No. 21-1326

IN THE

Supreme Court of the United States

UNITED STATES OF AMERICA, ET AL.,
EX REL. TRACY SCHUTTE & MICHAEL YARBERRY,

Petitioners,

v.

SUPERVALU, INC., ET AL.

Respondents.

On Petition for a Writ of Certiorari
to the United States Court of Appeals
for the Seventh Circuit

REPLY BRIEF FOR PETITIONERS

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases

REPLY BRIEF FOR PETITIONERS

The question presented is roiling the courts of appeals. The petition described a four-to-four circuit conflict, with further internal divisions. *See* Pet. 13-23. Since the petition was filed, additional decisions involving the FCA's[1] scienter standard have aggravated the conflict. And the Fourth Circuit just went *en banc*, vacating an opinion agreeing with the decision below. *See United States ex rel. Sheldon v. Allergan Sales, LLC*, 2022 WL 1467710 (4th Cir. May 10, 2022).

The conflict is unsurprising, as the question goes to the heart of the FCA, providing a key distinction between actionable misconduct and innocent mistakes. No surprise, then, that prominent amici have weighed in on both sides. The United States government argued that the decision below "will significantly impair the government's ability to combat fraud." U.S. C.A. Reh'g Br. 5. Senator Grassley, the FCA's principal architect, describes the Seventh Circuit's many errors and explains that the decision below "badly distorted Congress's plain language in reaching a result that opens a gaping hole in the government's primary fraud-fighting tool." Grassley Amicus Br. 23. And Taxpayers Against Fraud Education Fund, the nation's most prominent whistleblower advocacy organization, warns of "far-reaching consequences" if the decision below is not reversed. TAFEF Amicus Br. 2.

On the other side, the Chamber of Commerce, Pharmaceutical Research and Manufacturers of America, the National Association of Chain Drug Stores, and the Washington Legal Foundation filed

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[1] Abbreviations are defined in the petition.

briefs below supporting respondents. The issue has accordingly been fully ventilated, including in multiple sharply divided decisions.

The circuits are divided; the question is important; and this case is an ideal vehicle. The Court should accordingly grant certiorari or—given the law enforcement interests at play—call for the views of the Solicitor General.

I. The Circuits Are Divided Over the Appropriate Scienter Standard in False Claims Act Cases

Respondents elide the circuit conflict posed by the petition, arguing that "no circuit has declined to apply *Safeco*'s objective standard to the FCA where falsity turned on an unclear legal obligation." BIO 16. But the question is not whether courts cite *Safeco*. *See* Pet. 22-23 (anticipating and refuting this argument). Instead, the question is "[w]hether and when a defendant's contemporaneous subjective understanding or beliefs about the lawfulness of its conduct are relevant to whether it 'knowingly' violated the False Claims Act." Pet. i. The difference matters because *Safeco* does not compel the Seventh Circuit's holding that a defendant's subjective understanding or beliefs are irrelevant to scienter. *See* Pet. 34. On the contrary, many courts cite *Safeco* as relevant precedent *and* hold that a defendant's subjective understanding matters.

On the actual question, circuits disagree. In the Seventh Circuit, "a defendant's subjective intent does not matter." Pet. App. 27a. Thus, "it is irrelevant" whether the defendant "believed it was violating" the law "and arrived at its 'interpretation'" of the law only

"after the fact." *Id*. at 26a. Here, that rule allowed respondents to escape liability despite robust evidence showing that respondents believed that they were augmenting their revenues by misreporting U&C prices to the government. *See* Pet. 6-9.[2]

After the petition was filed, the Seventh Circuit in *United States ex rel. Proctor v. Safeway, Inc.*, 30 F.4th 649, 658 (7th Cir. 2022), reiterated its rule that it does not matter "whether the relator can point to evidence of the defendant's subjective awareness that its interpretation might be wrong." A dissent argued that the majority's approach will facilitate "many frauds that loot the federal treasury," and called on the court to "overrule" the decision below. *Id*. at 663-64 (Hamilton, J., dissenting). The Seventh Circuit refused. *Id*. at 658 n.10 (majority op.).

The Eleventh Circuit, by contrast, rejects the "conclusion that a finding of scienter can be precluded by a defendant's identification of a reasonable interpretation of an ambiguous regulation that would have permitted its conduct." *United States ex rel. Phalp v. Lincare Holdings, Inc.*, 857 F.3d 1148, 1155 (11th Cir. 2017). Instead, the defendant is liable if it "knew or should have known that its conduct violated a regulation in light of any ambiguity at the time of the alleged violation." *Ibid*. Thus, "the defendant's [subjective] understanding" can support scienter "despite ambiguity in the regulation." *Ibid*.

