

The Legal Intelligencer

Stimulus Fraud: How Agencies Investigate It and What Happens When They Find It

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In Part I of our series, we analyzed the spending features of the COVID-19 stimulus packages and introduced the Troubled Asset Relief Program (TARP) as the closest historical analogue to them. In Part II, we discussed TARP in greater detail and highlighted the various ways fraudsters exploited it. Here we dive into how federal agencies coordinated to investigate TARP fraud and discuss representative cases to understand what those fraud investigations related to the COVID-19 stimulus programs.

INTRODUCTION

For more than 10 years, federal investigators, led by the Special Inspector General for the TARP (SIGTARP) have, in coordination with the Department of Justice (DOJ), Federal Bureau of Investigations (FBI), Securities Exchange Commission (SEC), Internal Revenue Service (IRS), Financial Crimes Enforcement Network (FinCEN), Small Business Administration (SBA) and other investigative agencies, investigated criminal conduct in connection with the 2008 recession-era TARP program. From those investigations, U.S. Attorneys across the country brought cases and earned convictions for offenses spanning the federal criminal code.

We can expect that these same agencies will use the same techniques and strategies to investigate crimes and bring cases involving fraud related to the COVID-19 stimulus packages. Just over a month removed from passage of the CARES Act, it has already begun. The SEC has halted trading and brought enforcement actions against companies misrepresenting their ability to fight COVID-19 and the financial impact the pandemic has and will continue to have on their businesses. The DOJ has charged individuals for allegedly defrauding the Payroll Protection Program (PPP). The Treasury Department has announced the automatic audit of large recipients of PPP loans. Yet, these actions do not even represent the tip of the iceberg; they are merely foreshadowing.

TARP FRAUD—WHO INVESTIGATED IT AND HOW

SIGTARP was established by the Emergency Economic Stabilization Act of 2008 (EESA) and authorized to conduct, supervise and coordinate audits and investigations of any actions taken under the TARP. SIGTARP was and remains a proactive investigative agency. To detect fraud in connection with TARP spending, SIGTARP employs investigative techniques analyzing transactional data for trends and patterns that might indicate fraud. Taking an analytical approach, SIGTARP has been able to identify industry hotspots for fraud, characteristics indicating potential fraudulent conduct and profiles of potential fraudsters and with that information obtain nearly 400 convictions and recover more than \$11 billion.

But, SIGTARP has not operated on analytics alone. Around half of SIGTARP's investigations were spurred by tips from victims, insiders and other members of the public. Also, importantly, SIGTARP has worked extensively with other law enforcement agencies to expand its reach and leverage its resources. SIGTARP's partnerships has enabled it to reach beyond crimes solely related to acquisition of funds through TARP to other associated offenses including accounting fraud, securities fraud, insider trading, bank fraud, mortgage fraud, mortgage modification fraud, wire fraud, false statements to the government, false entries on bank records, obstruction of justice, money laundering and more.

REPRESENTATIVE TARP PROSECUTIONS

Investigations flowing from TARP snared fraudsters of all stripes: individuals and businesses stealing money from the stimulus programs, executives deceiving investors, bank employees exploiting the crisis for their personal gain, professionals assisting those wrongdoers and many others.

On March 15, 2010, the U.S. Attorney for the Southern District of New York brought the first charges against a defendant for defrauding TARP. The defendant was charged with and ultimately pleaded guilty to attempting to fraudulently obtain more than \$11 million worth of taxpayer rescue funds from TARP. The defendant pleaded guilty to making a “round-trip transaction” through which he fraudulently borrowed \$6.5 million from the bank at which he was president through various entities he controlled, which he then claimed as his personal assets and surreptitiously redeposited in order to inflate the bank's financial position. Relying on the inflated capital position of the bank, the defendant had the bank apply for \$11 million in rescue funds through TARP. Investigators from SIGTARP, working with the New York State Banking Department (NYSBD), the FBI and the Federal Deposit Insurance Corporation Inspector General (FDIC IG) found that as part of his scheme to defraud TARP, the defendant also exploited a bankrupt entity to conceal the fraudulent loans, forged bank notes, made misrepresentations to auditors and lied to bank regulators. In top of that, investigators found that the defendant engaged in various investment fraud schemes, self-dealing, bank bribery and embezzlement. The defendant agreed to forfeit \$11.25 million in various assets and was ultimately sentenced to 30 months in prison.

