

State FCA Considerations For Cos. Seeking COVID-19 Relief

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The press has devoted significant coverage to the federal government's rollout of COVID-19 relief programs — and the people who have found themselves in hot water with the U.S. Department of Justice after unlawfully securing relief funds by including false statements on their federal applications.

In many cases, those individuals who took advantage of the federal Paycheck Protection Program or U.S. Small Business Administration grants later found themselves staring down the barrel of a DOJ investigation for violations of the federal False Claims Act.[1]

News outlets have devoted decidedly less coverage to state and municipal COVID-19 relief funds — and the significant resources at the disposal of state governments, particularly state attorneys general, to bring enforcement actions similar to those of the DOJ for violating state-implemented false claims acts.

Indeed, many states have created programs to provide financial assistance to businesses and nonprofit organizations that have suffered economic harm as a result of the pandemic. Any business or nonprofit should be cognizant that providing inaccurate information in an application for public COVID-19 relief funds can entail significant legal exposure for violating state false claims acts.

As explained in more detail below, there are some commonsense steps that applicants can take when seeking state or local COVID-19 relief funds to avoid running afoul of state false claims acts.

Background: State-Level COVID-19 Relief Funds

State and municipal governments have rolled out COVID-19 relief programs that aim to provide financial assistance to small businesses, nonprofits and landlords that have taken financial hits because of the pandemic. But these programs are not designed to provide no-strings-attached funding to struggling businesses.



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Each program comes with its own eligibility requirements and, in most cases, restricts how businesses may use the funds they obtain.

Below, as examples of how state governments have reacted to the current crisis, we provide a brief overview of state-level COVID-19 relief programs in New York, New Jersey and Delaware.

New York

The New York Forward Loan Fund, or NYFLF, is a \$100 million program in which New York state, in partnership with private banking institutions, will provide low-interest loans of up to \$100,000 to small businesses, nonprofit organizations and landlords that have suffered economic hardship because of COVID-19.[2]

With respect to small businesses and nonprofits, the NYFLF restricts eligibility to those entities that employ no more than 20 full-time equivalent employees, have gross revenues or operating budgets of less than \$3 million annually, have been in operation for at least one year at the time of application, and are located in New York state.[3]

Importantly, the NYFLF does not permit participation in the program by small businesses and nonprofits that either obtained more than \$50,000 through the federal Paycheck Protection Program or that have obtained a federal economic injury disaster loan for COVID-19 for any amount — except for an advance grant of up to \$10,000.[4]

Additionally, NYFLF applicants must attest (that is, affirmatively represent) that they have "suffered a direct economic hardship as a result of COVID-19 related social distancing policies and stay-at-home order[s] that have materially impacted their operations" and provide a description of COVID-19's impact on the entity's jobs and revenues.[5]

Perhaps most importantly, the NYFLF restricts how loan recipients may use the proceeds. NYFLF funds may be used only for "working capital, inventory, marketing, refitting for new social distancing guidelines, operating and emergency maintenance, property taxes, utilities, rent, [and] supplies." [6] This limitation expressly prohibits recipients from using NYFLF funds to refinance existing loans.[7]

New Jersey

The New Jersey Economic Development Authority recently rolled out Phase 3 of the Small Business Emergency Assistance Grant Program, a \$70 million program that will award grants ranging from \$5,000 to \$20,000 to businesses or nonprofits with up to 50 full-time equivalent employees.[8]

The New Jersey Small Business Lease Emergency Assistance Grant Program requires applicants to have been in existence and operational as of Feb. 15, be fully registered to do business with the New Jersey Department of Treasury, be in good standing with the New Jersey Department of Labor and Workforce Development, and have a physical location in the state of New Jersey.[9]

Applicants also must certify their intentions to "make best efforts not to furlough or lay off any workers from the time of application through six months after the end of the declared state of emergency," or, if the business has already furloughed or laid off workers, "make a best-effort pledge to re-hire the furloughed or laid off workers as soon as possible." [10]

Additionally, applicants must certify that they have been "negatively impacted by the COVID-19 declared state of emergency" and that they have "a material financial need as a result of COVID-19 that cannot be overcome without the grant."[11]

Finally, this program limits businesses or nonprofits to using grant funding to reimburse revenue lost as a result of a business interruption caused by COVID-19 and precludes using grants for capital expenses.[12]

Delaware

Delaware has rolled out the DE Relief Grants program, which will distribute a total of \$100 million in grants to small businesses and nonprofits impacted by COVID-19.[13] And, like New York's program, DE Relief Grants will award up to \$100,000 to eligible businesses and nonprofits.

