

Potomac
LAW GROUP



Paycheck Protection Program: Overview & Risks for Community Banks

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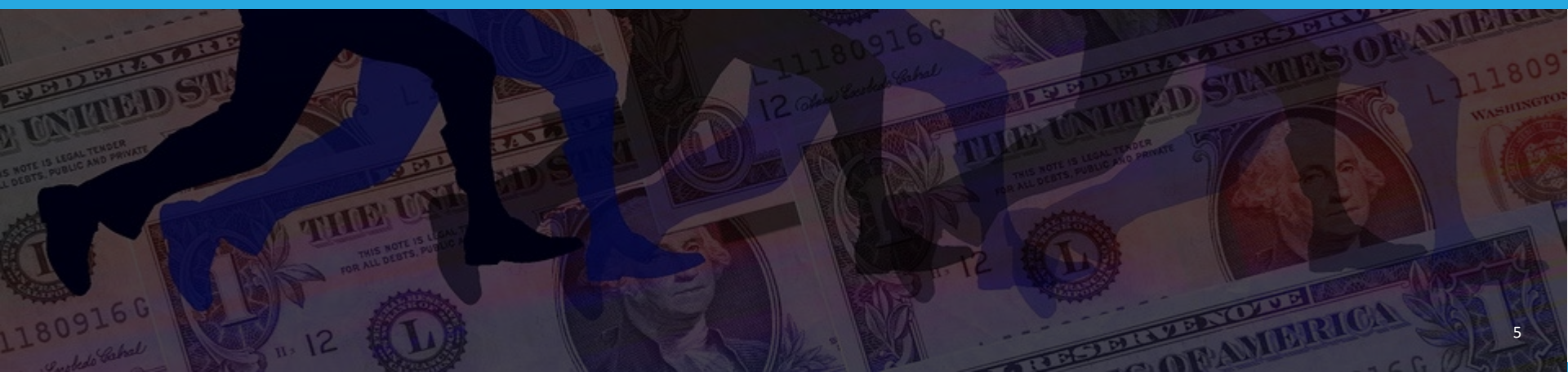
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Agenda

- PPP Overview & Program Statistics
- PPP Lender Eligibility Overview
- Lenders Held Harmless?
- Enforcement



PPP Overview & Program Statistics



Keeping Track of PPP Statutes



The Coronavirus Aid, Relief, and Economic Security Act (“CARES Act”)

- March 27, 2020 - \$349 billion in PPP funds



Paycheck Protection Program and Health Care Enforcement Act (“PPPHCEA”)

- April 24, 2020 - \$310 billion in PPP funds (total of \$659 billion)



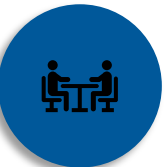
Paycheck Protection Program Flexibility Act (“PPP Flexibility Act”)

- June 5, 2020 - Extended loan forgiveness covered period from 8 to 24 weeks
- Created business activity level safe harbor



Economic Act to Hard-Hit Small Businesses, Nonprofits and Venues Act (“Economic Aid Act”)

