White Collar

E-ALERT

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President Obama Signs Fraud Enforcement and Recovery Act of 2009

On May 20, 2009, President Obama signed the Fraud Enforcement and Recovery Act of 2009 ("FERA" or "Act") into law. FERA amends criminal and civil fraud statutes to strengthen law enforcement's ability to investigate and prosecute all forms of financial fraud, including fraud involving the Troubled Asset Relief Program ("TARP"). In his signing statement, President Obama stated that FERA "provides Federal investigators with significant new criminal and civil tools to assist in holding accountable those who have committed financial fraud" and to crack down on the "twin scourges of mortgage fraud and predatory lending."

FERA was initially sponsored by Senators Charles Grassley (R-IA) and Patrick Leahy (D-VT), and passed the Senate and House with broad bipartisan support. The legislation responds to concerns among members of Congress over the role financial fraud played in the current economic crisis as well as the perceived need to prevent fraud in financial rescue programs designed to stabilize the U.S. banking sector.[1] An April 21 report by the Special Inspector General for the TARP highlighted the need for legislation like FERA to enhance oversight of the TARP.

The following is a summary of the key FERA provisions that address federal criminal statutes, the False Claims Act, and the creation of a commission to investigate the causes of the current financial crisis.

Federal Criminal Law Provisions

The Act contains several provisions that strengthen the federal government's ability to prosecute financial fraud, including mortgage fraud, commodities fraud, and fraud involving the government's economic recovery programs, such as the TARP.

First, the Act enhances the government's investigative and prosecutorial resources by appropriating more than $500 million in 2010 and 2011 for the express purpose of combating financial fraud. This sum includes:

- $140 million for the Federal Bureau of Investigation;
- $100 million for the U.S. Attorneys' offices;
- $40 million for the Criminal Division of the U.S. Department of Justice;
- $10 million for the Tax Division of the U.S. Department of Justice; and
- $42 million for the Securities and Exchange Commission.

[1] For an overview of the fraud and fraud-related issues arising in connection with programs such as the Troubled Asset Relief Program, please see our prior E-Alert *The "Lincoln Law" Meets the Bank Bailout: The False Claims Act and Financial Recovery Measures* (Mar. 4, 2009).

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Second, the Act expands the reach of several key federal fraud statutes to encompass mortgage and other financial fraud. The Act:

- Amends the definition of "financial institution" in the U.S. criminal code to include mortgage lending businesses. Private mortgage lenders will now be subject to criminal liability under various fraud statutes, including the bank fraud statute, 18 U.S.C. § 1344;
- Amends the so-called major fraud statute, 18 U.S.C. § 1031, to permit prosecution of fraud involving funds disbursed under TARP and other federal economic stimulus, recovery or rescue programs; and
- Amends the federal securities fraud statute, 18 U.S.C. § 1348, to permit prosecution of commodities fraud.

Finally, the Act extends the reach of the federal money laundering laws. Last year, in *United States v. Santos*, 128 S. Ct. 2020 (2008), the U.S. Supreme Court held that the term "proceeds" in the primary money laundering statute, 18 U.S.C. § 1956, refers only to the "profits" of illegal activity. The Act abrogates *Santos* by specifying that the word "proceeds" in 18 U.S.C. § 1956 and its companion statute, 18 U.S.C. § 1957, also refers to the activity's "gross receipts."

False Claims Act Provisions

The Act amends the False Claims Act to impose liability on subcontractors and entities that contract with government grantees or other recipients of government funds. These amendments abrogate three recent decisions: *Allison Engine Co. v. United States ex rel. Sanders*, 128 S. Ct. 2123 (2008); *United States ex rel. Totten v. Bombardier Corp.*, 380 F.3d 488 (D.C. Cir. 2004); and *United States ex rel. DRC, Inc. v. Custer Battles, LLC*, 444 F. Supp. 2d 678 (E.D. Va. 2006), *rev'd*, 562 F.3d 295 (4th Cir. 2009).

In *Allison Engine*, the U.S. Supreme Court held that False Claims Act liability requires proof that the defendant "intend[ed] that the Government itself [would] pay the claim," not merely proof that the entity intended to be paid by a contractor using public funds. 128 S. Ct. at 2128. In *Totten*, the D.C. Circuit held that the False Claims Act's "presentment" clause requires that the false claim be made to the U.S. government itself, not merely to a government grantee, such as Amtrak. And in *Custer Battles*, which was later reversed by the Fourth Circuit, the U.S. District Court for the Eastern District of Virginia held that a contractor could not be held liable for fraudulent claims made to the Iraqi Coalition Provisional Authority, because the U.S. government no longer held title to the funds it provided to the Authority.

The amendments provide that defendants can be held liable for false statements made "to a contractor, grantee, or other recipient, if the money or property is to be spent or used on the Government's behalf" and if the Government has provided the contractor with or will reimburse the contractor for any portion of the funds, and "whether or not the United States has title to the money" at issue.

The amendments also provide broader liability for so-called "reverse" false claims: false statements made to "conceal, avoid, or decrease an obligation to pay or transmit money or property to the Government." Among other changes, a triggering "obligation" can include contingent obligations, such as fixed, unliquidated obligations and contingent, unfixed obligations, and also that defendants can be held liable for knowingly retaining overpayments from the government.

Financial Crisis Inquiry Commission

FERA establishes a ten-member bipartisan Financial Crisis Inquiry Commission to examine both the domestic and global causes of the current U.S. financial and economic crisis. Congress instructed the Commission to examine the causes of the collapse of each major financial institution that failed from August 2007 to April 2009; to submit a report on its findings to Congress; to refer to the U.S. Attorney General and any appropriate State attorney general any person that the Commission finds may have violated U.S. laws in relation to the crisis; and to build upon the work of other entities by reviewing the record of various other agencies and committees with respect to the current financial and economic crisis. The Commission must report its findings to Congress on December 15, 2010.

As part of its broad power to conduct investigations, the Commission is empowered to hold hearings, take testimony, receive evidence, administer oaths, and request documents and information from other United States departments and agencies. The Commission may also issue subpoenas upon a majority vote, which must include at least one vote from a Republican member of the Commission.

Attorneys in the White Collar Defense & Investigations and Financial Institutions practices at Covington have advised and defended a broad range of individuals and companies in criminal prosecutions and investigations, False Claims Act matters and matters involving the Administration's financial rescue efforts.

Attorneys from both practices will be co-hosting a webinar with the American Conference Institute on Thursday, June 4, 2009 covering the False Claims Act and other fraud-related aspects of the recent financial recovery programs. To register please click here.

If you have any questions concerning the material discussed in this client alert, please contact the following members of our White Collar Defense & Investigations and Financial Institutions practice groups:

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