Administration turning attention to banks in PPP fraud probe

Thursday, May 5, 2022 8:48 AM ET

By Alison Bennett
Market Intelligence

Banks will face greater scrutiny as the Biden administration shifts the focus of its Paycheck Protection Program fraud probe toward lenders.

"The government is absolutely going to be and already is looking at lenders," said Chris Cooke, a defense and investigations attorney at Norton Rose Fulbright. "Banks should expect to hear from the enforcement community. If you're a bank you need to get your arms wrapped around what your [Paycheck Protection Program] profile looks like."

The U.S. Department of Justice is leading the anti-fraud effort, announcing a new chief prosecutor, Associate Deputy Attorney General Kevin Chambers, to pull together the administration's efforts across a range of initiatives including the Paycheck Protection Program, or PPP. The agency also said it would put in place interagency "strike forces" to track down COVID-19 relief fraud.

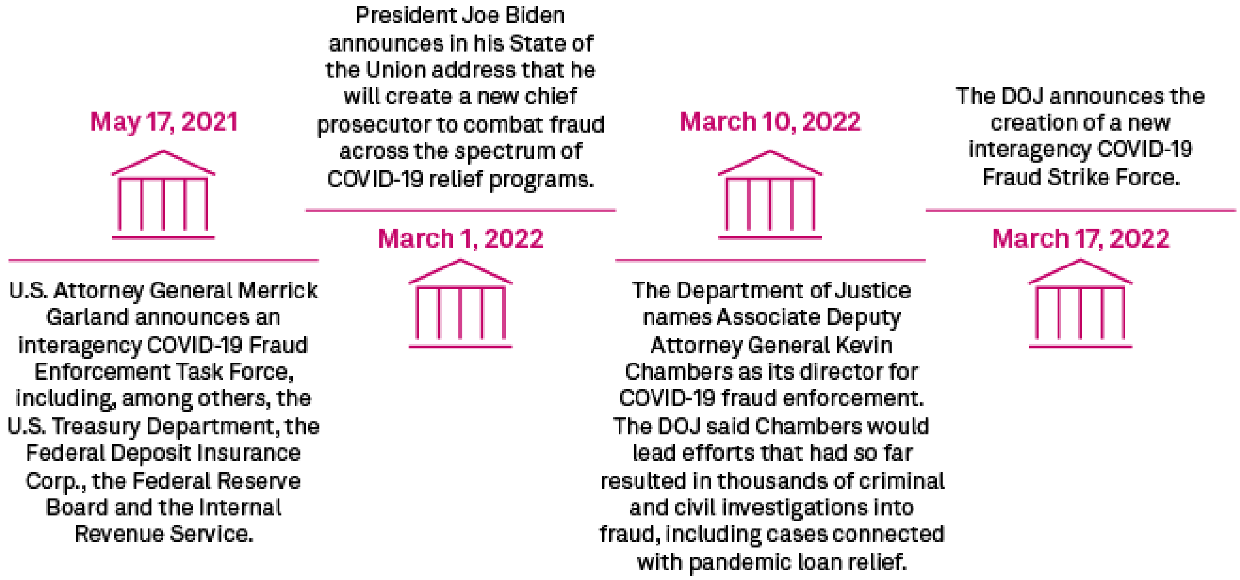
More complex cases

First enacted in April 2020 and closed in May 2021, the PPP allowed banks to lend up to $10 million to businesses in need of help, with the ability to get those loans forgiven over time. While banks have since gotten a large majority of PPP loans forgiven, some remain on the books.

The agency has brought the majority of PPP fraud cases against borrowers, but the DOJ and other banking agencies will be moving on from those simpler cases to more complex ones that likely will include inquiries into banks and other financial services companies, enforcement specialists said in interviews.

"The government may now be looking at [financial technology] servicers, banks or bank employees that advised people to borrow money through the [PPP]," said former federal prosecutor Sean McDonnell, now a partner in the global litigation and dispute resolution practice at Mayer Brown LLP.

Efforts to prosecute fraud through COVID-19 pandemic relief programs



Created May 4, 2022.
Source: S&P Global Market Intelligence

In the first criminal prosecution of a PPP lender on March 1, the Justice Department arrested the CEO of PPP lender MBE Capital Partners, Rafael Martinez, on multiple charges of fraudulent loan and lender applications.

And in April, the Federal Reserve banned from the financial industry six former bank employees, including two who had previously worked in Bank of America's wealth management unit, for approving fraudulent pandemic relief under the administration's Economic Injury Disaster Loan program.

Loan activity scrutinized

The government will be looking at banks to see how many loans they disbursed and where the money went, said Norton Rose Fulbright's Cooke, who was previously special counsel to the administration's special inspector general for pandemic recovery.

As the efforts continue, the administration is likely to widen the net to find PPP wrongdoing, according to Kevin Toomey, a partner at Arnold & Porter who represents banks and other financial services companies before the DOJ, the Federal Reserve and other federal financial agencies.

"I think you will see more cases involving the misuse of loan proceeds and ineligible borrowers," Toomey said in an interview. "There will likely also be more complex cases involving networks of individuals working together to defraud the government."

Joint effort

Cooperation between agencies, including partnerships between the DOJ, FBI and IRS, is already leading to more complex cases.

Partnerships enable agencies to use data analytics more effectively to find fraud, said Adam Braverman, a partner in Morrison & Foerster's Investigations + White Collar Defense group.

The administration also is taking more action under the False Claims Act, a tool that the DOJ uses to unearth fraud in government programs, said Braverman. Braverman was formerly U.S. associate deputy attorney general and U.S. attorney for the Southern District of California.

With big swaths of data already available from banks, the DOJ is using indicators from that data to identify troublesome loans.

In looking at financial services providers, "If there are big pots of problematic loans, a pattern that was processed by certain loan providers or run through certain servicers, the government is getting much better at pattern recognition," Mayer Brown's McDonnell said.

However, some attorneys expressed a belief that financial institutions may not be an appropriate target of the Justice Department and other agencies. Most banks simply were doing the best they could to help businesses, as encouraged by the government during a difficult time, they said.

"Banks should be viewed as answering the call," said Arnold & Porter's Toomey. "The world was a very different place in the spring of 2020. Every borrower thought that layoffs were imminent, and lenders were doing everything they could to get funds to businesses as quickly as possible."

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