

BORROWER BEWARE II: WHISTLEBLOWER WORKERS PUT PPP BORROWERS IN THE GOVERNMENT'S CROSSHAIRS FOR FALSE CLAIMS ACT AND CRIMINAL INVESTIGATIONS

Hodgson Russ COVID-19 Litigation & Employment Action Team Alert
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The Paycheck Protection Program (“PPP”), created by the CARES Act to help small businesses keep workers on the payroll during the COVID-19 pandemic, has closed its doors to new borrowers. While operational, the PPP resulted in more than 5.2 million loans for \$525 billion in funding.[1] But what do those numbers mean? Did the program really help small businesses weather the most significant public health crisis in our lifetime?

According to many, the answer is no. As discussed in our first Borrower Beware alert which can be viewed here, the program was riddled with uncertainties and evolving guidance that proved difficult for borrowers to navigate, prompting fears about potential forgiveness denials and government enforcement if the borrower is later found to be ineligible or misapplied the funds. Media headlines on the program have been critical and accusatory, suggesting a common perception: the PPP funds didn’t get to the small businesses and workers they were intended to help and were, instead, captured by large, established companies or by illegitimate fraudsters taking advantage of the system.[2] Public perception is supported by statements from elected leaders. According to a memorandum released by House Democrats, PPP funds were subject to significant fraud, waste, and abuse, with over \$1 billion in loans going to companies that received multiple loans (in violation of SBA requirements), over \$96 million in loans going to companies excluded from doing business with the government, and almost \$3 billion in loans disbursed to borrowers with “red flags,” including inconsistent identifying information provided to various government agencies and non-existent addresses on loan applications.[3]

So what does this mean for borrowers acting in good faith? Regardless of whether you think you did anything wrong, you may be caught up in years of audits and investigations into eligibility for, and uses of, PPP funds conducted by any (or all) of the many federal agencies with jurisdiction over the program. And these agencies may be getting their information from those most directly affected by the PPP – workers.

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Whistleblowers and Government Informants

The False Claims Act (“FCA”) is a Civil-War era statute that allows the government to recover treble damages from those who present, or cause to be presented, false claims for payment or approval. To prove liability, the government does not have to show that the defendant intended to do anything wrong, but only that the defendant was “reckless” as to the truth or falsity of any potential claim. So what do workers have to do with government enforcement under the FCA? In fact, they play a key role in enforcement because the FCA expressly allows a private individual (*i.e.*, a whistleblower) to bring an action on behalf of the government and obtain between 15%-30% of the proceeds of any recovery. The prospect of a financial windfall may incentivize workers to investigate and attempt to uncover PPP-related fraud by their employers in order to bring an FCA case.

And because of its wide net (“causing” a false claim to be presented), relatively low burden of proof (“recklessness”), and the recovery of three times the amount of claimed damages, the FCA has become the government’s weapon of choice for civil fraud cases. In fiscal year 2019, the government recovered more than \$3 billion under the statute; of this amount, over \$2.1 billion came from lawsuits filed by whistleblowers.[4] And the statute’s importance to the government has only increased in light of the pandemic and PPP disbursements. In a speech on June 26 to the U.S. Chamber of Commerce, then-Principal Deputy Assistant Attorney General for the DOJ’s Civil Division Ethan David made clear that the DOJ “will make it a priority to use the False Claims Act to combat fraud” in the PPP. More recently, Senator Grassley – a staunch supporter of whistleblowers – noted in remarks to Congress on July 20 that “the False Claims Act has never been more important than it is right now in 2020” given the “massive increase in government funding to address the Covid-19 crisis,” which has “created new opportunities for fraudsters trying to cheat the government and steal hard-earned taxpayer dollars.” He also noted the “dramatic increase” in whistleblower complaints made specifically to the SEC.[5]

But FCA cases aren’t the only way that employees are driving government investigations and enforcement. They appear to be shaping criminal investigations and charges, as well. In the initial months after the PPP became operational, a number of indictments were issued for blatant – and easily identified – fraud in the program. For example, on September 3, an attorney was charged with fraudulently obtaining approximately \$9 million in PPP funds by fabricating employee information and bank and tax records. The attorney used the funds for personal expenses, including the purchase of an almost \$1 million dollar home, remodeling expenses, and investing millions in the stock market.[6] On August 4, a Texas man was accused of fraudulently obtaining more than \$1.6 million in PPP loans by falsely claiming that certain entities had numerous employees and significant payroll expenses. In reality, neither entity had any employees nor paid the wages claimed. And the CEO identified for one of the companies had died a month before the application was submitted. The funds were spent on luxury items, including a Lamborghini and a Rolex, and also at strip clubs and other night clubs.[7]