On Feb. 20—just under ten years after the first case dropped—SIGTARP announced the most recent indictment related to the program, which resulted from a joint investigation by the Federal Housing Finance Agency (FHFA), FDIC, SIGTARP and the SBA Inspector General. The former president and chief executive officer of a Maryland bank was indicted on charges of conspiracy to commit bank fraud and related crimes. According to the indictment, the defendant, through a straw purchaser, had over the course of several years defrauded the bank, which had received \$11,560,000 in TARP funds in 2008 under the Capital Purchase Program, of real property. The defendant and her co-conspirators orchestrated fake appraisals for the bank's inventory of foreclosed properties and acquired those properties from the bank for far below market value.

In between, law enforcement detected and prosecuted the full panoply of federal crimes. Closer to home, in 2015, the U.S. Attorney's Office in Philadelphia charged the president and CEO and chairman of the board of a now defunct bank for attempting to defraud TARP of over \$13 million. Following a trial, the two defendants were found guilty of conspiring to inflate the bank's capital position in order to support its application for \$13.5 million in TARP funding.

On March 23, 2016, the former CEO of a Nebraska bank—a TARP applicant—was sentenced for his role in defrauding shareholders and misleading regulators by concealing more than \$100 million in losses in the bank's loan and real estate portfolio in a case investigated by the FBI, SIGTARP and the SEC. The 74-year old defendant was sentenced to 132 months in prison and ordered to pay a \$1.2 million fine.

On Aug. 3, 2018, the former CEO and the former chief loan officer of a California bank and their attorney were sentenced to 100, 100 and 80 months in prison, respectively, after being convicted of conspiracy, wire fraud, money laundering and other charges. For years, the three had engaged in a scheme whereby they caused the bank to commit tens of millions to co-conspirators acting as straw borrowers. They then funneled those proceeds into California real estate projects. All told, their fraud caused the failure of the bank, \$11.5 million in losses to the FDIC and \$8.65 million in losses to TARP. The prosecution resulted from a collaborative investigation between SIGTARP and FDIC investigators.

COVID-19 STIMULUS INVESTIGATIONS

In her April 30 report to Congress, current SIGTARP Christie Goldsmith Romero described the circumstances around the creation of her office: “as normal life was upended, financial markets crashed, and uncertainty about what was next ruled the day.” She continued, noting that “crisis related crimes are crimes of opportunity, ... expertise in TARP and bailed-out industries means we can see the same opportunities that criminals see. Our auditors identify fraud risk and vulnerabilities. Our investigators use an innovative intelligence-based strategy to find crime.” It is hard to hear anything in her words but a promise and a warning to those committing fraud under the COVID-19 stimulus packages.

It is important to note that TARP, for all its size, was designed and implemented to buttress the financial industry specifically. Higher education, lower education, health care, small businesses, the self-employed, the unemployed—these and other intended beneficiaries of the COVID-19 stimulus programs had no benefits to seek from TARP. And yet, as we’ve seen, fraud was rampant. At over five times the size of TARP and designed to forestall ruin across the American economy, the COVID-19 stimulus packages touch individuals and businesses in nearly every sector of society. Fraud may be literally everywhere, from the large publicly-traded businesses that have sought millions in PPP money, to the hospitals seeking funds to cover health care-related expenses, to the municipalities seeking funding to pay for COVID-19 response efforts. And, as we’ve seen, people and businesses will commit additional crimes incident to defrauding the stimulus programs. Whether involving public companies communicating important information concerning their financial well-being during this crisis seeking to assuage investors’ concerns, companies and individuals filing tax returns reflecting the needs they did or did not have in acquiring stimulus funds, companies and individuals lobbying public officials for funding related to efforts to combat COVID-19, communications, actions and efforts even tangentially related to applying for or receiving stimulus funding presents an opportunity for deceit. Investigators are already marshaling their resources to detect and prosecute those deceptions.

The DOJ has announced that it will employ teams of auditors, investigators and prosecutors dedicated solely to reviewing and analyzing data in order to spot anomalies that might indicate criminal activity. The SEC is reviewing and analyzing any public statements companies make concerning COVID-19 for potential misrepresentations. Treasury has announced the automatic audit of any PPP loan over \$2 million. But these are just initial efforts. The CARES Act provides for the creation of a Special Inspector General for Pandemic Recovery (SIGPR) and allocates \$25 million for the office’s initial budget. The White House has appointed Brian D. Miller, a former federal prosecutor and Inspector General for the General Services Administration to serve as SIGPR and his confirmation is winding its way through the Senate. If and when Miller is confirmed, the work of SIGPR can begin in earnest. Operating through a central investigative hub, regulatory and criminal oversight of the COVID-19 stimulus packages will be in full swing working with the knowledge and expertise developed from experience.



In the final piece in our series, we will examine in greater detail the oversight provisions of the COVID-19 stimulus packages and their overlap with other investigative bodies.

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