that they are being carried out for legitimate purposes of ISC and not for the personal benefit of any control person, officer, director or employee of ISC or its subsidiaries or affiliates; to review and inquire into the activities of ISC to determine whether assets of ISC have been directed for the use and benefit of any control person, officer, director or employee of ISC; to determine whether ISC entered into any transactions involving expenditures of substantial funds or assets which appear not to have been engaged in for legitimate business or are not adequately explained on ISC's books and records; to recover any funds or assets or enforce any liability to ISC; to oversee ISC's filings with the Commission; and to authorize the agent to report his findings to the Court within 60 days.

**\*2** The affidavit in support of the preliminary injunction specifies in detail the amounts of questionable and illicit payments made, the individuals to whom made, the governmental positions or associations they had, if any, and the projects in connection with which they were made, in Iran, Algeria and Saudi Arabia. The affidavit details the methods of payment and identifies the foreign bank accounts, including accounts in Switzerland, Lichtenstein, France and Lebanon to which payments were sent. The affidavit sets forth agreements with suppliers and contractors relating to rebates and kickbacks and the payment to ISC or its subsidiaries of amounts by which such contractors or suppliers inflated their bills. It is alleged that in Iran the amount of inflated costs was approximately \$3.5 million. It was also alleged that ISC

made a fictitious escalation claim to the Iranian government of which \$8.2 million at fiscal year 1978 were still being treated as an asset on the financial statements of ISC.

The affidavit and the Complaint assert that false statements regarding use of intermediaries were made to government-owned entities in Iran and Algeria and that ISC's ability to collect approximately \$31 million in its "unbilled receivables" is further jeopardized by its questionable and illicit payments, the inflation of suppliers' invoices, the inability of ISC and its subsidiaries to satisfy the governmental contracting authorities as to the true costs incurred on the various projects and the false statements filed with those authorities.

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