NO. 21-1326

In the
Supreme Court of the United States

UNITED STATES OF AMERICA EX. REL.
TRACY SCHUTTE AND MICHAEL YARBERRY,

Petitioners,

v.

SUPERVALU INC., et al.,

Respondents.

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

RESPONDENTS' SUPPLEMENTAL BRIEF

JAMES F. HURST
ANDREW A. KASSOF
BRENTON ROGERS
NICHOLAS M. RUGE
KIRKLAND & ELLIS LLP
300 North LaSalle
Chicago, IL 60654

JOHN C. O'QUINN
Counsel of Record
KIRKLAND & ELLIS LLP
1301 Pennsylvania Ave., NW
Washington, DC 20004
(202) 389-5000
john.oquinn@kirkland.com

Counsel for Respondents

December 20, 2022

TABLE OF CONTENTS

INTRODUCTION 1

I. The Seventh Circuit's Decision Is Correct..... 3

A. The Seventh Circuit's Modest Decision Does Not Hold Subjective Bad Faith Is Irrelevant To Scienter Under The FCA..... 3

B. The Seventh Circuit Properly Applied *Safeco*'s Reasoning To The FCA. 6

II. The Decision In This Case Does Not Warrant Review. 8

A. The Government's Parade Of Horribles Is Unavailing (But Does Illustrate The Breadth Of Its Position). 8

B. The Government Fails To Show A Circuit Split. 10

C. This Case Is A Poor Vehicle. 11

CONCLUSION 13

TABLE OF AUTHORITIES

Cases

Page(s)

Buffington v. McDonough,
143 S.Ct. 14 (2022) 9

Comm'r v. Acker,
361 U.S. 87 (1959) 9

Halo Electronics Inc.
v. Pulse Electronics, Inc.,
136 S.Ct. 1923 (2016) 7

Intel Corp. v. Sulyma,
140 S.Ct. 768 (2020) 5

Safeco Ins. Co. of Am. v. Burr,
551 U.S. 47 (2007) ..... *passim*

Screws v. U.S.,
325 U.S. 91 (1945) 5

U.S. ex rel. Complin v. N.C. Baptist Hosp.,
818 F.App'x 179 (4th Cir. 2020) 11

U.S. ex rel. Gugenheim
v. Meridian Senior Living, LLC,
36 F.4th 173 (4th Cir. 2022) 11

U.S. ex rel. McGrath v. Microsemi Corp.,
690 F.App'x 551 (9th Cir. 2017),
cert. denied, 138 S.Ct. 407 (2017) 11

U.S. ex rel. Purcell v. MWI Corp.,
807 F.3d 281 (D.C. Cir. 2015),
cert. denied, 137 S.Ct. 625 (2017) 2, 8

U.S. ex rel. Sheldon v. Allergan Sales, LLC,
24 F.4th 340 (4th Cir.),
vacated on reh'g en banc,
49 F.4th 873 (4th Cir. 2022) 8, 11

U.S. ex rel. Swoben v. UHI Co.,
848 F.3d 1161 (9th Cir. 2016) 10

U.S. v. Lanier,
520 U.S. 259 (1997) 8

Universal Health Servs.
v. U.S. ex rel. Escobar,
579 U.S. 176 (2016) 8, 10

Statutes

35 U.S.C. §284 7

42 U.S.C. §1395w-111(i) 12

Regulations

42 C.F.R. §447.512(b)(2) 13

Other Authorities

Prosser, *Handbook of the Law of Torts*
(4th Ed. 1971) 7

INTRODUCTION

The government's brief sensationalizes the facts, mischaracterizes the Seventh Circuit's decision, identifies no actual circuit split (relying on snippets from cases that do not address the question presented), and conjures a parade of horribles that has not materialized in the decade in which courts have applied the *Safeco* standard to the False Claims Act (FCA). That is lamentable but perhaps understandable given the government's financial interest in this case, as well as in expanding the FCA's reach to conduct that was allegedly erroneous but *objectively reasonable* at the time it occurred, where falsity turns on an ambiguous legal obligation.