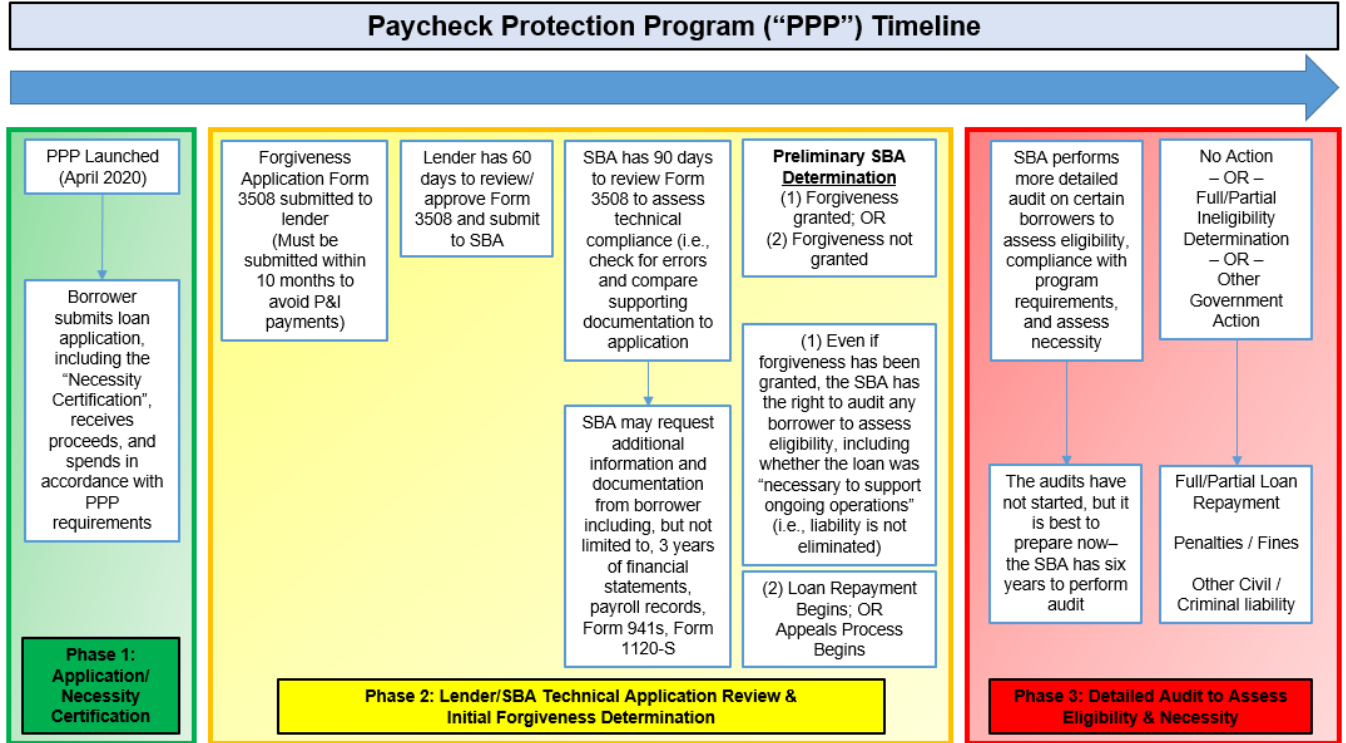
- December 27, 2020 - \$284 billion in PPP funds (total of \$806.45 billion)
- Reopens “First Draw” PPP loans and creates “Second Draw” loans



The American Rescue Plan Act of 2021 (“Rescue Plan Act”)

- March 11, 2021 - \$7.25 billion in PPP funds (total of \$813.7 billion)
- Additional nonprofits and larger nonprofits eligible

PPP Process Overview



PPP Statistics

Loan Origination (Statistics as of May 31, 2021, Program Close Date)

- Total Loans Approved = 11,823,594
- Total Net Dollars Loaned = \$799,832,866,520
- Average Loan Amount = \$67,647
- Total Lenders = 5,467

Loan Forgiveness (Statistics as of July 30, 2021)

- Total PPP Volume = 11,482,745; \$791.4 billion
- Applications for Forgiveness Received = 5,049,007; \$469.6 billion
- Forgiveness Payments Processed = 4,875,333; \$441.8 billion

Source: <https://www.sba.gov/funding-programs/loans/covid-19-relief-options/paycheck-protection-program/ppp-data>

Lender Types for 2021 PPP

Lender Type	Lender Count	Loans Approved	Net Dollars
Banks and S&Ls(\$10B or more)	112	1,807,532	\$118,331,350,203
Banks and S&Ls(less than \$10B)	4,105	1,812,102	\$101,504,685,266
Fintechs (and other State Regulated)	41	1,210,098	\$21,918,632,833
Small Business Lending Companies	13	823,576	\$15,463,750,507
Microlenders	34	532,480	\$8,540,740,467
Credit Unions (less than \$10B)	851	152,366	\$5,160,428,953
Non Bank CDFI Funds	9	276,271	\$5,047,040,642
Farm Credit Lenders	47	35,923	\$870,150,045
Credit Unions (\$10B or more)	8	14,903	\$438,573,935
Certified Development Companies	19	16,409	\$419,677,207
To Be Confirmed	2	250	\$4,779,785
BIDCOs	1	19	\$298,236
Total	5,242	6,681,929	\$277,700,108,079

