

Fox Rothschild Podcast

The Presumption of Innocence Podcast Series: Episode 1 The Anatomy of a PPP Fraud Investigation

Featuring Matthew Adams of Fox Rothschild LLP and Jessica Hollobaugh, CPA, of Withum

Adams: Hello everyone, and welcome to the inaugural episode of “The Presumption of Innocence,” a new podcast brought to you by the white-collar criminal defense and regulatory compliance practice at Fox Rothschild.

I'm your host today, Matthew Adams, and I am one of the co-chairs of our practice group. I have the great pleasure of being joined by Jessica Hollobaugh, CPA, who is a partner in the forensic evaluation services group at Withum. She also is the market leader of the forensics investigations and white-collar criminal defense practice.

Each episode of “The Presumption of Innocence” will feature a different guest where we will talk about and unpack a hot topic in the world of white-collar criminal and regulatory enforcement.

Today with Ms. Hollobaugh, we are going to discuss the Paycheck Protection Program and fraud enforcement that surrounds it. Let's jump right into it and talk a little bit about the background.

As many of you may know, the CARES Act was originally authorized into law by Congress on March 29, 2020. Among other things, it intended to fend off the impact, financially and economically, from the Covid19 pandemic. The CARES Act authorized the Paycheck Protection Program, which created a \$349 billion fund of forgivable loans that were intended for small business to ensure job retention and other certain expenses to keep businesses afloat during the pandemic, and the related consequences that flowed from it.

That PPP program has expanded dramatically, and there is even a second iteration that was signed into law at the early part of 2021. What has resulted is a significant, significant amount of capital into the economy stimulating, or intended to be stimulating, to small and mid-sized businesses and allow for them to fend off catastrophic failure. What we have come to find with PPP is that it is an area that I would call a target-rich environment for prosecution and regulatory enforcement action because of the inherent amount of fraud that has been brought into the program.

In a way, there is a tremendous overlap between what we do at Fox Rothschild in our white-collar practice and what forensic accountants like Jessica do in her line of work.

Jess, I want to kick the first question to you about really what it is, and what are the most frequent engagements that you have been doing the most of as it relates to PPP over the last year plus.

Hollobaugh: Sure. So, first of all, thank you for having me today. This is very exciting to be part of the first podcast.

As a forensic accountant, I've really been seeing PPP engagements on two ends of the spectrum. The first one being as an expert in the litigation support role. So as you just mentioned, there's been a lot of enforcement activity with respect to the PPP program and some of these first cases were clearly more egregious examples, right? Companies didn't exist or companies that never had employees are now receiving large loan amounts. But what we've been seeing more recently, particularly as borrowers begin to file for forgiveness, is that these investigations have begun to expand a bit more. Those investigations had really started to give rise to the need for forensic accounting support. And the second area there that I've been getting involved with is the earlier stage, what I'll call consultative engagements. So there has been an uptick in enforcement, and as that increase in activity has been more highly publicized, that's really prompted many borrowers to take a step back before applying for forgiveness to ensure that they're in compliance with all the terms of the loan program.

So, in that respect, I've been brought into consult on these matters under Kovel arrangements with various attorneys.

Adams: Great, and you mentioned something that's critically important to our discussion today, and that is to note the nature of a Kovel arrangement. Suffice to say from the outset, this is a critical area where the accountant almost can be brought into the attorney-client privilege in a translation role.

I think it's kind of funny because apparently, the Kovel dynamic is this notion that lawyers are not very good at math. And I think that's probably true.

Kovel really started because of this analogy to a translator. Just like a foreign language speaker cannot essentially communicate with their client without a translator interpreting what's being said, so too can a lawyer not effectively discharge their duties to a client without someone sometimes translating numbers and being able to interpret and trace, and tick and tie if you will, the various numbers that might be associated with the given circumstance, and the provision of legal counsel, legal services, that's associated with it.

