A bad bounce

Neil Williams discusses the costs of bounce back loan fraud, and the lessons learned

As the economy seeks to recover from the pandemic, the UK has been thrust into 'Plan B'. Attention had already been turning to public finances, where monies were spent, and how to recoup some for the public purse. What the Chancellor and lenders did not need was the announcement from the Department for Business, Energy, and Industrial Strategy (BEIS) estimating £27bn costs to the taxpayer in bounce back loan (BBL) fraud.

As we enter another stage of uncertainty and businesses begin to ask again for financial support, what lessons have we learnt from the initial government handouts falling to fraud?

Only half the story

A report from the National Audit Office (NAO), published on 3 December 2021, found that the Government failed to put adequate measures in place to prevent fraudsters stealing billions of pounds through its BBL scheme. In fact, it is said that up to £17bn out of over £47bn credit provided through COVID-19 related loans will not be repaid. Further reports estimate as much as £4.9bn of the credit is thought to have been taken by fraudsters.

To add insult to injury, it appears that the BEIS is looking to blame the lenders who stepped up very quickly to produce these loans, as they stated in June that as the Treasury had given a 100% taxpayer guarantee, the Department was left *"reliant on banks that it admits lack incentives given it is not their money on the line"*.

Of all the schemes made available at the start of the pandemic, the BBL scheme[1] has been particularly susceptible to fraud. The vulnerability of the scheme, and the risk to the taxpayer for recovery purposes, is underpinned by the 100% government guarantee for the loans. As discussed, this has led to suggestions from the BEIS that lenders may not have sufficient 'incentives' to recover losses due to fraud, given that the risks to them are mitigated by the guarantees. This, however, is perhaps only half the story, and does not truly reflect the obligations placed on lenders, no matter what the circumstances at the time of lending.

These statements from the BEIS do not sufficiently reflect their own role in the introduction of the support schemes themselves, and whether they should have done more to mitigate the potential risks. Earlier this year, the House of Commons Committee of Public Accounts published its Fraud and Error report, which included analysis of the implementation of the schemes, and in particular the BBL initiative.[2]

The potential for fraud and the risks to governmental departments when implementing such policies have been known for some time, giving rise to the implementation of the Government Counter Fraud Function (CFF) in October 2018. The CFF brings together the many thousands of counter fraud experts within government. A central feature of its purpose is to assess fraud risk in government departmental initiatives. If ever there was a project which it should have been consulted on, the BBL scheme should have been at the front of the queue. It appears, however, as consultation with the CFF is not mandatory, that the BEIS didn't draw on its resources which no doubt would have resulted in a reduced risk to the public purse.

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Act now worry later

The fundamental purpose of the BBL Scheme was to provide businesses with capital to get them through the COVID-19 lockdown. Introduced in March 2020 as the UK went into the first lockdown, it was quickly ushered through. This was understandable as the economy was vulnerable and urgent measures were being conjured up to prevent collapse.

There were concerns over the flaws in the approval service, but these were overshadowed by an 'act now and worry later' policy. Applications for funding amounts between £2,000 to £50,000 were invited, and the government website provided application guidance suggesting that a short online application form would need to be completed, and self-declarations to confirm eligibility would be acceptable. For those looking for ►

some easy, quick cash, this was perhaps akin to a car being left unlocked on the drive with the keys in the ignition.

The ease of access to funding and the lowering of approval scrutiny meant that there was always a risk. Fraud and over-stated (or under-declared) applications slipped through the net. Huge numbers of applications were received within the first six weeks, and 860,000 loans were approved during this period.

In order to get the money out to applicants as quickly as possible, scrutiny of applications was lowered, with only certain conditions still being required to meet eligibility.

Since the loans were approved and those doing the back-office legwork have had time to catch a breath, the Cabinet Office has identified detailed examples of different types of fraud:

- **Hard fraud** – large-scale fraud, often committed by organised criminal gangs. Examples include the impersonation of a legitimate business or person, submitting multiple fraudulent applications with different lenders, and using money mules to accept the loans and then filing for bankruptcy.
- **Soft fraud** – where an organisation exaggerated an aspect of its business to acquire a loan, normally by way of inflating annual turnover figures.

The BEIS estimates that approximately £5bn of the overall losses will be attributable to fraud, which equates to just over 6% of the total amount lenders paid out.

A powerful tool

The National Crime Agency (NCA), HM Revenue & Customs (HMRC) and the police are today at the forefront of investigating pandemic-related fraud. The NCA's focus will always be on organised crime, while HMRC is using the extra funding and resources made available through the creation of the Taxpayer Protection Taskforce to investigate COVID-19 fraud.

However, it appears that it is actually through several less illustrious agencies, rather than the latter, that the cumulative nature and scale of frauds against these schemes are being identified. The Insolvency Service is one prime example. It has lauded its successes[3] in resisting attempts to dissolve or strike off companies from the register, where it was suspected that this was being done to evade investigation and recovery of inappropriately obtained funding.

The investigative powers of the Insolvency Service are soon to be bolstered by the passage of the Rating (Coronavirus) and Directors Disqualification (Dissolved Companies) Bill[4], which will allow it to specifically target, and pursue, directors who have chosen to close their companies by dissolving them to avoid outstanding debts. The new powers will now be retrospective and will apply to those who sought dissolution in the two years prior to the implementation of the legislation.

In an attempt to prevent a company from being struck off where directors may have outstanding BBL debts, the company directors can now reasonably expect to receive an 'Objection to Company Strike-Off Notice', which will also afford other creditors the opportunity to register objections.

A powerful tool in the Insolvency Service's armoury, it will now allow them to look at the conduct of directors in the lead-up to the proposed strike-out, and even peer back in time to look at companies which have already been dissolved. Sanctions such as disqualification of directors, and recovery of liabilities from personal assets, are retrospectively available. Prior to this, the process had proved to be cumbersome and difficult.

Lenders' duties

What of the duties of lenders when there is suspected fraud? Can they realistically just wait for the government and other agencies to act? In many respects, while the schemes were new and transient, the obligations of lenders remain the same. It is right that the ability of lenders to fully scrutinise the applications at the height of the pandemic may have been hampered by the lockdown measures in place, but it is important to remember that as these have now peeled away, at least for the time being, attention must turn to what has happened to the money that had been made available.

At the forefront of these enquiries are the lenders themselves, given the information that they have in their possession following funds being approved and paid out. Despite the BEIS's suggestion that banks may lack the incentive to recover funds, anti-money laundering (AML) obligations are more important than ever, given the scale of the fraud which could potentially have occurred.

Lenders will no doubt want to comply with their regulatory obligations and avoid the onerous sanctions which can follow if they don't. Now that the nature and extent of fraudulent activity is being revealed, the requirement to monitor transactions is becoming increasingly important.

The volume of applications which were granted, and the sums involved, mean that this is no small task. As we now find ourselves in Plan B with the potential of heightened restrictions if the Omicron variant can't be controlled, there is every chance that the Treasury will have to cough up again and back further loans. Adapting existing AML compliance procedures to incorporate potentially new markers will help to recoup any past or future losses. Moreover, I, for one, cannot see the government allowing lenders to take a laid-back approach in these cases – not with so much at risk!

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1. https://www.reeds.co.uk/business-law/furlough-fraud-solicitors/
2. https://publications.parliament.uk/pa/cm5802/cmselect/cmpubacc/253/25306.htm#_idTextAnchor006
3. https://www.gov.uk/government/news/insolvency-service-cracks-down-on-bounce-back-loan-abusers
4. https://bills.parliament.uk/bills/2861