The Foreign Corrupt Practices Act: A Cautionary Tale

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Public companies planning to expand internationally — particularly into “high-risk” markets — should be wary of the Foreign Corrupt Practices Act (FCPA). This was enacted for the purpose of making it unlawful for certain classes of persons and entities to make payments to foreign government officials to assist in obtaining or retaining business. Without an appropriate FCPA compliance program and strong internal controls designed to prevent and detect violations, companies risk steep monetary penalties, reputational damage, and even jail time for officers or employees guilty of bribing foreign officials.

Smith & Wesson learned this lesson the hard way. In July 2014, the gun manufacturer settled an FCPA enforcement action with the SEC, consenting — without admitting or denying wrongdoing — to pay a $2 million penalty. The penalty eclipsed the company’s profits attributable to its alleged bribery, which was just over $100,000. The company must also report to the SEC on its FCPA compliance efforts for the next two years.

What The Act Prohibits

The FCPA has two main provisions:

- **Anti-bribery.** It’s unlawful for public companies to pay or offer to pay (directly or through an intermediary) money or anything of value to a foreign official for the purpose of obtaining or retaining business.

- **Accounting.** Public companies are required to keep accurate books and records and to maintain effective internal accounting controls.

The FCPA prohibits bribes even if they’re legal (or tolerated) in the country where they’re made. And, while the Act is directed toward bribery of foreign officials, it also prohibits payments to agents or other private parties that are used to influence an official.

Proving a bribe can be a challenge, but many companies have been found guilty of FCPA violations due to inadequate records or internal controls — even without evidence of bribery. In addition to penalties, FCPA violators may be required to disgorge any profits attributable to a violation and to report their remediation efforts to the SEC.

How Smith & Wesson Violated The Act

According to the SEC, from 2007 through early 2010, in an effort to break into international markets, Smith & Wesson’s employees and agents “engaged in a pervasive practice of making, authorizing and offering improper payments to foreign government officials as a means of obtaining or retaining international business.” Examples of these improper payments include the following:

- In 2008, Smith & Wesson’s Vice President of International Sales and its Regional Director of International Sales authorized a third-party agent in Pakistan to provide more than $11,000 worth of guns to Pakistani police officials as gifts, and to make additional cash payments to those officials. The company sold 548 pistols to the Pakistani police for more than $200,000, earning just over $100,000 in profits.

- In 2009, the same officers authorized improper payments, through a third-party agent, to Indonesian police officials to win a firearms contract. The payments were disguised as legitimate firearm lab testing costs. Although the payments were made, a deal was never consummated.

- Also in 2009, the company made improper payments through a third-party agent to Turkish officials in an effort to win contracts to sell handcuffs to the Turkish police and firearms to the Turkish military. Again, neither deal was consummated.

Based on these and other improper payments, the SEC charged Smith & Wesson with anti-bribery violations. It also charged the company with books and records violations and for internal controls violations.

The SEC noted that the company had a corporate policy prohibiting bribery, but failed to implement a reasonable system of controls to effectuate that policy, particularly in light of its decision to grow sales in new, high-risk markets. The SEC criticized the manufacturer for failing to perform an anticorruption risk assessment and for conducting “virtually no due diligence” on its third-party agents in countries with a history of corruption.

The company also failed to establish policies and procedures for gifts, commission payments and advances, or use of samples for testing. What’s more, its Vice President of International Sales had nearly complete control over the company’s international
business, including sole authority to approve most commissions. Finally, Smith & Wesson’s FCPA-related policies, procedures, 
training and supervision were deemed inadequate.

**Review Your Compliance Program**

If you do business overseas, or plan to expand internationally, make sure you have policies, procedures and controls in place to 
prevent and detect FCPA violations. In the event of a violation, act quickly to address the issue and take steps to prevent similar 
ocurrences in the future. Doing so can help mitigate penalties in the event the SEC brings an enforcement action against your 
company.

**Softening The Blow**

Establishing a solid FCPA compliance program and strong system of internal controls can help your company reduce or avoid 
penalties in the event of a violation. In the case of Smith & Wesson (see main article), even though the manufacturer’s compliance 
program and internal controls were inadequate, its prompt action to remediate its FCPA issues helped avoid even greater 
penalties. For example, the company:

- Conducted an internal investigation,
- Fired the international sales staff,
- Terminated pending international sales transactions,
- Re-evaluated the international markets it had targeted, and
- Implemented significant measures to improve its internal controls and compliance processes.

These measures included new internal audit procedures designed to identify FCPA issues, more robust controls on payments, gifts 
and other international transactions, and enhanced FCPA compliance policies and procedures. The company also established a 
business ethics and compliance committee.