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[2] Respondents provide their version of the facts. BIO 6-7. This presentation only undermines respondents' argument that such facts don't matter to the scienter inquiry. Instead, the contrasting factual presentations show why scienter should be a jury question.

Respondents take a sentence fragment from *Phalp* out of context to minimize the split. Thus, respondents argue that scienter is negated only if the defendant has "actual knowledge of a different authoritative interpretation." BIO 18 (quoting *Phalp*, 857 F.3d at 1155). This language merely described the erroneous logic of the district court in *Phalp*, which rejected scienter even in that circumstance. But the Eleventh Circuit's rule goes further, requiring defendants facing legal ambiguity "to make a limited inquiry to ensure the claims they submit are accurate." 857 F.3d at 1155-56 (quotation marks omitted).

Respondents argue that an unpublished decision in *Olhausen v. Arriva Medical, LLC*, 2022 WL 1203023 (11th Cir. Apr. 22, 2022), applied *Safeco* to the FCA. *Olhausen*, however, did not hold that a defendant's subjective beliefs are irrelevant. Instead, it held that liability "does not reach an innocent, good-faith mistake about the meaning of an applicable rule or regulation, nor does it reach claims made based on reasonable but erroneous interpretations of a defendant's legal obligations." *See id.* at *2 (quotation marks omitted). A defendant accordingly must have believed its interpretation at the time (either because it held that interpretation in "good faith," or because the claims were "based on" that interpretation). The Seventh Circuit rejects this requirement.

To the extent *Olhausen* diverges from *Phalp*, *Olhausen* is irrelevant because "[u]npublished opinions are not controlling authority." *Bonilla v. Baker Concrete Constr., Inc.*, 487 F.3d 1340, 1345 (11th Cir.

2007).[3] Even if *Olhausen* had been published, the prior decision in *Phalp* would control. *See United States v. Hornaday*, 392 F.3d 1306, 1316 (11th Cir. 2004).

Insofar as respondents regard *Olhausen* as evidence that *Phalp* is consistent with the Seventh Circuit's decisions, that is wrong—as *Phalp* itself makes clear. *See* Pet. 14, 22. Tellingly, although *Olhausen* relied on out-of-circuit precedents, it did not cite this case—which had been out for approximately eight months when *Olhausen* was decided.

Respondents' answer vis-à-vis the Ninth Circuit's precedents is similarly unpersuasive. Respondents do not seriously dispute that the two published cases cited in the petition, *United States ex rel. Oliver v. Parsons Co.*, 195 F.3d 457 (9th Cir. 1999), and *United States v. Mackby*, 261 F.3d 821 (9th Cir. 2001), conflict with the decision below. *See* Pet. 15-16. Instead, respondents cite *United States ex rel. McGrath v. Microsemi Corp.*, 690 F. App'x 551 (9th Cir. 2017), an unpublished decision where the scienter analysis is two sentences long. But although *McGrath* cited *Safeco*, it placed dispositive weight on the fact that the defendant subjectively held its interpretation, in good faith, when it presented claims. *See* 690 F. App'x at 552 (finding no scienter because the defendant's "good faith interpretation . . . at that time was reasonable").

Respondents accuse petitioners of ignoring *United States ex rel. Swoben v. United Healthcare Insurance*

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[3] Respondents argue that whether a decision is published carries no weight. BIO 19. But respondents' cases show only that this Court reviews unpublished decisions. They do not hold that unpublished decisions can erase a circuit split among precedential decisions.

Company, 848 F.3d 1161 (9th Cir. 2016). That case supports petitioners. In *Swoben*, the regulation required the defendant to certify that its data was "accurate, complete, and truthful" based on its "best knowledge, information, and belief." *See id.* at 1166 (citation omitted). The relator alleged that the defendant knowingly submitted skewed data, and therefore falsely certified compliance with this regulation. The Ninth Circuit rejected the defendant's argument that it had behaved reasonably.

In the process, the court held that the good-faith standard under the regulation was "the same standard as the one establishing liability under the False Claims Act—*i.e.*, that it encompasses not only actual knowledge of falsity but also reckless disregard and deliberate ignorance." *Swoben*, 848 F.3d at 1174. In the Ninth Circuit, this standard reaches "what has become known as the 'ostrich' type situation where an individual has buried his head in the sand and failed to make simple inquiries which would alert him that false claims are being submitted." *Ibid*. (quotation marks omitted). Thus, a defendant must "take affirmative steps" to ensure the accuracy and completeness of its data. *Ibid*.