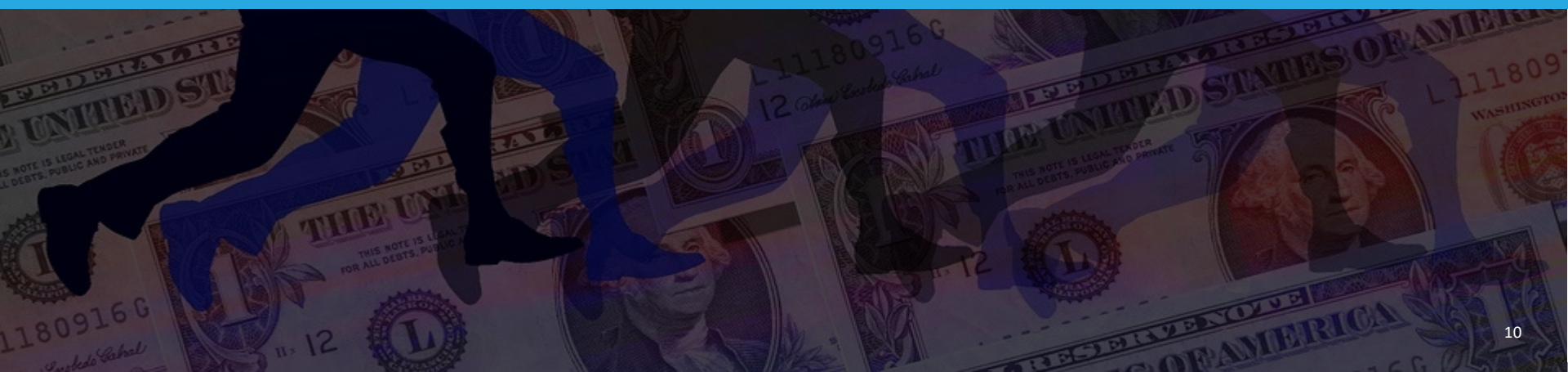
Key Takeaway: Banks, S&Ls, and Credit Unions < \$10 billion originated a total of 1,964,468, or 29.4%, of the total PPP loans approved in 2021, representing \$106.7 billion, or 38.4% of the net dollars.

Source: <https://www.sba.gov/funding-programs/loans/covid-19-relief-options/paycheck-protection-program/ppp-data>

PPP Statistics



PPP Lender Eligibility Overview



PPP Lender Eligibility Overview

PPP Interim Final Rules

- Who is eligible to originate PPP loans?
 - Any federally insured depository institution or any federally insured credit union.
 - “All SBA 7(a) lenders are automatically approved to make PPP loans on a delegated basis.”
 - EXCEPTION: “Unless the [financial institution is] currently designated in Troubled Condition by their primary federal regulator or are subject to a formal enforcement action with their primary federal regulator that addresses unsafe or unsound lending practices.”
 - Any depository or non-depository financing provider that:
 - Originates, maintains, and services business loans or other commercial financial receivables and participation interests;
 - Has a formalized compliance program;

PPP Lender Eligibility Overview

PPP Interim Final Rules

- Applies the requirements under the BSA as a federally regulated financial institution, or the BSA requirements of an equivalent federally regulated financial institution;
- Has been operating since at least February 15, 2019, and has originated, maintained, and serviced more than \$50 million in business loans or other commercial financial receivables during a consecutive 12-month period in the past 36 months, or is a service provider to any insured depository institution that has a contract to support such institution's lending activities in accordance with 12 U.S.C. § 1867(c) and is in good standing with the appropriate Federal banking agency.

PPP Lender Eligibility Overview

Bank Secrecy Act/Anti-Money Laundering Requirements

- **Financial institutions must follow “BSA protocols when making PPP loans to either new or existing customers who are eligible borrowers under the PPP.** PPP loans for existing customers will not require re-verification under applicable BSA requirements, unless otherwise indicated by the institution’s risk-based approach to BSA compliance.”
- “Entities that are not presently subject to the requirements of the BSA, should, prior to engaging in PPP lending activities, including making PPP loans to either new or existing customers who are eligible borrowers under the PPP, establish an [AML] compliance program equivalent to that of a comparable federally regulated institution.”
- “[S]uch a program may include a customer identification program (CIP), which includes identifying and verifying their PPP borrowers’ identities (including e.g., date of birth, address, and taxpayer identification number), and, if that PPP borrower is a company, following any applicable beneficial ownership information collection requirements.”

