Penalties for Paycheck Protection Program Related Fraud

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Recent publicity regarding large business entities obtaining millions of dollars in Paycheck Protection Program ("PPP") loans has resulted in additional guidance from the Department of Treasury and the Small Business Administration ("SBA") regarding eligibility for the PPP. In particular, the Treasury Department has issued guidance indicating that large companies with adequate sources of liquidity to support the business's ongoing operations are likely not eligible for PPP loans because such a business could not attest in good faith that "current economic uncertainty makes [a PPP] loan request necessary to support the ongoing operations" of the business. This alert provides guidance regarding the interpretation of the foregoing certification and the mechanisms utilized by the government to enforce the provisions of the CARES Act related to PPP loans.

1. **Necessity of a PPP Loan**

As referenced above, in order to obtain a PPP loan, a business must certify in good faith that "current economic uncertainty made this loan request necessary to support the ongoing operations" of the business. The Treasury Department has clarified that in order to make this certification in good faith, the business must take into account its current business activity and their ability to access other sources of liquidity sufficient to support its ongoing operations in a manner that is not significantly detrimental to the business.

Congress eliminated the normal "credit elsewhere" requirement imposed on many SBA loan programs, which requires applicants to demonstrate that they have attempted to obtain loan funds from all other sources, including the business's owners. Thus, it is clear Congress did not intend to force businesses to show likely foreclosure or dissolution without the PPP loan funds. However, the SBA appears likely to consider whether the business had sufficient cash reserves, had access to capital from related sources, issued projections showing limited impact during the COVID-19 pandemic, or was otherwise in a strong financial position prior to applying for the PPP loan or for loan forgiveness.

If a business is uncertain whether it fully met the necessary requirements to make the certification in good faith, the SBA has provided a safe harbor that any company which has received a PPP loan prior to the issuance of its guidance and which returns the full amount of such loan by May 7, 2020 will be deemed to have made its original certification in good faith. Essentially, a "no harm, no foul" rule at this

point to allow a business to return the funds if they are sufficiently concerned about the validity of their certification.

If a business does not elect to use this safe harbor, then that business should document conditions that demonstrate the need for the PPP loan as they existed in the days and weeks prior to submitting an application for a PPP loan, the date the loan application was submitted, and the weeks and months that follow until the business applies for loan forgiveness. This documentation should include information supporting the need for the PPP funds, including records regarding employee count and hour requirements, pre-COVID-19 operations and subsequent decline, and the cost of, availability, and access to capital, cash reserves, budget forecasts, and other financial metrics. This documentation should be updated throughout the COVID-19 crisis and should include an analysis of current and future revenue, net assets of the business and the availability of cash reserves, and how detrimental it would be to the business to access alternative sources of financing or capital. This document will assist the business in demonstrating the good faith basis for making the necessity certification, if such certification should be questioned in the future.

2.**Enforcement Mechanisms**

PPP loans were funded through the CARES Act. Congress included a new enforcement regime in the CARES Act, consisting of three newly created entities: (i) the Office of the Special Inspector General for Pandemic Recovery; (ii) the Pandemic Response Accountability Committee; and (iii) the Congressional Oversight Commission. These three entities will work with the U.S. Department of Justice, agency inspectors general, audit entities like the U.S. Government Accountability Office, and whistleblowers.

The Treasury Secretary announced on April 28, 2020 that the SBA will perform a full audit on any company that obtained a PPP loan of more than $2 million prior to the company obtaining loan forgiveness, with a particular focus on the certification that a PPP loan was necessary for that business. While this threshold may change based on the average amount of loans obtained in the second wave of funding allocated by Congress, it is safe to assume that the SBA will review applications for loan forgiveness with heightened scrutiny, particularly with higher dollar amounts.

Companies that are found to have committed fraud in obtaining a PPP loan face civil, or even criminal, enforcement. The PPP loan application identifies several criminal statutes that would potentially be violated by an applicant that provides false information on the application. These criminal statutes include false statements to federal officials, misrepresentation of size status, false statements to a lending institution, criminal fraud claims, bank fraud, mail fraud, wire fraud, and criminal conspiracy. These statutes require proof of a criminal level of fraud, which is a high bar (the prosecution must show intent to defraud the Government) and will most likely be used to enforce claims against companies that committed affirmative fraud in order to obtain a PPP loan.

Companies also may face civil liability under the False Claims Act (the “FCA”) due to false certification on the PPP loan application. Violation of the FCA may result in treble damages and per-claim penalties exceeding $21,000. The FCA also includes a “reverse false claims” provision that would require the business to repay the entire amount of the PPP loan. The FCA provides a right of action not only for the government, but also for private whistleblowers. Whistleblowers can file, under seal, a lawsuit in the name of the government (a *qui tam* case) against the business. The whistleblower is entitled to a significant portion of the recovery in the lawsuit as a reward for bringing the lawsuit. To be found liable under the FCA, the business must have submitted a false claim or a false statement that was material to a false claim. Unlike criminal fraud, the FCA does not require a specific intent to defraud the government. A business can be found liable for recklessly disregarding the rules.

Additionally, the FCA also includes a civil charge of conspiracy to engage in conduct under the FCA.

This provision could be used to pursue affiliate companies, owners, or other individuals that participated in the loan process.

Our attorneys continue to monitor updates from the SBA and other entities related to the PPP program and will update this guidance if additional information is provided.

This article is general in nature and does not constitute legal advice. Please note that new guidance is being provided by authorities on a daily basis so please monitor new developments and guidance. Readers with legal questions about how these orders apply to your business and your employees should consult the authors Bailie Schnackenberg (bailies@sb-kc.com) Char Heins at (cheins@sb-kc.com) or John Fuchs (jfuchs@sb-kc.com) or your regular contact at Seigfreid Bingham at 816-421-4460.

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