

Inside The First Paycheck Protection Program Fraud Charges

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Within the span of eight days, the U.S. Department of Justice filed three criminal actions against three individuals for alleged schemes to defraud the Paycheck Protection Program established by the Coronavirus Aid, Relief, and Economic Security, or CARES, Act.[1]

The three named defendants are the first individuals in the country to be charged criminally in connection with schemes to defraud the PPP. These criminal charges send a strong message about the rigor with which the government will proceed in order to root out abuse of the CARES Act relief programs and to bring those responsible to justice.

The cases also serve to demonstrate some of the circumstances under which the government will pursue criminal charges based on alleged fraud in connection with the PPP and as a reminder of the importance of implementing strong compliance measures.

The first set of criminal charges were filed on May 4 against David A. Staveley (aka Kurt D. Sanborn) and David Butziger for allegedly engaging in fraudulent schemes to obtain PPP loans guaranteed by the Small Business Administration.[2]

Both defendants are charged with conspiracy to commit bank fraud and conspiracy to make false statements to influence the SBA in violation of U.S. Code Title 18 Sections 1349 and 371, respectively. In addition, Butziger is charged with bank fraud in violation of U.S. Code Title 18 Section 1344(2), and Staveley is charged with aggravated identity theft in violation of U.S. Code Title 18 Section 1028A, stemming from his alleged use of his brother's identity in connection with, among other things, applying for PPP loans.

According to the government's allegations, the defendants claimed to have dozens of employees earning wages at four different businesses. They sought more than \$500,000 in bank loans under the PPP (\$438,500 by Staveley and \$105,381 by Butziger) to pay their purported employees due to the economic downturn caused by COVID-19. However, according to the DOJ's press release, three of the businesses allegedly were not operating prior to the COVID-19 pandemic and had no salaried employees, and the fourth business was not owned by the loan applicant.

The affidavit submitted by a special agent of the Federal Bureau of Investigation in support of the criminal complaints against Butziger and Staveley reveals that a complaining witness initially brought suspicions of COVID-19 relief fraud by Staveley to the local police. The investigation that ensued included a search warrant relating to three email accounts tied to Staveley to obtain the defendants' emails, the use of an undercover agent posing as a bank compliance officer, and law enforcement interviews of certain people whom defendants claimed to employ.

Through these aggressive investigative tactics, the government obtained email correspondence between the defendants about their plan to create fraudulent loan applications and supporting documents; corroborating witness information regarding the absence of salaried employees; and verbal statements made by the defendants directly to undercover agents, including one defendant's statement to the undercover agent that he was seeking PPP bank loans to pay employees of a business that the government determined had no employees.

For example, in one email exchange, Butziger wrote to Staveley, "I can create a bull shit 2020q1 for [one business] if you want." Staveley responded, "We are going to need the same stuff for [that business] and [another business]. However we dream that up."

During a recorded conversation with an FBI special agent posing as a bank compliance officer, an individual believed to be Staveley told the undercover special agent that he owned three restaurants, employing roughly 25 employees at each location, and that he had paid all the employees until the end of March, when he was forced to furlough them. In what was characterized by the government as "an ironic twist," the individual believed to be Staveley "complained about the reports of large businesses being able to obtain SBA loans under the Paycheck Protection Program, saying that 'the whole thing has become a little bit of a sham.'"

Eight days later, on May 12, the government filed criminal charges against Shashank Rai for allegedly submitting fraudulent bank loan applications to two different lenders, seeking a total of more than \$10 million in PPP loans.[3] Rai was charged with wire fraud in violation of U.S. Code Title 18 Section 1343, bank fraud in violation of U.S. Code Title 18 Section 1344, making false statements to a financial institution in violation of U.S. Code Title 18 Section 1014, and making false statements to the SBA in violation of U.S. Code Title 15 Section 645(a).

