COVID-19: What History Tells Us About the Importance of the False Claims Act in a Time of Pandemic

May 11, 2020

This is the first in a series of client alerts addressing the likely role of the False Claims Act in the wake of the massive federal government response to the COVID-19 pandemic.

On March 20, 2020, the Department of Justice announced that Attorney General William Barr had directed all US Attorneys to prioritize the investigation and prosecution of coronavirus-related frauds.[1] A week later, the President signed into law the Coronavirus Aid, Relief, and Economic Security (CARES) Act, a $2 trillion stimulus package—the largest in American history—that will make available hundreds of billions of dollars in loans and other financial assistance to distressed companies.

It should come as no surprise, then, that the CARES Act also contains a number of provisions that define the eligibility criteria for companies to avail themselves of the Act's benefits—some of which require express certifications that the beneficiaries meet them. Making false certifications (or providing false information) in order to establish eligibility for federal funds is a quintessential example of how a company (or an individual) could run afoul of the False Claims Act (FCA)—which is the federal government's most potent civil anti-fraud statute. The magnitude of the CARES Act—and the extensive oversight mechanisms established under the Act itself—means that increased scrutiny will no doubt be placed on those companies that seek to participate in its programs.

FCA Risks Under the CARES Act

The FCA requires companies and individuals seeking federal monies to be truthful in the promises they make about their entitlement to those funds. 31 U.S.C. § 3729 *et seq*. The CARES Act

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[1] Department of Justice, *Attorney General William P. Barr Urges American Public to Report COVID-19 Fraud* (Mar. 20, 2020), https://www.justice.gov/opa/pr/attorney-general-william-p-barr-urges-american-public-report-covid-19-fraud.

requires businesses seeking relief from the Department of the Treasury or from Federal Reserve facilities funded by the Act to make a number of express certifications regarding their eligibility, including, for example, that economic conditions make the loan "necessary" to support the "ongoing operations" of the recipient; that the loan will be "used to retain at least 90 percent of the recipient's workforce" until September 30, 2020; and that the recipient intends to restore at least 90 percent of its workforce that existed as of February 1, 2020, no later than four months after the end of the public health emergency.[2]

Businesses seeking to participate in the Paycheck Protection Program (PPP), which is administered by the US Small Business Administration (SBA), must, as borrowers, certify that the loan will be "used to retain workers and maintain payroll or make mortgage payments, lease payments, and utility payments"; that the recipient does not have another application pending for a PPP loan and "duplicative of amounts applied for or received under a covered loan"; and that between February 15, 2020, and December 31, 2020, the recipient has not received amounts under the subsection for the same purpose.[3] And lenders that participate in the PPP must also, at the time of loan origination, make various certifications to the SBA about confirming borrower eligibility, as well as compliance with the Bank Secrecy Act and Know-Your-Customer obligations.[4] The PPP's loan forgiveness procedure—in which a PPP loan may be forgiven if 75 percent of the amount of the loan was dedicated to payroll expenses[5]—involves further representations to the SBA that may present FCA risk to lenders and borrowers alike.

The CARES Act itself recognizes the potential for fraud in the programs it establishes and includes several provisions that are designed to fight it. For example, it creates several new watchdog entities that have broad oversight and investigative authority. The Act creates the Special Inspector General for Pandemic Recovery, who will provide oversight of Department of the Treasury loans and investments and track and investigate disbursements made under the Act.[6] It also creates the Pandemic Response Accountability Committee, made up of existing Inspectors General, which will

[2] CARES Act § 4003(c)(3)(D)(i)(I)-(III). The meaning and scope of the terms "necessary" and "ongoing operations" are also subject to interpretation and could present certification issues to borrowers. Other sections that implicate potential risk under the FCA include Section 4004, which places limits on executive compensation, and Section 4019, which requires an entity seeking to enter into a transaction under Section 4003 to certify that the entity is eligible to engage in that transaction. Note that the precise terms of the Federal Reserve and Department of the Treasury programs have yet to be determined.

[3] CARES Act § 1102(a)(2) (amending Section 7(a) of the Small Business Act, 15 U.S.C. § 636(a)).

[4] Department of the Treasury, *Paycheck Protection Program (PPP) Information Sheet: Lenders*, https://home.treasury.gov/system/files/136/PPP%20Lender%20Information%20Fact%20Sheet.pdf.

[5] *Business Loan Program Temporary Changes; Paycheck Protection Program*, 85 Fed. Reg. 20811, 20813-14 (Apr. 15, 2020).

