

THE CARES ACT AUDITORS ARE COMING! WILL YOU BE READY?

Under the Coronavirus Aid, Relief, and Economic Security Act (“CARES Act”) and three other coronavirus related acts, Congress provided emergency relief to individuals and businesses adversely affected by COVID-19. With this legislation, Congress funded over \$2 trillion in relief in lending programs, grants to businesses, and support for American workers.

Many of these loan and grant programs have specific limitations and restrictions on how loan proceeds and grant funding may be used. Some require participants to submit certifications and attestations that they are following the terms and conditions of the program.

The passage of such extraordinary relief funding for so many individuals and businesses is likely to create substantial opportunities for fraud and will trigger audits and investigations for years to come. Multiple government entities in both the legislative and executive branches will target fraud and mismanagement of these programs.

This legislation created new oversight functions, including the Congressional Oversight Commission, the Special Inspector General for Pandemic Relief, the Pandemic Response Accountability Committee, which consists of 9 statutory inspectors general plus 12 non-statutory inspectors general, and a House Select Committee. These entities will supplement existing Congressional Committees, and investigations and prosecutions brought by the Department of Justice.

These funding programs are already getting intense scrutiny. Just this week the Treasury Secretary warned of criminal prosecutions and that loans for more than \$2 million from the Paycheck Protection Program would face full audits and that smaller amounts would be subject to spot check audits. A week ago, a Senate Committee asked the SBA Inspector General to look at issues related to big companies receiving loans at the expense of smaller companies.

History also suggests that these programs will be closely examined for waste, abuse, and fraud. Following the 2008, Financial Crisis, for example, Congress created a Special Inspector General to oversee the Troubled Asset Relief Program, which only disbursed \$431 billion. Yet, the Inspector General’s work led to the recovery of more than \$10 billion and hundreds of convictions.

Even efforts to help will be scrutinized. Following Hurricane Katrina, Carnival Cruise Lines was subjected to a GAO investigation requested by the Chairman of a House Committee for canceling 120,000 reservations and moving ships to New Orleans from Houston to house first responders and displaced residents.

We can also anticipate that every tool within the government's arsenal will be used to recover fraudulently obtained funding, including the False Claims Act (FCA), which provides a potent remedy in civil actions, permitting the government to recover treble damages plus other civil penalties.

What does this mean? It means that any business participating in these lending or grant programs should be prepared for a potential audit or examination to ensure that they are in compliance with the terms and conditions of the agreements and provided truthful information to the government in connection with the receipt of such funding. A failure to do so will create substantial exposure.

To protect themselves, participants must ensure that they have robust compliance procedures in place to verify the accuracy of the information submitted to the government and maintain records that support such submissions. In addition, such procedures should include at least a secondary review by management demonstrating that procedures were properly followed, and any issues potentially identified by these reviews were appropriately resolved.

Below is a summary of the most significant lending and grant programs created by the CARES Act and coronavirus related acts and the issues for which participants in these programs are likely to be audited or examined. Participants in these programs would be wise to put strong compliance procedures in place to prevent potential mishaps or worse.

SBA Paycheck Protection Program (PPP): Under the CARES Act, Congress appropriated over \$650 billion to provide emergency relief to businesses adversely impacted by the crisis. Under the PPP, eligible banks may lend to any small business that employs no more than 500 employees and paid salaries and payroll taxes prior to February 15, 2020. Banks may lend the lesser of 2.5 times a borrower's average monthly payroll costs, up to \$10 million. The program is intended to provide small businesses with eight weeks of funds to cover payroll and certain business expenses such as mortgage and utilities.

The PPP places several restrictions and requirements on both lenders and borrowers that potentially are subject to future audits and exams. For example, borrowers must certify that loan proceeds will be used for payroll and covered expenses. To be eligible for loan forgiveness, a borrower must also submit documentation verifying the number of employees on payroll and that the proceeds were used on payroll and certain other specific covered expenses.

Similarly, lenders are restricted from charging an interest rate greater than 4% annually over ten years (the initial rate is 1%) and may not charge loan fees or a prepayment penalty to borrowers. Lenders are also required to gather borrower certifications and verifying documentation showing that funds were used for payroll and covered expenses.

Health Care Provider Relief Fund: Congress appropriated \$100 billion in relief funds to hospitals and other healthcare providers used to support healthcare-related expenses or lost revenue attributable to COVID-19. The Department of Health and Human Services (HHS) immediately infused \$30 billion of that funding into the healthcare system with payments arriving via direct deposit to certain recipients beginning April 10, 2020.