Importantly, incorporation in the state, by itself, does not allow a business or nonprofit to qualify for grant funds. Delaware's program expressly provides that businesses and nonprofits whose sole connection to Delaware is that they are incorporated in the state are not eligible to apply for funding through the program. Instead, DE Relief Grants requires that at least 51% of the business's or nonprofit's operations be physically located in Delaware.[14]

DE Relief Grants also restricts how recipients may use the proceeds, and limits eligible expenses to those "the business incurred due to COVID-19 that it would not have expected to incur during the regular course of business."[15] These include, but are not limited to, purchases of personal protective equipment and Plexiglas barriers, advertising efforts undertaken because of COVID-19, and even refinancing of debt incurred because of the pandemic.[16]

In addition, DE Relief Grants prohibits recipients from using relief funds to cover personnel expenses such as employee benefits or wages, legal expenses, and payment of taxes or fines to government authorities.[17]

State False Claims Acts

Small businesses and nonprofits that apply to state or local government programs like those outlined above should keep in mind that a majority of states — including New York, New Jersey and Delaware — have passed their own versions of the federal False Claims Act.[18]

These state false claims statutes generally make it unlawful to submit false or fraudulent information when applying for public funds — which would cover loans or grants from state-funded COVID-19 relief programs. Violating state false claims acts can result in steep penalties and can present significant legal risks to businesses already struggling with pandemic-related financial strains.

Although state false claims statutes may not use identical wording, they share some important common threads. First, the acts broadly define a claim to include any request or demand for money from a governmental body, or even a government contractor that is advancing a state interest using government-provided funds.[19]

It seems apparent that an application for COVID-19 relief would likely qualify as a claim, since, at the very least, it is a request to a state agency for money.

Second, applicants seeking public funding can violate false claims statutes even if they do not specifically intend to defraud a state or local government. Public funding applicants can run afoul of state false claims acts when they knowingly provide false information about their businesses or nonprofits — which includes instances where the applicant showed deliberate ignorance to, or reckless disregard for, the information's truth or falsity.[20]

In other words, state enforcement officials are not required to prove that an applicant who received funding had the specific intent to defraud the state agency issuing the grant. While an accidental mistake may not be enough to prove liability, the legal standard is not clear and convincing evidence that normally attaches to traditional fraud claims.

Third, state false claims statutes typically empower state attorneys general to investigate suspected false claims act violations.[21] Attorneys general have significant investigatory powers at their disposal — indeed, the New York attorney general is currently investigating a sitting president — and even a successful defense against an aggressive investigation may prove quite costly.

Also, whistleblowers can bring cases on behalf of state governments as relators, which gives the whistleblower a financial motivation to call out fraud against the state government.[22]

Fourth, it is only a slight exaggeration to call the damages regimes under state false claims acts draconian. As with the federal FCA, state false claims act violators face the prospect of paying civil penalties worth tens of thousands of dollars as well as treble damages.[23]

So, for example, if a small business fraudulently obtained a \$100,000 loan through the NYFLF program outlined above and is found liable for violating New York's false claims act, it could pay more than \$300,000 in damages.

Suggestions for Small Businesses and Nonprofits

If you are a small business or nonprofit seeking COVID-19 relief funds through a state or local government program, there are some straightforward steps you can take to avoid the prospect of dealing with an unpleasant phone call or email from your state attorney general:

- Make sure that the information you include in your application is accurate and not misleading.
- If you have obtained COVID-19 relief funding through a state or local government program, understand how you can spend the money and what costs are prohibited. Meticulously document your purchases and expenditures. As stated above, these programs typically restrict how your business or nonprofit may use relief funds.
- Have documentary proof to back up any representations you make regarding COVID-19's impact to your business.
- Make sure your paperwork is up to date. State or local COVID-19 relief programs may require you to provide your business license or nonprofit registration, recent tax returns or business expense reports when applying.
- Check whether the state or local COVID-19 relief program that you're applying to imposes any eligibility restrictions on businesses that have received federal COVID-19 relief funding — e.g.,

through the Paycheck Protection Program. Some state programs restrict federal funding recipients from applying.