But the Government will not limit itself to prosecuting these types of obvious criminal conduct – particularly when there are numerous sources of information regarding the use of PPP funds, *i.e.*, the workers the program was intended to keep on the payroll. Hannibal Ware, the inspector general of the SBA, has noted that these initial indictments are “the smallest, tiniest piece of the tip of the iceberg.”[8] And we know that workers are blowing the whistle. The SBA’s fraud hotline has already received 42,000 tips on potential fraud.[9] A recent New York Times investigation spoke with workers who were aware of – and disclosed – instances of PPP fraud, including being asked by their employers to repay a portion of their

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earnings or work for free in the future – both actions that are prohibited by the program rules.[10]

Unsurprisingly, in light of the number of tips received, and the media's assistance, the government is aware of these types of schemes.[11] And, with so many workers having inside information as to the eligibility for, and use of, the PPP funds, businesses have to take seriously the risk of being subject to government investigations or enforcement actions.

So What's a PPP-Receiving Business to Do?

Document and explain. There is no greater defense against allegations of fraud in the PPP program than to have – and preserve – contemporaneous documentation explaining decisions surrounding PPP funds. For example, prudent businesses should work with their financial and legal advisors to create a timeline and narrative of their outlook at the time they requested and obtained PPP funds to prove their good faith in making the “necessity certification” (*i.e.*, “[c]urrent economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant”). Documentation including emails or voicemails from customers, suppliers, or vendors that factored into their economic outlook should be included in the narrative. With respect to loan forgiveness, financial documentation showing where the funds went and how they were spent is critical. And each certification made by a business as part of the eligibility or forgiveness applications (not just the necessity certification) should be supported by documentation and, if possible, with advice from counsel.

And don't leave workers in the dark! They are reading these articles and exposés and may be alert to financial incentives for them to “blow the whistle” on what they perceive to be fraud. To the extent possible, explain to them why certain decisions were made as to eligibility and use of the funds and how those decisions affect them. Answer questions they pose honestly and completely – with documentation, if needed. Workers who feel heard and valued are much less likely to leave a “tip” on a hotline, speak to the media, or try to bring a False Claims Act case.

The PPP program has been a lifesaver to many small businesses, but the compliance challenges are many. If you have questions about the PPP and how to protect your business from government scrutiny, please contact Reetuparna Dutta (716.848.1626), Benjamin Zuffranieri (716.848.1469), or Jason Markel (716.848.1395).

For more information on the coronavirus pandemic please check our Coronavirus Resource Center to view many other alerts our attorneys in various practice areas have published.

[1] See Dan Nordberg, SBA National Director for Rural Affairs and Region 8 Administrator, *The SBA is Proud of the Role it Played in Rolling out the Paycheck Protection Program*, Montana Standard (Aug. 30, 2020) available here: https://mtstandard.com/opinion/columnists/guest-view-sba-proud-of-role-in-paycheck-protection-program/article_a45d37ab-3460-54fe-82b7-41e79608b19d.html.

[2] See *e.g.*, Joshua Franklin, *Investment Banks Got Aid Intended for U.S. Small Businesses*, Reuters (July 24, 2020); Ryan Tracy, Chad Day, and Heather Haddon, *Small Business Loans Helped the Well-Heeled and Connected, Too*, WSJ (July 6, 2020).

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[3] The memorandum is available at: <https://coronavirus.house.gov/sites/democrats.coronavirus.house.gov/files/2020-09-01.PPP%20Interim%20Report.pdf>

[4] The DOJ's press release on FCA recoveries in Fiscal Year 2019 can be found here: <https://www.justice.gov/opa/pr/justice-department-recovers-over-3-billion-false-claims-act-cases-fiscal-year-2019>.

[5] Senator Grassley's remarks can be viewed here: <https://www.grassley.senate.gov/news/news-releases/grassley-celebrating-whistleblower-appreciation-day>.

[6] The DOJ's press release on the indictment can be found here: <https://www.justice.gov/opa/pr/new-jersey-attorney-charged-fraudulently-obtaining-9-million-loans-meant-help-small>.

[7] The DOJ's press release on the indictment can be found here: <https://www.justice.gov/opa/pr/texas-entrepreneur-charged-spending-covid-relief-funds-improper-expenses-including>.

[8] Stacy Cowley, Spotting \$62 Million in Alleged P.P.P. Fraud was the Easy Part, New York Times (Aug. 28, 2020) available at <https://www.nytimes.com/2020/08/28/business/ppp-small-business-fraud-coronavirus.html>.

[9] *Id.*

[10] *Id.*

[11] *Id.*