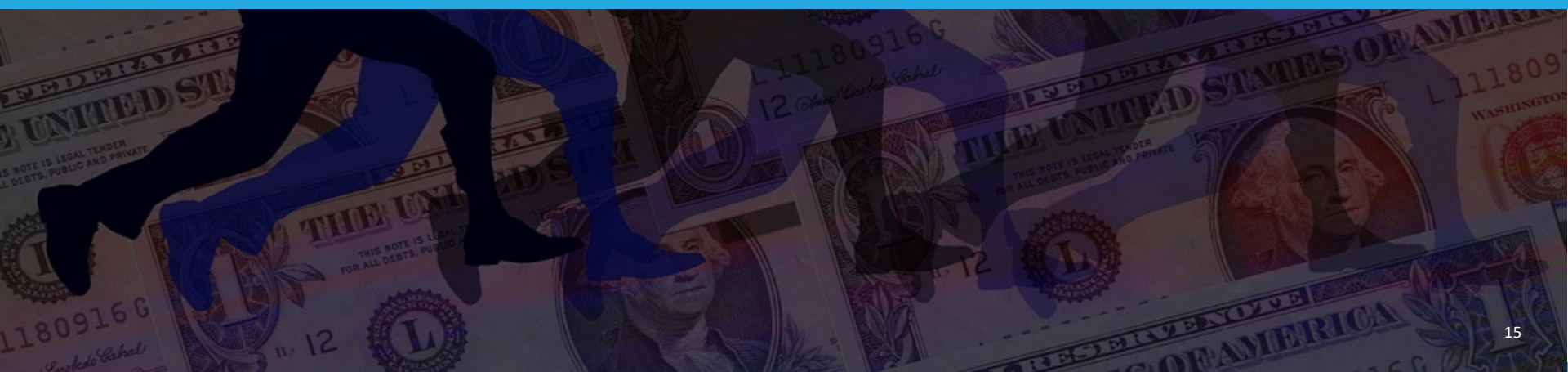
PPP Lender Eligibility Overview

Bank Secrecy Act/Anti-Money Laundering Requirements

- Why are the BSA/AML requirements related to lender PPP eligibility important?
 - Regulatory examinations
 - Lenders could have followed the PPP origination guidance but run afoul of the BSA/AML rules/regulations resulting in:
 - MRA/MRIA
 - Regulatory enforcement actions/Consent Order
 - BSA/AML compliance program remediation
 - Penalties/fines
 - O&D bars
 - Personal liability



Lenders Held Harmless?



Lenders Held Harmless?

Will Lenders Truly be Held Harmless?

CARES Act

- Section 1102(F)(ii) Delegated Authority
 - Lender “shall consider”
 - Borrower in operation on 2/15/2020 & had employees that were paid salaries and taxes, or independent contractors
- Section 1106(h) “Hold Harmless”
 - Lender must receive documents from “eligible recipient” attesting to accuracy of information
 - If received, then no enforcement action taken by SBA nor any penalties imposed by SBA against lender

Lenders Held Harmless?

Will Lenders Truly be Held Harmless?

Economic Aid Act

- Amended Section 1106(h) “Hold Harmless”
 - May rely on borrower documentation/certifications from “applicant” or “eligible recipient/entity” if:
 - Submitted pursuant to all applicable statutory requirements, regulations, and guidance
 - Contains necessary certifications
 - No enforcement action by SBA if lender “acts in good faith” and all other lender requirements met

Lenders Held Harmless?

Will Lenders Truly be Held Harmless?

Interim Final Rules

- 3.b.(i)-(iii) of First IFR (Docket No. 2020-0015)
 - Confirm receipt of borrower certifications
 - Confirm receipt of 2.15.2020 “in operation” information
 - Confirm dollar amount of average monthly payroll costs by reviewing payroll documentation
 - Follow applicable BSA requirements (e.g., establish AML compliance program)
- IV.7 of Consolidated IFR (Docket No. 2021-0006)
 - Can rely on certification/documentation if:
 - Submitted pursuant to all applicable statutory requirements, regulations, and guidance; and
 - Contains necessary borrower certifications
 - Lender must act “in good faith” and satisfy all other statutory or regulatory requirements applicable to the PPP loan
- (h)(2)(i) of IFR for Second Draw Loans (Docket No. 2021-0002)
 - Same requirements plus review of revenue reduction for qualification

Lenders Held Harmless?

Will Lenders Truly be Held Harmless?

FAQ 1

- Must the lender replicate the borrower's calculations?
 - No, but "Lenders are expected to perform a good faith review, in a reasonable time, of the borrower's calculations and supporting documents concerning average monthly payroll cost."

FAQ 4

- Are lenders required to make determination regarding affiliation rules?
 - No

FAQ 25

- Collection of beneficial ownership information for new customers?
 - Yes, for 20%+ owners

FAQ 31

- Lender may rely on borrower's certification of loan necessity

Lenders Held Harmless?