[6] CARES Act § 4018. President Trump nominated Brian D. Miller, special assistant to the President and senior associate counsel in the White House Office of Legal Counsel, for this position, and the Senate Banking Committee held a confirmation hearing on May 5, 2020.

have authority to investigate, issue and enforce subpoenas, and hold public hearings in connection with funds disbursed under the Act or other federal programs.[7] It creates a Congressional Oversight Commission, which will examine decisions made by the Treasury Department and Federal Reserve and monitor how aid is spent.[8] And the Act grants the US Comptroller General the authority to monitor and audit the use of the disbursed funds.[9]

These oversight functions acknowledge the multiple public warnings in recent weeks about the potential for large-scale fraud related to any stimulus package passed in response to the COVID-19 crisis.[10]

One way to understand the potential FCA risks posed by participating in the CARES Act's many new programs is to look back a decade to the 2008 financial crisis. The government programs enacted in response to that national crisis expanded the reach of the FCA and put large financial institutions in its crosshairs.

To be sure, the crisis we face today is different than the housing and financial crisis of a decade ago. Many of the financial institutions that received federal bailout money in the wake of that crisis and were targets of subsequent FCA investigations were alleged to have engaged in mortgage lending conduct that contributed to the financial crisis itself. That won't be the case with this public health emergency. Regardless, though, as the Second Circuit has noted quite recently: "fraud during a national emergency" against entities "established by the government to address that emergency by lending or spending billions of dollars" is precisely the sort of fraud that Congress wanted to target by enacting the FCA.

The FCA Was Made for a National Crisis

That a national crisis amplifies the risk for widespread fraud is not a new phenomenon. Indeed, the FCA was enacted in 1863, in the midst of the Civil War. Congressional testimony at the time "painted a sordid picture of how the United States had been billed for nonexistent or worthless

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[7] CARES Act § 15010(b). The Pandemic Response Accountability Committee is led by Acting Chair Michael E. Horowitz, Inspector General of the US Department of Justice, and Vice-Chair Paul K. Martin, Inspector General of the National Aeronautics and Space Administration.

[8] CARES Act § 4020.

[9] CARES Act § 19010(b).

[10] *See, e.g.*, Walter Pavlo, *Fraud in a Post COVID-19 World*, FORBES (Mar. 24, 2020), https://www.forbes.com/sites/walterpavlo/2020/03/24/fraud-in-a-post-covid-19-world/#1d61e18b11fe; Scott F. Roybal, Matthew T. Lin, *Guard Against False Claims as Massive Government Spending Rolls Out to Combat COVID-19*, THE NATIONAL LAW REVIEW (Mar. 19, 2020), https://www.natlawreview.com/article/guard-against-false-claims-massive-government-spending-rolls-out-to-combat-covid-19; Jessica L. Westerman, *Renewed Importance of False Claims Act Enforcement Under the CARES Act*, THE NATIONAL LAW REVIEW (Apr. 15, 2020), https://www.natlawreview.com/article/renewed-importance-false-claims-act-enforcement-under-cares-act

goods, charged exorbitant prices for goods delivered, and generally robbed in the purchasing of necessities of war." *United States v. McNinch*, 356 U.S. 595, 599 (1958).

Because of these serious claims and the belief that war profiteers had used the crisis of war to defraud the nation, Congress passed the FCA—colloquially known as "Lincoln's Law"—making any person who knowingly submitted false claims to the government liable for double the government's damages plus a penalty of $2,000 per claim. Since then, the FCA has been amended several times, including in 1986 when Congress imposed treble damages and civil penalties of $5,000 to $10,000 for each false claim (which are currently, when adjusted for inflation, $11,463 to $23,331),[11] and increased rewards for insiders who filed claims on behalf of the government (known as *qui tam* plaintiffs).

Particularly since the 1986 amendments, the FCA has been used with increasing frequency as an effective tool to combat fraud against the government, particularly in times of national crisis. For example, after Hurricane Katrina in 2005, there was a spike in FCA claims against government contractors for defrauding the government in relation to disaster relief funds.[12] And in the wake of the 2008 financial crisis, numerous FCA claims arose against large corporations, resulting in multimillion-dollar—and sometimes multibillion-dollar—settlements with whistleblowers and the Department of Justice.

Increased FCA Enforcement Following the 2008 Financial Crisis

In response to the 2008 financial crisis, Congress enacted the Emergency Economic Stabilization Act of 2008, which created the Trouble Asset Relief Program (TARP). Under TARP, the Treasury Department received the authority to purchase up to $700 billion in "troubled assets," which included "residential or commercial mortgages and any securities, obligations, or other instruments that are based on or related to such mortgage," the purchase of which would promote financial market stability.[13]

TARP, like the CARES Act, required participating financial institutions to meet standards for executive compensation and corporate governance[14] and to make other reports and disclosures to various agencies. And, like the CARES Act, it established oversight offices, including the Special Inspector General for the Trouble Asset Relief Program (SIGTARP), which was a watchdog that

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[11] 15 CFR § 6.3(a)(3) (Jan. 15, 2020).

