

Clients & Friends Memo

The Law's Long Reach: Recent Actions Show Federal Enforcement Agencies Are Not "Locked Down" by Social-Distancing and Quarantine Orders

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For federal law enforcement agencies – like the rest of government and society at large – the COVID-19 pandemic has ushered in a host of interrupted routines, unforeseen challenges, and new priorities. For businesses, understanding how these agencies are adapting and focusing their resources is critical to navigating a fast-changing regulatory environment. This article examines the response to COVID-19 of three key federal agencies: the Department of Justice ("DOJ"), the Securities and Exchange Commission ("SEC"), and the Office of Foreign Assets Control ("OFAC"). The record of these agencies over the last two months reflects a commitment to combating fraud and other abuses in connection with the public health response to COVID-19, while also pushing forward existing cases and providing guidance to help companies and individuals stay compliant during trying times. Cadwalader has [observed](#) a similar dynamic with respect to antitrust enforcement, and the same vigor on the part of enforcement agencies is apparent across the pond, as our colleagues in the United Kingdom write [here](#).

Department of Justice

The DOJ responded to COVID-19 almost immediately as opportunities for fraud sprouted nearly as fast as public concern over the virus. In a March 16 [letter](#) to all U.S. Attorneys, Attorney General William P. Barr noted that "[t]he pandemic is dangerous enough without wrongdoers seeking to profit from public panic." The letter specifically warned against fake cures, phishing emails from persons claiming to represent the World Health Organization, and malicious software embedded in mobile apps claiming to track the spread of the coronavirus.

The DOJ's COVID-19 response [website](#) encourages the reporting of hoarding and price gouging, warns against criminals posing as Internal Revenue Service ("IRS") employees, and highlights the risk of cryptocurrency frauds involving blackmail and investment scams. And the DOJ has designated the National Center for Disaster Fraud ("NCDF") – a national coordinating agency within the DOJ's Criminal Division – to receive [complaints](#) from the public related to the coronavirus.

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Law enforcement has wasted no time responding to the Attorney General's directives, as evidenced by a growing wave of arrests and charges. For example, on May 5 the DOJ [announced](#) that two men were charged in the District of Rhode Island with seeking a fraudulent loan of over \$500,000, which would have been forgivable under the Small Business Administration's Paycheck Protection Program ("PPP") and the Coronavirus Aid, Relief, and Economic Security ("CARES") Act. The DOJ alleged that the men falsely claimed to have dozens of employees, whose wages would have been safeguarded by the loan, when in fact these employees did not exist. Based on the allegations against these defendants, this appears to be a case of brazen fraud – and there may be many more such cases, given the hundreds of billions of dollars made available under the PPP. It remains to be seen how aggressively the DOJ will pursue more borderline cases involving legitimate businesses that may run afoul of rules requiring that loans be "necessary," among other requirements. (Cadwalader has covered the PPP and the potential for related audits and criminal enforcement, including with respect to the concept of "necessity," [here](#), [here](#), and [here](#).)

In addition, the U.S. Attorney's Office for the Eastern District of New York [announced](#) on April 28 that two individuals were arrested in connection with an alleged scheme to sell protective masks in New York City at a 50 percent mark-up. According to the criminal complaint, this conduct violated the Defense Production Act ("DPA") and executive orders invoking the President's authority under that law to make it illegal to hoard, or sell at excessive prices, medical supplies and devices designated by the Secretary of Health and Human Services ("HHS") as scarce. Also in the Eastern District of New York, a third individual was [charged](#) in a similar scheme to hoard personal protective equipment ("PPE") and price-gouge customers at his retail store, and another man was [arrested](#) for stealing COVID-19 government stimulus checks from the mail.

And on May 15, the DOJ [announced](#) charges against a woman accused of attempting to defraud Medicare, a federally funded health care benefit program. The defendant, who lives in Georgia, was under investigation for a number of years for her role in submitting false and fraudulent claims for genetic testing. Of late, however, she allegedly expanded her scheme to include paying and receiving kickbacks from COVID-19 testing laboratories, in violation of the Anti-Kickback Statute and health care fraud statutes.

The DOJ has been joined by a number of other federal agencies in rooting out COVID-19-related fraud. Since the start of the pandemic, the Food and Drug Administration ("FDA") and the Federal Trade Commission ("FTC") have issued dozens of "Warning Letters" to companies accused of marketing unapproved treatments and cures. Typically, these letters demand corrective actions within 48 hours, and threaten legal action if recipients do not comply. In at least one case, the FDA worked with the U.S. Attorney's Office in the District of Utah to institute such legal action, [requesting](#) and [obtaining](#) a temporary restraining order and other relief against an individual and two companies accused of promoting "ingestible silver products" as protection against the coronavirus. Other enforcement actions evidence a similarly high level of cooperation with an array of agencies, including the Internal Revenue Service ("IRS"), the U.S. Postal Inspection Service, and local law enforcement authorities.

