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Preparing for the Coming Onslaught of Government Investigations and Audits of COVID-19 Relief Funds and Contracting—Part I

*By Merle M. DeLancey Jr. and Craig Stetson**

This is the first in a series of articles concerning the audits and investigations related to the contracts and grants awarded, and relief funds provided, in response to the COVID-19 pandemic. In this article, the authors discuss the enforcers and the likely targets of audits and investigations related to COVID-19.

Pursuant to the Coronavirus Aid, Relief, and Economic Security Act (“CARES Act”), which created the Paycheck Protection Program (“PPP”), and supplemental funding such as the Families First Coronavirus Response Act, the United States government already has made available an estimated four trillion dollars in relief funds to businesses and individuals, and the Biden administration has proposed roughly two trillion dollars more.

In addition to the relief funds, the government has easily awarded more than billions in pandemic-related contracts for everything from vaccines to personal protective equipment (“PPE”) to hand sanitizers. These levels of funding and spending are unprecedented and have been made at breakneck speed (for the government). Based on these factors and lessons from the past, audits of relief recipients and contractors to confirm appropriate use of government funds are inevitable. And the government has said as much. Of course, if an audit reveals potential wrongdoing or malfeasance, relief recipients and contractors should expect follow-on investigations and enforcement activity.

This article first identifies the myriad of entities that are or will be reviewing—and potentially investigating—relief recipient and contractor representations made to obtain, and subsequent use of, government funds. It then identifies three categories of programs, contracts, and companies we believe are more likely to be investigated or audited.

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THE ENFORCERS

Department of Justice

The U.S. Department of Justice (“DOJ”) and 93 U.S. Attorneys’ Offices will be very active with pandemic-related investigations and prosecutions.

DOJ already has settled one matter which alleged fraud involving PPP loans. Other prosecutions involving alleged misrepresentations in order to obtain PPP loans are ongoing. DOJ also has established the DOJ Hoarding and Price Gouging Task Force.

The FBI has created a COVID-19 Working Group and a PPP Fraud Working Group.

The DOJ Civil Division’s Consumer Protection Branch is pursuing companies and individuals for, among other issues, fraudulent and otherwise illegal tests, treatments and purported cures, and scammers preying on the elderly.

Offices of Inspector General

Agency Offices of Inspector General (“OIG”) will be on the front lines of pandemic-funding audits.

First, Section 4018 of the CARES Act created the Special Inspector General of Pandemic Recovery (the “SIGPR”) and provided it with initial funding of \$25 million. The SIGPR’s primary duty is to audit and investigate the distribution of funds under the CARES Act.

Second, Section 15010 of the CARES Act created the Council of the Inspector Generals on Integrity and Efficiency (“CIGIE”). CIGIE has created the Pandemic Response Accountability Committee (“PRAC”), which consists of more than 20 Offices of Inspector General. PRAC intends to focus its reviews on financial management; grant and guaranteed loan management; information technology security and management; and protecting health and safety.

Third, either as a member of PRAC or on their own, certain Offices of Inspector General will take the lead in audit activity. These include:

- The Department of Health and Human Services OIG because of the billions of dollars in health care grant and contract awards, including awards made by the Centers for Disease Control and Prevention (“CDC”) and contract awards for the replenishment of the Strategic National Stockpile (“SNS”);
- The Department of Labor, Small Business Administration OIG, which is taking the lead in reviewing PPP payments and loans;
- The Department of Defense OIG;

- The Department of the Treasury OIG, including the Treasury Inspector General for Tax Administration (“TIGTA”), also involved in review of PPP payments and loans; and
- The Department of Homeland Security OIG, due in large part to the large role of the Federal Emergency Management Agency (“FEMA”) in awarding contracts to respond to the pandemic.

Department of Defense Contract Administration and Audit

The Defense Contract Management Agency (“DCMA”) and Defense Contract Audit Agency (“DCAA”) both are actively involved in administering and auditing CARES Act monies requested or received by defense contractors. Currently, these efforts are rooted in CARES Act Sections 1102 and 3610.

