

OPINION: Get ready

Avoiding the coming crisis caused by government loans to businesses

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The government forced small businesses to close during the COVID-19 emergency. Then officials claimed they would provide “help” with a loan and vague promises of possible forgiveness. Predictably, small businesses began scrambling to find banks to submit loan applications. The regulations and guidelines were changing daily. The programs were a mess. Now that the dust has settled, the government is investigating small businesses for spending the money that these businesses were basically coerced into taking. This is a collision course given that government bureaucrats work for one of the largest organizations in the world and often do not understand the way small businesses operate. They often have never faced the difficulties of running a business and have unreasonable expectations.

There is a widespread push in many federal agencies to investigate small businesses that borrowed funds from the Small Business Authority and/or the Payroll Protection Program (PPP). Small businesses as well as their owners

now need protection against governmental agencies that have turned against those small businesses they claimed they were trying to help. These investigations are dangerous because they can result in both criminal and civil penalties that can destroy a business and its owners. It is important to keep in mind a number of factors that can make the difference between an investigation becoming a minor inconvenience or a life changing event.

Triggering Factors. An investigation may be triggered by a variety of different factors. They can begin with a complaint from a disgruntled employee, former business partners or a revenge-seeking spouse. They also can be triggered from new reports that business owners have used PPP funds on lavish spending such as vacations and expensive cars. Nothing promises an investigation more than politicians and governmental agencies that become embarrassed by bad press. It is never a good idea to “poke the bear” by engaging in flagrant violations of any governmental program.

Investigations can also be triggered by more subtle indicators. Government agencies often look into suspicious activity reports submitted by financial institutions, such as banks and other lenders, through the Treasury Department. In this scenario, a bank or lender may submit a suspicious activity report flagging impermissible business expenses such as exaggerated payroll, non-essential purchases, or exaggerated market losses. The best way to avoid an investigation is to make sure that PPP or Economic Injury Disaster Loan application documents are accurate and that funds are properly accounted for.

Navigating a PPP or EIDL Loan Investigation. Even if your business has taken all the preventative measures, investigations may be unavoidable. If you or your business is being investigated, you must act quickly because early mistakes can lead to disastrous results. Immediately seek counsel with extensive experience handling such investigations. It is important to communicate with the government only through counsel so that your statements will not be misused by overly zealous bureaucrats.

Furthermore, there are categories of information that must be provided and there is information that is not subject to the jurisdiction of the investigators. The “goldilocks approach” of providing just enough information to be compliant without producing documents that are beyond the scope of the investigation is critical. This is a legal minefield that must be handled with care.

Second, there must be a “litigation hold” to prevent the inadvertent destruction of documents related to your EIDL or PPP loan. The destruction of documents alone can result in civil and criminal penalties.

Third, use your accountants, operations department, financial partners, or payroll specialists to account for the use of PPP or EIDL funds. Most investigations into PPP or EIDL loans focus on expenditures and a solid defense can sometimes be found with proper accounting.

Finally, thoroughly review all documents submitted in support of your loan application for accuracy and be prepared to provide an explanation for any mistakes.

Important Documents to Preserve. It is extremely important to preserve all documents relating to the EIDL or PPP loan. Those documents often contain explanations and defenses that can be used during investigations. For instance, documents that indicate that the business needed loans to support ongoing operations are critical. Likewise, e-mails, letters, text messages or other communications with financial lenders may establish that the business was working in good faith when seeking to procure the loans.

In addition, any records that reflect how the proceeds from the PPP or EIDL fund were spent are critical. Ideally, there will be records demonstrating that the loan proceeds were kept separate from other funds and only used on legitimate expenses. Regardless of whether the



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funds were segregated, records demonstrating that the PPP or EIDL funds were used for proper payroll and other legitimate expenses are essential. Preservation is key.

In short, these investigations are similar to crime show investigations. The targets that “lawyer up” at the beginning of the process, often have better results than those who handle the investigation themselves. Even if your business did nothing wrong, without proper guidance, governmental investigators will find a technicality that was violated. Without protection, it will be easier for the government to target your business.

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