Notwithstanding remote working adaptations and reliance on electronic processes, there has undoubtedly been some disruption to the DOJ's normal investigative and prosecutorial functions. Many courts have instituted prohibitions on in-person hearings, extended filing deadlines, and delayed jury trials, including in criminal cases (discussed [here](#) and [here](#)). Similarly, grand jury activities have been curtailed, impacting federal prosecutors' ability to return indictments. However, procedural changes and technology allow some activities to continue – especially through the use of videoconferencing and teleconferencing. Indeed, the defendants accused of selling protective masks at inflated prices in New York City, discussed above, each made their initial appearance in federal court via teleconference.

Securities and Exchange Commission

The SEC has been active in its response to the COVID-19 crisis and has taken a number of actions to make sure the U.S. markets stay open and function well. The Commission is emphasizing its monitoring of market functions and system risks, providing regulatory relief and guidance to those impacted by COVID-19, and maintaining its enforcement efforts. The SEC has provided exemptive relief and/or guidance to market participants in a wide range of areas, including: shareholder meetings and certain public company filing deadlines (discussed [here](#)); registered investment advisers' ability to borrow funds; broker-dealer financial responsibility rules; crowdfunding; and issues of concern to business development companies, registered investment companies, transfer agents, registered municipal advisors, and others. A summary of the actions taken by the SEC in response to the crisis is available on its website [here](#).

On the enforcement front, the SEC has reassured the public that its commitment to investor protection is unwavering and that it will maintain its enforcement efforts during the crisis. In a recent speech given on May 12, 2020, SEC Division of Enforcement Co-Director Steven Peikin discussed recent efforts made by the Division to address the heightened risk and protect investors during the COVID-19 pandemic. One of these efforts is the formation of the Coronavirus Steering Committee to coordinate the Division's response to the crisis. The mandate of the committee is “to proactively identify and monitor areas of potential misconduct, ensure appropriate allocation of our resources, avoid duplication of efforts, coordinate responses as appropriate with other state and federal agencies, and ensure consistency in the manner in which the women and men of the Division address coronavirus-related matters.” The Coronavirus Steering Committee is focused on:

- coordinating with the Division's Microcap Task Force and the Office of Market Intelligence to analyze the microcap market and “triage” matters for action;
- collaborating with the Division's Market Abuse Unit to watch trading activity for potential market manipulation, especially relating to issuer announcements that are from industries heavily affected by the coronavirus;

- developing a system to rapidly review public filings of highly impacted industries “with a focus on identifying disclosures that appear to be significantly out of step with others in the same industry”;
- working with the Division’s specialty units such as the Asset Management Unit and Complex Financial Instruments Unit to monitor the impact of the crisis on various industries for potential issues; and
- communicating with other regulators to coordinate efforts to protect investors.

The Division has also worked to communicate with investors and keep market participants updated on the coronavirus’ impact on the market and the Division’s response.

The SEC’s recent enforcement actions have been laser-focused on COVID-19-related misconduct that could harm main street investors. Towards this end, it has used its authority to suspend trading in the securities of more than thirty companies since the onset of the crisis due to issues with the adequacy and accuracy of information in the market related to COVID-19. In particular, the SEC has cited concerns with companies’ claims regarding the availability of personal protective equipment, tests, treatments, and vaccines for COVID-19.¹ In its first enforcement action related to the crisis, the SEC [charged](#) one of these companies and its CEO with securities fraud for falsely claiming that the company had acquired for sale a large number of N95 masks and had established a “direct pipeline from manufacturers and suppliers to buyers” when it had done neither. The SEC also recently [charged](#) two more companies (one along with its CEO) for misleading claims about COVID-19. We expect that these are the first wave in what will likely be a significant number of SEC enforcement actions for false statements related to COVID-19.

The SEC has also emphasized the importance of maintaining market integrity and following corporate controls and procedures during the crisis. This includes the prohibitions on illegal insider trading and the proper treatment of material nonpublic information. In a [statement](#) issued on March 23, 2020, the Co-Directors of the Division of Enforcement stressed that material nonpublic information available to corporate insiders may be even more valuable during the COVID-19 crisis and cautioned people with access to material non-public information – including “directors, officers, employees, consultants and other outside professions” – to be “mindful of their obligations to keep this information confidential and comply with the prohibitions on illegal securities trading.” They urged public companies to be aware of their disclosure obligations, including “established disclosure controls and procedures, insider trading prohibitions, codes of ethics, and Regulation FD and selective disclosure prohibitions[.]” The Co-Directors also reminded investment professionals that they must comply with policies and procedures designed to prevent misuse of material nonpublic

¹ More information about the SEC’s trading suspensions related to COVID-19 can be found [here](#).

information. We expect that the SEC will be watching the markets closely for unusual trading patterns and will investigate when it identifies outliers that look suspicious.

