The Future Of Renewable Energy And The False Claims Act

Law360, New York (March 07, 2012, 1:04 PM ET) -- The renewable energy industry is currently in the midst of applying for and receiving tens of billions of dollars in cash grants from the United States government. Companies are structuring their operations to maximize their eligibility for these funds and several key deadlines for applying for these funds loom in the near horizon.

At the same time, recent events like the Solyndra LLC bankruptcy and ensuing criminal and other enforcement investigations underscore the need for careful scrutiny and the implementation of rigorous compliance programs in the administration of these projects.

For those in this field, it is important to incorporate into their planning and implementation processes appropriate review and compliance programs to prevent and address, if necessary, issues that implicate the False Claims Act (FCA) and related criminal statutes in their application to these renewable energy grant programs.

Background

Recent years have seen a massive flow of government funding in support of the renewable energy industry and project development. Under the American Recovery and Reinvestment Act of 2009 (Recovery Act), the U.S. Department of Energy (DOE) received more than $35 billion to fund various initiatives, including many in renewable energy.[1] It also received authority to make or guarantee as much as $52 billion in energy-related loans.[2]

Similarly, the Recovery Act initiated the popular “Section 1603” cash grant program, pursuant to which the U.S. Department of the Treasury (DOT) provides upfront grants for renewable energy projects in lieu of tax credits that would otherwise be available. As of the last accounting, $9.2 billion of grants had been issued under the Section 1603 grant program.[3]

Despite the passage of two years since these programs were enacted — and notwithstanding that the Section 1603 program expired at the end of 2011 — these programs have not yet been fully implemented and funds remain unspent. The DOE’s inspector general reported that as of Dec. 31, 2011, while 98 percent of its Recovery Act funds had been obligated, only 60 percent had been paid out.

Meanwhile, the Section 1603 cash grant program “grandfathered” projects that were under construction prior to the end of 2011. Provided these projects are completed by their “credit termination date” which, for certain types of popular projects, including solar energy projects, runs as far out as the end of 2016, these projects will likely qualify for grant payments.

Notwithstanding, the Section 1603 program requires at least a preliminary application to be filed no later than Sept. 30, 2012, in order to be eligible for a cash grant. As the Section 1603 program does not have a spending cap, the government will not learn the extent of its obligations with respect to the program until the time of these applications.

The availability of federal funding and the various filing requirements means that many actual or hopeful recipients of federal incentives under these programs are now in the process of determining whether — and the extent to which — they qualify for these funds. They are also in the process of preparing applications and other paperwork to receive these funds.

In light of the lessons learned as part of the high profile Solyndra bankruptcy and related ongoing investigations, as well as the DOE’s inspector general statement that his office has completed 70 Recovery Act reviews and has “many more ongoing investigation and evaluations,”[4] it is clear that the teams administering these programs will be scrutinizing applications to ensure that funding recipients are entitled to the proceeds awarded to them. Sophisticated applicants should plan for such scrutiny and implement robust review and compliance programs to prevent problems.

Key Aspects of Eligibility for Renewable Energy Stimulus Funding and Cash Grants

Whether a project owner can qualify for renewable energy stimulus funding — and the amount of funding available — depends in large part on the characteristics of the project.

For example, the Section 1603 program is designed to promote the development of domestic projects relying on renewable energy sources that would otherwise be eligible for investment or production tax credits under the Internal Revenue Code. Among others, projects utilizing solar, wind, geothermal, biomass and fuel cell sources may all be eligible for Section 1603 cash grants.

Within the various Recovery Act initiatives, there are several key factors the government will look at in deciding whether and the extent to which projects are eligible for funds.

For example, in the Section 1603 program, one is the project must be "placed in service" — meaning, ready and available for its intended use — during 2009 to 2011, or after 2011 and before the applicable credit termination date, provided that "construction" of the project commenced during 2009 to 2011.

A second is the cost of the project tied to energy generation. The amount of the Section 1603 grant is calculated based on the cost of the property included in the project which is directly or indirectly involved in energy generation, other than real property.

For cash grant purposes, this property is known as the "specified energy property" included in the project. While not a concern for Section 1603, other Recovery Act initiatives consider the number of jobs estimated to be created or retained by the property. Applicants are also required to submit supporting documentation along with their applications.

As one might expect, these types of eligibility requirements provide tempting opportunities for abuse by grant applicants. For example, because the Section 1603 grant is based on the cost of the specified energy property included in the project, the grant applicant may be tempted to inflate costs that are allocable to these components in order to maximize the grant award.

Another abuse would be in the case of a project that was not commenced prior to the end of 2011. Here, the applicant may be tempted to exaggerate the extent of its 2011 activities in order to satisfy the construction commencement requirement.

Considering the volume of applications for government support under the Recovery Act initiatives — the number of Section 1603 grant program awards alone have exceed 22,000[5] — an applicant may view the chances of avoiding scrutiny as unlikely.

However, the applicant's misrepresentations may have serious implications. For example, a Section 1603 grant application requires the submission of statements made under penalty of perjury by the applicant and/or other project participants in support of program eligibility.

As such, the applicant and its representatives could find themselves in the uncomfortable position of having to defend themselves against criminal and civil FCA investigations and possible prosecution by the U.S. government, all of which may occur after the renewable energy grant has been awarded.

