No. 22-111

IN THE

Supreme Court of the United States

UNITED STATES OF AMERICA, ET AL.,
EX REL. THOMAS PROCTOR,

Petitioner,

v.

SAFEWAY, INC.

Respondent.

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

REPLY BRIEF FOR PETITIONER

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REPLY BRIEF FOR PETITIONER

In each and every case in which the question presented is dispositive, the defendant broke the law by presenting false claims for payment, or making or using false statements or records that are material to false claims. The question is whether the defendant should nevertheless keep its ill-gotten gains because it can identify a reasonable interpretation of the law that would have permitted its conduct.

On that point, petitioner does not dispute that a defendant that sincerely held an erroneous belief about the law has a viable defense. Of course, the defendant's sincerity would seldom go uncontested, and so the matter would typically have to be resolved by a jury. But if the jury believed the defendant's story, and determined that the defendant made an innocent mistake or acted only negligently, the defendant should win. Thus, the issue is not about—and has never been about—protecting defendants that try their best to conform their conduct to the law, but come up short.

Instead, the issue concerns an altogether different fact pattern, where a defendant that broke the law—and does not show that it was acting in good faith at the time—seeks to prevail merely by showing that its unlawful conduct can be shoehorned (after the fact) into an "objectively reasonable" interpretation of the relevant legal requirement that has not been specifically foreclosed by authoritative guidance. That is the outcome the Seventh Circuit's rule requires. It is flatly wrong, and inconsistent with other appellate decisions that determine scienter by evaluating the defendant's subjective understandings and beliefs at the time it broke the law.

This issue goes to the heart of the False Claims Act (FCA) and is undeniably important. This Court has already called for the views of the Solicitor General in a case presenting this question. *See United States ex rel. Schutte v. SuperValu, Inc.*, No. 21-1326. Although the parties in that case and this one differ, counsel for both sides are the same, the legal issues largely overlap, and the briefing in both is quite similar. The best course would be to hold this case and consider both petitions together. When the time comes, this Court should grant certiorari in both cases, or grant certiorari in one and hold the other.

I. The Circuits Are Divided Over the Question Presented

The petition explained that there is a split between circuits that regard a defendant's subjective understanding and beliefs as central to the scienter inquiry, and courts that deem those same facts irrelevant. Pet. 13-18. Most of respondent's split arguments are addressed comprehensively in the briefing in *Schutte*, and there is little need to revisit those points here. Instead, we focus on the few differences raised in this case.

First, as in *Schutte*, respondent elides the real conflict, arguing that the circuits all apply *Safeco Insurance Company of America v. Burr*, 551 U.S. 47 (2007), to the False Claims Act. BIO 15-16. But here, as in *Schutte*, the question isn't whether *Safeco* is relevant precedent. 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. 17-18 (anticipating respondent's argument and refuting it). On the contrary, many courts cite *Safeco* as relevant precedent *and* hold that a defendant's subjective understanding matters, such that if a defendant did not believe it was acting lawfully, it can be held liable.

Respondent argues that the Seventh Circuit doesn't hold that a defendant's subjective beliefs are irrelevant to scienter; but instead holds only that those beliefs are "irrelevant to addressing the question *Safeco* asks," and that the defendant's subjective beliefs become relevant if the *Safeco* "floor" is cleared. BIO 17. This is a distinction without a difference because once the floor is cleared, *i.e.*, once it is determined that the defendant's conduct was objectively unreasonable, the plaintiff doesn't need to prove anything else to establish recklessness—and nothing the defendant shows will cause it to win. In other words, saying that the floor has been cleared is another way of saying the scienter element is satisfied—and no further inquiry is warranted. Accordingly, the Seventh Circuit's rule is tantamount to holding that the defendant's subjective understanding and beliefs are irrelevant to the only scienter inquiry that matters.

The discussion of the other circuits' rules is addressed in the *Schutte* briefing, which addresses respondent's efforts to minimize the split. Recent developments in the Fourth Circuit, however, deserve extra attention. When the petition was filed, the Fourth Circuit had taken the issue *en banc*. *See United States ex rel. Sheldon v. Allergan Sales, LLC*, 2022 WL 1467710,

at *1 (4th Cir. May 10, 2022). After hearing oral argument—where the relator and the United States took the same position as petitioner here, and the defendant took the same position as respondent here—the Fourth Circuit's judges split seven-to-seven, issuing no opinion. *See United States ex rel. Sheldon v. Allergan Sales, LLC*, 49 F.4th 873, 874 (4th Cir. 2022).

In effect, the full court threw up its hands, and now the law in the Fourth Circuit will likely depend on which appellate panel the next parties litigating this question happen to draw. Until then, Fourth Circuit precedent conflicts with the decision below. *See* Pet. 15-16. But the Fourth Circuit's inability to reach consensus—or even a majority view—despite its recognition of the issue's importance shows that this question will continue to roil the courts of appeals until this Court resolves it.