Public companies' disclosures and public statements will likely draw enforcement scrutiny from the SEC in the coming months. This includes public companies' disclosures and statements about the impact of the crisis on their businesses as well as pre-existing accounting or disclosure improprieties. In particular, the SEC is looking for disclosures "that may attempt to disguise previously undisclosed problems or weaknesses as coronavirus-related." While it is important for companies to be careful about any public statements made about the crisis and its impact, the SEC has tried to provide some comfort for companies making good faith disclosures in this uncertain environment. In a [joint statement](#) issued on April 8, 2020, Chairman Jay Clayton and the Director of the Division of Corporate Finance provided guidance on what kind of disclosures the SEC wants to see from public companies during the crisis, encouraged companies to make robust forward-looking disclosures, and assured companies that the SEC "would not expect to second guess good faith attempts to provide investors and the other market participants appropriately framed forward-looking information."

The SEC is also looking closely at aspects of the investment management industry. In addition to statements made by investment advisers to their clients about COVID-19's impact on their businesses, the SEC has indicated that it is particularly interested in failures to honor redemptions by private funds and investment companies and the improper marketing and sale of structured products to retail investors.

As the SEC works to maintain its enforcement efforts, COVID-19 is impacting the way the SEC is investigating and litigating these cases. Of course, just like the DOJ, the SEC's cases in active litigation are being impacted by the various court closures and related delays throughout the country. COVID-19 is also changing the way the SEC can conduct investigations. Social distancing guidelines are preventing the SEC from conducting many routine investigative steps in person. This includes important events such as investigative testimony, Wells and pre-Wells meetings, evidence reviews, and attorney proffers. As a result, SEC staff are now requesting that testimony and other in-person meetings take place telephonically, by videoconference, or via web-based programs. While the staff has agreed to accept informal phone interviews or attorney proffers in lieu of official sworn testimony in some situations, entities and individuals who are involved in ongoing investigations should expect requests of this nature to continue going forward.

Office of Foreign Assets Control

While much of the country has been sheltering at home, OFAC – like the DOJ and SEC – has continued to carry out its mission.

Of particular importance, OFAC has issued two important pieces of COVID-19-related guidance. First, on April 16 OFAC published a [Fact Sheet](#) explaining the applicability of existing OFAC exemptions, exceptions, and authorizations related to the provision of

humanitarian assistance to combat COVID-19, even where certain sanctioned persons or jurisdictions are involved. In the Fact Sheet, OFAC stated that it “encourages those interested in providing such assistance during the COVID-19 crisis to avail themselves” of these authorities.

Second, on April 20 OFAC [urged](#) financial institutions and other businesses to notify the agency of any anticipated delays in meeting certain regulatory reporting requirements and deadlines, including those related to blocked and rejected transaction reports. OFAC also recognized that, consistent with a risk-based approach to sanctions compliance, companies may need to respond to COVID-19-related technical and resource challenges by “temporarily reallocating sanctions compliance resources” to other areas. OFAC suggested that it would view such challenges as a mitigating factor in future enforcement actions related to violations that may occur during the pandemic.

OFAC has also remained active on non-COVID-19 related matters. For example, the agency has announced two enforcement actions, [here](#) and [here](#). While this represents a decrease compared to the same period last year – when six actions were announced – there is no indication that the reduction is related to the effects of COVID-19, or that it portends a longer-term trend. The agency also has made significant sanctions designations, including the imposition of blocking measures against the [subsidiary](#) of Russia’s largest oil company, as well as [entities](#) involved in the sale of Iranian oil and petrochemicals. In addition, OFAC has found time to: extend General Licenses related to its [Nicaragua](#)-, [Ukraine](#)-, and [Venezuela](#)-related sanctions programs; publish [amendments](#) to the North Korea Sanctions Regulations; and, along with other agencies, issue two detailed advisories regarding sanctions risk in the [maritime industry](#) and North Korea’s “[malicious cyber activities](#).”

Conclusion

For federal enforcement agencies, the COVID-19 pandemic has been a time of change, but by no means a time of inactivity. As agencies (and the courts) continue to adapt with increased reliance on remote work and electronic processes, and as steps are taken towards re-opening offices across the country, companies should expect that enforcement activity will proceed with fewer disruptions than in the earliest days of the crisis. In addition, we are certain to see a focus on investigations stemming from potential fraud and other misconduct in the response to the pandemic, underscoring the need for businesses to prioritize their compliance efforts – even as they grapple with the unprecedented uncertainty that is the universal hallmark of this COVID-19 era.

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