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Will DBE Fraud Continue to Be Prosecuted? The Impact of the *Kousisis* Decision in the Shifting Affirmative Action Landscape

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On May 22, the Supreme Court in *Kousisis, et al., v. United States*,[1] affirmed the convictions of a painting subcontractor and its owner (defendants) under the federal wire fraud statute for conspiring to defraud the Department of Transportation (DOT) and the Pennsylvania Department of Transportation (PennDOT) by exploiting the DOT's disadvantaged business enterprise (DBE) program in connection with two Philadelphia construction projects.[2] As explained below, the Court resolved a divide among the circuits over the validity of a federal fraud conviction where the defendant did not seek to cause the victim net pecuniary loss. The Court held that where a fraudster seeks to induce the government into a transfer of its money or property, that loss is sufficient to sustain a fraud conviction, regardless of whether the government has suffered pecuniary loss.

The Court's decision clarifies that DBE fraud remains a legally viable prosecution theory. However, the chances that the Department of Justice (DOJ) will pursue such prosecutions during this administration will almost certainly be tempered in light of the executive branch's direction to excise references to diversity, equity, and inclusion (DEI) and diversity, equity, inclusion, and accessibility (DEIA) principles from federal acquisition and contracting,[3] and the DOT's recent concession that the DBE "program's use of race- and sex-based presumptions is unconstitutional."[4] In fact, on May 28, 2025, the DOT filed a joint motion for entry of consent order in *Mid-Am. Milling Co., LLC v. United States DOT*, requesting that the U.S. District Court for the Eastern District of Kentucky approve a settlement agreement that prohibits the DOT from approving "any federal, state, or local DOT-funded projects with DBE contract goals where any DBE in that jurisdiction was determined to be eligible based on a race- or sex-based presumption."[5]

At least at the federal level, these recent developments strongly signal the near-term end of traditional race and gender-based DBE programs and sharply reduced prosecutorial interest in federal civil and criminal cases predicated on DBE fraud going forward. However, suppliers are not necessarily in the clear and may remain caught in the middle[6] if their customers have requested or continue to request that they use a DBE as a pass-through for services on government-funded projects.

The *Kousisis* Case

The *Kousisis* defendants' convictions arose out of their false representations to PennDOT that they would obtain paint supplies from Markias, Inc., a prequalified DBE, in connection with the renovation of the Girard Point Bridge and Amtrak 30th Street Train Station projects in Philadelphia. Markias, however, functioned only as a pass-through entity, "funneling checks and invoices to and from [defendants'] actual suppliers," thereby violating

federal regulations that require DBEs to perform a “commercially useful function.” Through the scheme, defendants turned a gross profit of more than $20 million.

On these facts, a grand jury in Philadelphia indicted defendants for wire fraud and conspiracy to commit wire fraud. The charges were premised on the fraudulent-inducement theory, *i.e.*, defendants fraudulently induced PennDOT to award them the painting contracts under materially false pretenses regarding their DBE participation. A jury found defendants guilty on three counts of wire fraud and one count of conspiracy. Defendants moved for judgment of acquittal, arguing that because their work met PennDOT’s expectations, PennDOT had received the full economic benefit of its bargain and had not been defrauded of money or property, as the federal wire fraud statute requires. The district court rejected this argument, and the Third Circuit Court of Appeals affirmed, concluding that obtaining the government’s money or property was precisely the object of the defendants’ fraudulent scheme as they had set out to obtain millions of dollars that they would not have received but for their fraudulent misrepresentations to PennDOT.

Defendants sought review by the Supreme Court, arguing that their convictions should not stand because defendants did not seek to “hurt the victim’s bottom line.” The Supreme Court granted *certiorari*, noting that the circuits are divided over the validity of a federal fraud conviction in the absence of net pecuniary loss. While the Third, Seventh, Eighth, and Tenth Circuits permit such convictions to stand, the Second, Sixth, Ninth, Eleventh, and District of Columbia Circuits disagree. The Supreme Court sided with the former and affirmed the defendants’ convictions, holding that a defendant can be convicted of federal fraud as long as it induced a transaction under materially false pretenses, even in the absence of economic loss.[7]

The Court began its analysis by reiterating the test for federal wire fraud, explaining that a defendant commits such a crime only if he “both engaged in deception and had money or property as an object of his fraud.” The Court explained that from these rules, defendants attempted to create another: that a federal fraud conviction cannot stand unless the defendant sought to hurt the victim’s bottom line. The Court rejected this argument because the fraudulent-inducement theory is devoid of an economic-loss requirement; instead, the theory supports a finding of liability anytime a defendant uses falsehoods to induce a victim to enter into a transaction.

The Court concluded that its endorsement of the fraudulent-inducement theory comports with the wire fraud statute and the Court’s prior precedent interpreting it. The Court explained that the wire fraud statute “does not so much as mention loss, let alone require it.” Instead, a defendant violates the statute by scheming to obtain the victim’s money or property, regardless of whether he seeks to leave the victim economically worse off. Thus, where the fraudster seeks to induce the government into a transfer of its money or property, that loss is sufficient to sustain a fraud conviction, even where (as here), defendants’ work met expectations.

The Court further explained that the common law does not uniformly condition actions sounding in fraud on a plaintiff’s ability to prove economic loss. For example, in claims for contract rescission or prosecutions for false pretenses, most courts require only that the victim received property of a different character than was promised, even if of equal value. Thus, the Court refused to read economic loss as a requirement of the wire fraud statute. The Court concluded that defendants’ scheme to obtain money from PennDOT through false representations about their compliance with DBE requirements constituted wire fraud, even despite defendants providing something of value in in exchange for payments received.[8]

The Court also addressed defendants' warning that, if the fraudulent-inducement theory is endorsed, every intentional misrepresentation designed to induce someone to transact in property would constitute fraud. The Court rejected this argument, concluding that the "demanding" materiality requirement of fraud claims substantially narrows the universe of actionable misrepresentations.[9] The Court explained that the theory "criminalizes a particular species of fraud: intentionally lying to induce a victim into a transaction that will cost her money or property." And while the language of the wire fraud statute is "undeniably broad," it is up to Congress to change it.

