CARES Act Enforcement: A Landscape of Potential Risk

April 14, 2020

On March 27, 2020, President Trump signed into law the Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act")—a sweeping economic relief package that will deliver an unprecedented $2 trillion to businesses, governments, and individuals impacted by the coronavirus. **With the historic size and scope of the CARES Act, however, comes the potential for widespread fraud and abuse, and the inevitable investigation and prosecution of that conduct.**

The CARES Act itself includes a number of accountability and oversight measures targeted at such abuse. Like the Troubled Asset Relief Program in 2008, the CARES Act stands up a new special inspector general—the Special Inspector General for Pandemic Recovery—and a Congressional Oversight Commission. And as with the American Recovery and Investment Act of 2009, it also expands the capacity of existing oversight functions, by increasing funding for agency inspectors general across the federal government and creating a new Pandemic Response Accountability Committee to coordinate this work. Under existing authority, inspectors general can conduct audits and investigations backed by subpoena power, issue reports to Congress, and work closely with the Department of Justice ("DOJ") and other agencies, in certain circumstances, to bring civil or criminal enforcement actions. Apart from these measures, we expect significant media, political and law enforcement scrutiny of how CARES Act funds are deployed.

Taken together, these formal and informal accountability and oversight measures create a landscape of potential risk, both for the recipients and borrowers of CARES Act funds and the many financial and non-financial lenders responsible for administering the programs and distributing these funds.

This Memorandum serves as a preliminary guide to this risk landscape. It describes the oversight and accountability features of the CARES Act and, by reference to the Troubled Asset Relief Program, sets out what borrowers and lenders should be thinking about as they evaluate the short-term and long-term risks of participating in CARES Act programs. It also addresses possible False Claims Act liability, and potential risks with respect to the newly created Paycheck Protection Program.

CARES Act Accountability and Oversight Measures

The CARES Act includes four principal accountability and oversight measures: (1) the Pandemic Response Accountability Committee, (2) a Special Inspector General for Pandemic Recovery, (3) increased funding for existing inspectors general, and (4) the Congressional Oversight Commission.

Pandemic Response Accountability Committee ("PRAC")[1]

PRAC is charged with preventing and detecting fraud, waste, abuse, and mismanagement, and mitigating major risks that cut across programs and government agencies, with respect to all federal coronavirus-related funds. It has authority over the $2 trillion in CARES Act funds, as well as the funds appropriated by two earlier coronavirus-related stimulus packages—the Coronavirus Preparedness and Response

[1] *See* Section 15010 of the CARES Act.

Supplemental Appropriations Act, and the Families First Coronavirus Response Act—and any Phase 4 or other future coronavirus-related stimulus package.

Consistent with the role of other inspectors general, PRAC is authorized to conduct its own independent investigations, audits, and reviews, and collaborate on audits and reviews with other inspectors general. To carry out its mandate, PRAC has the authority set out under Section 6 of the Inspector General Act, including the authority to:

- request and inspect all relevant federal documents and records,
- convene public hearings,
- issue and enforce document subpoenas, and
- issue and enforce subpoenas compelling the testimony of private persons outside of the Federal government.

In addition, each of the inspectors general that comprises PRAC retains their existing authority.

The CARES Act sets out a detailed, nonexclusive list of PRAC functions, including "expeditiously reporting to the Attorney General [of the United States] any instance in which the Committee has reasonable grounds to believe there has been a violation of Federal criminal law." The CARES Act also sets out extensive informational and reporting requirements for PRAC, some of which are consistent with the ordinary reporting obligations of inspectors general, including:

- making periodic and biannual reports to the president and Congress summarizing PRAC findings, and identifying potential management, risk, and funding problems that require immediate attention; and
- establishing and maintaining a robust, public-facing website that provides accountability information, including any relevant PRAC, inspector general or Government Accountability Office reports; detailed data on all expenditures of federal funds in excess of $150,000; and data on the estimated number of jobs created or sustained under the CARES Act.