- If you have received funding from a state or local COVID-19 relief program and you are unsure whether you have complied with that program's eligibility requirements, consider returning the funds or assessing your potential legal exposure.

If you have any concerns about whether you may have included false information in your application or used funds for improper purposes, you should determine as soon as possible whether the issue can be addressed through a voluntary disclosure and/or return of the funds — before a subpoena from the government or a lawsuit from a private relator arrives.

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[1] 31 U.S.C. §§ 3729 et seq.

[2] New York Forward Loan Fund FAQs (Sept. 23, 2020), available at <https://esd.ny.gov/sites/default/files/NYFLF-FAQ-092320.pdf> (last accessed Nov. 3, 2020). The NYFLF program limits nonprofit participation to 501(c)(3) entities or faith-based organizations (although funds cannot be used to support religious worship or activities). *Id.*

[3] New York Forward Loan Fund Presentation, at 7, 19 (Sept. 24, 2020), available at <https://esd.ny.gov/sites/default/files/NYFLF-Presentation-092420.pdf> (last accessed Nov. 3, 2020).

[4] *Id.* at 2.

[5] *Id.* at 7, 9, 15, 20.

[6] *Id.* at 6, 12, 18.

[7] *Id.*

[8] Information for Phase 3 of the NJEDA Small Business Emergency Assistance Grant (Nov. 2, 2020), available at <https://faq.business.nj.gov/en/articles/3835237-what-is-the-status-of-the-njeda-small-business-emergency-assistance-grant-program-phase-3-pre-registration-now-open> (last accessed Nov. 3, 2020) [hereinafter "NJEDA Grant Information"].

[9] NJEDA Small Business Emergency Assistance Grant Phase 3 FAQs, available

at <https://www.njeda.com/web/pdf/Grant%20Phase%203%20FAQs%2010%209%202020%20updated%2010%2015%2020%20v1.pdf> (last accessed Nov. 3, 2020) [hereinafter "NJEDA FAQs"].

[10] *Id.*

[11] *Id.*

[12] NJEDA Grant Information.

[13] DE Relief Grants FAQs, available at <https://business.delaware.gov/relief/> (last accessed Nov. 3, 2020). The program limits nonprofit participation to all 501(c)(6) and 501(c)(19) entities and certain 501(c)(3) entities that operate in a "disproportionately impacted industry" as defined in the program's eligibility requirements.

[14] *Id.*

[15] Delaware Division of Small Business, "Definition of Eligible Expenses," available at https://business.delaware.gov/wp-content/uploads/sites/118/2020/10/DE-Relief-Grants-Eligible-Expenses_FULLL.pdf (last accessed Nov. 3, 2020) [hereinafter "DE Eligible Expenses"].

[16] *Id.*

[17] *Id.*

[18] New York, New Jersey and Delaware have codified their False Claims Acts respectively as follows: N.Y. State Fin. L. §§ 187 et seq.; N.J. Stat. Ann. §§ 2A:32C-1 et seq.; 6 Del. Code Ann. §§ 1201 et seq.

[19] N.Y. Fin. L. § 188; see also, e.g., N.J. Stat. Ann. § 2A:32C-2; 6 Del. Code Ann. § 1202.

[20] See, e.g., *id.*

[21] 6 Del. Code Ann. § 1203(a); N.J. Stat. Ann. § 2A:32C-5(a); N.Y. Fin. L. § 190.

[22] 6 Del. Code Ann. § 1203(b); N.J. Stat. Ann. § 2A:32C-5(b)-(c); N.Y. Fin. L. §190(2)(a)-(b).

[23] 6 Del. Code Ann. § 1201(a); N.J. Stat. Ann. § 2A:32C-3; N.Y. Fin. L. § 189.