Indeed, as of now, dozens of federal appellate judges have weighed in on the question presented. Although petitioner and respondent disagree about which side some of those judges fall, it is undeniable that at least eight (the seven votes for the plaintiff in *Sheldon*, and the dissent in this case) disagree with the decision below. A fairer count is that more than a dozen appellate judges (including the judges in the other circuit court opinions identified in the petition) have concluded that the Seventh Circuit's rule is wrong. That is more than enough disagreement to justify this Court's immediate review.

II. The Decision Below Is Incorrect

1. In light of the split, this Court should grant certiorari regardless of its sense of the merits. Respond-

ent's merits arguments in this case are also particularly weak. The petition cited two important cases from this Court: *Halo Electronics Inc. v. Pulse Electronics, Inc.*, 579 U.S. 93 (2016), which rejected the proposition that subjective intent ought to be irrelevant for scienter purposes; and *Heckler v. Community Health Services of Crawford County*, *Inc.*, 467 U.S. 51 (1984), which explained that when private parties seek reimbursement from the government (specifically Medicare), it is their obligation to confirm the validity of their claims before presenting them—and not the government's obligation to address every potential ambiguity. Pet. 4, 22-23. Respondent does not even mention these cases, but they show why importing respondent's version of the *Safeco* standard to this context makes no sense: this is an area where parties who claim money that they subjectively believe they are not owed have always been held accountable.

This case also shows just how extreme the Seventh Circuit's rule is. Here, as in *Schutte*, the underlying issue is whether respondent accurately reported its "usual and customary" (U&C) prices for certain prescription drugs when it reported its higher "retail" prices instead of its "discount" prices—even when those discounts affected the majority of cash sales for those drugs. The court of appeals recognized that the answer is "no," *i.e.*, that respondent's reports were false because they omitted discount prices available to the general public, thus causing the government to pay more for drugs than it should have. *See* Pet. App. 16a (explaining that "all agree that . . . reporting a pharmacy's retail price as its U&C price would satisfy the FCA's falsity prong"). Moreover, petitioner catalogued

many instances in which third parties advised respondent that its practices were illegal—and evidence also emerged that respondent designed the program specifically to be deceptive and opaque to the government. *See* Pet. 6-9 (cataloguing evidence). The court nevertheless held that respondent did not act knowingly *as a matter of law* because the government had not specifically addressed the kinds of discounts respondent offered (price-matching, and discount clubs that required customers to fill out an enrollment form to join) in sufficiently authoritative documents.

The resulting opinion is notable for its brazenness. For example, all parties recognized that when respondent operated a program like Wal-Mart's, which offered generic drugs to all members of the general public for $4, it had to report $4 as the U&C price. *See* Pet. App. 6a. Respondent then replaced that program with a "discount club" program—under which it continued to offer generic drugs to the general public for $4 for a 30-day supply, $8 for a 60-day supply, and $12 for a 90-day supply. *Id*. at 6a-7a. The only real difference between the discount club program and the $4 generics program is that customers had to enroll. But "[t]here was no enrollment fee, and the enrollment form provided no meaningful information to Safeway." *Id.* at 7a. The Seventh Circuit thus acknowledged that the barrier to entering the club was "minimal." *Id*. at 17a.

Here is the kicker: the Seventh Circuit went so far as to recognize that "Safeway effectively used its enrollment forms as a fig leaf to disguise a Wal-Mart-style generics program without reporting those prices as U&C." Pet. App. 17a. But despite that recognition,

the court held that respondent was entitled to judgment as a matter of law on the issue of scienter. In effect, the Seventh Circuit has invited lawbreakers to later concoct some "fig leaf" justification for their misconduct—assuring them that if they do so, they can escape liability. That result is absurd.

2. Respondent does not seriously grapple with any of that. Instead, respondent argues that because recklessness is an objective inquiry under the common law, the FCA's incorporation of recklessness means that FCA scienter should be purely objective. BIO 24-25. There are multiple obvious problems with this. First, even if it is the correct description of recklessness in this context, the FCA's scienter standard isn't limited to recklessness, but also includes deliberate ignorance and actual knowledge, neither of which is a purely objective inquiry. *See* 31 U.S.C. § 3729(b)(1). Under those standards, a defendant that either believes it is violating the law or that refuses to learn the correct interpretation of the law acts with scienter no matter what recklessness means.

Second, respondent's description of a monolithic recklessness standard is inconsistent with *Safeco* itself, where the Court explained that "the term recklessness is not self-defining." *Safeco*, 551 U.S. at 68 (quotation marks omitted). In the FCA context, there is clear evidence that when Congress spoke of constructive knowledge, it intended specifically to reach defendants "who ignore 'red flags'" suggesting that their claims are false. H.R. Rep. No. 99-66, at 21 (1986). Congress further explained that "the civil False Claims Act should recognize that those doing business with the Government have an obligation to

make a limited inquiry to ensure the claims they submit are accurate"—and a company that fails to undertake such basic diligence should be held to account. S. Rep. No. 99-345, at 7 (1986). And this Court explained in *Heckler* that companies claiming government funds are "held to the most demanding standards," and "are expected to know the law," including by seeking "an interpretation of the applicable regulations" when confronted with doubt. 467 U.S. at 63-64.

