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Insights

WHAT RECIPIENTS OF PPP LOANS NEED TO KNOW AND DO TO MITIGATE FRAUD RISK

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SUMMARY

While the Paycheck Protection Program (PPP) loans under the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) have given businesses a lifeline during these uncertain times, they also present a risk for fraud claims down the road. Recipients of larger PPP loans may become targets of False Claims Act (FCA) allegations, which can be made not only by the government, but also by individual whistleblowers. We discuss below this increased risk and how companies can mitigate that risk.

The PPP and the FCA

Under the PPP, applicants are required to make various certifications, including the necessity of the funds, how the funds will be used, and the applicant's payroll history.

Although the PPP application specifically states that applicants can be subject to criminal liability for the provision of false information or certifications in connection with the application, there is another source of liability that is likely a more significant risk – the FCA.

The FCA imposes civil liability with significant monetary penalties. It is important to note that the Department of Justice (DOJ) is not the only source for an FCA action. FCA actions may be initiated by private whistleblowers known as relators in a qui tam lawsuit.

At a very high level, the FCA is what the government uses each year to recover billions of dollars from individuals and companies that defraud the government. Not only are the fraudulently received funds recovered, but the damages can be up to triple the amount the government paid, and there are also very high monetary penalties for each false claim that is submitted. The aggregate amount of damages and penalties can quickly add up resulting in exposure to potential liability that is many times more than the amount initially received from the government.

Because the FCA imposes civil liability, the standard for proving fraud under the FCA is significantly lower than the requirement in criminal cases to prove intentional fraud. Under the FCA, “actual knowledge, deliberate ignorance or reckless disregard of the truth or falsity of information” is enough to prove fraud.

History Repeats Itself

In addition to FCA liability, which will be spearheaded by the plaintiffs’ bar, government enforcement typically intensifies during times of crisis that are accompanied by significant government outlays. Taxpayers also want accountability for fraud that occurs in connection with government programs, especially those related to stimulus efforts.

The past is a clear indicator that recovery from crisis-related fraud will be significant. The most recent financial crisis in 2008 led to the creation of the Troubled Asset Relief Program. As of last year, fraud under this program was still being prosecuted, with $900 million recovered in 2019 and over $11 billion recovered to date.

The government has already said combating this fraud will be a top priority. As of April 30, 2020, the DOJ initiated a preliminary inquiry into possible instances of fraud in the PPP and contacted 15 to 20 of the largest lenders, as well as the Small Business Administration (SBA). The DOJ noted it already found possible fraud among businesses seeking relief. While not FCA cases, within a span of nine days, the DOJ announced federal charges in four separate cases against defendants accused of committing fraud related to PPP loans.

How to Protect Yourself and Mitigate Risk

Now is the time to act. Taking the time now to document and establish controls will pay dividends. While DOJ’s immediate focus is on false statements made in the PPP loan applications, the scope is almost guaranteed to broaden to include other areas such as recipients’ use of the loan proceeds and the forgiveness process.

If the recipient of PPP funds becomes the subject of a FCA inquiry by the DOJ or other government agency, or is alerted by a whistleblower of potential wrongdoing, the initial response is critical and has long-lasting consequences to the entire life of the investigation or lawsuit.

Below are some immediate steps that can be taken. Next week we will provide a deeper dive into best practices for mitigating risk and responding to fraud allegations in connection with PPP funds.

1. Document the rationale and support for each certification now. It could be years before allegations of wrong doing come to light. As time passes, memories fade. Having documentation made now that explains how decisions were made to support the basis for each certification will be invaluable.

2. Implement controls to ensure the funds received are deployed as required under the PPP.

3. If you become aware of an issue, either through a whistleblower or through a government investigation, immediately retain experienced counsel to conduct an independent, internal investigation and represent the company through the life of the matter.

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