

The CARES Act and lessons from the past: What prior investigative responses to crises tell us about the future

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The Coronavirus Aid, Relief, and Economic Security Act provides an expansive outlay of federal funds and other relief to support individuals and companies impacted by the coronavirus outbreak.

In tandem with the relief, the CARES Act also outlines several new layers of oversight, one of which comes in the form of the newly created Office of the Special Inspector General for Pandemic Recovery, situated in the Treasury Department, and vested with the authority to supervise, by the way of audits and investigations, the loans, loan guarantees and other investments made by the secretary of the Treasury pursuant to CARES Act programs.

Like other inspectors general, the SIGPR has the authority to access all records and materials relevant to its areas of oversight; to determine which audits, investigations and reviews are necessary (and conduct such reviews under its authority); to issue administrative subpoenas for documents and execute warrants; and to refer criminal and civil matters to prosecuting authorities such as the Justice Department.

If past is prologue, prior federal investigative responses under SIGTARP and in the wake of Hurricanes Katrina and Rita suggest that the SIGPR will undertake a significant amount of audit and investigative work.

While much is unknown about the types of audits and investigations that the SIGPR will pursue, an evaluation of past government efforts to oversee spending associated with crises is an instructive guide for companies now weighing how to best protect themselves when applying for and using CARES Act funds.

Two such prior efforts provide good benchmarks for government oversight of emergency funding — the Office of the Special Investigator General for the Troubled Asset Relief Program and the government response across multiple agencies following the recovery efforts necessitated by Hurricanes Katrina and Rita and more recently Hurricane Maria.

Each also serves as a guide for specific compliance advice for companies pursuing CARES Act funding and related governmental relief, to help mitigate downstream risk associated with prospective audits and government scrutiny.

SIGTARP AS A GUIDE

SIGPR appears to be largely modeled after SIGTARP.

SIGTARP, also situated in the Treasury Department, was created as an investigatory body with oversight authority over TARP — the Treasury Department initiative that invested billions of dollars in banks and other institutions following the 2008 financial crisis.

SIGTARP remains operational today. Although the circumstances that led to the creation of SIGTARP are far different from those that have led to the creation of SIGPR, Congress similarly granted SIGTARP broad statutory authority to investigate companies that received federal funds.

SIGTARP's investigative activity therefore provides a useful framework for the type and volume of investigative activity we might expect to see from SIGPR.

Since its inception, SIGTARP has aggressively pursued its mandate, conducting investigations that have resulted in the recovery of more than \$11 billion as of September 2019 (including nearly \$900 million in 2019 alone), hundreds of prosecutorial referrals and 381 criminal convictions.²

SIGTARP's investigative work also led to 24 enforcement actions brought by the DOJ, Securities and Exchange Commission and other regulators.³

Such efforts rooted out misconduct within the more than 150 banks and institutions that received money under TARP. The efforts included investigations of financial fraud in banks where the Treasury holds securities and investigations related to failed or otherwise defunct financial institutions.

Some combination of the DOJ, SEC, other federal regulators (including the Federal Reserve and Consumer Financial Protection Bureau) and/or state-law enforcement agencies spearheaded the

resulting enforcement actions, which in addition to targeting the financial sector, ensnared a number of external auditing firms with charges related to negligence and professional failures.

The DOJ and its counterparts frequently used the federal False Claims Act statute to pursue these actions, targeting institutions that submitted false or misleading information in connection with TARP funds or failed to disclose negative information concerning loans and derivative securities to federal regulators.⁴

Each of these enforcement actions came with a significant price tag — most involved penalty amounts in the millions of dollars, with one such penalty tipping the scale at \$13 billion.⁵

In addition to targeting corporate institutions, SIGTARP's investigative work led to criminal charges against 430 individual defendants and 381 criminal convictions.⁶ This number includes individual bankers who committed crimes at banks that received TARP funds, those who targeted homeowners with false promises of entry into TARP assistance programs, and individuals who defrauded banks participating in TARP programs.

As noted in SIGTARP's most recent semiannual report submitted to Congress, as of Sept. 30, 2019, 291 of those charged and convicted were sentenced to prison.⁷

LESSONS LEARNED FROM NATURAL DISASTER RECOVERY

The coronavirus pandemic was not triggered by economic shortcomings. Nor was it exacerbated by any one industry.

