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White Collar Corner: Small businesses likely target of False Claims Act liability for CARES Act fraud

On March 27, the President signed into law the largest economic stimulus bill in U.S. history known as the Coronavirus Aid, Relief, and Economic Security (CARES) Act. The CARES Act provides more than $2 trillion in federal economic assistance for individuals, businesses, public health, and state and local governments to help mitigate the effects of the COVID-19 pandemic.

Among the major programs and initiatives that will be attractive to small business owners are the Paycheck Protection Program and the Small Business Debt Relief program. These programs offer expedited economic relief to small businesses with little regulation or significant guidance. The lure of easy money can bring with it harsh consequences for abuse.

Following enactment of the Troubled Asset Relief Program (TARP) in 2008, the U.S. Department of Justice (DOJ) used the federal False Claims Act (FCA) to recover funds allegedly obtained from the government in a false or fraudulent manner. Policing of TARP funding resulted in numerous criminal convictions and huge financial settlements for the government, as described below. The same can be expected with CARES Act funding.

DOJ and the False Claims Act

The DOJ has already announced that it will focus resources on COVID-19-related fraud. On March 20, Attorney General William Barr "directed all U.S. attorneys to prioritize the investigation and prosecution of coronavirus-related fraud schemes." The FCA is a powerful investigative and enforcement tool to employ against any person who submits (or conspires to submit) a claim to the federal government that he or she knows (or should know) is false. Persons who violate the FCA are liable for "treble" damages, as well as penalties and attorneys' fees. Many FCA actions are filed under its "qui tam" provision, which allows individuals to file lawsuits on behalf of the government. If successful in the action, the whistleblower, also known as the relator, can receive up to 30 percent of the recovery amount. Unsurprisingly, the qui tam plaintiffs' bar is already seeking whistleblowers to bring FCA actions based on CARES Act fraud.

The FCA also provides for criminal penalties. The DOJ has a history of investigating and prosecuting individuals for FCA crimes. FCA criminal penalties include significant fines and possible jail time. Since corporations cannot be put in prison, the DOJ will frequently begin an investigation into a company, but end up pursuing criminal charges against corporate officers or directors.

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Oversight under the CARES Act

The CARES Act establishes three separate bodies charged with oversight of stimulus funds:

The Office of the Special Inspector General for Pandemic Recovery (SIGPR) within the Treasury Department;

The Pandemic Response Accountability Committee (PRAC); and The Congressional Oversight Commission (COC).

SIGPR will conduct, supervise and coordinate "audits and investigations of the making, purchase, management and sale of loans, loan guarantees, and other investments" by the Treasury Secretary under any program established by the CARES Act. SIGPR is authorized to conduct investigations, issue reports and refer matters to the DOJ for criminal or civil investigation.

PRAC will support inspectors general in the oversight of stimulus funds in order to "detect and prevent fraud, waste, abuse, and mismanagement; and mitigate major risks that cut across programs and agency boundaries." PRAC also has the ability to conduct investigations and to refer matters to the DOJ for criminal or civil investigation.

Lastly, the COC will oversee the implementation of the CARES Act stimulus package by the Treasury Department and Federal Reserve Board, and with assessing its effectiveness. The COC is authorized to hold hearings, to take testimony, to receive evidence and to issue reports.

Comparison with 2008 TARP oversight

Similar oversight mechanisms of a stimulus package have been utilized before, as during TARP, the $700 billion bank bailout passed during the 2008 financial crisis. Like the CARES Act, TARP established the Office of the Special Inspector General for the Troubled Asset Relief Program (SIGTARP) to investigate fraud associated with TARP funds. SIGTARP remains active today. Its investigations have targeted countless recipients of TARP stimulus funds. SIGTARP and the DOJ have used the FCA to pursue thousands of investigations related to the 2008 financial crisis. Their work has recovered more than $10 billion and led to the convictions of 364 criminal defendants. Notable investigations by SIGTARP include:

- In 2012, Regions Financial Corp. settled an FCA action alleging that it undervalued a promissory note in order to qualify for money under TARP, and then lied to investigators about its need for government assistance.
- In 2015, Fifth Third Bank paid $85 million to settle FCA claims that its employees made false representations to the U.S. Department of Housing and Urban Development about the quality of the residential mortgages the bank originated.
- In 2015, the estate of a former owner and president of a corporation settled an FCA action for $4 million based on allegations of false statements made about the financial condition of his corporation and the intended use of TARP funds.
- In 2018, SIGTARP settled an FCA action with Martin Enterprises for fraudulently submitting claims for federal TARP Blight Elimination Program funds for improperly performed demolition work.

One glaring difference between the oversight of TARP funds and that of the CARES Act is the range of relief fund recipients. TARP beneficiaries primarily consisted of a limited number of financial institutions and large corporations. The CARES Act, however, makes relief funds available to an indefinite number of individuals and small businesses affected by COVID-19 across nearly every industry, which will result in expansive policing efforts by SIGPR and the DOJ.

In its recovery efforts, the government often relies upon a certification theory of liability, under which "a claim for payment is false when it rests on a false representation of compliance with an applicable federal statute, federal regulation, or contractual term." In other words, FCA liability can be grounded on false certifications of eligibility related to government contracts and loans. The DOJ will surely apply these same theories in pursuing fraud under the CARES Act, as many programs have certification requirements built in.

Conclusion

We can expect SIGPR, like SIGTARP, to investigate the applications for — and use of — CARES Act stimulus funds, and to work closely with the DOJ to prosecute misconduct. The DOJ will continue to utilize the FCA to police these new and expanded programs. However, while the agencies charged with the oversight of TARP funds focused their enforcement efforts primarily on financial institutions and large corporations, SIGPR and the DOJ will also focus their scrutiny on individuals and small businesses.

Takeaways: Businesses are well-advised to take extra precautions when applying for relief through CARES Act initiatives such as the Paycheck Protection Program and the Small Business Debt Relief program. These programs require applicants to certify that they are eligible for relief, and that they will use the funds for authorized purposes only. Any knowingly false or misleading statements made in order to obtain financial assistance from the government could trigger liability. Anyone accepting government funding should ensure that all information provided in connection with these programs is true and accurate. Applicants should also seek legal guidance when necessary to ensure compliance and the appropriate use of program funds.

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