Section 1102, also known as the PPP, has morphed into a government contract compliance matter for small business contractors who have had PPP loans forgiven and also perform under flexibly priced federal contracts.

Section 3610 creates request for equitable adjustment (“REA”) opportunities for eligible contractors to seek reimbursement for idle time-related costs caused by the pandemic.

Both DCMA and DCAA have responsibilities to oversee these funding sources and assess whether monies received were accounted for properly and in compliance with the myriad of published Department of Defense (“DoD”) guidance and instruction.

Other Agency Auditors

Several non-DoD agencies maintain contract administration and auditing objectives that align with DCMA and DCAA. These objectives are carried out by internal agency-specific personnel or outsourced to third parties; for example, independent accounting firms. The non-DoD agencies have not been as visible with creation of specific guidance or instruction related to the administration and oversight of contractors in receipt of CARES Act funding, but the potential for downstream audits or investigations is real.

Congress

Both the U.S. Senate and the House of Representatives already have been active in review of pandemic spending. The CARES Act created the COVID-19 Congressional Oversight Commission. In addition, the House Coronavirus Crises Select Subcommittee has initiated investigations of meatpacking companies and nursing homes. Other standing House committees, including the Committee on Financial Services, Committee on Oversight and Reform, Committee on Energy and Commerce, and Subcommittee on National Security, have initiated pandemic-related inquiries.

Several Senate committees also have shown interest in the oversight of pandemic spending. These include the Judiciary Committee; Committee on Banking, Housing, and Urban Affairs; Committee on Finance; and Permanent Subcommittee on Investigations.

In addition, Senator Elizabeth Warren's office includes full time oversight staff expected to focus on consumer finance and medical supply chain issues.

Government Accountability Office

The CARES Act directed the Government Accountability Office ("GAO") to report bimonthly on its ongoing monitoring and oversight efforts related to the pandemic. In addition to other areas, GAO's review has included loans, loan guarantees, and other investments under Section 4003 of the CARES Act.

State Attorneys General

State Attorneys General Offices ("AGOs") also have initiated reviews and investigations related to the pandemic. For example, several State AGOs have begun reviews of nursing homes' practices and procedures during the pandemic.

In addition, states have awarded pandemic-related contracts for such services as COVID-19 testing for state employees which also could be subject to review.

Whistleblowers

Obviously, whistleblowers are not auditors, but they are often the impetus behind audits and investigations. Even prior to the pandemic, government auditors and inspector generals were unable to audit or review all government spending. Pandemic relief funding and contracting has made matters even worse. Just as with audits unrelated to the pandemic, the source of many pandemic-related audits will be whistleblower—who can be current or former, and often disgruntled, employees.

THE LIKELY TARGETS OF COVID-19-RELATED AUDITS AND INVESTIGATIONS

There are three categories of programs, contracts, and companies we believe are more likely to be investigated or audited.

Programs/Contracts

The first group of companies ripe for audits are those accepting COVID-19 relief funding and contractors performing large COVID-19-specific contracts, as well as contractors performing traditional government contracts that entail certain COVID-19-related twists impacting performance.

Companies accepting COVID-19 relief funds are likely at the top of auditors' lists for several reasons.

First, because of the magnitude of funds at issue.

Second, due to the complex and ambiguous eligibility, use, and reporting requirements. For example, the CARES Act and supplemental legislation appropriated funds to reimburse eligible healthcare providers for healthcare-related expenses or lost revenues attributable to COVID-19. Receipt of funds was easy. Most recipients' funds were automatically deposited into their bank accounts. But healthcare provider recipients have not yet been required to file reports attesting to the proper utilization of the relief funds.

Relief funds recipients in other non-healthcare industries may also be affected. Certain monies received under the CARES Act also involve ongoing and downstream reporting requirements by companies regarding statutory limitations on compensation paid to certain employees and the receipt of a variety of potential tax credits. Thus, recipients' use of funds has not been tested, and it is unlikely that all usage has been in compliance with the ambiguous requirements and multiple rounds of agency guidance and interpretations.

