

## CLIENT ALERT

JUNE 2007

### PRIVATE INVESTORS ENTER THE FCPA ARENA

On June 22, 2007, an arrest was made in a characteristic Foreign Corrupt Practices Act (FCPA) case that involved an uncharacteristic player: a private equity investment firm. Leo Winston Smith, a former executive of Santa Ana, CA-based Pacific Consolidated Industries LP (PCI), was arrested for allegedly violating the FCPA by conspiring to bribe a United Kingdom Ministry of Defence official. The case was brought after the private investors who acquired PCI discovered suspicious payments and referred the matter to the Department of Justice (DOJ).

The alleged FCPA violations described in the federal grand jury indictment against Smith tell a familiar tale of a wayward sales executive wining, dining, and bribing his way to a lucrative defense contract for his company. According to the DOJ press release, Smith was the executive vice president and director of sales and marketing at PCI, a private manufacturer of portable air separation equipment for global commercial and military end-users; he had been with the company for more than 25 years. Between 1993 and 2003, Smith allegedly conspired to violate the FCPA by offering more than \$300,000 in bribes to a project manager in the UK Ministry of Defence to secure equipment contracts for PCI valued at over \$11 million. The payments included wire transfers from PCI bank accounts in California to banks in England and Spain, some of which were used by the project manager to purchase a Spanish villa. According to news reports, Smith also allegedly provided lavish hospitality to the project manager and his

wife, including travel to the U.S., stays in exclusive hotels, and entertainment on Smith's luxury yacht.

Although the allegations against Smith are somewhat run-of-the-mill, they were sparked by a group not typically associated with the FCPA—private investors. In November 2003, PCI was acquired by private equity investment group Cherington Capital and re-named Pacific Consolidated Industries, LLC (PCI LLC). Thereafter, during a post-acquisition audit, PCI LLC discovered nine suspicious payments made by Smith to the project manager. PCI LLC then referred the matter to the DOJ and fully cooperated in the subsequent investigation.

The Smith case highlights the fact that groups such as private equity investment and venture capital firms are not outside the reach of the FCPA, and that they should consider potential FCPA liability when making investments and acquisitions. FCPA violations provide front-page fodder for federal law enforcement. Recent matters, such as the indictment of Louisiana Congressman William Jefferson and the investigation of BAE, demonstrate the strong interest the DOJ is taking in FCPA cases. More than ever, U.S. investment entities will need to identify and remedy potential FCPA issues. Without taking precautions such as conducting FCPA-specific audits or proper due diligence as PCI LLC did, private investors could find themselves liable for pre-acquisition or pre-investment violations.

Accordingly, we recommend that investors: (1) ensure that their due diligence includes FCPA troubleshooting, and (2) determine whether additional FCPA compliance or training materials need to be put in place. For more information about this topic or related FCPA issues, please contact Lisa Prager or Leo Cunningham in Wilson Sonsini Goodrich & Rosati's white collar crime and internal investigations practice.



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