The issue in this case is not—as the government would have it—whether "the Seventh Circuit erred in holding that subjective bad faith is never sufficient to establish scienter under the FCA," (U.S.Br.9), because the Seventh Circuit held no such thing. All the Seventh Circuit held is a party cannot knowingly violate (or be deliberately ignorant of) an *ambiguous legal obligation* for which there has been no authoritative guidance. That should be obvious. As Judge St. Eve succinctly put it, a "defendant might suspect, believe, or intend to file a false claim, but it cannot *know* that its claim is false if the requirements for that claim are unknown." Pet.App.21a (original emphasis). To be sure, a party can still *recklessly* violate an ambiguous obligation—when no reasonable interpretation of the ambiguous obligation would permit the party's conduct. But conversely, if the conduct was consistent with an interpretation a court reasonably could have adopted, and there was no

authoritative guidance to the contrary, such *objectively reasonable* conduct cannot be actionable under the FCA—with no need to inquire into subjectively-held views.

That unremarkable proposition applies narrowly to limited circumstances where falsity is predicated on *ambiguous legal requirements*—not facts. As the Solicitor General previously advocated in *Safeco* (in which the government had no financial stake), that is the proper approach where falsity turns on a "legal question … of first impression … not settled by statutory text, formal agency guidance, or case law." U.S. Amicus Br., *Safeco*, 2006 WL 3336481, *8 ("U.S.*Safeco*.Br."). That is the approach this Court adopted in *Safeco*; it is consistent with every circuit to decide the issue; and it vindicates the constitutional requirement of notice before a party may be punished. At the same time, *Safeco* does not restrict the panoply of regulatory or restitutionary remedies available to the government if a party's reasonable conduct was erroneous.

In all events, none of this Court's usual criteria for granting certiorari is present. Tellingly, the government is 18 pages in before asserting a circuit split, and then cannot point to any circuit actually adopting its position. Instead, the uniform rule is that acting reasonably when faced with an ambiguous legal obligation is not fraud. The circuits have applied that rule to the FCA for a decade, at least since Judge Rogers' decision for the D.C. Circuit in *U.S. ex rel. Purcell v. MWI Corp.*, 807 F.3d 281 (D.C. Cir. 2015), *cert. denied*, 137 S.Ct. 625 (2017), in which now-Justice Kavanaugh joined. Nor is there any issue of

great public importance—the sky has not fallen since.

This case is also a poor vehicle to indulge the government's opportunism. The obligations at issue do not turn on a singular federal-law standard, but instead were overwhelmingly a matter of private contracts that were admittedly not uniform. Although some were ambiguous, others expressly permitted price-matching without affecting so-called "usual and customary" (U&C) prices. Likewise, several state Medicaid agencies confirmed price-matching did not alter U&C prices. While that highlights the reasonableness of Supervalu's conduct, it also demonstrates there is no controlling definition at issue, let alone one this Court could use in the manner the Solicitor General invites. U.S.Br.23.

The petition should be denied.

I. The Seventh Circuit's Decision Is Correct.

A. The Seventh Circuit's Modest Decision Does Not Hold Subjective Bad Faith Is Irrelevant To Scienter Under The FCA.

The government's brief, like the dissent on which it draws, "fundamentally misapprehends" the Seventh Circuit's holding and *Safeco*. Pet.App.21a. The government presents a (different) gerrymandered question (highlighting how context-specific the issue is) and then asserts the Seventh Circuit categorically held "a defendant's subjective state of mind is 'irrelevant' under the FCA," (U.S.Br.13), and proceeds to attack that strawman. The Seventh Circuit did nothing of the sort.

First, the decision below—like *Safeco*—is limited to circumstances where a defendant is alleged to have

some degree of knowledge it is violating an *ambiguous legal obligation*. As *Safeco* held, a defendant cannot be deemed "a knowing *or* reckless violator" of a legal obligation if that obligation "allow[s] for more than one reasonable interpretation" and the defendant acted consistent with "one such [reasonable] interpretation." *Safeco Ins. Co. of Am. v. Burr*, 551 U.S. 47, 70 & n.20 (2007). Further, as the Seventh Circuit held, *Safeco* applies only when a defendant "cannot *know* that its claim is false [because] the requirements for that claim are unknown." Pet.App.21a. In those circumstances, a defendant cannot—as a matter of law—"know" (or be "deliberately ignorant" of) a legal obligation, precisely because it is unsettled.

Safeco held conduct can nonetheless potentially be *reckless* (the most capacious form of scienter) if it was not objectively reasonable. But, as the Solicitor General previously (successfully) advocated, recklessness "in the civil context" requires "*objective*" unreasonableness. U.S.*Safeco*.Br.*22. The government explained when "the recklessness standard is framed in terms of compliance with the law, and the statutory standard itself is not necessarily well-established," "courts must undertake an *objective inquiry* to determine whether the defendant's conduct reflected a colorable interpretation of the law." *Id.* In such circumstances, reckless disregard "requires violation of clearly established law or indifference to an objectively high and obvious risk of unlawfulness"—analogous to qualified immunity. U.S.*Safeco*.Br.*23. That is, in the government's words, a "purely legal inquiry into … objective recklessness" and courts should not

"collapse[] the objective and subjective components of recklessness into a single inquiry." *Id.* at *24.