The court accordingly held that when the defendants' data-review processes "were designed in bad faith" to skew the data in the defendants' favor, that supported an inference of scienter. *Swoben*, 848 F.3d at 1176. The defendant's "lack of diligence and an absence of good faith" were relevant to the inquiry. *Ibid*.

The Ninth Circuit also rejected the defendants' argument that "their certifications could not have been knowingly false because their conduct between 2005

and 2012 represented at least an objectively reasonable interpretation of their obligations," and cited *Safeco* in the process. *See Swoben*, 848 F.3d at 1178. But the rest of the decision shows that the Ninth Circuit's *rejection* of that argument cannot be read as an *endorsement* of the Seventh Circuit's extreme rule that the defendant's subjective understanding is irrelevant.

Respondents cite *Hagood v. Sonoma County Water Agency*, 81 F.3d 1465 (9th Cir. 1996). BIO 20. But neither *Hagood* nor any other Ninth Circuit case has ever held that a defendant's subjective understanding is irrelevant to scienter. And the Ninth Circuit has expressly clarified that "*Hagood* does not stand for the proposition that a 'reasonable interpretation' of a regulation precludes falsity." *Oliver*, 195 F.3d at 463.

Respondents argue that the Sixth Circuit's decisions do not conflict with the Seventh's because the Sixth Circuit cases involved assertedly unclear facts, as opposed to unclear law. BIO 22. Not so. In *United States ex rel. Prather v. Brookdale Senior Living Communities, Inc.*, 892 F.3d 822 (6th Cir. 2018), the defendant argued that a finding of scienter was impossible because "no court or Government entity had interpreted the decades-old signature-timing requirement to prohibit the conduct alleged," and the Sixth Circuit itself had been "'left to interpret the regulation's language' in the first instance" during the FCA case. *Prather* Appellee Br., 2017 WL 5495615, at *42-43. The defendant argued that because the Sixth Circuit "interpreted the regulation as a matter of first impression in 2016 . . . there was no way [the defendant] could have known it was violating the regulation in 2011." *Id*. at *43.

That defense is indistinguishable from respondents' argument that there was no authoritative interpretation of U&C pricing vis-à-vis discount programs before the Seventh Circuit's decision in *United States ex rel. Garbe v. Kmart Corp.*, 824 F.3d 632 (7th Cir. 2016). But although the argument worked in the Seventh Circuit, it failed in the Sixth because the defendant took steps to avoid learning whether its conduct violated the regulation and ignored internal warnings that it was noncompliant. *See Prather*, 892 F.3d at 837. In the Sixth Circuit, unlike the Seventh, the defendant's subjective understanding was key to the inquiry. That difference shows a circuit conflict.

Respondents' answer appears to be that because the regulation in *Prather* was clear, the defendant there also would have lost in the Seventh Circuit. But what matters is that this case would have come out differently in the Sixth Circuit. Respondents have not shown otherwise.

Respondents observe that the defendants in the Tenth Circuit cases won. BIO 23. But respondents ignore the court's emphasis on the defendants' subjective understanding of the asserted legal requirements, which the Seventh Circuit deems irrelevant. Respondents have no basis to argue that this case would have come out the same way in the Tenth Circuit—and it would not have. *See* Pet. 18, 23.

Finally, the Fourth Circuit has now changed positions. That court previously agreed with the decision below. *See United States ex rel. Sheldon v. Allergan Sales, LLC*, 24 F.4th 340, 343-44 (4th Cir. 2022). The relator, however, sought rehearing en banc, and the United States filed a brief supporting that petition (as it did in this case). Unlike the Seventh Circuit, the

Fourth Circuit granted the petition and vacated the panel opinion pending rehearing.

Meanwhile, the Fourth Circuit issued another divided opinion regarding FCA scienter, which held that a relator's scienter claim failed when, "[a]s evidence of scienter," the plaintiff "relie[d] almost exclusively on the supposed clarity of" the legal requirement—which was "not as clear as [the plaintiff] claims." *United States ex rel. Gugenheim v. Meridian Senior Living, LLC*, 36 F.4th 173, 179 (4th Cir. 2022). The court found it significant that the relator had not provided "any evidence that Defendants attempted to avoid discovering how the regulation applied . . . or plowed ahead with a dubious interpretation despite serious doubts about its accuracy." *See id.* at 181-82. Thus, *Gugenheim* recognizes, in conflict with the decision below, that a defendant's subjective understanding is relevant.