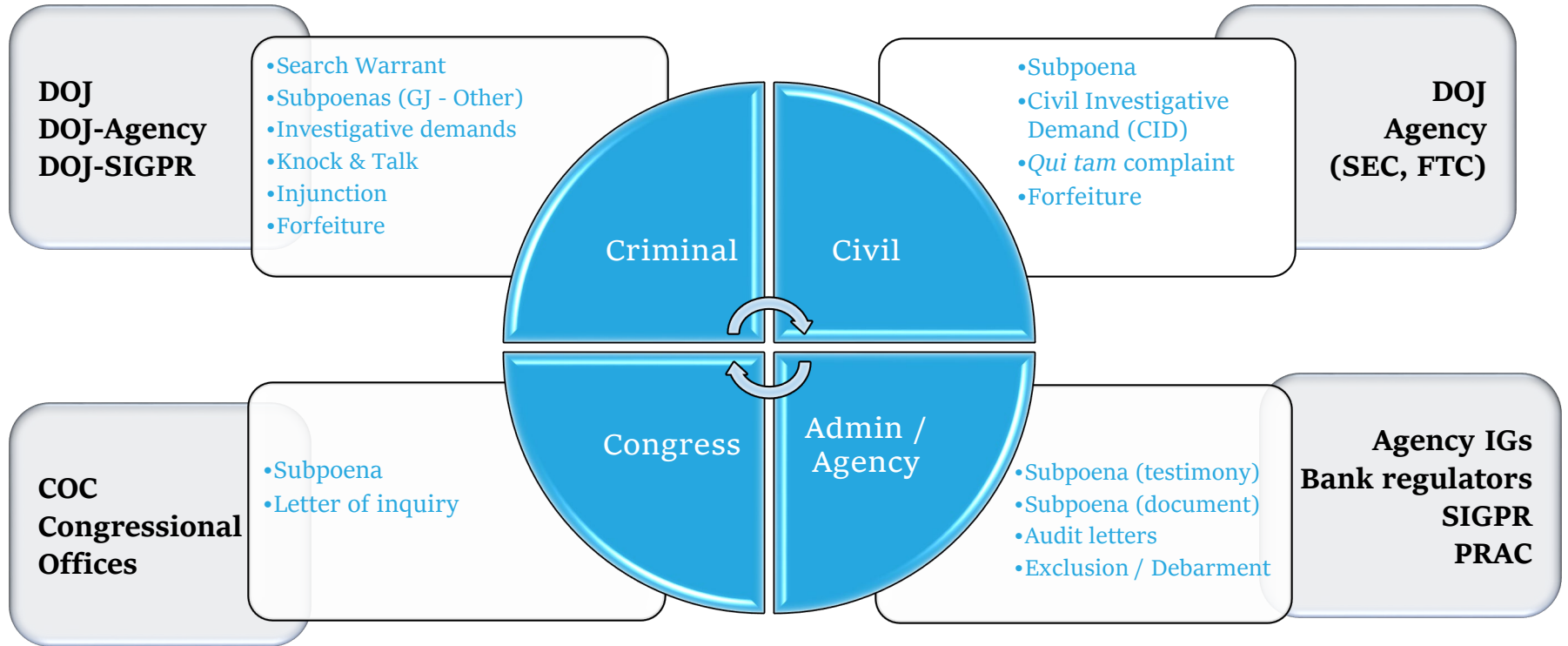
Will Lenders Truly be Held Harmless?

- What if a financial institution originated a large number of fraudulent/misrepresented loans?
- What will the implications be if a financial institution is deemed to be non-compliant with its BSA/AML obligations?
- What if a financial institution originated a disproportionate number of loans that are deemed to be “higher-risk”?
 - Foreign owned businesses
 - Private Equity owned businesses
 - Public companies
 - Loans at or near the maximum amount of \$10 million
 - Just below certain key thresholds, such as \$2 million
 - Non-customers
- What, if anything, can/should a financial institution do now to help mitigate its risks?