This distinction between objective and subjective inquiries for recklessness is deeply rooted in common law. U.S.*Safeco*.Br.*20-24. But it would have been meaningless in *Safeco* if the same subjective evidence would have supported a finding of *actual knowledge* or *deliberate ignorance*, as the government now advocates. There would have been no need to address recklessness in the first place if a "defendant acts with 'actual knowledge'" when it subjectively believes "it is violating" an "ambiguous legal condition[]." U.S.Br.11. Instead, it was understood a defendant "cannot *know*" it is committing a violation when the law is ambiguous. Pet.App.21a. As this Court explained, "actual knowledge" means "knowledge that is actual"—"existing in fact or reality"—and "not merely a possible inference from ambiguous circumstances." *Intel Corp. v. Sulyma*, 140 S.Ct. 768, 775 (2020). Whatever a defendant subjectively believed, "willful conduct cannot make definite that which is undefined." *Screws v. U.S.*, 325 U.S. 91, 105 (1945). Regardless, given the mine-run of FCA cases involve settled law or factual knowledge (or both), *Safeco*'s reasoning and the Seventh Circuit's holding are inapplicable in most circumstances. U.S.*Safeco*.Br.*22 (distinguishing "well-established duties").

Second, the Seventh Circuit did not hold subjective intent is categorically "irrelevant" even where scienter turns on ambiguous legal obligations. Rather, as the government advocated in *Safeco*, if the alleged conduct is objectively unreasonable (or inconsistent with authoritative guidance), then

subjective intent matters. "Only if the defendant's failure to comply with the law was objectively reckless would it become necessary for a court to probe … the defendant's subjective good faith." U.S.*Safeco*.Br.*23. So too here. The Seventh Circuit made clear its holding reflects only the FCA's "baseline requirement" for recklessness; a "scienter floor." Pet.App.15a. Once satisfied, courts proceed to discovery or trial on subjective intent.

Although the government highlights snippets from a voluminous record (many merely showing Supervalu trying to ensure price-matches did not affect its U&C prices) and a subset of specific drug sales in a single year (not overall drug sales), it does not challenge the *reasonableness* of Supervalu's conduct. Instead, the government contends defendants should face treble-damages liability for conduct that was *objectively reasonable* at the time, based solely on whatever a jury might be convinced about a defendant's *subjective* views regarding ambiguous legal obligations. That is not the law in any circuit and this Court should decline to make it so.

B. The Seventh Circuit Properly Applied *Safeco*'s Reasoning To The FCA.

The government's attempt to cabin *Safeco*'s reasoning to the Fair Credit Reporting Act (FCRA) is unavailing.

First, the government asserts that the scienter provisions of the FCA and FCRA "contain significantly different language." U.S.Br.15. That is a distinction without a difference. *Safeco* first determined whether the FCRA *also* reached recklessness (as the FCA expressly does). Then, its relevant holding applied to

both "knowing" and "reckless" violations, applying general common-law principles. 551 U.S. at 70 & n.20.

Second, the government argues *Safeco* derived its meaning for recklessness from a different branch of the common law—"physical safety" of consumers—rather than the "distinct tort" of fraudulent misrepresentation. U.S.Br.15. But *Safeco* recited the "general[]" understanding of recklessness "in the sphere of civil liability." 551 U.S. at 68; U.S.*Safeco*.Br.*11; Prosser, *Handbook of the Law of Torts*, §34, 185 (4th Ed. 1971).

Third, the government repeats petitioners' arguments about *Halo Electronics Inc. v. Pulse Electronics, Inc.*, 136 S.Ct. 1923 (2016), while ignoring Supervalu's response. BIO.32-33. The government's description of *Halo* makes clear it concerned alleged violations of clearly-established law and *factual* knowledge. U.S.Br.16. Regardless, *Halo* involved 35 U.S.C. §284, which provides for enhancement but has no express scienter standard. Willful infringement had historically been required for enhancement and, as *Safeco* acknowledged, "willfully" is a "word of many meanings whose construction is often dependent on the context in which it appears." 551 U.S. at 57. In the historical context of patent law, "bad-faith infringement" was a sufficient basis for enhancement. *Halo*, 136 S.Ct. at 1930. Those patent-specific concepts do not inform the "general[]" common-law standard the FCA incorporates and *Safeco* interpreted.