In support of these reporting obligations, each agency involved in the coronavirus response is required to issue monthly reports to PRAC, among others, regarding any obligation or expenditure of coronavirus-related funds in excess of $150,000. Any recipient of such funds also is required to make quarterly reports to PRAC regarding the manner in which any received funds were used.

PRAC is housed within the existing Council of the Inspectors General on Integrity and Efficiency ("CIGIE"), an independent, executive branch entity that coordinates the work of inspectors general across the federal government. The CARES Act earmarks $80 million for PRAC, with PRAC's mandate set to terminate on September 30, 2025.

PRAC will be led by a Chairperson and Vice Chairperson, and is composed of the following inspectors general:

- the Inspectors General of the Departments of Defense, Education, Health and Human Services, Homeland Security, Justice, Labor, and the Treasury;
- the Inspector General of the Small Business Administration;
- the Treasury Inspector General for Tax Administration; and
- any other Inspector General, as designated by the Chairperson.

The Committee will be staffed by an Executive Director and Deputy Executive Director appointed in consultation with the majority leader of the Senate, the Speaker of the House of Representatives, the minority leader of the Senate, and the minority leader of the House of Representatives.[2] PRAC also is required to coordinate its work with the Comptroller General and state auditors.

On March 30, 2020, CIGIE announced that Glenn A. Fine, the acting Inspector General of the Department of Defense, had been appointed the Chairman of PRAC, and on April 1, 2020, twelve additional inspectors general were named to PRAC, including the Office of Inspector General for the Board of Governors of the Federal Reserve System and the Consumer Financial Protection Bureau and the Special Inspector General for Pandemic Recovery (once confirmed by the Senate). In addition, Paul K. Martin, the current Inspector General of NASA, was named PRAC's Vice Chairman.

On April 7, 2020, President Trump announced that he had removed Fine as acting Inspector General of the Department of Defense, making him ineligible to serve as PRAC Chairman. CIGIE has not yet chosen a new chair, and the Executive Director and Deputy Executive Director positions have not yet been filled.

Special Inspector General for Pandemic Recovery ("SIGPR")

Unlike PRAC, which has authority over all coronavirus-related funds, the authority of SIGPR is limited to the $500 billion in economic stabilization funds the CARES Act makes available for eligible businesses (including air carriers and businesses key to national security), states, and municipalities. For more information about the CARES Act's economic stabilization funds, please see our separate memorandum, available **here**.

Under the CARES Act, SIGPR is responsible for collecting and summarizing key information regarding Treasury's deployment of economic stabilization funds, including:

- descriptions of the categories of loans, loan guarantees, and other investments made by Treasury;
- lists of the eligible businesses receiving each loan, loan guarantee, or other investments;
- explanations of the reasons Treasury determined it was appropriate to make each loan, loan guarantee, or other investment; and
- detailed financial reports with respect to the status of each loan, loan guarantee, and other investment made by Treasury.

SIGPR is also required to issue quarterly reports to Congress summarizing SIGPR's activities and providing a detailed statement of all loans, loan guarantees, other transactions, obligations, expenditures, and revenues associated with any economic stabilization program established by Treasury under the CARES Act.

In connection with its mandate, SIGPR is given the same authorities as other inspectors general and the PRAC, including the authority to issue enforceable document subpoenas.

SIGPR must report to Congress any circumstance in which any federal department or agency declines to provide information requested by SIGPR, although upon signing the CARES Act, President Trump issued a statement that he does "not understand . . . this provision as permitting the SIGPR to issue reports to the Congress without the presidential supervision required by the Take Care Clause."

[2] Upon signing the CARES Act, President Trump stated that he considered the requirement of Congressional consultation in connection with the appointment of the Executive Director and Deputy Executive Director hortatory rather than mandatory.

