

Client Alert

Financial Markets Developments

President Barack Obama Signs Legislation Amending the False Claims Act ("FCA") and Creating the Financial Crisis Inquiry Commission. Although Introduced to Combat Fraud in Connection with Federal Assistance Fraud in the Current Economic Crisis, the Legislation Will Impact False Claims Act Litigation Generally and Will Greatly Expand Federal Enforcement Resources Resulting in a Substantial Increase in Enforcement Activity.

On May 20, President Obama signed into law the Fraud Enforcement and Recovery Act of 2009 ("FERA"). At the signing of the bill, President Obama stated:

[This bill] allows DOJ to prosecute anyone who fraudulently obtains Recovery Act or TARP funds—precious taxpayer dollars we've carefully invested in order to turn this crisis around. And... it creates a bipartisan financial markets commission to investigate the financial practices that brought us to this point, so that we make sure a crisis like this never happens again.

Senators Charles Grassley (R-IA) and Patrick Leahy (D-VT) introduced FERA to provide additional funding for prosecutors and investigators and to amend numerous statutes, including the FCA, for the purpose of prosecuting financial fraud and criminalizing the misuse of federal assistance under the Troubled Asset Relief Program ("TARP"). When he introduced FERA in the Senate, Senator Leahy explained that:

The False Claims Act must quickly be corrected and clarified in order to protect from fraud the Federal assistance and relief funds expended in response to our current economic crisis.

In addition to amending the FCA and providing more funding for enforcement authorities, FERA creates the Financial Crisis Inquiry Commission, whose purpose is "to examine the causes, domestic and global, of the current financial and economic crisis." FERA also modifies several criminal statutes to address perceived abuses of TARP funds.

FERA Authorizes Over US\$500 Million for Fraud Prosecutions

FERA provides additional funding in 2010 and 2011 to enforcement authorities focused on increasing criminal prosecutions and civil administrative proceedings to combat mortgage fraud, securities and commodities fraud, and federal economic assistance fraud. The funding includes **US\$330 million for the Department of Justice ("DOJ")**, **US\$40 million for the Securities and Exchange Commission ("SEC")**, and an additional US\$160 million for other agencies, including the Postal Inspection Service, Department of Housing and Urban Development, and Secret Service. The additional funding is expected to result in **200 more DOJ prosecutors and 300 more FBI agents**.



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If you have questions or comments regarding this Alert, please contact one of the lawyers listed below:

George J. Terwilliger III
Partner
+ 1 202 626 3600
gterwilliger@whitecase.com

Darryl S. Lew
Partner
+ 1 202 626 3674
dlew@whitecase.com

Daniel B. Levin
Partner
+ 1 202 626 3634
dlevin@whitecase.com

White & Case LLP
701 Thirteenth Street, NW
Washington, DC
20005-3807
United States
+ 1 202 626 3600

www.whitecase.com

FERA Overturns Recent Federal Court Caselaw by Broadly Defining a Viable “Claim” in a Qui Tam Whistleblower Action

FERA significantly amends the FCA. Specifically, the FERA defines a “claim” subject to the FCA as:

*[A]ny request or demand... for money or property and **whether or not the United States has title to the money or property, that is presented to an officer, employee, or agent of the United States; or is made to a contractor, grantee, or other recipient...** if the United States Government provides or has provided any portion of the money or property requested or demanded; or will reimburse such contractor, grantee, or other recipient for any portion of the money or property...*

The emphasized text overrules several recent court decisions that limited claims that can be the basis for qui tam actions to:

- Claims directly presented to the federal government, not contractors or grantees
- Claims concerning funds belonging to the United States, not third party funds administered or controlled by the federal government.