The record here includes the evidence missing from *Gugenheim*, and so would have come out differently in the Fourth Circuit. That is especially clear because *Gugenheim* itself provoked a dissent arguing that even on the slimmer record in that case, the FCA required the defendant to make more of an inquiry than it did. *See* 36 F.4th at 183-84 (Traxler, J., dissenting).

This split—between circuits that treat subjective understanding as relevant to scienter and circuits that refuse to do so—calls out for this Court's review. The conflict is entrenched because the Seventh Circuit has rejected calls to change its rule. Only this Court can bring uniformity to the law.

II. Respondents' Merits and Policy Arguments Are Not Reasons to Deny Certiorari

In light of the split, this Court should grant certiorari regardless of the merits. If—as petitioners, the government, Senator Grassley, and TAFEF all argued—the Seventh Circuit's decision distorts the FCA's text and the relevant precedents, this Court should grant certiorari to reverse. If the decision below is correct, this Court should affirm. Either way, certiorari is warranted.

Respondents' merits and policy arguments are also wrong. Respondents stress that *Safeco* applies only to ambiguous legal requirements, and not to knowledge of facts. Thus, respondents apparently think that if a defendant believes that its conduct might violate a clear law, the FCA obligates the defendant to conduct an inquiry into the facts—but if a defendant believes that its conduct violates an ambiguous law, it has no obligation to inquire as to what the law means.

This shows why respondents' rule is wrong. The FCA does not have different scienter standards for issues of fact and law. But respondents believe the word "recklessly" simultaneously carries two meanings—requiring further inquiry into ambiguous factual issues, but not legal ones. That cannot be reconciled with the "fundamental rule[] of statutory interpretation" that "a single use of a statutory phrase must have a fixed meaning." *Cochise Consultancy, Inc. v. United States ex rel. Hunt*, 139 S. Ct. 1507, 1512 (2019).

Anyway, respondents' law vs. facts distinction does not help them much. Respondents use this argument to gerrymander away hypotheticals about defendants who deliberately remain ignorant of facts. *See* BIO 34. Yet under respondents' rule, a defendant could correctly believe that it is violating the law—and *want* to violate the law—but escape liability if the defendant's lawyers later concoct an interpretation that permits the defendant's conduct. Pet. 2-3, 28. That result is just as absurd as a defendant that refuses to learn facts. It discredits any rule that would produce it.

Respondents' contention that their interpretation does not conflate the FCA's three scienter requirements is likewise wrong. Their argument depends on two contested propositions: (1) that recklessness is purely objective; and (2) that if they defeat recklessness, they necessarily defeat actual knowledge and deliberate ignorance. However, recklessness has a subjective component (awareness of risk). *See* Pet. 29. Independently, the other two scienter standards are not subsets of recklessness; they are distinct concepts directed at different states of mind—so even if respondents were not reckless, that does not mean, *a fortiori*, that they did not act with actual knowledge or deliberate ignorance. *See* Pet. 28-29; Grassley Amicus Br. 4-10, 15-16.

Respondents' interpretation also conflicts with this Court's precedents. Respondents argue that *Heckler v. Community Health Services of Crawford County, Inc.*, 467 U.S. 51 (1984), was not about the FCA. BIO 32. But neither was *Safeco*. As between the two cases, *Heckler*—which was about the obligations of parties

seeking public funds from government health care programs to inform themselves of the law and to conform their conduct to it—is far closer to being on point.

Respondents' treatment of *Halo Electronics Inc. v. Pulse Electronics, Inc.*, 579 U.S. 93 (2016), is *egregious*. This Court explained that scienter inquiries are context-dependent, so that even if subjective bad faith is irrelevant "in considering whether there had been a knowing or reckless violation of the Fair Credit Reporting Act," it is dispositive for enhanced damages in the patent infringement context. *See id*. at 106 n.*. Respondents argue that this footnote means the opposite of what it says. BIO 33 (arguing that *Halo* "reaffirmed *Safeco's* objective standard for 'knowing or reckless violation[s]' and reiterated *Safeco*'s holding that a 'showing of bad faith was not relevant absent a showing of objective recklessness.'") (quoting 579 U.S. at 106 n.*). As *Halo* makes clear, this Court rejected respondents' rule. *See* 579 U.S. at 105-06.

Finally, the practical consequences of allowing the decision below to stand will be significant. Pet. 23-27. The Court need not take our word for it. Multiple amici have filed in support of the petition, and the government has already highlighted the importance of this issue in multiple circuit courts. Nothing has undermined those statements, but if the Court wants confirmation, it can invite the Solicitor General's views.

CONCLUSION

Certiorari should be granted.

Respectfully submitted,

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