On April 6, 2020, President Trump **nominated** his special assistant and senior associate counsel, Brian D. Miller, to the position of SIGPR. Mr. Miller previously served for nearly 10 years as the Inspector General of the General Services Administration. His nomination is subject to the advice and consent of the Senate, which has not yet acted on the nomination, although it is expected that Mr. Miller will be confirmed easily given the Republican majority in the Senate. The office of SIGPR will be housed within Treasury, and is funded by a $25 million appropriation, with SIGPR's authority set to terminate on March 27, 2025.

Overall, the SIGPR statutory framework is nearly identical to the statutory framework for the Special Inspector General for the Troubled Asset Relief Program ("SIGTARP"). SIGPR, however, was appropriated significantly less funding than SIGTARP—$25 million versus a $50 million initial budget for SIGTARP, which has since been supplemented by additional appropriations. SIGPR also has a fixed termination date, whereas SIGTARP's authority terminates once the last asset acquired as part of TARP, including any loan issued as part of TARP, has been sold or transferred out of government ownership.

Increased Funding for Existing Inspectors General

In addition to establishing PRAC, the CARES Act includes significant increases in funding for existing inspectors general, especially for those agencies centrally involved in the administration of CARES Act programs and funds. This includes a $25 million appropriation for the Inspector General of the Small Business Administrations; $25 million for the Inspector General of the Department of Labor; and $35 million for the Inspector General of the Department of Treasury. This means that, in the aggregate, there is more funding for inspector general oversight under the CARES Act than there was under TARP, although the amount of funds available under the CARES Act is nearly three times larger than what was appropriated under TARP.

Congressional Oversight Commission (the "Commission")

The Commission, unlike SIGPR and PRAC, involves legislative oversight, rather than executive oversight. Like SIGPR, it has oversight authority for Treasury's economic stabilization programs and funds, as well as Treasury's support for coronavirus-related programs established by the Board of Governors of the Federal Reserve System (the "Fed"). In connection with this oversight mandate, the Commission is authorized to hold public hearings, take testimony (including under oath), and receive evidence.

The Commission is required to submit monthly reports to Congress that address, among other things:

- the economic stabilization efforts of the Treasury and the Fed;
- the impact of related loans, loan guarantees, and investments on the financial well-being of the "people of the United States"; the U.S. economy, financial markets, and financial institutions; and market transparency; and
- the effectiveness of the loans, loan guarantees, and investments in minimizing costs to, and maximizing benefits for taxpayers.

The Commission is directly modeled on the Congressional Oversight Panel ("COP") established in connection with TARP. Like COP, the Commission will be composed of five members:

- one appointed by the Speaker of the House;
- one appointed by the minority leader of the House;
- one appointed by the Senate majority leader;
- one appointed by the minority leader of the Senate; and
- a chairperson appointed by the Speaker of the House and the Senate majority leader, in consultation with the minority leaders of the Senate and the House.

On April 7, 2020, the Senate minority leader (Sen. Schumer, D-NY) **named** Bharat Ramamurti, a former aide to Sen. Warren (D-Mass.), to the Commission. The other four members of the Commission have not yet been named.

The Commission will be funded on an annual basis out of the accounts of the House and the Senate, and is set to expire on September 30, 2025.

CARES Act Oversight and Accountability: What Lies Ahead?

The CARES Act was enacted to provide economic support to individuals, businesses, and state and local governments hard hit by the global spread of the coronavirus. The urgency and depth of this economic need, coupled with the sheer size and scope of the CARES Act and the desire to push CARES Act funds into the economy as quickly as possible, has sparked serious concerns about fraud, abuse, and other misconduct. These concerns, in turn, have led to widespread demands for accountability, and an environment of intense scrutiny for beneficiaries of, and participants in CARES Act funds and programs.

