

U.S. SECURITIES AND EXCHANGE COMMISSION

Litigation Release No. 21616 / August 5, 2010

Securities and Exchange Commission v. James W. McIntosh, et al., Civil Action No. 10-cv-4903 (N.D. Ill.) (August 4, 2010).

Securities and Exchange Commission v. Mark T. Schwetschenau, Civil Action No. 10-cv-4904 (N.D. Ill.) (August 4, 2010).

NAVISTAR SETTLES WITH COMMISSION OVER CERTAIN RESTATED 2002-2005 FINANCIAL RESULTS

SETTLED ORDER FINDS THAT CEO AND FORMER CFO WERE CAUSES OF NAVISTAR'S INTERNAL CONTROL VIOLATIONS, AND THEY AGREE TO RETURN MORE THAN \$2 MILLION IN BONUSES RECEIVED DURING THE RESTATEMENT PERIOD

COMMISSION SETTLES WITH FIVE OTHER CURRENT AND FORMER NAVISTAR EMPLOYEES INCLUDING FRAUD CHARGES AGAINST CERTAIN INDIVIDUALS

FORMER COMPANY CONTROLLER AGREES TO SUSPENSION FROM APPEARING OR PRACTICING BEFORE COMMISSION AS ACCOUNTANT; CAN RE-APPLY AFTER ONE YEAR

On August 5, 2010, the United States Securities and Exchange Commission (Commission) issued a cease-and-desist order against Navistar International Corporation (Navistar), CEO Daniel C. Ustian (Ustian), former CFO Robert C. Lannert (Lannert), Thomas M. Akers, Jr. (Akers), James W. McIntosh (McIntosh), James J. Stanaway (Stanaway), Ernest A. Stinsa (Stinsa) and Michael J. Schultz (Schultz). Each Respondent consented to the issuance of the Order without admitting or denying the Commission's findings as part of a global settlement.

The Order finds that at times from 2001 through 2005, Navistar overstated its pre-tax income by a total of approximately \$137 million as the result of various instances of misconduct. Fraud by certain individuals at a Wisconsin foundry and in connection with certain vendor rebates and vendor tooling transactions accounted for approximately \$58 million of that total. The remaining approximately \$79 million resulted from improper accounting for certain warranty reserves and deferred expenses.

More specifically, the Order finds, among other things, that:

- Navistar had numerous deficiencies throughout its system of internal controls during the relevant period, including fifteen material weaknesses during 2005-06 that were attributable, in part, to the Company's failure to dedicate sufficient resources to those controls.
- From 2001 through 2004, Navistar improperly booked as many as 30 vendor rebates and related receivables from its suppliers. While these rebates and receivables took different forms — including volume-based rebates and so-called "signing bonuses" for Navistar's award of new business — all were improperly booked as income in their entirety upfront, even though, in whole or in part, they were earned in future periods. The Company's eventual restatement of these rebates and receivables totaled \$9.7 million of pre-tax income in 2004, which represented 27.7 percent of that year's restated loss before income taxes.
- In 2003, Navistar improperly accounted for certain tooling buyback agreements by recapturing and booking as income the previously-paid amortization on those agreements and then improperly deferring the related depreciation costs. The Company continued to utilize this improper accounting treatment in 2004 to record 60 days of amortization from the buyback agreements as income, despite

employees' warnings that doing so would be inconsistent with the outside auditor's guidance.

- From 2001 to 2005, Schultz, the Waukesha, Wisconsin plant controller, engaged in various fraudulent accounting practices that collectively caused income during that period to be overstated by a total of approximately \$38 million.
- Beginning in fiscal year 1999, Navistar inappropriately included various "below-the-line" items in the Company's warranty reserve calculation, which caused the warranty reserve expense to be understated by \$17 million in fiscal year 2002 and by \$18.5 million in fiscal year 2003. The \$18.5 million total represented 5.9 percent of the restated loss before income tax for that year.
- Navistar, through its senior accounting staff, deferred certain start-up costs from the fourth quarter of 2001 through the fourth quarter of 2002 that were not in compliance with Generally Accepted Accounting Principles (GAAP). Specifically, the Company deferred \$4.3 million in the fourth quarter of fiscal year 2001, \$12.8 million in the first quarter of fiscal year 2002, and \$13.3 million in each of the second and third quarters of fiscal year 2002.
- Navistar, from the first quarter of fiscal year 2004 through the third quarter of 2005, failed to report its Parts group as a segment in its publicly-filed financial statements and notes, and instead allocated the Parts group's results between its Truck and Engine divisions' results. This resulted in investors not being able to view the Parts group in the same manner as senior management and the Board. The Company's Forms 10-K for at least fiscal year 2004 and Forms 10-Q for 2004 and the first three quarters of 2005 failed to provide complete segment information required by GAAP and Commission rules.

Based on the above, the Order directs Navistar to cease and desist from committing or causing any violations and any future violations of Sections 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act and Rules 12b-20, 13a-1, and 13a-13 thereunder and Ustian, Navistar's CEO, and Lannert, Navistar's former CFO, to cease and desist from causing any violations and any future violations of Section 13(b)(2)(B) of the Exchange Act.

Ustian and Lannert also agreed to comply with the forfeiture provisions of Section 304(a) of the Sarbanes-Oxley Act of 2002. Ustian consented to tender to the Company shares of Navistar common stock currently owned by Ustian in the amount of \$1,320,000 and Lannert consented to pay \$1,049,503 to the Company. Those dollar amounts reflect monetary bonuses that each received during the restatement period.

Additionally, the Order directs McIntosh to cease and desist from committing or causing any violations and any future violations of Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rules 10b-5 and 13b2-1 thereunder and from causing any violations and any future violations of Sections 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act; Akers, Schultz and Stanaway to cease and desist from committing or causing any violations and any future violations of Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rules 10b-5 and 13b2-1 thereunder and from causing any violations and any future violations of Section 13(b)(2)(A) of the Exchange Act; and Stinsa to cease and desist from committing or causing any violations and any future violations of Exchange Act Rule 13b2-1 and from causing any violations and any future violations of Section 13(b)(2)(A) of the Exchange Act.

The Commission filed a parallel civil action in the United States District Court for the Northern District of Illinois against Akers, McIntosh, Stanaway, Stinsa and Schultz, in which each consented to pay civil penalties as follows: Akers — \$100,000; McIntosh — \$150,000; Stanaway — \$50,000; and Stinsa — \$25,000. A civil penalty was not imposed against Schultz because of a demonstrated inability to pay. These individuals consented to the filing of this complaint without admitting or denying its allegations.

Additionally, on August 5, 2010, the Commission issued a separate settled order concerning Navistar's former Controller, Mark T. Schwetschenau. The Order directs

Schwetschenau to cease and desist from causing any violations and any future violations of Sections 13(a) and 13(b)(2)(B) of the Exchange Act. The Order also denies him the privilege of appearing or practicing before the Commission with the right to request reinstatement after one year pursuant to Section 102(e)(1)(ii) of the Commission's Rules of Practice.

The Commission filed a parallel civil action in the United States District Court for the Northern District of Illinois against Schwetschenau in which he consented to pay \$37,500 in civil penalties. Schwetschenau neither admitted nor denied the Commission's findings and allegations.

See Also: SEC Complaints v. [James W. McIntosh et al.](#) and [Mark T. Schwetschenau](#)

<http://www.sec.gov/litigation/litreleases/2010/lr21616.htm>

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