Third, common law recklessness incorporates not only objectively high risks of harm, but also subjectively known risks of harm. *See, e.g.*, *Safeco*, 551 U.S. at 68 (explaining that common law recklessness covers "action entailing an unjustifiably high risk of harm that is either known or so obvious that it should be known") (quotation marks omitted). When a defendant knows or should know that the government disagrees with its view of the applicable regulation, but presents claims or makes statements that are inconsistent with the government's understanding, the defendant acts recklessly. And nothing in the common law suggests that the defendant can only be placed on notice of the government's interpretation by specific, authoritative guidance in the form of regulations having the force of law, or appellate court decisions. Myriad sources, including informal advice from public and private sources, can place the defendant on notice and compel it to take an inquiry before claiming public funds.

3. Respondent argues that unless and until authoritative guidance fixes the meaning of the law, there is no such thing as a "correct" interpretation at all, and so a defendant cannot "know" that its claims are false before that time. BIO 27-28. The Seventh Circuit likewise embraced this proposition in *Schutte*,

holding that "[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." *United States ex rel. Schutte v. Supervalu Inc.*, 9 F.4th 455, 468 (7th Cir. 2021).

This argument rests on far too narrow an understanding of what it means to "know" something in the fraud context. As the Restatement of Torts explains, misrepresentations are fraudulent if the maker "knows or believes that the matter is not as he represents it to be," "does not have the confidence in the accuracy of his representation that he states or implies," or "knows that he does not have the basis for his representation that he states or implies." Restatement (Second) of Torts § 526. And "[t]he word 'fraudulent' is here used as referring *solely to the maker's knowledge of the untrue character of his representation. This element of the defendant's conduct frequently is called 'scienter' by the courts.*" *Id*. § 526 cmt. a (emphasis added). Thus, ordinary common law fraud principles—which plainly inform the FCA's scienter standard—establish that if the defendant acts with a belief that it is doing wrong, that is sufficient to establish scienter, even if the defendant is not metaphysically certain that it is in the wrong.

The bottom line is that the Seventh Circuit's rule allows a defendant who wants to break the law, and who actually breaks the law, to get away with it if the defendant's lawyers can later invent a "reasonable interpretation" that the defendant could have adopted (but did not) to justify the misconduct. That is outrageous, and this Court should not countenance it.

III. This Case Is a Suitable Vehicle to Decide the Question

Respondent argues that this case and *Schutte* are bad vehicles to decide the question presented because there was no single federal definition of U&C prices during the relevant time period. BIO 31. This is a straw argument. First, in this case, as the Seventh Circuit noted, "[t]he parties agree that the U&C price of a prescription drug generally refers to the cash price charged to the general public." Pet. App. 4a (quotation marks omitted). The court further explained that "it is now settled in this circuit that pharmacies should report [discount-program] prices as U&C." *Ibid*. Moreover, all parties agree that after the Seventh Circuit's decision in *United States ex rel. Garbe v. Kmart Corp.*, 824 F.3d 632 (7th Cir. 2016), "reporting a pharmacy's retail price as its U&C price would satisfy the FCA's falsity prong." Pet. App. 16a. Thus, for purposes of this appeal, there is an agreed definition of U&C prices, and a further agreement that respondent's practice, which was to report its infrequently charged "retail" prices, contravenes that definition.

Even if petitioner accepts for purposes of this appeal that respondent's practice was not foreclosed by controlling law prior to *Garbe*, that doesn't make this case a bad vehicle. In fact, it tees up the question perfectly, because it allows the Court to consider the scienter issue in the factual context in which it will most often arise: the defendant had lots of reasons to think that its interpretation was wrong, but there was no on-point appellate case or federal regulation explicitly foreclosing that interpretation.

In any event, whether there was a single federal definition of U&C prices is completely irrelevant to the question presented (which is about how FCA scienter works)—and is indeed irrelevant to the resolution of this case because the ultimate question is not whether respondent violated a single federal definition of U&C prices, but instead whether respondent violated whatever definition of U&C prices applied in a given jurisdiction. That issue is one of falsity, has not been decided in respondent's favor, and is not before the Court. Indeed, in *Schutte*, the district court granted summary judgment to the plaintiffs on this question; the decision below was made solely on scienter grounds without reference to falsity, but the outcome in *Schutte* suggests that petitioner will likewise prevail on remand. Ultimately, the dust respondent seeks to kick up around falsity does not in any way undermine this Court's ability to decide the question presented, and therefore does not undermine the quality of this case (or *Schutte*) as a vehicle to consider the meaning of the FCA's scienter requirement.

CONCLUSION

This Court should consider this petition alongside *Schutte* and grant certiorari in both cases, or grant one and hold the other.

Respectfully submitted,

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