Perhaps more so than in any other area – maybe rivaling tax, but more so, than most other areas – this whole idea of PPP investigations is one where that Kovel dynamic is so critically important. So, it's really important to sort of set that forth at the outset, and make sure everybody knows exactly why it is that accountants and lawyers are working so closely together in this particular area. It's also important to just mention from the outset that in the fall of 2020, a congressional subcommittee essentially determined that there was a woeful lack of internal controls associated with the Paycheck Protection Program and from that political argument began the notion that this program was going to be raw with fraud and abuse. From there, it has spawned what I would argue is one of the largest white-collar criminal investigations, or maybe will be the largest white-collar criminal investigation when all is said and done, in U.S. history.

Jess, let's take it a little bit further and maybe unpack a little about the concepts that you just mentioned. You talked about what you were doing with respect to consultative work for your clients, and I think you properly said that a lot of people are hearing about some of the

enforcement activity that's going on. They're getting worried that they might have either received the wrong amount, or that when they make an application for forgiveness, there will be a problem. What, and again against the backdrop of that Kovel relationship that I just described, are the most common types of accounting analysis that you're doing in that consultative type of engagement?

Hollobaugh: Sure, Matt. So like you just mentioned, this is largely borrowers that are coming in and they're now seeking to apply for forgiveness and they have some type of concern with either the amount of the loan that they received, whether it made them miscalculated, or a lot of these borrowers ended up having very good financial years and they're getting to the end of this covered period and they're looking back and want to make sure now that their economic necessity certification can be fully supported.

The two most common types of analyses that I have been handling are, first, the max loan calculations to determine if the loan amount which they received was appropriate. Secondly, we've been coming in and we've been doing some analysis on the projected cash flows, which the borrowers utilize to substantiate their economic necessity at the time of filing.

Adams: So, let's start with that first one, the maximum award calculation. I know you've done a number of those for my clients. What exactly do you do to assess the appropriateness or the accuracy of that maximum or award calculation for a client?

Hollobaugh: That one is fairly straightforward. The PPP loans had a designated formula from which you would calculate the amount of loan that the company was eligible for. So, in very basic terms, that formula is two and a half months of a company's 2019 average payroll cost, and the average payroll cost included gross payroll up to \$100,000 per employee on an annualized basis; the employer's payment of state and local taxes assessed on the wages and employer contributions to group health and retirement plans.

Unfortunately, particularly in the beginning of the program, there was a lot of confusion as to what could, and could not be, included in that payroll number or in that calculation.

That's where we're really seeing a lot of errors, where companies applied for and usually ended up receiving more funds than they were otherwise eligible.

Adams: You mentioned this idea of confusion, and the confusion leading to errors, and I want to be careful and say that an unintentional error is one thing, and then a deliberate fraud is quite another thing. There's a value-add proposition to assessing whether you have either of those circumstances, which we'll discuss in a moment.

Talking through the idea of problems with the max award calculation, and, let's assume that it's an unintentional problem ... what are the most common errors that you're seeing as it relates to the maximum award calculations?

Hollobaugh: The most common error has actually originated from companies relying on PPP reports that were being generated from their payroll company, unfortunately. So more often than not, the borrowers would get these PPP reports and assume they were correct without actually understanding what was being included in the numbers.

I'll give you an example. One of the largest and most well-known payroll providers were originally generating PPP reports that included the employer portion of Social Security and Medicare taxes as an eligible payroll total. And as we just went through before, that's not something that should have been included in the loan amount.

So, in that instance, many of the borrowers actually just relied upon that report that was being generated by their payroll provider and applied for an inflated loan amount.

Along the same lines, I mentioned earlier that the gross payroll calculated loan amount included up to \$100,000 per employee on an annualized basis. What we've seen a lot is that borrowers failed to account for the annualization component with respect to that \$100,000 limit.

So, with that \$100,000 limit, if you had a workforce that was maintained throughout the entire 2019 year, it's a pretty straightforward calculation.

But where we ended up seeing problems with this annualization component is when there was a turnover of a higher paying position.

For example, if you had a CEO who made \$150,000 in the first six months, and ultimately left the company and a replacement CEO was hired, and they made \$150,000 in the second six months, what many of the companies were doing was allowing for \$100,000 per each one of those employees, when it really should have been annualized for the six months that each employee worked.

Adams: Interesting. Let's unpack them the second of the two most common types of analysis that you talked about, which was this cash flow sensitivity analysis. What exactly is that?