Lessons from the Last Crisis

As was the case during the 2008 global financial crisis, we expect that this environment of intense scrutiny will place significant pressure on PRAC, SIGPR, and existing oversight functions to investigate and identify bad actors and—together with federal law enforcement agencies, the Securities and Exchange Commission ("SEC"), banking regulators, and other civil enforcement agencies who may act on PRAC or SIGPR findings—to bring high-profile cases to punish and deter fraudulent or abusive conduct. This will almost certainly include pressure to bring enforcement actions against corporate beneficiaries of the CARES Act, both because of a broad popular concern that large companies will benefit more than ordinary Americans, and because large companies are bigger targets, both financially and optically.

For instance, SIGTARP's investigations, some of which remain ongoing, have resulted in criminal convictions or successful civil enforcement actions against 380 defendants to date. This includes 24 enforcement actions brought by the SEC, DOJ, and other regulators as a result of SIGTARP's investigations. Altogether, SIGTARP has to date collected more than $11 billion from defendants.

Overall, SIGTARP has not brought a significant number of cases against large companies, but it has brought at least a few high-profile corporate criminal enforcement actions, including cases where the alleged criminal violations related to failures to timely process recipient applications under TARP programs, or purported misrepresentations to program recipients regarding program expectations.

The cases brought by SIGTARP are instructive. They highlight, among other things:

- the anticipated degree of cooperation between PRAC, SIGPR, and existing oversight and law enforcement agencies, with PRAC and SIGPR acting as a conduit to existing enforcement capabilities across the country; and
- the risks that come from programs designed and implemented on an emergency basis, and that require program participants to act quickly without clear or otherwise adequate guidance.

Large financial institutions, in particular, will be pressured to deliver enormous sums of money quickly to struggling businesses and individuals pursuant to regulations and other guidance that may be ambiguous, incomplete, unevenly administered, or subject to frequent amendment. As past precedent shows, moreover, what seems clear now may turn out to be less clear later, especially as the political focus shifts from response to oversight and assessment.

In other words, program participants should expect substantial regulatory second-guessing—especially if there end up being widespread complications with or delays to program implementation. Any investigations by PRAC, SIGPR, or existing oversight functions will culminate years later, when the political landscape may be entirely different, with little appreciation for the circumstances that exist today.

Many of the large companies that will benefit from or otherwise participate in CARES Act programs have existing internal controls and compliance programs that will help minimize these risks, but the speed with which the CARES Act programs are being implemented and deploying funds nevertheless merits a careful and conservative posture, and a considered approach as to when and how outside legal advice is sought.

The Paycheck Protection Program: A Case Study

One of the cornerstone programs of the CARES Act is the $349 billion Paycheck Protection Program ("PPP"), which expands an existing loan guarantee program for eligible small businesses. A comprehensive overview of the PPP is available **here**, but among other things, it increases the size and percentage of the loan principal guaranteed by the Small Business Administration ("SBA"), expands the scope of businesses that are eligible as borrowers, and provides for forgiveness of significant portions of the loan principal, subject to certain conditions.

Existing SBA lenders, as well as a range of new lenders, including banks, will act as intermediaries for the $349 billion in new loans, with delegated authority to make loans to private borrowers with the full guarantee of the SBA. Program rules issued by the SBA and Treasury set out the minimal due diligence required of lenders—and also state that lenders will be held harmless for the failure of borrowers to comply with program criteria (e.g., borrower determinations of whether they are eligible for the PPP).

In ordinary times, "hold harmless" language of this nature generally would be viewed as offering adequate protection for lenders, at least insofar as lenders do not engage in grossly reckless or intentional misconduct, for instance, by making loans to borrowers they know are ineligible. As the last financial crisis demonstrated, however, ostensible protections can fall away during times of significant administrative stress and political scrutiny, with lenders who were criticized for not making loans quickly enough later accused of lending to unqualified or fraudulent borrowers.