Enforcement

Enforcement Tools & Mechanisms



Enforcement

Oversight Entities Created by the CARES Act

Pandemic Response Accountability Committee (PRAC)

- Run by an Executive Director and Deputy Executive Director
- Consists of IGs from DOJ (chair), NASA (vice-chair), Federal Reserve, DOEd., Peace Corps, DHS, HUD, Treasury, DOT, Ag, Tax, NRO, HHS, NSF, FDIC, SIGPR, VA, DOD, SBA, USPS

Special Inspector General for Pandemic Recovery (SIGPR)

- Brian Miller, Former GSA OIG and AUSA USAO-EDVA

Congressional Oversight Commission (COC)

- Representative French Hill, Arkansas
- Bharat Ramamurti, Managing Dir. of Corporate Power Program at Roosevelt Institute
- Rep. Donna Shalala, Florida
- Sen. Pat Toomey, Pennsylvania

Enforcement

Banking Regulatory Agencies

Federal Reserve, FDIC, OCC, NCUA, Treasury/FinCEN

- As previously discussed, the PPP required originators to “follow BSA protocols when making PPP loans to either new or existing customers who are eligible borrowers under the PPP.”
- Under BSA protocols, originators are required to perform customer due diligence and monitor for potentially suspicious activity.
 - Financial institutions that had a high number of fraudulent PPP loans, especially if undetected/unreported, may have adverse BSA/AML examination findings resulting in MRA, MRIA, consent order, civil monetary penalties, etc.
 - If a financial institution lacked good faith with originating PPP loans (i.e., did not perform adequate levels of due diligence and/or follow required BSA/AML procedures), there may be False Claims Act and/or FIRREA liability (civil and/or criminal).
- Some FIs are now, retroactively, performing fraud/misrep focused loan reviews on their entire PPP portfolio to detect and report suspected fraud.

Enforcement

Department of Justice

Criminal Division of the Department of Justice

“Prominent among the department’s efforts have been cases brought by the Criminal Division’s Fraud Section involving at least 120 defendants charged with PPP fraud.” March 26, 2021: DOJ Press Release on CARES Act Enforcement.

Civil Division of the Department of Justice

- “Going forward, the Civil Division will make it a priority to use the False Claims Act to combat fraud in the Paycheck Protection Program.” Principal Deputy Assistant Attorney General, June 26, 2020.
- Three civil False Claims Act/FIRREA settlements to date
- Significant risks to borrowers (all loans over \$2m reviewed)
- Risks to lenders re “good faith” caveat, review of underlying documentation, and *qui tam* actions

Enforcement

Department of Justice Criminal PPP Enforcement

- As of August 13, 2021, all DOJ enforcement related to PPP has been against borrowers.
- As of March 26, 2021, the DOJ has publicly charged:
 - 474 defendants with criminal offenses related to COVID fraud
 - 56 federal districts involved
 - \$569 million in federal funds
 - Related to PPP, EIDL, and Unemployment Insurance

Enforcement

Department of Justice False Claims Act (FCA) PPP Enforcement

- Three settlements as of June 2, 2021
- Sandeep S. Walia, M.D. and its owner, Dr. Walia, agreed to pay \$70,000 in damages and penalties tied to allegations that Dr. Walia falsely certified in a second PPP loan application that his medical practice had not previously received a PPP loan after it had already received one from a different lender. Walia PMC also agreed to repay the second PPP loan for \$430,000.
- SlideBelts Inc., an internet retail company, and Brigham Taylor, the company's president and CEO, agreed to pay \$100,000 in penalties and damages to resolve alleged violations of the FCA. SlideBelts filed for bankruptcy on August 25, 2019. Despite the PPP application and SBA's interim final rules explicitly prohibiting debtors in bankruptcy proceedings at the time of application or any time before the loan is disbursed from receiving PPP funds, on April 3, 2020, SlideBelts submitted an application for a PPP loan for approximately \$300,000, and a few days later submitted a second PPP loan application to a second financial institution for \$350,000.

Enforcement

Department of Justice False Claims Act (FCA) PPP Enforcement

- On June 2, 2021, the EDVA USAO resolved allegations that KC Investments Group, LLC (“KC, LLC”) and KC Investment Groups, Inc. (“KC, Inc.”), through their owner, Sunu P. K.C. (“Sunu”), respectively obtained loans under the PPP, but that KC, LLC was not operating at the time of its PPP loan. In addition, the EDVA USAO alleged that KC, LLC’s loan funds were deposited into KC, Inc.’s bank account, which rendered false KC, Inc.’s representation that it would not receive multiple PPP loans. The government alleged that the forgoing conduct violated the FCA and the FIRREA. This resulted in a civil monetary penalty in the amount of \$230,414.

Questions

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