[12] Roybal, *supra* note 10.

[13] Emergency Economic Stabilization Act of 2008, 12 U.S.C. § 5202(9).

[14] 12 U.S.C. § 5221.

targeted fraud related to TARP.[15] Shortly thereafter, in February 2009, President Barack Obama signed into law the American Recovery and Reinvestment Act of 2009, an economic stimulus package.

Recognizing that such large economic stimulus programs could be abused, legislators pushed for measures to increase oversight and strengthen enforcement of anti-fraud statutes, including by utilizing the FCA to pursue allegations of fraud related to TARP.[16]

In response, Congress enacted the Fraud Enforcement and Recovery Act (FERA) in 2009, which amended and expanded the reach of the FCA, for instance, by redefining "claim" to include demands for payments made by subcontractors on government-funded projects. 31 U.S.C. § 3729. It also required that any alleged false statement be only "material" to a payment by the government, overruling *Allison Engine Co., Inc. v. United States ex rel. Sanders*, 553 U.S. 662 (2008), which had held that FCA liability required a showing that the defendant *intended* that the false statement be used to obtain government money. And President Obama established the Financial Fraud Enforcement Task Force led by the Justice Department to "investigate and prosecute significant financial crimes and other violations relating to the current financial crisis and economic recovery efforts."[17]

The increased oversight mechanisms established alongside the economic stimulus programs in 2008 and 2009 made financial institutions that received federal money the targets of increased scrutiny, especially for FCA violations.

For example, in 2012 and for years thereafter, the United States intervened in multiple *qui tam* suits against various banks, generally alleging that the banks violated the FCA by selling to Fannie Mae and Freddie Mac defective residential loans that later defaulted. These cases often shared similar allegations: for example, that the banks misrepresented to government entities that the loans were investment-quality and that they complied with U.S. rules and regulations regarding the quality of the mortgages. As alleged, such misrepresentations were material to the government's decision to insure the loans and resulted in losses to the government when the loans defaulted. And in announcing certain of these lawsuits, the SIGTARP specifically noted that the financial institutions were TARP fund recipients. As noted above, these cases were generally resolved through

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[15] 12 U.S.C. § 5231; *see also* SIGTARP, "About Us," https://www.sigtarp.gov/Pages/aboutus.aspx (last accessed Apr. 2, 2020).

[16] *See* Ltr. from the Hon. Charles E. Grassley, US Senator, to the Hons. Henry M. Paulson, Jr., Secretary of the Treasury, and Michael B. Mukasey, Attorney General (Nov. 17, 2008), https://www.grassley.senate.gov/news/news-releases/grassley-urges-federal-government-utilize-%E2%80%9Clincoln%E2%80%99s-law%E2%80%9D-help-protect-and.

[17] Executive Order 13519, "Establishment of the Financial Fraud Enforcement Task Force" (Nov. 17, 2009), https://obamawhitehouse.archives.gov/the-press-office/executive-order-financial-fraud-enforcement-task-force.

settlements with the government and *qui tam* plaintiffs amounting to hundreds of millions of dollars or more.

In addition to increasing oversight over institutions that received financial assistance (and that were alleged to have engaged in conduct that resulted in the crisis), the 2008 stimulus legislation made available federal funds that the government also alleged were obtained by institutions that falsely stated their eligibility to receive the funds. For example, the United States settled an FCA action against the estate of a former owner and president of a bank, alleging that the bank had violated the FCA by making false statements about the financial condition of the bank in order to receive TARP funds.

These lawsuits (and the many resulting settlements of significant size) demonstrate the exposure that companies (and individuals) may face for participating in government-funded assistance programs in emergency situations, including the nation's current crisis. Companies that are considering participation in CARES Act programs need to be mindful of these risks, or they could find themselves in the crosshairs of one of the many new oversight agencies created by the Act and face allegations of violating the FCA.

With a team of veteran litigators, prosecutors and former Justice and Defense Department lawyers, WilmerHale brings significant knowledge and experience to defending against FCA litigation brought by relators, the Department of Justice and state attorneys general. Please reach out to the authors of this alert or your WilmerHale contacts should you have any questions.

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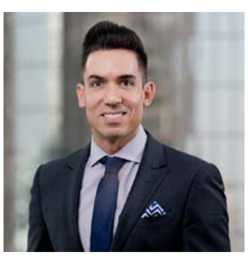

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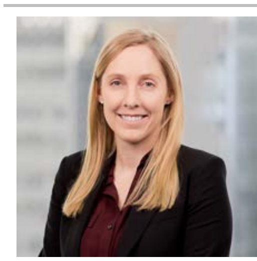

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