Hollobaugh: So that really boils down to the cash flow projections that the borrower relied upon in their economic necessity certification. What we do in those situations is we perform a sensitivity analysis, or it's really a test on the cash flow that they relied upon.

Adams: And how does that test work?

Hollobaugh: The first thing that you need to keep in mind is we are testing these cash flow analyses. Although the borrower could be coming to us months later and may have prospered through Covid, or done better than expected, the projection that they relied upon needs to be assessed as if we were standing back on the date that the loan was applied for.

Generally, the first thing that we'll do is take a look at the borrower's projections that they used, and we want to understand the assumptions that they built into that analysis and their reasoning for why those assumptions were used.

Then what we do from there is we take a look at the historical financial statements. We review the company's operations and take a deeper look at that cash flow projection to perform this sensitivity analysis. What I mean by sensitivity analysis, to put it in simpler terms, is, for example, if the borrower projected that revenues were going to decrease 75%, and by virtue of that 75% decrease, the bottom was going to drop out from underneath this company, and therefore they needed this PPP loan to survive.

What part of our sensitivity analysis would do is fluctuate that percentage, for example, instead of using the 75%. If we assume that the borrower had projected revenues of only 50%, what does the cash flow then look like?

If fluctuating that decrease to 50% resulted in the cash flow model projecting a positive cash position, as opposed to the negative position that was obtained number 75%, we now know that that revenue projection was a critical assumption. What that allows us to do is go back and provide that information to counsel, so that we're sure that we are able to support a reason that the borrower thought the 75% reduction was a reasonable estimate at the time.

Adams: You hit the nail on the head right there when you said, "provide to counsel." That really underpins the importance of the Kovel arrangement, because there are risks and rewards to doing this. The reward is that if everything ties out the appropriate way, you can move forward with confidence. If there is some discrepancy, or there are problems noted in that analysis, the idea that it's protected by the Kovel privilege ensures that it doesn't see the light of day in the event of a public discrepancy, and also allows and affords counsel to operate and productively or proactively guide the client through corrective steps that might very well save them on the back end from a much more expensive and much more risky proposition like civil enforcement action, or in the worst instance, criminal enforcement action.

I think just the two of us have worked on a number of these engagements together, where we found the whole gamut of different types of outcomes when we do those types of max award calculations and cash flow analyses.

I'm thinking of a couple instances where we found clients that were in the seven figures excessive of where they should have been as it relates to a max award calculation. To the same notion, we've seen clients with significant cash flow on hand, but when you do a thorough analysis, with the guidance of the forensic accountant, like yourself, you actually determine that that company's burn rate was such at a high level that even though they might have presented as flushed with cash, on its face, they really didn't necessarily have the wherewithal to survive very long without the influx that the PPP loan provided.

So, I think when you boil it down, the risk and reward of doing this under the protection of Kovel is almost a no brainer.

We've had, I think together, a number of clients that had multimillion-dollar PPP loans where the cost of conducting these types of collaborative exercises between accountant and lawyer under the protections of a Kovel were really worth their weight in gold. Can you talk a little bit about that particular facet ... the value adds of bringing this properly constructed Kovel accounting relationship into the attorney client relationship in these instances? Talk to us a little bit about the cost and the economics of that and how it might play out in real life.

Hollobaugh: Absolutely. So, I have been involved in these cases on both sides of the spectrum: in the consulting engagement, and then later on in the investigations and litigation phase. I can tell you that what I've seen is once these investigations open, they have been very fast moving and they have gotten expensive very, very, quickly.

What the consulting engagements are really allowing us to do is prepare ahead of time for any potential issues so that documentation is accumulated, and proper actions are taken before any potential investigation is underway. I think what we've seen there is that it's really saving the clients a lot of money in that regard.

Adams: I know from working with you, there's a couple of instances where we've actually found other tax credits and the like that were perhaps not initially apparent on their face. Can you speak a little bit to that in terms of what opening the hood and looking kicking the tires, so to speak, does for some of these other programs that might be out there?

Hollobaugh: Sure. So, there are many of the consulting agreements. What we found is that some of these companies were not only eligible for the PPP loan, but they were also eligible for the new credit, the employee retention credit.

