

COVID-19: PLANNING FOR WAVE OF CARES ACT ENFORCEMENT FOR AVIATION INDUSTRY

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As detailed in prior alerts,¹ the Coronavirus Aid, Relief, and Economic Security Act of 2020 (the “CARES Act” or the “Act”) provides, among other things, financial assistance to the aviation industry through payroll support² (the “Payroll Support Program”) and through loans and loan guarantees³ (the “Loan Program”).⁴ Although such assistance is welcome in the wake of unprecedented losses, with ramped up rhetoric regarding “severe consequences” and possible “criminal liability”⁵ for false certifications related to the Act’s loan programs, it is imperative that the aviation industry proceed with caution when receiving funds.

WAVE OF ENFORCEMENT ACTIONS LIKELY COMING THROUGH CERTIFICATIONS

Potential Pitfall: Ongoing Compliance with Certifications

Application for and receipt of financial assistance does not come without risks, as evidenced by negotiations around the Payroll Support Program and ongoing confusion around the Act’s Payroll Protection Program. Since broad discretion is granted to the Secretary of the Treasury, the Department of the Treasury (“Treasury”) can enforce its positions, likely through breach of the terms of any agreements or upon evidence that the original certifications were fraudulent.

Thus, it is critical for passenger and cargo air carriers and related contractors (“Permitted Aviation Borrowers”) to understand the terms of undertaken Payroll Support and/or Loan Program agreements and to engage in ongoing compliance with respect to all certifications. Similarly, lenders and lessors need to understand the restrictions in order to best protect assets currently operated by Permitted Aviation Borrowers.

Indeed, the Payroll Support Program calls for certain “required assurances” to be eligible for support. Every recipient will be required to sign a Payroll Support Agreement (“PSA”) agreeing to comply with certain restrictions on staffing and pay cuts, stock buy-backs and dividend distribution, compensation exceeding \$425,000, and continuation of service requirements.⁶ The form PSA also requires:

- Acknowledgment that materially false statements or omissions may result in penalties;
- Submission of periodic reports to Treasury certifying compliance; notification to Treasury and the Office of the Treasury Inspector General (“Treasury Inspector General”) of facts materially affecting compliance or of indications of fraud, waste, abuse, or potential criminal activity; and compliance with requests for information;
- Maintenance of funds in an account over which Treasury has a security interest;

- Establishment of effective internal controls around compliance with the PSA;
- Retention of all records related to receipt of funds, compliance with the PSA, and substantiation of the application, including by suspending automatic deletion functions;
- Protection of whistleblowers;
- Representation and warranty that the PSA was duly authorized and will not result in violation of any applicable law or constitute an event of default under any material contract the Permitted Aviation Borrower is a party; and
- Completion of a certification requiring, among other things, affirmation that information and certifications provided with the application were true and accurate.

While Treasury has not released a form agreement for the Loan Program, the program imposes similar restrictions on staffing and pay cuts, stock buy-backs and dividend distribution, and certain compensation levels. Per the terms of the Act, the Loan Program also requires Permitted Aviation Borrowers to demonstrate: (1) credit “is not reasonably available” elsewhere; (2) the loan is “prudently incurred”; (3) it incurred or is expected to incur covered losses jeopardizing continued operations; and (4) it is a U.S. business. As with the Payroll Support Program, Permitted Aviation Borrowers must certify the applications are true and correct. Permitted Aviation Borrowers will also likely be limited in their ability to incur additional debt obligations without consent and may need to give certain operation concessions.

SIGPR: Means of Monitoring and Investigating Compliance

To ensure Permitted Aviation Borrowers are complying with program terms, Congress created the Office of the Special Inspector General for Pandemic Recovery (“SIGPR”) with broad authority to conduct, supervise, and coordinate audits and investigations related to the CARES Act loan programs for a period of five years and with a budget of \$25 million. Similarly, Congress tasked the Treasury Inspector General with auditing Payroll Support Program awardable amount certifications. Permitted Aviation Borrowers should expect that SIGPR will follow in the footsteps of the Office of the Special Inspector General for the Troubled Asset Relief Program (“SIGTARP”). Established after the 2008 financial crisis, SIGTARP-supported investigations have resulted in 381 convictions and recovery of \$11 billion.⁷ For detailed examination of SIGTARP as a precursor of enforcement actions to come, review our analysis [here](#).

BEST PRACTICES TO PREPARE FOR COMING WAVE OF ENFORCEMENT

It is imperative that Permitted Aviation Borrowers proceed with caution, understanding that oversight, investigations, and scrutiny may be coming from SIGPR, the U.S. Department of Justice (“DOJ”), and other regulators. Permitted Aviation Borrowers can prepare by:

- Leveraging legal expertise. Permitted Aviation Borrowers must stay up to date on the latest guidance from Treasury and how that guidance may impact certifications. Permitted Aviation Borrowers should consult with in-house and external counsel early and often to ensure compliance with the spirit and letter of the law.
- Ensuring oversight by the Board of Directors and senior management. Applications,⁸ ongoing diligence requests, and periodic reporting are material matters that should involve senior management preparing,

evaluating, and reviewing information submitted on behalf of a Permitted Aviation Borrower. The Board of Directors should be apprised of and sign off on any certifications and should not rubber-stamp the materials prepared by senior management.