Although these payments are not loans and will not need to be repaid, recipients must sign an attestation confirming the receipt of funds and agreeing to the terms and conditions of the agreement. By signing the attestation, the recipient agrees, for example, that it provides or provided diagnoses, testing, or care for individuals with possible or actual cases of COVID-19. The recipient further certifies that the payment will only be used to prevent, prepare for, and respond to coronavirus, and shall seek reimbursement only for health care related expenses or lost revenues that are attributable to coronavirus.

Health care providers should anticipate that they will be audited by the government to ensure that they are by abiding by the attestation and the terms and conditions of these agreements.

Department of Treasury Loan Programs: Under the CARES Act, Congress appropriated \$454 billion to the Department of the Treasury to establish emergency lending facilities through the Federal Reserve. These programs will “make loans and loan guarantees to, and other investments in, programs or facilities established by the Federal Reserve for the purpose of providing liquidity to the financial system that supports lending to eligible businesses, States or municipalities.”

Borrowers participating in this loan program will be prohibited for the life of the loan and one year following from repurchasing equity securities (or buybacks) and issuing dividends. Borrowers will also have to abide by certain executive compensation restrictions.

The CARES Act also specifies that the Federal Reserve may establish a Midsized Business Lending Program to provide financing to banks and other lenders that make direct loans to eligible businesses including nonprofit organizations with between 500 and 10,000 employees. The annual interest rate may not be higher than 2% for these loans.

Under this program, borrowers are prohibited from outsourcing or offshoring jobs for the term of the loan and two years after and includes other restrictions relating union activities. Borrowers must also certify to, among other things, that the uncertainty of its economic conditions makes the loan request necessary to support operations and that the loan proceeds will be used to retain at least 90% of the workforce at full compensation and benefits until September 30, 2020. Borrowers are subject to the same buyback, dividends, and compensation restrictions listed above.

Given the recent comments from the Secretary of the Treasury, borrowers should be prepared to be audited on the restrictions set out for borrowers for these programs.

Funding for Passenger Airlines, Cargo Air Carriers, and Businesses Critical to Maintaining National Security: The CARES Act allotted \$46 billion in loans and loan guarantees for airlines, cargo air carriers, and businesses critical to

maintaining national security. The Act also designates direct grants of \$32 billion for passenger airlines, cargo air carriers, and contractors to be used for payroll expenses.

To be eligible for a loan, borrowers must agree not to buy back stock nor pay dividends for the life of the loan and the year following. They must also agree to certain executive compensation restrictions. With regard to the grants, in addition to the above restrictions, recipients must agree not to furlough or cut the pay rates of employees through September 30, 2020.

The Act also makes available \$10 billion in grants to help publicly owned and commercial airports to address the COVID-19 crisis. The grant funds are available for airport capital expenditures, airport operating expenses including payroll and utilities, and airport debt payments. Recipients of the grants must agree to retain 90% of their employees through December 31, 2020 and must retain complete records to support all grant payments.

Again, participants in these programs should expect close scrutiny by the government.

Public Transit: the CARES Act provides \$25 billion in grants for public transit authorities. The Federal Transit Association (FTA) will provide these funds through 4 different grant programs. According to the FTA, CARES Act funding will be available for planning, capital (preventive maintenance, rolling stock, equipment, etc.), and operations (to include paying of admin leave of operations personnel due to reductions in service or quarantine).

Amtrak will also receive \$1 billion in grants through the CARES Act: \$492 million for the Northeast Corridor grants; and \$526 for the National Network grants. The CARES Act funding is provided to help maintain Amtrak services and it to be used to offset the loss of ticket revenue, which is used to pay Amtrak's employees, buy fuel for its operations and construction materials for its projects, and otherwise maintain Amtrak's network of intercity passenger routes, including routes in rural areas that have seen total cancellation in service.

These grants are limited, however, and to be used for prevention, preparation, and response to COVID-19. All federal transit program requirements apply to CARES Act funding.

Federal government agencies responsible for this funding should expect the same level of scrutiny as private businesses. State, local, territorial, and tribal governments should also be sure to be able to account for the funding they receive.

In sum, everyone needs to be ready to account for the trillions of dollars in spending. Get ready before an Inspector General, a Congressional Committee, or the Justice Department starts to look.



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