According to the government, in one loan application seeking \$10 million, Rai fraudulently claimed to have 250 employees with an average monthly payroll of \$4 million; and in the other loan application seeking approximately \$3 million, Rai fraudulently claimed to have 250 employees with an average monthly payroll of roughly \$1.2 million. Texas agencies, however, had no record of revenues or payment of employee wages in 2020 by Rai or his purported business, Rai Family LLC.

The government also found handwritten notes in the trash outside Rai's residence that appear to describe an investment strategy based on a \$3 million investment — the same amount of money that Rai allegedly sought as a PPP loan from the second lender.

The allegations in these cases suggest that the government found relatively egregious facts believed to be consistent with an intent to defraud rising to the level of criminal culpability. Such facts stand in stark contrast to situations in which PPP applicants try in good faith to comply with program requirements, but unintentionally or unknowingly make a false statement without any intent to defraud, such as where an eligibility requirement may be vague or ambiguous and/or the subject of evolving guidance.

Nonetheless, these cases are important reminders of the need to implement appropriate procedures to ensure compliance with all applicable government program requirements. Specifically, all those seeking to secure funding under the CARES Act should carefully analyze all eligibility requirements and document the bases for the determinations that such requirements have been met before applying for funding.

In particular, applicants for PPP loans should identify, carefully consider, and document the specific bases for the applicant's determination and related certification that "[c]urrent economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant," which has been the subject of evolving SBA guidance.[4]

Further, controls should be implemented to ensure that funds received under the CARES Act are utilized as required under the relevant program and that any necessary reporting requirements are in place. In addition to the many statements, task forces, oversight committees, and other law enforcement initiatives demonstrating the government's commitment to investigate and prosecute those who seek to abuse the various COVID-19-related relief programs, the SBA recently announced that it will individually review every PPP loan greater than \$2 million once the application for loan forgiveness is received. Accordingly, it is critical that all those seeking to participate in the PPP and other relief programs have appropriate compliance procedures in place in order to be able to respond fully and effectively to any and all government inquiries that may be made.

Of course, the government's charges against Butziger, Staveley and Rai are merely allegations and any defenses that may be asserted by defendants have not yet been made public. But, the swift and aggressive investigations and filing of criminal complaints in these cases serve as a forceful message of deterrence against those who may seek to defraud CARES Act relief programs.

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[1] The three criminal cases are United States v. Butziger, No. 20-mj-33 (D.R.I. May 4, 2020), United States v. Staveley, No. 20-mj-34 (D.R.I. May 4, 2020), and United States v. Rai, No. 20-mj-95 (E.D. Tex. May 12, 2020).

[2] See U.S. Dep't of Justice, Two Charged in Rhode Island with Stimulus Fraud, dated May 5, 2020, available at <https://www.justice.gov/opa/pr/two-charged-rhode-island-stimulus-fraud>.

[3] See United States v. Rai, No. 20-mj-95 (E.D. Tex. May 12, 2020); U.S. Dep't of Justice, Engineer Charged in Texas with COVID-Relief Fraud: Texas Engineer Fraudulently Sought More than \$10 Million in CARES Act SBA Paycheck Protection Loans, dated May 13, 2020, available at <https://www.justice.gov/opa/pr/engineer-charged-texas-covid-relief-fraud>.

[4] On May 13, 2020, the SBA issued additional guidance on the referenced necessity certification requirement and further delineated the circumstances under which borrowers would be deemed by the SBA to have made the certification in good faith and the circumstances under which the SBA would decline to take administrative enforcement action or make a referral to other enforcement agencies. See Question #46, Paycheck Protection Program Loans: Frequently Asked Questions (FAQs), dated May 13, 2020, available at <https://home.treasury.gov/system/files/136/Paycheck-Protection-Program-Frequently-Asked-Questions.pdf>. It should be noted, however, that this additional guidance does not shield a borrower from investigation by law enforcement or an action by the government or a whistleblower where it is determined that the borrower engaged in conduct in violation of law, such as the knowing and intentional submission of a material false statement in connection with the PPP.

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