This new definition—which is not limited to FCA claims related to recovery funds received in the current financial crisis—significantly **increases the scope of federal activity on which relators can bring qui tam actions**. The overruled cases had limited the scope of the FCA and reduced the liability for companies involved in government contracts. The amendments will impact all potential FCA defendants, not only companies receiving federal funds as part of TARP or other federal assistance programs resulting from the current economic crisis. The amendments also highlight Congress’s willingness to overrule court opinions and portends future such amendments. Pending legislation, the False Claims Clarification Act (“FCCA”), would amend FCA provisions regarding the public disclosure bar, which requires that a qui tam relator be an original source of information with independent knowledge of the facts on which the claim is based.

FERA Creates the Financial Crisis Inquiry Commission and Provides the Commission with Broad Powers

FERA creates the Financial Crisis Inquiry Commission and empowers the Commission with subpoena authority and **the responsibility to refer evidence of illegal activity to the Attorney General or state attorneys general**.

The Commission will be comprised of ten members with expertise in “banking, regulation of markets, taxation, finance, economics, consumer protection, and housing.” The Commission will examine issues related to the financial and economic crisis, including mortgage fraud, regulatory oversight, international capital flows, accounting policies, taxation, credit rating agencies, financial industry bankruptcies, corporate governance, compensation, derivative and other financial instruments, and the structure and systems of financial institutions. The Commission will, in effect, be **a further augmentation of enforcement resources and likely result in additional enforcement actions**.

FERA Also Impacts Other Significant Criminal Statutes

FERA’s provisions amend other criminal statutes. The changes include:

- Amending the general definition of “financial institution” in the US criminal code to include entities involved in the mortgage lending business that are not directly regulated or insured by the federal government. This expands the reach of federal fraud statutes to include private mortgage businesses.
- Amending 18 USC § 1014, prohibiting false statements on any loan or credit application, to cover false statements made by mortgage brokers or agents of mortgage lending businesses.

- Amending the major frauds statute, 18 USC § 1031, to include fraud in connection with TARP funds among the enumerated offenses covered by the statute.
- Amending the securities fraud statute, 18 USC § 1348, to proscribe fraud involving options and futures in commodities.
- Expanding the definition of “proceeds” in the money laundering statutes, 18 USC §§ 1956 and 1957, to include **gross receipts** of criminal activities, not just profits. This particular measure was made in response to the Supreme Court’s 2008 decision in *United States v. Santos*, which limited the definition of proceeds to **profits** of illegal activities. Senator Leahy stated that the amendment was necessary because “financial criminals escap[ed] culpability simply by claiming their illegal scams had not made a profit.”

Considerations Going Forward

All companies doing business with the federal government or benefitting from any federally-funded programs, not just current or potential recipients of federal bailout or stimulus assistance, will be affected by the new legislation. The economic crisis has given new life to congressional efforts to undo recent judicial opinions narrowly interpreting the FCA, and the passage of this bill shows

that, in the current political climate, congressional responses to the current economic crisis have increased the risk for recipients of federal assistance. Additionally, the FCA amendments apply generally, and increase liability for all potential defendants, regardless of whether they receive federal assistance. Other pending legislation proposing additional FCA amendments would also increase compliance risk.

In addition to the statutory amendments, the Financial Crisis Inquiry Commission will increase the enforcement risk for companies. Federal prosecutors will be well aware of the Commission’s activities and will receive referrals from the Commission. In essence, the Commission is a new investigatory tool for prosecutors that will uncover evidence and elicit testimony from witnesses. Additionally, the increased publicity associated with the Commission’s activities will increase expectations that prosecutors will vigorously pursue criminal convictions and civil remedies related to the financial crisis.

Business organizations would be well advised, especially given the treble damages potentially available for FCA violations, to carefully review current compliance systems relating to activities involving federal programs, or the federal government directly, in anticipation of the expected increase in enforcement resulting from enhanced enforcement resources and the Financial Crisis Inquiry Commission.

White & Case’s White Collar Practice Group will continue to provide updates regarding emerging white collar enforcement actions.

The text of the FERA can be found [here](#).

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