This gets a bit tricky because the same wages can't be used for both the PPP loan forgiveness and the ERC credit, but what these consulting engagements have allowed us to do is to get in and assess their eligibility and make sure the companies are maximizing the benefits of both the PPP forgiveness and the ERC credit at the same time.

Adams: Shifting out of that consulting engagement for a moment, I want to start honing in on some of the more adversarial scenarios that we've also encountered in this particular space. There is generally no question that there has been a pretty significant amount of prosecutorial action in this space.

I know we're going to talk about a case study that you've been involved in, in a moment, but I think it bears noting for our audience that really the inherent character of white-collar investigations provides a little bit of an opportunity to push back on the government from the outset. What that means is that maybe unlike a street crime, where there is an event, the police investigated and then there's an arrest, white-collar cases are generally the byproduct of months, if not years-long investigation.

Now, in some instances, these PPP cases have been exceptionally fast to be prosecuted, but the general nature and character of a white-collar investigation does afford some opportunity on the part of a skilled criminal defense lawyer to actually interact with the government and influence charging decisions. That influence could range anywhere from convincing a prosecutor not to pursue charges, to potentially the opportunity to maybe result in lesser charges than may have been on the table at the outset. We've worked on a couple of these matters that have provided us with the opportunity to push back on the government's narrative through what I'll call a tracing exercise. Can you walk us through a little bit about how that plays out in a PPP investigation pre-indictment from the accountant's perspective?

Hollobaugh: Yes. So many of these pre-action investigations have been focused on tracing, and it's essentially on the use of the funds. After the date the borrower received the PPP funds, what the government is looking at is what was the activity in that account thereafter so that they can make a determination as to what the funds were utilized for, and whether they were utilized for the intended purpose.

One of the issues that we're seeing is that many companies utilized more than one bank account. For instance, if PPP funds were deposited into one account, but all the payroll is paid out of another, on its face if you look at just the PPP account, it may look like the funds aren't being used for their intended purpose. But under the theory that cash is fungible, we can actually combine all those accounts into one and provide a tracing analysis, which can show different results.

Alternatively, I have done these forensic analyses, and it hasn't provided the results we would hope it would. In some of those cases, there may be the opportunity to maybe go in with a different vision. So maybe instead of focusing on this direct tracing during this phase, we instead go in and demonstrate that during the 24-week period, the borrower expended forgivable payroll amounts in excess of the loan amount.

I think it's just important to understand from the onset what the actual tracing is and what the results of that tracing are.

Adams: I agree. I would agree entirely that tracing analysis is critically important to trying to influence pre-indictment, that is: influence charging decisions and try to reset the narrative of a prosecutor.

Now, a lot has been made in connection with PPP about economic necessity. I would say that this is one of those big and amorphous terms that is employed through the CARES Act, and one of the certifications in the application for PPP. Quite frankly, it is an ill-defined concept that is somewhat objective, but mixed in with somewhat of some subjective criteria if you look at things like the 3509, which was promulgated by the SBA as part of the forgiveness program, and is now falling out of this favor after it's been challenged.

But when push comes to shove, Jess, I think that there are real problems for the government in making a criminal case out of economic necessity because of all of the vagaries that surround it. At the same token, economic necessity is such a vital portion of the real purpose behind PPP in the first instance, and really is the bellwether prerequisite for qualifying for the program. Unto itself, I think much of what starts these investigations really arises from this perception or narrative by the government that companies sometimes got loans that they shouldn't have necessarily received just because they're trying to maximize on the receipt of free money.

That very well might be the case in certain instances. But in many instances, economic necessity, when you peel back the layers of the onion, will reveal all kinds of things that might not be exactly visible on the surface. I mentioned one a short while ago as it pertained to cash flow and the idea that yes, a company might have many millions of dollars on their books, but when you examine their expense activity, that could easily be depleted in a very short space of time due to the fact that their expense activity is just so high.

What are ways that, from use of this Kovel forensic accounting analysis, you can help lawyers like me push back on the false narrative that a company didn't really need the money, but they just wanted to maximize the opportunity to get free money from the government?

