May 5, 2020

DOJ Announces Preliminary Inquiry into Potential Fraud in the Paycheck Protection Program

Note: Two relevant developments occurred following the drafting of this memorandum. On May 5, 2020, the SBA announced in an FAQ (available here) that it is extending to May 14, 2020 the repayment date under the limited safe harbor created for borrowers who applied for a PPP loan prior to April 24, 2020 and who repay the loan in full. The SBA also stated that it plans to provide additional guidance on how it will review the "economic uncertainty" certification. Also on May 5, 2020, the Department of Justice announced criminal charges against two individuals for allegedly filing false applications for PPP loans. (The DOJ press release is available here.) The defendants allegedly claimed to have dozens of employees earning wages at four different business entities when, in fact, there were no employees working for any of the businesses. One of the defendants allegedly made some of these false statements on a telephone call with an undercover FBI agent posing as a bank compliance offer. The charges are the first in the nation for defrauding the CARES Act PPP.

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Key Takeaways

- *On April 30, 2020, Assistant Attorney General Brian Benczkowski of the U.S. Department of Justice ("DOJ") stated publicly that the DOJ has initiated a preliminary inquiry into possible instances of fraud in the Paycheck Protection Program ("PPP"). According to Mr. Benczkowski, the DOJ has contacted 15 to 20 of the largest lenders and has already found possible fraud among businesses seeking relief.*

- *Although the DOJ's current inquiry appears to be focused on potential false statements made in PPP loan applications, the scope of inquiries by DOJ and other agencies will likely expand to other aspects of the program, including recipients' use of loan proceeds and the forgiveness process. Banks and other lenders also may be subject to scrutiny regarding the manner in which they made PPP loans.*

- *The PPP and related relief programs also can be expected to attract significant investigative interest from other federal and state enforcement authorities, new and existing oversight agencies, regulators, and Congressional committees.*

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In our March 31, 2020 client memorandum on "White-Collar Enforcement Priorities in the Wake of COVID-19" (available here), we described our expectation that law enforcement and other government agencies would focus on investigating potential fraud and abuse by recipients of relief funds made available under the Coronavirus Aid Relief and Economic Security Act (the "CARES Act"). That appeared likely based on public pronouncements by several government authorities, the precedent provided by prior federal relief programs such as the Troubled Asset Relief Program ("TARP"), and the substantial amount of money being made available through the CARES Act.

More recently, on April 30, 2020, the Assistant Attorney General in charge of the Criminal Division of the U.S. Department of Justice ("DOJ"), Brian Benczkowski, stated publicly that DOJ has initiated a preliminary inquiry into possible instances of fraud in the Paycheck Protection Program ("PPP").[1] The PPP, established pursuant to the CARES Act, offers forgivable loans to eligible businesses and self-employed individuals affected by the COVID-19 outbreak.[2] The program's initial $349 billion funding was depleted in two weeks, and an additional $310 billion was authorized on April 24, 2020. According to Mr. Benczkowski, in connection with its inquiry, the DOJ has contacted 15 to 20 of the largest lenders, as well as the Small Business Administration (which administers the PPP), and already has found possible fraud among businesses seeking relief.[3]

In order to receive PPP funds, the applicant must complete and certify an application that includes representations about its business, payroll history and intended uses of the loan proceeds. An applicant who knowingly submits a false application could face criminal liability under a number of federal statutes (including statutes prohibiting making false statements to a federal agency, mail and wire fraud, and bank fraud), as well as civil liability under the False Claims Act ("FCA"). Notably, FCA actions may be initiated by the DOJ or by private whistleblowers known as relators in a *qui tam* lawsuit.

Mr. Benczkowski flagged examples of areas of concern in the PPP applications, stating: "There are unfortunately businesses that are sending in loan applications for large amounts of money that are overstating their payroll costs, overstating the number of employees they've had, overstating the nature of their business."[4] Applicants must certify, among other things, that "[c]urrent economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant."[5] This certification has been the subject of recent attention following the SBA's issuance of new guidance interpreting this standard and

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1 *See* Tom Schoenber and Christian Berthelsen, *Justice Department Sees Early Fraud Signs in SBA Loan Flurry*, Bloomberg (Apr. 30, 2020), available here.