The Implications for Suppliers

Suppliers are left to wonder whether the DOJ will continue to investigate and prosecute DBE fraud now that the Supreme Court has upheld the legal validity of their federal wire fraud theory. The easy answer would be "no" given that the DOT and DOJ have made clear in the past week these programs are unconstitutional and DBE requirements can no longer be enforced. However, there are several nuances suppliers must consider before deciding they are in the clear:

First, the fact that a program is unconstitutional is not a legal defense to a fraud charge. The focus of a fraud charge is on the defendant's conduct and the intent to deceive or mislead, not the validity of the underlying program. The constitutionality of a program and the commission of fraud are separate legal issues. Even if a program is unconstitutional, it does not provide a legal justification or excuse for committing fraud.

Second, the statute of limitations for a federal False Claims Act Claim is generally six years from the date of the violation. The statute of limitations for federal criminal wire and mail fraud is generally five years. Prior instances of DBE fraud may remain actionable if a new administration takes office in 2029 and DOJ policies shift.

Third, the potential remains for False Claims Act relators to attempt to bring DBE fraud cases against suppliers and for state agencies to pursue criminal and civil investigations and enforcement actions under applicable state law. Even without DOJ intervention, *qui tam* and/or state false claims act cases can proceed.

Going forward, suppliers are likely to see a sharp drop-off in requests from customers that they work with DBEs. Suppliers will have to evaluate any such requests carefully if they may be asked to certify they are not participating in any such programs as a prerequisite to participating in federally funded projects. However, to the extent suppliers are continuing to work with DBEs, they must continue their commitment to DBE compliance, including making sure that the DBE is fulfilling a commercially useful function and is not a mere pass-through. While the underlying DBE programs will continue to face challenges on constitutional and political grounds, a strong compliance program that ensures companies are not using "pass through entities" to fulfill their commitments should remain at the forefront of suppliers' minds.

Troutman Pepper Locke's White Collar + Government Investigations and Construction practice groups are well-suited to help suppliers, prime contractors, and subcontractors navigate the challenges inherent in these situations. Please contact one of the authors of this article to learn more about Troutman Pepper Locke's capabilities regarding DBE compliance on government-funded projects.

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[1] *Kousisis v. United States*, No. 23-909, 2025 U.S. LEXIS 1982 (May 22, 2025).

[2] Justice Barrett delivered the opinion of the Court, in which Chief Justice Roberts, and Justices Thomas, Alito, Kagan, Kavanaugh, and Jackson joined. Justices Thomas, Gorsuch, and Sotomayor authored concurring opinions.

[3] Exec. Order No. 14173, 90 Fed. Reg. 8633 (Jan. 31, 2025) (titled "Ending Illegal Discrimination and Restoring Merit-Based Opportunity").

[4] *Mid-Am. Milling Co., LLC v. United States DOT*, No. 3:23-cv-00072-GFVT, ECF No. 82-1 (Consent Order, May 28, 2025), ¶ 5 ("Defendants, upon review of the DBE program and their position in this litigation, have determined that the program's use of race- and sex-based presumptions is unconstitutional."), ¶ 7 ("USDOT has determined that race- and sex-based presumptions in its DBE program can no longer pass constitutional scrutiny."). On May 29, 2025, a group of DBEs and advocacy groups informed the court that they intend to oppose the entry of the proposed consent order and would be filing their opposition on or before June 18, 2025. *Id.* at ECF No. 83 (Notice of Intent to File Response in Opposition, May 29, 2025).

[5] *Mid-Am. Milling Co., LLC v. United States DOT*, No. 3:23-cv-00072-GFVT, ECF No. 82-1 (Consent Order, May 28, 2025), ¶¶ 11-12.

[6] Suppliers Beware: US Government Continues Prosecution of DBE Fraud Cases Involving Supplies Passed Through DBEs | Troutman Pepper Locke ; Caught in the Middle: What Is a Supplier Supposed to Do When Its Customers Ask to Use a DBE as a Pass-Through? | Troutman Pepper Locke.

[7] In a concurring opinion, Justice Sotomayor agreed with this "bottom-line decision" to affirm, but advocated for a more restrained holding. Justice Sotomayor explained that a defendant may not escape liability by asserting the victim suffered no net economic loss, but took the position that the Court need not have opined on a class of fraudulent-inducement cases distinct from the one before it, namely, "those in which a defendant provides exactly the goods or services that they promised to deliver, but lies in other ways to induce the transaction."

[8] Justice Gorsuch opined that the Court appears to have "spurn[ed] fraud's historic injury rule" because its opinion suggests that it does not matter if the putative victim receives all he was promised. Justice Gorsuch explained that this runs the risk of "turning victimless lies … into federal felonies," which "cannot be the law." To mitigate such risk, Justice Gorsuch urged that "[l]ies without injury are not criminal frauds."

[9] Notably, because the defendants did not contest that their misrepresentations were material, the Court did not address the materiality of their statements regarding DBE compliance. Nevertheless, in a concurring opinion, Justice Thomas opined on the materiality requirement of the federal wire fraud statute and explained his skepticism regarding the materiality of defendants' statements. Justice Thomas explained that the Government must satisfy the materiality element in any federal wire-fraud prosecution, which requires that a misrepresentation "went to the very essence of the bargain," and indicated his "serious[] doubt that the DBE provisions [in this case] can meet this standard."

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