Hollobaugh: I think that narrative, like you mentioned, really begins largely with companies that may have a large cash on-hand sitting on their balance sheet.

It's important to note the cash on-hand, certainly, isn't the end all-be all. It's an easy number for the government to obtain. It sits flatly on the face of the bank statement. I'm sure it's something that they're going to take a look at, but there's definitely legitimate arguments to be made about the need to preserve that cash for operations going forward.

One of those arguments is just your basic working capital argument. Historically, if the company has maintained cash in order to fund its operations, it's fairly clear that the cash is needed to be maintained on a going-forward basis. COVID hasn't changed that. In fact, it probably made it worse.

Some of the other arguments can be much more specific to the company. I can give you an example: one being professional service companies. Going into COVID, many of these service companies were deemed to be essential, but they had valid concerns that the individuals or the companies that owed them money – their receivables – were going to be impacted by slow payment. But those service companies still had a fixed-cost structure. They still pay salaries. They still have to pay rent, equipment, leases and loan payments. So, even though they may have been considered essential and are continuing to operate, there was a cash burn rate that was embedded into their projections, where this extra cash was going to be needed to keep the entity afloat during this period of uncertainty.

Some of the other arguments that have come across are much more company or industry specific. One company that I came across operated in commodities and really needed to maintain cash to consider fluctuations in prices.

I had another company that experienced supply chain issues, so they were being forced to split their purchases between various vendors. In that instance, we were able to support their need for additional cash because there was going to be this uncertainty and the changes in their cost along with shorter payment terms that were going to be required.

I think there's certainly a lot of arguments to be made with respect to economic necessity.

Adams: I can think of a couple of examples as well, in terms of where we're analyzing cash flow and the idea of potentially a line of credit is considered, and whether or not that was appropriately drawn down before going to the well, so to speak.

In a couple of instances, the need to preserve that line of credit was really an industry-specific thing. You mentioned the commodities in terms of the line of credit, being a protection against overnight fluctuations in that commodity. During the pandemic, we certainly saw market forces at play, causing dramatic ebbs and flows and fluctuations in certain commodity prices, from oil to other things, that really need to be considered on an industry-by-industry basis.

Now let's shift out of that pre-action investigation role and get right down to it. Assume all bets are off, and you mentioned that you're working in the sort of litigation support role. You know, I think you'll agree with me at that point in time, all efforts have essentially either failed at the intervening from an outset, or they failed to capitalize on the opportunity to do this consultative kind of engagement. Or they just couldn't do it quick enough and the government beat them to the punch.

There are literally at this point hundreds, if not thousands, of cases where PPP fraud has been prosecuted, and there are criminal actions that are filed against borrowers for failure to do any number of things appropriately as it relates to this program. I mentioned at the outset, there was this sort of target-rich environment. I use that phrase a lot when referring to PPP, because the way that the program was administered, it invoked literally dozens and dozens of federal criminal statutes: from a false statement to a bank, to simple lying to a federal investigator who might be coming to conduct an audit, from something that eliminated out of a SAR report or other compulsory financial reporting that banks are required to do.

This whole area is just exploding right now, and it's a good opportunity for me to give a little bit of a plug to something that Fox Rothschild is doing. We have a what we're calling our Fraud Prosecution Tracker - where we are in real time tracking the number of new filings associated with the whole array of COVID-19 stimulus-related cases throughout the United States.

We're tracking those in real time, and we're making those available to the public. If you'd like to subscribe to our Fraud Prosecution Tracker, please send me an email at madams@foxrothschild.com, and I'd be happy to have our team add you so that you can get real time updates on this very emerging area of the law. You can start to see some of the trends that arise from where the government is sinking its resources.

Jess, I know that you happen to be in a prime litigation support role in one of the, if not the, first case to go to criminal trial related to fraud in the United States, and that is the *Crowther* case in the Middle District of Florida. I'd like to talk to you about that, but I'll make it known that I'm only going to ask you questions that speak to things that were revealed during the public trial. I don't want you to reveal any confidences, and I know you wouldn't anyway, but I want to make that known to our audience that I'm only asking questions about things that went on and the observations from trial.