II. The Decision In This Case Does Not Warrant Review.

A. The Government's Parade Of Horribles Is Unavailing (But Does Illustrate The Breadth Of Its Position).

Despite a decade of precedent applying *Safeco* to the FCA, the government warns this decision "could significantly disrupt government programs involving everything from medical insurance to military equipment," U.S.Br.22, without pointing to any example over the past decade. The FCA, however, "is not an all-purpose antifraud statute" and not a substitute for regulatory enforcement. *Universal Health Servs. v. U.S. ex rel. Escobar*, 579 U.S. 176, 194 (2016). Applying *Safeco* does not leave the government without regulatory or contractual remedies where a defendant has erred (even reasonably).

The government's real complaint is the FCA may be unavailable in some cases unless the government proactively clarifies regulatory ambiguities. U.S.Br.22. That is a virtue, not a vice. As Judges Rogers and Wilkinson observed, "it is not too much" to ask the government to speak clearly when establishing rules it enforces with punitive liability. *Purcell*, 807 F.3d at 291; *U.S. ex rel. Sheldon v. Allergan Sales, LLC*, 24 F.4th 340, 344, *vacated on reh'g en banc*, 49 F.4th 873 (4th Cir. 2022). That opens no floodgates: Courts can discern when a "rule already identified in the decisional law may apply with obvious clarity to the specific conduct in question, even though the very action in question has not previously been held unlawful." *U.S. v. Lanier*, 520 U.S. 259, 271 (1997).

By contrast, in the Solicitor General's America, parties whose activities touch government transactions would need to affirmatively seek "clarification" (read: permission) from the government when the law is ambiguous. U.S.Br.16, 22-23. Given the ubiquity of the government in everyday life (here prescriptions for private patients, reimbursed by private PBMs, which only sometimes represent government-backed insurance plans), the threat of treble damages and crushing penalties is expansive. That *in terrorem* effect enables the government to coerce compliance with its views of ambiguous laws, rather than promulgate judicially-reviewable guidance. The government's invocation of "administrative complexity," U.S.Br.22, to shift risks from ambiguity onto private parties, is a problem of the government's own making.

Shifting the burden to private parties to "seek[] clarification" when the government has failed to clarify ambiguities is exactly backwards. U.S.Br.22.[1] In our system, due process requires that the government give fair notice before punitive measures like the FCA can be brought to bear. *Comm'r v. Acker*, 361 U.S. 87, 91 (1959) ("[O]ne 'is not to be subjected to a penalty unless the words of the statute plainly impose it.'"); *Buffington v. McDonough*, 143 S.Ct. 14, 19 (2022) (Gorsuch, J., dissenting from denial of cert.) ("Traditionally, too, our courts have long understood that, 'as between the government and the individual, the benefit of the doubt' about the meaning of an

[1] It is also illusory. Supervalu sought clarification from several state Medicaid agencies. R.172-26,27; R.174-112,113. The government says it should have asked more. U.S.Br.6.

ambiguous law must be 'given to the individual, not to authority; for the state makes the laws.'"). *Escobar* made clear that "concerns about fair notice and open-ended liability" under the FCA would be policed "through strict enforcement of the Act's materiality and scienter requirements." 579 U.S. at 192. Applying *Safeco* does just that.

B. The Government Fails To Show A Circuit Split.

As Supervalu demonstrated, BIO.15-25, there is no split. When the government finally reaches this issue, it does not embrace petitioners' characterization of most cases and has little to say other than piecing together snippets it likes, while failing to engage with Supervalu's opposition. What the government calls "disagreement in the courts of appeals" merely reflects the bounds of *Safeco*'s narrow holding, as *applied to specific facts*. U.S.Br.18. And the cases the government does cite do not map onto the question framed by the government.

Regardless, Supervalu explained at length why *Phalp*, *Prather*, and *Chen* are consistent with the decision here. BIO.17-22. The government deflects rather than respond. It says the Court should ignore the Eleventh Circuit's decision in *Olhausen* because it is unpublished. U.S.Br.19 n*.[2] It then relies on an unpublished Ninth Circuit decision, without acknowledging the subsequent *precedential* decision applying *Safeco* to the FCA. U.S.Br.20*; *U.S. ex rel.*

[2] *Olhausen* contradicts the government's reading of *Phalp*, since the panel (Judges Wilson, Rosenbaum, and Covington (by designation)) were bound by, cited, and applied *Phalp*. BIO.18.

