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Government Contracts ADVISORY ■

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Congress' Creation of Privately Funded and Privately Managed Federal Program Not Enough to Trigger False Claims Act Liability

In a decision that may have far-reaching implications to the Federal Government's efforts to oversee the E-Rate Program, the Fifth Circuit Court of Appeals recently reversed a district court decision denying several technology companies' motion to dismiss a False Claims Act (FCA) case arising out of the defendants' participation in the E-Rate Program. The Fifth Circuit held that E-Rate funds are not "provided by" the Federal Government merely because Congress established the program, thereby concluding at least some financial harm to the U.S. Treasury is required before FCA liability can attach. Alston & Bird Government Contracts attorneys Jeff Belkin, Andy Howard, and Jessica Sharron represent two defendants (only one of which was involved in the appeal) in the case.

Created by the Telecommunications Act of 1996, the E-Rate Program, among other things, provides financial assistance to eligible public schools and libraries for the acquisition of telecommunication services, internet access, and internal (network) connections. Funding for the E-Rate Program is provided by tariffs levied on telecommunications services providers (and passed along to consumers) that are paid into the Universal Service Fund (USF). The Universal Service Administrative Company (USAC), a private non-profit corporation that operates under the direction of the Federal Communications Commission (FCC), administers the E-Rate Program.

The Fifth Circuit's decision arose in a *qui tam* case under the FCA, *U.S. ex rel. Shupe v. Cisco Systems, Inc., et al.*, Case No. 13-40807 (S.D. Tex). There, the relator sued three unrelated telecommunications companies (one, his former employer) alleging they violated the FCA by failing to comply with competitive bidding rules and "gold-plating," i.e., selling higher quality equipment than required, among other things. By engaging in this conduct, the relator claimed, the defendants violated the FCA by (1) presenting to the government false or fraudulent claims for payment or approval, (2) using or causing to be used false records or statements, and (3) conspiring with each other to defraud the government. The government chose not to intervene in the case.

In the trial court the defendants moved to dismiss the complaint on various grounds, including that the FCA does not apply to requests for reimbursement under the E-Rate Program because USAC, the entity to which such reimbursement requests are submitted, is not "the government" nor are the funds it disburses "provided by" the government. Both of these, the defendants argued, precluded liability under the FCA statutory definition of a "claim".

The district court rejected this argument, concluding that it was not a requirement of the FCA that funds be deposited into the U.S. Treasury and/or distributed by a government body to qualify as government funds under the FCA. According to the court, the only requirement is that the government provides or reimburses a portion of the money requested. The court further concluded that under the E-Rate Program, the government "provides" the funds because USAC was created by the FCC under a congressional mandate, it is the recipient and grantee of the USF funds, and therefore it acts as an agent of government in distributing those funds. The defendants appealed.

On appeal, the Fifth Circuit reversed. Rejecting the arguments by the realtor and the United States – which participated separately in briefing and in oral argument as amicus curiae– the Fifth Circuit focused on two major points: (1) the source of the USF funds; and (2) the entity to which the claims were being made. The court found that the E-Rate Program does not trigger FCA liability because it does not involve federal funds and its relationship to the government is too tenuous.

With regard to the question of whether E-Rate funds were "provided" by the government, the Fifth Circuit explained that the FCA applies when the government "provides any portion" of the money requested or demanded. Importantly, the court of appeals observed that in the 2009 amendments to the FCA, Congress left unaltered that portion of the definition of the term "claim," that requires the Government "provide" funds, which the appellate panel observed made their holding applicable to cases arising under either version of the FCA. In the case of the E-Rate Program, the court of appeals concluded that because the money in the USF is untraceable to the U.S. Treasury, "the government does not have a financial stake in its fraudulent losses," and thus no FCA liability can attach.

Further, with regard to whether government oversight of USAC was enough to make false or fraudulent claims submitted to USAC fall within the scope of the FCA, the court of appeals held that it is not. Notwithstanding that the FCC maintains regulatory supervision over USAC and the E-Rate Program, USAC is a private corporation, not the government, the appellate panel observed.

The court ultimately held that because there are no federal funds involved in the E-Rate Program, and because USAC is not itself the government, alleged fraud in the E-Rate Program cannot be policed under the anti-fraud provisions of the FCA. The court therefore reversed the district court's decision on this issue and remanded the case for further proceedings, which, unless reversed on further appeal, should result in the dismissal of the entire action as against the appellants.

Although subject to further appellate review, the Fifth Circuit's decision is grounded in a common sense interpretation of the plain language of the FCA. And, it represents an important limitation on the FCA, which in recent years has been used seemingly as an all-purpose fraud statute contrary to its roots. Moreover, the FCC and USAC will be required to utilize less draconian tools – such as contractual remedies and "commitment adjustments," both of which are subject to challenge – in order to enforce the regulatory requirements of the E-Rate Program upon service providers, applicants, and other participants in the E-Rate Program.

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