- Appoint a point of contact for Treasury and SIGPR. A Permitted Aviation Borrower should consider designating one individual as the point of contact for Treasury and SIGPR so that the Permitted Aviation Borrower remains fully apprised of all contact from those entities and is able to quickly and efficiently marshal resources to respond to requests for information or any other inquiries.
- Preserve an accurate document record. Per the terms of its PSA, a Permitted Aviation Borrower must maintain documentation demonstrating why it applied for the Payroll Support Program, as well as any and all documentary support for the application, certifications, and compliance with agreement conditions. Permitted Aviation Borrowers applying to the Loan Program should take the same steps.
- Maintain funds in a separate account. Per the terms of its PSA, a Permitted Aviation Borrower must maintain Payroll Support Program funds in a separate account. Permitted Aviation Borrowers should also consider maintaining any Loan Program funds in a separate account in order to easily track such funds and quickly and efficiently address any inquiries from Treasury or SIGPR.
- Implement an effective whistleblower program. A Permitted Aviation Borrower should ensure that it has an effective whistleblower program and that its employees are aware of the program. Through an effective program, a Permitted Aviation Borrower can take steps to address allegations of fraud—and document those steps—before an inquiry is initiated by SIGPR or a qui tam action is brought by a private litigant.
- Monitor ongoing compliance with funding requirements. Permitted Aviation Borrowers should establish internal audit procedures to ensure compliance with evolving conditions and expectations. Permitted Aviation Borrowers should also establish reporting structures, such that key audit issues are shared internally while still preserving potential attorney-client privilege and attorney work product protections.
- Lenders and lessors. Lenders and lessors should reach out to air carriers to ensure existing loan and lease documentation are not in technical default by reason of entering into a loan agreement or PSA. Limited conditional waivers can be conditioned on compliance with new financial covenants or default sections and can further require the air carriers to take all reasonable actions to avoid having payroll support grants being involuntarily recast as loans. Moreover, notice provisions relating specifically to any enforcement action by Treasury and SIGPR should be required.

FOOTNOTES

¹ This is the fifth installment in a series that delves into possible government enforcement efforts related to the CARES Act and that identifies best practices for companies in the wake of the nation's largest emergency relief package. To learn more, please see [“COVID-19: Looming False Claims Act Liability for Paycheck Protection Program Loans,”](#) [“COVID-19: Congressional Investigations and Pandemic Relief Oversight Mechanisms,”](#) [“COVID-19: Federal Stimulus Today, Federal Investigation Tomorrow: What TARP Can Tell Us about the Coming Wave of CARES Act Enforcement,”](#) and [“COVID-19: Labs Beware! – EKRA Expands DOJ's Enforcement Arsenal](#)

[in the COVID-19 Fraud Battle.”](#)

² Subtitle B in Title IV of the CARES Act allocates funds for the continued payment of employee wages, salaries, and benefits, with up to \$25 billion allocated to passenger air carriers, \$4 billion to cargo air carriers, and \$3 billion to contractors—a group which is narrowly defined. Demand for the Payroll Support Program has been so high that we understand that for passenger air carriers, in agreements over \$100 million, thirty percent of the funds must be repaid as low-interest loans and that the carrier must issue stock warrants equal to ten percent of the value of the loan. Cargo air carriers receiving more than \$50 million and contractors receiving more than \$37.5 million will also be required to issue financial instruments to the government.

³ Subtitle A in Title IV of the CARES Act allocated funds for loans and loan guarantees to provide liquidity related to losses incurred as a result of the COVID-19 pandemic. The Act allocates up to \$25 billion for passenger air carriers, Part-145 certified repair station operators, and ticket agents; \$4 billion for cargo air carriers; and \$17 billion for businesses critical to maintaining national security. No Loan Program agreements have been finalized; however, many airlines have been advised of the amount of loans to be provided, and negotiations are ongoing.

⁴ This is the third installment in a series focusing on the CARES Act and stimulus funding available to the aviation industry. To learn more, please see [“COVID-19: UPDATED The Promise of the “CARES Act” on the Airline Industry”](#) and [“COVID-19: Air Carrier Work Support under the CARES Act.”](#)

⁵ See Mario Parker, [Trump Says He'll Ask Bigger Companies to Return Emergency Loans](#), WASH. POST (Apr. 22, 2020, 4:22 AM), (threatening “severe consequences” for big companies that take money intended to help small businesses); Paul Kiernan, [Mnuchin Says Big Companies Should Apologize for Taking Small Business Loans](#), WALL ST. J. (Apr. 28, 2020, 3:37 PM).

⁶ Dep't of Treasury, [Form Payroll Support Agreement](#). The PSA may also contain individualized terms and conditions.

⁷ Letter from the Special Inspector General, SIGTARP's Quarterly Report, at 2 (Oct. 1, 2019 – Dec. 31, 2019), [available here](#).

⁸ Applications for the Payroll Support Program were due on April 3, 2020. Applications for passenger and cargo carriers for the Loan Program were due on April 30, 2020, though Treasury may consider, in its discretion and subject to availability of funds, applications received after that date. Applications for businesses critical to maintaining national security were due on May 1, 2020, though Treasury may, in its discretion and subject to the availability of funds, consider applications received after that date.

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