In this respect, the current national emergency is very much unlike the 2008 financial crisis.

Rather, it represents a natural disaster of unprecedented scale, meaning that oversight of CARES Act funds may take on a form similar to oversight in the wake of other natural disasters such as Hurricanes Katrina and Rita and more recently Hurricane Maria.

The 2005 hurricane season was a record-breaking season for storms, and Hurricanes Katrina and Rita wreaked havoc on the Gulf Coast. The wide-ranging cleanup operation and need to house victims caused the federal government to let tens of billions of dollars in contracts.

Oversight efforts followed in short order, with audits, investigations and (where necessary) prosecutions for procurement and other fraud.

Given the massive recovery effort, the government formed collaborative multiagency organizations in the wake of the devastation — one to audit recovery relief contracts (the Hurricane Katrina Contract Audit Task Force), and the other to deter, detect and prosecute recovery-related fraud (the Hurricane Katrina Fraud Task Force).

By mid-2006, 261 defendants had been charged in 218 cases across 24 different judicial districts.⁸

Forty-four of those defendants had been convicted, and approximately 465 government auditors were at work reviewing over 6,665 contracts valued at \$10 billion.⁹

Just over one year later, those numbers had grown with more than 768 defendants charged across 41 judicial districts for hurricane-related fraud, including ongoing investigations and prosecutions related to procurement fraud, public corruption and other issues.¹⁰

Following Hurricane Maria in 2017, the federal government provided billions in relief to help rebuild Puerto Rico's electric grid and to pay for temporary housing and other services.

Recent SEC guidance suggests that if an issuer anticipates receiving federal or state financial assistance due to the pandemic, it should carefully consider how such relief may have a material effect on its financial condition or operations and tailor its disclosures accordingly.

In September 2019, a federal grand jury in Puerto Rico indicted two senior Federal Emergency Management Agency officials for illegally accepting bribes in exchange for steering contracts to rebuild the electrical grid to a specific contractor, who was also indicted.¹¹

The case was investigated by the Department of Homeland Security Office of Inspector General with assistance from the FBI.¹²

COMPLIANCE TIPS FOR CARES ACT BENEFICIARIES

If past is prologue, prior federal investigative responses under SIGTARP and in the wake of Hurricanes Katrina and Rita suggest that the SIGPR will undertake a significant amount of audit and investigative work.

SIGPR will almost certainly train its investigative eye on both companies and individuals and make a significant number of prosecutorial referrals to federal and state enforcement agencies.

So, what can and should companies do now to protect themselves from downstream audit, investigation and enforcement-related risk associated with the CARES Act?

Recipients of federal relief should carefully evaluate all government requirements and other obligations related to CARES Act funds, ensure that their representations to the government when applying for and using government funds are accurate and complete, and maintain adequate records.

PAY CLOSE ATTENTION TO COMPLIANCE REQUIREMENTS

Recipients of CARES Act funds should carefully consider the compliance requirements and other obligations (e.g., agency-specific regulations and/or terms and conditions, where applicable) tied to federal funds and interactions with federal government officials.

Creating a compliance matrix of reporting and related compliance obligations to track the various requirements and ensure that they are fulfilled is a good first step.

Beyond that, recipients should adopt policies and procedures to satisfy the conditions and restrictions associated with CARES Act funds, closely monitor for and review any agency guidance related to such restrictions and implement controls to ensure that CARES Act funds are used on authorized expenses only.

Proactive training for those handling CARES Act funding regarding the use of the funds and restrictions attached to them, and good record keeping of such training, is also advisable.

BE CANDID WITH THE GOVERNMENT

Beginning with any applications for CARES Act relief and funds, prospective beneficiaries should ensure that any representations to the government are accurate and complete.

The same approach should be adopted for any required reports submitted to the government as a condition of receiving CARES Act funds. Companies should also carefully weigh what other non-CARES Act obligations financial relief under the act might trigger.