Similarly, based on the dollars involved and the speed in making awards, contractors receiving large COVID-19-specific contracts are likely candidates for government audits.

For example, notwithstanding their success, we expect government auditors to delve into the Operation Warp Speed contracts to test the contractors' representations and certifications.

And notwithstanding their similar stepping-up to respond to the pandemic, we expect Project Airbridge contracts and those awarded pursuant to the Defense Production Act will not be immune from auditor review. Auditors are not swayed by the fact that these contractors stepped in at the eleventh hour to help the country respond to the pandemic. Auditors follow their manuals and checklists and allow others with higher authority decide whether pandemic heroism trumps questioned costs.

In addition, we anticipate auditors testing Department of Defense and Department of Health and Human Services use of other transaction authority ("OTA") to make COVID-19-related awards because of the speed of such awards and the perception that OTAs are used to avoid following federal acquisition regulations. Although OTAs are generally not subject to the Federal Acquisition Regulation, or related Agency Supplements, the DCAA has inserted themselves into the audit process of these arrangements. In its 2020 annual report to Congress, the DCAA announced an initiative to expand audit services to OTAs and that it has developed corresponding audit procedures covering the full life cycle of an OTA, from incorporation of terms and conditions on the front end to review of contractor payments on the back end.

Finally, ongoing government contracts—not COVID-19-specific—which are subjected to routine audits, will not be able to avoid COVID-19-related inquiries. Routine DCAA audits will necessarily include financial reporting issues as a result of the pandemic under cost reimbursement contracts.

Such issues include, for example, financial forecasting and changed projections stemming from the pandemic; idle office space as a result of the pandemic and whether such costs are allowable and, if so, for how long; and the allowability of costs related to decreased employee productivity or the simple fact that tasks take longer as a result of employees working remotely.

This remains a fluid situation and the DCAA's audit objectives are generally in their formative stages; i.e., expect more to come and expansion of oversight.

The Unscrupulous

The second category of likely targets subject to investigation are companies and individuals trying to take improper advantage of COVID-19 relief efforts. Enforcement in this area has already started. In January 2021, the Justice Department settled allegations of fraud involving loans issued pursuant to the PPP.

Similarly, New York federal prosecutors brought charges against an individual for allegedly making false claims in applying for PPP loans that his companies had hundreds of employees and a multimillion-dollar payroll, submitting false business records and financial statements, and falsely claiming to be a medical equipment supplier.

And Rhode Island prosecutors brought criminal charges against a PPP loan applicant who falsely claimed to have dozens of employees at three restaurants even though the restaurants were not even open for business. Other fraud indicators include applicants seeking loans to “open” new businesses and withdrawing loan funds in cash or transferring the funds to personal and/or newly opened bank accounts.

Others falling into this category are profiteers seeking to price gouge, hoard, and/or misrepresent products related to the sale of PPE. Companies and individuals seeking substantial profit margins or engaged in PPE scams by selling fake or counterfeit products also are low-hanging fruit for investigators.

Political Targeting

Finally, some companies and individuals may find themselves being audited or investigated because, whether or not accurate, they are perceived to have been aligned with the Trump administration. Given the current political environment in Washington, one cannot dismiss the notion that certain companies and contractors may find themselves in the crosshairs of congressional investigations.

For example, it is reported that the GAO initiated a review of a contractor based on a telephone call from a U.S. senator. There have been numerous media reports regarding Trump associates and supporters receiving millions in PPP loans.

Any company whose CEO appeared in a White House Rose Garden ceremony where its efforts responding to the pandemic were touted should not be surprised to have its contracts audited or, if applicable, eligibility for relief funds reviewed.

CONCLUSION

We expect the collective government agencies to cast a very wide net and, as a result, even companies that do not necessarily fall into one of the categories above may be swept into the government's audits and investigations. Companies need to prepare for this possibility now.