

## ADVISORY | Financial Institutions

January 29, 2013

### FINANCIAL INSTITUTIONS FACE INCREASING EXPOSURE UNDER THE FALSE CLAIMS ACT

On January 25, 2013, PNC Bank agreed to pay the United States government \$7.1 million to settle claims under the False Claims Act (FCA) concerning certain Small Business Administration (SBA) loans made by PNC.<sup>1</sup> This settlement is the latest in a series of recent FCA lawsuits brought by the Justice Department against financial institutions seeking to recover billions of dollars. Because FCA allegations may be brought by any private whistleblower, require intensive investigations, and may result in huge monetary settlements and penalties, this emerging trend has enormous implications for banks and other financial institutions that participate in government-sponsored programs.

#### BACKGROUND

The FCA provides that any person who, in relevant part, (A) “knowingly presents, or causes to be presented” a false claim to the government, or (B) “knowingly makes, uses, or causes to be made or used, a false record or statement material to a false or fraudulent claim” is liable to the U.S. government for a civil penalty of up to \$11,000 per claim as well as treble damages.<sup>2</sup> The Justice Department may file FCA suits directly, or private persons may file FCA suits on behalf of the government and receive 15 to 30 percent of the amount recovered.<sup>3</sup> These private suits, known as “*qui tam*” actions, provide substantial financial incentives for private persons to sue. Unsurprisingly, most successful FCA recoveries begin as *qui tam* actions.

Although the FCA began as an act against false claims submitted to the government, the Justice Department has been using the FCA more broadly and aggressively as a general antifraud statute to recover losses incurred by government programs.<sup>4</sup> Moreover, while the Justice Department previously used the FCA to recover billions of dollars from the health care and pharmaceutical industries,<sup>5</sup> it only recently started using this statute against financial institutions for federal lending programs.

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<sup>1</sup> Press Release, U.S. Dep’t of Justice, Pittsburgh-based Bank to Pay U.S. for Failing to Engage in Prudent Underwriting Practices on SBA Loan Guarantees (Jan. 25, 2013), available at <http://www.justice.gov/opa/pr/2013/January/13-civ-109.html>.

<sup>2</sup> 31 U.S.C. § 3729(a)(1)(A), (B).

<sup>3</sup> See *id.* § 3730.

<sup>4</sup> See, e.g., Press Release, U.S. Dep’t of Justice, Department of Justice Recovers Nearly \$5 Billion in False Claims Act Cases in Fiscal Year 2012 (Dec. 4, 2012), available at <http://www.justice.gov/opa/pr/2012/December/12-ag-1439.html>.

<sup>5</sup> See, e.g., Press Release, U.S. Dep’t of Justice, Department of Justice Recovers \$3 Billion in False Claims Cases in Fiscal Year 2010 (Nov. 22, 2010), available at <http://www.justice.gov/opa/pr/2010/November/10-civ-1335.html>.

## THE PNC SETTLEMENT

PNC issued 64 loans guaranteed by the SBA's Preferred Lender Program in 2005.<sup>6</sup> Since then, 36 of the loans have defaulted, with the SBA paying 75 percent of the balance of the defaulted loans.<sup>7</sup> The Justice Department alleged that PNC's failure to verify unaudited financial statements triggered liability under the FCA.<sup>8</sup>

The PNC settlement is the latest in a series of FCA suits against financial institutions. In 2012, for example, Bank of America settled an FCA suit involving Federal Housing Administration (FHA) residential mortgage loans for \$1 billion,<sup>9</sup> and Deutsche Bank settled a similar suit for \$200 million.<sup>10</sup> In both of these cases, the Justice Department alleged that the banks committed fraud against the government.

As these recent settlements demonstrate, the FCA is an area of increasing exposure for banks and other financial institutions. To a large extent, this trend against lending fraud parallels the trend against health care fraud over the past two decades, and several lessons from the health care industry may be applied to defend financial institutions against increasing FCA liability. Covington has extensive experience representing major pharmaceutical companies in leading FCA cases as well as representing financial institutions in FCA investigations (including with respect to SBA lending). We would be happy to discuss any of these issues with you further.

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<sup>6</sup> See Press Release, U.S. Dep't of Justice, Pittsburgh-based Bank to Pay U.S. for Failing to Engage in Prudent Underwriting Practices on SBA Loan Guarantees (Jan. 25, 2013), *available at* <http://www.justice.gov/opa/pr/2013/January/13-civ-109.html>.

<sup>7</sup> See *id.*

<sup>8</sup> See *id.*

<sup>9</sup> Press Release, U.S. Att'y Office Eastern District of New York, \$1 Billion to be Paid by the Bank of America to the United States; Largest False Claims Act Settlement Relating to Mortgage Fraud (Feb. 9, 2012), *available at* <http://www.justice.gov/usao/nye/pr/2012/2012feb09.html>.

<sup>10</sup> Press Release, U.S. Att'y Office Southern District of New York, Manhattan U.S. Attorney Recovers \$202.3 Million from Deutsche Bank and MortgageIT in Civil Fraud Case Alleging Reckless Mortgage Lending Practices and False Certifications to HUD (May 10, 2012), *available at* <http://www.justice.gov/usao/nys/pressreleases/May12/deutschebankmortgageitsettlement.html>.