For instance, recent SEC guidance suggests that if an issuer anticipates receiving federal or state financial assistance due to the pandemic, it should carefully consider how such relief may have a material effect on its financial condition or operations and tailor its disclosures accordingly.¹³

During an audit or other government inquiry, candor and cooperation in responding to government requests is essential. Companies may want to engage outside legal counsel to support them in dealing with government inquiries, and to help them avoid any pitfalls along the way.

MAINTAIN ADEQUATE RECORDS

Retain a file of key documentation related to CARES Act funding. It may become indispensable in the event of an audit and will demonstrate a good-faith effort to comply with funding requirements.

The file should include, at a minimum:

- The application for funds and diligence supporting the veracity of statements made in the application;

- Award/disbursement documents (if any) from the government;
- Training and records of attendance at such training for employees handling CARES Act funds;
- Any published guidance and/or communications with government officials related to the permissible use of funds (including any evidence of modifications to funding requirements). Records of communications with government officials should capture key information, including the date and time of communication, and the name and title of the official;
- Evidence that CARES Act funds were used for allowable purposes; and
- Evidence supporting compliance with government requirements (i.e., compliance matrix, if applicable).

Many continue to reel from the impact of the coronavirus pandemic. Companies have, understandably, prioritized immediate needs — not the least of which is the health and safety of their employees and the continued viability of their business.

Nevertheless, those contemplating receipt of CARES Act funding are wise to take steps on the front end to protect their business and employees from the risk associated with government scrutiny.

With precedent as a guide, once the immediate health emergency fades, the unprecedented aid contemplated by the CARES Act will almost certainly be followed by an unprecedented number of government audits, investigations and enforcement efforts.

Notes

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² Office of the Special Inspector General for the Troubled Asset Relief Program, Semiannual Report to Congress 3, 5 (Apr. 1, 2019 - Sept. 30, 2019), available at <https://bit.ly/3bwC9S5> (last visited Apr. 16, 2020); Office of the Special Inspector General for the Troubled Asset Relief Program, Quarterly Report to Congress 2 (Oct. 1, 2019 - Dec. 31, 2019), available at <https://bit.ly/3aAL2ch> (last visited Apr. 16, 2020).

³ SIGTARP, Semiannual Report to Congress, 6.

⁴ See generally Office of the Special Inspector General for the Troubled Asset Relief Program, Financial Institution Crimes & Fines Database, available at <https://bit.ly/2xlp1Lc> (last visited Apr. 16, 2020).

⁵ *Id.*

⁶ SIGTARP, Semiannual Report to Congress, 5; SIGTARP, Quarterly Report to Congress, 2.

⁷ SIGTARP, Semiannual Report to Congress, 5.

⁸ *After Katrina: The Role of the Department of Justice Katrina Fraud Task Force and Agency Inspectors General in Preventing Waste, Fraud and Abuse:*

Hearing Before the Subcomm. on Gov't Mgmt., Fin., and Accountability of the H. Comm on Gov't Reform, 109th Cong. 2 (2006) (statement of Alice Fisher, Assistant Att'y Gen. of the Criminal Div., U.S. Dep't of Justice).

⁹ *Id.* (statement of Alice Fisher, Assistant Att'y Gen. of the Criminal Div., U.S. Dep't of Justice; statement of Matt Jadacki, Spec. Inspector Gen. for Gulf Coast Hurricane Recovery, Dep't of Homeland Security).

¹⁰ Hurricane Katrina Fraud Task Force, Second Year Report to the Attorney General 4, (Sept. 2007), available at <https://bit.ly/2KrwfGc> (last visited Apr. 16, 2020).

¹¹ Press Release, U.S. Dep't of Justice, FEMA Deputy Reg'l Administrator, Former President of Cobra Acquisitions, LLC, and Another Former FEMA Employee Indicted for Conspiracy to Commit Bribery,

Honest Services Wire Fraud, Disaster Fraud, Among Other Charges (Sept. 10, 2019), available at <https://bit.ly/2yEtK0c> (last visited Apr. 16, 2020).

¹² *Id.*

¹³ See The Importance of Disclosure — For Investors, Markets and Our Fight Against COVID-19, Exchange Act Public Statement by Jay Clayton & William Hinman (Apr. 8, 2020), available at <https://bit.ly/357Fx3H> (last visited Apr. 16, 2020).

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