So, Jess, I understand that during the *Crowther* case at trial, an SBA expert testified. What were the highlights of that testimony?

Hollobaugh: So, we've been talking a lot about economic necessity today, and actually one of the key takeaways from the *Crowther* trial was that the government's SBA expert did come in and testify specifically to what economic necessity was. His testimony was very much what we've been speaking about today: the certification was in the eyes of the borrower as of the date of the application.

Matt, I'm sure you can explain a bit more about why that's important in terms of future enforcement, but what we did see in the *Crowther* case was that the government didn't necessarily put on a case directed at economic necessity, but they did use economic necessity kind of as a backdrop to their other arguments.

Adams: I can tell you that it's going to be very difficult to make a fraud case rooted entirely about economic necessity, simply because the essence of a fraud is the intent to defraud, and that scienter or mens rea or culpable mental state, if you will, is required to be proved by, or beyond a reasonable doubt by, the government.

And in light of testimony like that – that it's in the eyes of the borrower, which is really a subjective kind of approach – it's very difficult to make out that level of proof.

It also ... you also pointed to something very important though. I think that these cases are colored by the government's narratives either for or against economic necessity.

So, while a case might not be entirely predicated upon economic necessity, I certainly think that as it relates to triable issues now, we're talking about we've left the consultative, we failed or didn't get there in time to sort of convince the government otherwise in the pre-action phase, and now we are at trial.

I think there's a lot of jury appeal to the government trying to say things like, wow, look at this cash-lush company coming in here trying to borrow your money. Did you hear a lot of things like that at the trial? Your money, your money, taxpayer dollars, things of that nature?

Hollobaugh: We heard a lot of that - taxpayer dollars, who's going to be forced to pay this? It's going to be the taxpayers that will pay it. So, that was definitely the backdrop of their narrative.

Adams: From a defense perspective, to preserve that presumption of innocence, you really do need to be able to beat back that narrative. So, while I don't think it can form the basis for a standalone criminal prosecution, it can't be ignored.

Now, did anyone from the bank testify at trial during the *Crowther* case?

Hollobaugh: So, similar to the government's SBA expert, they did have the government did put on a representative from the bank. It was pretty interesting, because the bank representative took the stand and testified clearly that the bank was not injured and did not feel that they were a victim of the loan.

Adams: Did they articulate why?

Hollobaugh: Because it was a performing loan, and they had not lost any money on it.

Adams: And assumedly then this prosecution occurred before forgiveness, correct?

Hollobaugh: Correct.

Adams: Anything else about tracing that came up during the trial? We've talked a little bit about that today. And if we're going to use your experience with at least the publicly available aspects of the *Crowther* trial, did anything touching on tracing come up that we can learn from?

Hollobaugh: Absolutely. So, the government argued in the case that the PPP funds were deposited into a segregated account, not into the company's general operating account.

And then the government presented to the jury a snapshot of just that one segregated account, which included a transfer to a marina after the receipt of the PPP funds.

So, in that presentation, what the government was arguing was that the \$700,000 transferred to the marina was a boat purchase that came directly from PPP funds. And Crowther's attorneys argued the opposite.

They argued that the government's presentation failed to account for this fungibility of cash, and that forgivable expenses had already been paid out of the operating account during that 10-day period. So, it wasn't correct to just look at that segregated account.

Ultimately, the jury convicted Crowther, and one of those charges was specifically for an illegal monetary transaction related to that \$700,000. But I think the importance here is that it really shed some light on the direction that the government may go in some of these investigations, which, in this instance, was performing a direct tracing of proceeds instead of stepping back and taking that broader look at the overall 24-week period to see if forgivable expenses were expended in that 24-week period.

Adams: I think as a proactive step, that kind of highlights something I've been telling clients since this whole thing began, which is segregate, segregate, segregate that money and put it in a separate account.

And in that instance, it's pretty remarkable that, notwithstanding segregating the money, the government just did the direct tracing and suggested to heck with whatever else you've got in your bank accounts and ignored this idea of fungibility. I think there's some issues that are probably ripe for appeal, and we're going to learn even more about this subject as this case unfolds. Certainly, it's one worth watching.