The Section 1603 program guidance issued by the DOT makes clear that improperly awarded funds will be collected by all available means against any assets of the applicant, including enforcement by the U.S. Department of Justice (DOJ).[6]

How the False Claims Act Might Interact With Investigations Into Eligibility

In cases where there are questions about the eligibility of renewable energy projects for funds and grants that have been paid, the FCA will no doubt be one of the primary vehicles used to try to recover those funds. It is the tool of choice for the government to recover funds paid out due to fraud, and the

government has recovered many billions of dollars through the FCA just in recent years in a variety of other industries, with total recoveries by the DOJ reaching more than $3 billion in 2011.

Those in the renewable energy industry should understand the nature and scope of the FCA. It provides for up to treble damages, plus $11,000 in penalties per each fraudulent claim, attorneys' fees and generous whistleblower incentives that allow private whistleblowers to share in the percentage of the government's recovery.[7]

Contractors found liable under the FCA can also be disqualified from contracting with the government or receiving further government funds. This debarment possibility is a significant remedy that the agencies use to eliminate from contracting opportunities those vendors whom they view as fraudulent.

Under the FCA, a person can be liable for knowingly submitting a false or fraudulent claim for payment or approval; knowingly making, using or causing to be made or used a false record or statement that is either material to a false or fraudulent claim, or material to an obligation to pay the government; or knowingly concealing or knowingly and improperly avoiding or decreasing an obligation to pay or transmit money or property to the government.[8]

Each of these theories could implicate various aspects of the renewable energy grant application programs. For example, an application that contains false information about the project's "placed in service" or "construction" dates, or about its costs tied to energy generation could constitute a false or fraudulent claim for payment or approval.

They may also constitute false statements to avoid or decrease a tax payment obligation to the government, as the FCA's exception for "claims, records or statements made under the Internal Revenue Code of 1986" might not apply to affirmative statements in applications for grants under the Recovery Act, as opposed to simply statements on tax returns regarding renewable energy tax credits under the Internal Revenue Code of 1986.

Documents prepared and submitted in support of the application, if containing similar false information, could also subject the applicant, and even others who are not the direct applicants but working with the applicant, to liability for creating false records or statements material to a false or fraudulent claim.

False statements or claims must be "material." The government would no doubt argue that facts regarding core aspects of the applications, like the date of construction or placement into service as well as the costs tied to energy generation, are material to the government's decision about whether and how much to award in grant funds, since the grant programs are specifically intended to encourage timely creation of renewable energy projects.

Additionally, one should take note that the statute defines "knowingly" more broadly to not only include "actual knowledge of the information," but also "acting in deliberate ignorance of the truth or falsity of the information," or even "acting in reckless disregard of the truth or falsity of the information."

The FCA specifically provides that there is no requirement of "specific intent to defraud." Simply put, applicants cannot hide behind ignorance when preparing their applications. Care is needed.

But by the same token, applicants or project owners who find themselves faced with an investigation or lawsuit under the FCA should understand important potential defenses. An applicant may be able to argue that statements about future events cannot be considered false or fraudulent statements. One might also be able to argue that if the truth or falsity of a statement ultimately turns on interpretation of the Internal Revenue Code of 1986, then the FCA does not apply.

Or, depending on unique circumstances of the project, it is possible that certain statements within the application or supporting documents cannot be considered material to the government's ultimate decision to award a grant, or the entire grant.

For example, one might imagine that if an applicant simply overestimates in good faith the number of jobs a project might generate, the applicant might have an argument that the government would still have funded all, or at least some, of the project based on the projected renewable energy output or other factors, regardless of the particular jobs estimation.

Similarly, if an erroneous statement in the application or documentation is the result of a good faith effort to apply the complex regulations involved or make complicated projections, it may be difficult for the government to prove that the applicant acted with the required knowledge of the falsity or fraud.

Finally, in an action under the FCA, the government might try to claim damages in the amount of the entire grant, based on the theory that it would not have awarded any funds at all had it known that the project was not eligible for those funds in the first place. But project owners will find support for the argument that the government might not be entitled to damages in the full amount of the grant.

For example, project owners might argue that the government was not damaged in the entire amount of the grant if the project was only placed into service slightly later, or created some renewable energy or some renewable energy jobs but just not as much energy or as many jobs as anticipated.

This argument is strengthened where the project would have otherwise qualified for federal tax credits, as the government should be indifferent regarding the form of its support — specifically, whether to write a check to a recipient or to allow the recipient to reduce its taxable income by the same amount.

Conclusion

Those applying for and receiving funds under the various renewable energy grant programs should no doubt be cautious not to overstate the key aspects of their projects or overreach for grant funds. Faced with the possibility of treble damages under the FCA and possible criminal liability, if there is significant doubt about eligibility, applicants may be better off taking the more conservative approach in their applications, such as by scaling back their requests for grant funds, or breaking their requests up into separate applications.

By the same token, if faced with an FCA or criminal investigation, the project owner or its lawyer should carefully scrutinize the facts of their case through the lens of the FCA to ensure they explore all potential defenses. Looking into the crystal ball, the coming years are likely to witness interesting issues as the FCA is applied to the renewable energy industry and these grant programs.

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