Moreover, the protections afforded to program participants under the CARES Act—such as the hold harmless provisions for lenders—do not displace the government's existing enforcement tool kit, including garden variety conspiracy and mail and wire fraud provisions, and the False Claims Act. This existing tool kit already is robust, and if anything, given the widespread political scrutiny of CARES Act programs, there may be pressure to apply the existing criminal and civil enforcement laws even more aggressively.

In 2019 alone, DOJ obtained more than $3 billion in cases brought under the False Claims Act, a civil anti-fraud tool, pursuant to which anyone who submits a false claim or causes a false claim to be submitted to the government, can be held liable. Among other things, the False Claims Act allows for treble damages, sets out a knowledge requirement that includes reckless disregard, and offers significant financial incentives to whistleblowers and private individuals to bring *qui tam* actions on behalf of the government.[3] We think it is especially likely that, in the wake of the crisis, there will be actions brought under the False Claims Act against lending institutions alleging intentional or recklessly inaccurate statements in applications for government-guaranteed funding.

[3] The standard for control—i.e., when a parent or related company may be held liable for the conduct of its subsidiary or affiliate—is broader under the PPP than under the False Claims Act. Under the PPP, but for several narrow exceptions, entities are deemed affiliates "when one controls or has the power to control the other, or a third party or parties controls or has the power to control both," *see* 13 C.F.R. § 121.103, with affiliates aggregated together for the purposes of loan applications and determining borrower eligibility. Under the False Claims Act, by contrast, a parent or affiliate company that did not knowingly assist in the filing of false claims ordinarily can be held liable only by way of an alter ego theory of liability—through the piercing of the corporate veil. In other words, if a corporate relationship does not meet the test for control under the PPP, it is highly unlikely that there could be alter ego liability under the False Claims Act.

These considerations are not limited to the PPP. We expect similar issues with respect to other major CARES Act programs, including Treasury's economic stabilization programs, as well as the separate, but no less significant lending facilities announced by the Fed.

Conclusion

Because it is not possible to identify and map all of the potential risks that could emerge from the implementation of a relief package as large and as sweeping as the CARES Act, all potential program participants can do is take a cautious, risk-based approach to participation. This might include, for instance:

- Developing clear internal processes for identifying, assessing, and categorizing programmatic risks, with internal or external counsel given clearly defined roles with respect to the assessment and resolution of risks that exceed a certain threshold;
- Ensuring that all program documentation (e.g., application or loan materials) is aligned with any internal risk assessment processes, and has been subject to business and legal / compliance review; and
- Obtaining the advice of external counsel for especially significant programmatic considerations, in order to ensure that all potential compliance vulnerabilities are carefully scrutinized and to provide the basis for raising an advice-of-counsel defense should the need later arise.

Notwithstanding the immense pressure on CARES Act program participants to distribute or obtain funds as quickly as possible, participants should be careful to ensure that short-term needs are not unintentionally creating longer-term, more significant risks.

If you have any questions regarding the matters covered in this publication, please contact any of the lawyers listed below or your usual Davis Polk contact.

Greg D. Andres	+1 212 450 4724	greg.andres@davispolk.com
Martine M. Beamon	+1 212 450 4262	martine.beamon@davispolk.com
Angela T. Burgess	+1 212 450 4885	angela.burgess@davispolk.com
Neil H. MacBride	+1 202 962 7030 +1 212 450 3191	neil.macbride@davispolk.com
Tatiana R. Martins	+1 212 450 4085	tatiana.martins@davispolk.com
Fiona R. Moran	+1 202 962 7137	fiona.moran@davispolk.com
Paul J. Nathanson	+1 202 962 7055 +1 212 450 3133	paul.nathanson@davispolk.com
Kenneth L. Wainstein	+1 202 962 7141 +1 212 450 3152	ken.wainstein@davispolk.com
Michelle Adler	+1 212 450 3271	michelle.adler@davispolk.com
John A. Atchley III	+1 212 450 3469	john.atchley@davispolk.com