Because, as I understand, it is probably the first case that went to trial and there's been a couple more since. But at least from some of the precedential value of what I understand to be an appeal process that may very well follow, we'll be watching closely as some of these issues get flushed out, because I think for the jury to have ignored that fungibility issue, it may present some opportunities on the appeal.

Let's move then to some of your observations from sentencing, because as you mentioned Mr. Crowther unfortunately was convicted and, as I understand it, you actually testified during his sentencing. What was the nature of your testimony? Again, we're focusing on what went on in a public forum and during that proceeding, not anything that was related to work you did for the defense in any other capacity.

Hollobaugh: So, in very, very simple terms, I testified that during the 24-week covered period of the PPP loan, the business paid \$3.5 million of expenses that were eligible for forgiveness under the guidelines, and this was in stark contrast to a loan of only \$2.1 million. So, what we were showing is that not only did the company over this 24-week period maintain its payroll, which was the intent of the program, but they actually paid \$1.4 million more in these eligible forgivable expenses than would've been needed to qualify for full forgiveness of the loan.

Adams: Why was your focus on forgivable expenses?

Hollobaugh: So, with respect to the loss amounts for sentencing, the government was arguing that the full amount of the loan - all \$2.1 million - should be considered as the loss amount.

The purpose of my testimony was really to show that the loan was used for its intended purpose, and, in fact, was used beyond the amount required. And therefore, the argument was, there was no loss.

Adams: So, bottom line is, you were saying that there was cash on hand, plus the PPP funds, and when you subtracted the forgivable expenses, there was enough forgivable expenses to consume the entirety of that pot of money, regardless of where it came from? Am I correctly understanding that?

Hollobaugh: Correct. Not only cash on hand, there was availability from a line of credit and other things, but ultimately what we were doing is taking a step back and saying instead of looking at this on a day-by-day basis, let's look at the 24-week covered period because the forgiveness application does not require you to outline the exact expenses that were incurred every day. It just requires you to provide the total forgivable expenses that were expended during the 24 weeks.

So, that's what we did. We took that step back and we looked at what was expended during that full 24-week period.

Adams: Well, it sounds to me like you guys took an approach to sentencing that is reasonable, given the fungibility of money. I suspect that we might even hear from an appellate court later about some of the appropriateness of the right calculation, as they view it on how loss should be described to the defendant for purposes of sentencing.

Just so our audiences are aware, under Section 2B1.1 of the federal sentencing guidelines, the loss really drives that sentence, because while there are some others in nature and characteristics of the offender and nature and characteristics of the offense, that drive the federal sentencing guidelines – the primary driver of those guidelines in a fraud case, under 2B1.1 and the loss tables that are found there – really are the losses. That cuts directly to the amount of jail that a particular defendant sees when they get convicted of one of these offenses related to fraud or abuse.

What ultimately did the judge decide, Jess, as it relates to sentencing?

Hollobaugh: So, he ultimately determined the loss amount was the total of three identified payments that were made during the covered period, which the government had argued were disallowed under the program: one of which being a purchase of a boat, another being a payment on a loan to a former business partner, and the third being a principal payment on the business line of credit.

Adams: So that's pretty remarkable. The judge neither bought your argument – the defense argument – nor bought the government's argument that the entirety of the loan was the appropriate loss. Am I reading that correctly?

Hollobaugh: Correct.

Adams: Wow. I think we're likely to see some more on that from an appellant court down the line.



Well, Jess, I can't thank you enough for joining us today on this, our first-ever episode of The Presumption of Innocence podcast, and I look forward to the possibility of revisiting the subject as things in this case and the practice that you're engaged in as it relates to PPP fraud and abuse play out in the future.

I want to just once again reiterate that the Fox Rothschild PPP Fraud Prosecution Tracker is available for our listeners. Please shoot me an email at madams@foxrothschild.com and I'll make sure that we get you signed up for that.

That's all the time we have for today. We thank you a lot for joining us and look forward to the possibility of you joining us again for future editions of The Presumption of Innocence, where we will unpack, dissect and discuss the hottest topics in white-collar criminal defense and regulatory compliance.

I am Matt Adams, one of the co-chairs of the practice, and I would like to thank you for joining us. We'll see you next time.