Swoben v. UHI Co., 848 F.3d 1161, 1178 (9th Cir. 2016); *cf. U.S. ex rel. McGrath v. Microsemi Corp.*, 690 F.App'x 551, 552 (9th Cir. 2017), *cert. denied*, 138 S.Ct. 407 (2017).

The government's approach to Fourth Circuit law is similar. It argues the "governing law there [is] uncertain" because it was unable to sway the *en banc* court in *Sheldon* to its view. U.S.Br.22. An evenly divided court does not manufacture a split. And the government fails to acknowledge other Fourth Circuit authority applying *Safeco*'s reasoning. *U.S. ex rel. Gugenheim v. Meridian Senior Living, LLC*, 36 F.4th 173, 181 (2022); *U.S. ex rel. Complin v. N.C. Baptist Hosp.*, 818 F.App'x 179, 184 (2020). Absent further developments, *Gugenheim* remains "governing law" in the Fourth Circuit.

If the government's position has merit, it may yet convince a circuit to adopt it, and this Court will have the benefit of appellate opinions on both sides of the issue. As it is, the most the government can do is extract snippets from opinions that are consistent with the decision below and provide little guidance for this Court were certiorari granted.

C. This Case Is A Poor Vehicle.

Finally, although the government submits "[t]his case provides an appropriate vehicle" to decide the question presented, U.S.Br.23, the opposite is true. That is because there is no single controlling federal-law definition of "usual and customary" pricing under which to assess the "defendant's contemporaneous subjective understanding or beliefs" for purposes of determining whether the defendant "'knowingly' violated the [FCA]." Pet.i.; U.S.Br.23. The Court

would have to consider reasonableness when there is no single controlling obligation (let alone a federal one). That would be cumbersome at best and create confusion for future application of guiding principles. *See* No. 22-111 Safeway BIO.30-34.[3]

The disconnect arises from the unusual posture in which scienter was litigated below. Petitioners convinced the district court (over defendants' objections, *see* Supervalu CA7 Br.23 & n.5) that federal law establishes a single, uniform federal definition of "usual and customary prices" to establish falsity. BIO.10-11. Federal law does nothing of the sort: there is no single meaning, much less a federal one—just the opposite.

Federal law *prohibits* such a federal definition; Congress left that to private contracting. 42 U.S.C. §1395w-111(i) ("Noninterference": government "may not … institute a price structure"). The meaning of U&C price is the product of private negotiation between pharmacies and PBMs, varying from contract-to-contract. Some affirmatively said price-matching did not affect U&C price. BIO.8-9; R.174-26, R.176-28. Others were silent, including the one the government identifies (quoting an email the contractual counterparty rescinded). U.S.Br.5; Supervalu CA7 Br.15-16.[4]

---

[3] The phrase "usual and customary" is a misnomer. The contracts at issue exclude most transactions: those involving insurance payments (private or government). Supervalu CA7 Br.16-17. Despite the terminology, U&C is not a price usually or customarily charged (in ordinary parlance).

[4] This case is principally about contractual interactions with PBMs under *Medicare Part D*. Relators asserted limited

The government nonetheless urges that this Court could "hold that petitioners' evidence would allow a reasonable jury to conclude that respondents 'knowingly' misreported their 'usual and customary' prices by excluding … price-match[es]." U.S.Br.23. It is unclear how this Court could do so without wading through these differing definitions. Were the Court to grant review, the issue of whether the conduct was even inconsistent with those myriad contractual definitions would inevitably be raised at the merits stage—meaning the Court might never reach the question presented. The lack of one (federal) standard and the factual complexity here make this a poor vehicle.

CONCLUSION

The petition should be denied.

Respectfully submitted,

JAMES F. HURST, P.C.
ANDREW A. KASSOF, P.C.
BRENTON ROGERS, P.C.
NICHOLAS M. RUGE
KIRKLAND & ELLIS LLP
300 North LaSalle
Chicago, IL 60654

JOHN C. O'QUINN, P.C.
Counsel of Record
KIRKLAND & ELLIS LLP
1301 Pennsylvania Ave., NW
Washington, DC 20004
(202) 389-5000
john.oquinn@kirkland.com

Counsel for Respondents

December 20, 2022

Medicaid-related claims. Although 42 C.F.R. §447.512(b)(2) mentions U&C, it does not define it, leaving it to state agencies.