Alert

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COZEN O'CONNOR

PPP Fraud Is Ripe for Enforcement in 2021. Can Self-Disclosure & Cooperation Create a Path to Leniency?

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As we approach the one-year anniversary of passage of the Coronavirus Aid, Relief and Economic Security (CARES) Act, we are getting a better sense of how the government will address fraud arising out of this legislation. Between March 27, 2020, and August 8, 2020, financial institutions approved more than $5.2 million potentially forgivable loans through the Paycheck Protection Program (PPP), disbursing upwards of $525 billion guaranteed by the Small Business Administration (SBA) to assist small businesses and nonprofit entities. On December 27, 2020, the Economic Aid to Hard-Hit Small Businesses, Nonprofits and Venues Act (Economic Aid Act) provided nearly $285 billion in new PPP funding. When talking these kinds of numbers, it comes as no surprise that certain individuals or entities have exploited these programs for financial gain and sought relief payments under false and fraudulent pretenses.

If 2020 was any indication, the government will not take lightly abuse of the CARES Act, PPP, or Economic Aid Act. Early in the pandemic, the Department of Justice (DOJ) Criminal Division's Fraud Section established a team dedicated solely to PPP fraud, which led nationwide efforts to criminally prosecute those taking advantage of the relief act. The team's focus was falsified buyer information and the DOJ vowed "the severest of consequences" for those exploiting the PPP. By December 2020, the Criminal Division brought PPP-related charges against more than 90 individuals, representing $250 million in alleged losses.

Some of these charges include:

- In September 2020, an attorney in New Jersey was arrested and charged with three counts of bank fraud and one count of money laundering. DOJ alleged he fraudulently obtained approximately $9 million in PPP loans by fabricating the existence of hundreds of employees, manipulating bank and tax records, and falsifying a driver's license on an application.
- In November 2020, seven individuals were charged with conspiracy to commit wire fraud and wire fraud. DOJ asserted that they fraudulently obtained $16 million in PPP loans by fabricating PPP applications and spending the funds on luxury items, such as sports cars.
- In December 2020, three family members who ran family-owned nail salons in New York were arrested and charged with conspiracy to commit bank and wire fraud. According to DOJ, the family members fraudulently obtained more than $13 million in PPP loans by grossly overstating the number of employees and payroll at their nail salons and submitting fabricated payroll and tax records to obtain a larger loan.

We do not expect the government to stop there. Given the unprecedented nature of the PPP, it is certain that enforcement actions will continue into 2021 and beyond. The Economic Aid Act requires the SBA to submit an audit plan to House and Senate small business committees and provide monthly updates, and appropriates $50 million specifically for PPP fraud mitigation and enforcement.

A recent case from California provides helpful guidance on avoiding criminal charges and penalties for violations of the PPP.

On January 12, 2021, the U.S. Attorney's Office for the Eastern District of California entered into a settlement with the owner of SlideBelts, Inc. Despite public disclosure of charges against more than 90 individuals, SlideBelts is the only reported case that has resulted in a civil settlement and no criminal charges. So, what makes SlideBelts unique? SlideBelts' owner proactively corrected inaccuracies in his PPP loan application *before* either the lender or the government identified these inaccuracies. Quite simply, when SlideBelts' owner discovered that he had falsely represented the bankruptcy status of SlideBelts, he emailed the lender stating that SlideBelts "just realized that we may not have answered [Question 1] since we filled out the application quickly and wanted to bring it to your attention." The SlideBelts owner did not disclose this inaccuracy until after it had received the PPP loan, and SlideBelts did not return the loan to the lender in conjunction with notifying the lender of the inaccuracy. Ultimately, in addition to returning the loan to the lender, SlideBelts agreed to pay the government $100,000 (a majority of which SlideBelts will pay over time).

Recipients of PPP funds would be wise to view the SlideBelts settlement as instructive for avoiding criminal prosecution. Recipients should review any PPP loan application they submitted and explore opportunities to proactively correct any inaccuracies. By self-disclosing inaccuracies and cooperating with government officials, PPP recipients may similarly receive leniency from government enforcement.