2 *See* H.R. 748 § 1102.

3 *See* Schoenber, *supra* note 1.

4 *See* Schoenber, *supra* note 1.

5 Paycheck Protection Program Borrower Application Form at 2, available here.

its creation of a safe harbor for borrowers that fully return their PPP loans by May 7, 2020,[6] and will likely be the focus of inquiries by government agencies examining whether certain businesses may have improperly obtained relief funds. On April 28, 2020, for example, Treasury Secretary Steven Mnuchin and Small Business Administrator Jovita Carranza issued a joint statement in which they noted the number of companies that had repaid loans "in response to SBA guidance reminding all borrowers of an important certification required to obtain a PPP loan," and announced that the SBA will review all loans in excess of $2 million "[t]o further ensure PPP loans are limited to eligible borrowers."[7]

Although the initial focus of the DOJ's inquiry appears to be on false statements made in PPP loan applications, the scope of investigative inquiries by the DOJ and other agencies will likely extend to other aspects of the program, such as recipients' use of the loan proceeds and the forgiveness process. Banks and other lenders also may be subject to scrutiny regarding the manner in which they made PPP loans, and there is already litigation against certain lenders alleging that they improperly prioritized certain applicants.

The DOJ inquiry is being overseen by the Criminal Division's Fraud Section in Washington, DC, in coordination with various U.S. Attorneys across the country. While it is unclear whether or to what extent DOJ may be coordinating with other agencies in the current inquiry, other government agencies and oversight authorities at the federal and state levels are also likely to probe the receipt and disbursement of relief funds under the PPP and other CARES Act programs.

The Act itself establishes new oversight bodies and, if history guides, these oversight bodies could take an active role in investigations focused on the procurement of relief funds. The CARES Act provides for a three-body oversight structure: a Pandemic Response Accountability Committee with subpoena power staffed by Inspectors General of various federal agencies, a Congressional Oversight Commission, and a Special Inspector General for Pandemic Recovery ("SIGPR") who is awaiting confirmation by the Senate. The SIGPR is the CARES Act analogue to the Special Inspector General for the Troubled Asset Relief Program ("SIGTARP"), which, notably, conducted a wide range of investigations that extended beyond the specific circumstances under which businesses secured relief funds. The CARES Act also provided additional funding to the Inspector General of the SBA.

Members of the House and Senate from both parties have also signaled an intent to probe potential fraud or abuse in the procurement and disbursement of relief funds. For example, Senator Marco Rubio, Chairman of the Senate Committee on Small Business and Entrepreneurship, promised "aggressive

6 *See* Paycheck Protection Program Frequently Asked Questions, #31 (Apr. 23, 2020), available here; *see also* 13 C.F.R. 120 (Apr. 28, 2020), available here.

7 Joint Statement by Secretary Steven T. Mnuchin and Administrator Jovita Carranza on the Review Procedure for Paycheck Protection Program Loans (Apr. 28, 2020), available here.

oversight into the use of the PPP"[8] and tweeted that "[t]he certification language in #PPP is real & enforceable."[9] And, the House Committee on Oversight and Reform recently formed the Select Committee on the Coronavirus Crisis, to monitor how COVID-19 related funds are being spent.[10]

Based on the extraordinary dollar amount of relief funds disbursed under the CARES Act, various enforcement and oversight agencies are likely to devote substantial resources to examining potential fraud and abuse in the procurement of relief money under the PPP and related programs. Recent comments by Assistant Attorney General Benczkowski confirm that the DOJ already is actively investigating potentially false PPP loan applications and has found possible fraud among businesses seeking relief. The PPP and related programs also can be expected to attract investigative interest from new and existing oversight agencies, regulators, state Attorneys General, and Congressional committees.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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8 *See* Press Release, Sen. Marco Rubio, (Apr. 20, 2020), available here.

9 Marco Rubio (@marcorubio), Twitter (Apr. 20, 2020), available here.

10 *See* Press Release, Rep. Carolyn B. Maloney, (Apr. 29, 2020), available here.