Nos. 21-1326, 22-111

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.

UNITED STATES, EX REL. THOMAS PROCTOR,

Petitioner,

v.

SAFEWAY, INC.,

Respondent.

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

BRIEF FOR PETITIONERS

Tejinder Singh
Counsel of Record
SPARACINO PLLC
1920 L Street, NW
Suite 835
Washington, DC 20036
(202) 629-3530
tejinder@sparacinopllc.com

John Timothy Keller
Dale J. Aschemann
ASCHEMANN KELLER LLC
300 North Monroe St.
Marion, IL 62959-2326
(618) 998-9988

Additional Counsel Listed on Inside Cover

Rand J. Riklin
GOODE CASSEB JONES
RIKLIN CHOATE & WATSON
2122 North Main Avenue
P.O. Box 120480
San Antonio, TX 78212
(210) 733-6030

Gary M. Grossenbacher
ATTORNEY AT LAW
402 Vale Street
Rollingwood, TX 78746
(512) 699-5436

Glenn Grossenbacher
LAW OFFICE OF GLENN
GROSSENBACHER
24165 IwH-10 W.
Ste 217-766
San Antonio, TX 78257
(210) 271-3888

C. Jarrett Anderson
ANDERSON LLC
1409 Wathen Avenue
Austin, TX 78703-2527
(512) 619-4549

Paul B. Martins
Julie Webster Popham
James A. Tate
HELMER, MARTINS, TATE
& GARRETT CO., LPA
1745 Madison Road
Cincinnati, OH 45206
(513) 421-2400

Jason M. Idell
IDELL PLLC
6800 Westgate Blvd.
Ste 132 #301
Austin, TX 78745
(512) 689-3081

QUESTION PRESENTED

The False Claims Act imposes liability on any person who, *inter alia*, "knowingly presents, or causes to be presented, a false or fraudulent claim for payment or approval." 31 U.S.C. § 3729(a)(1)(A). The term "knowingly" is defined to "mean that a person, with respect to information—(i) has actual knowledge of the information; (ii) acts in deliberate ignorance of the truth or falsity of the information; or (iii) acts in reckless disregard of the truth or falsity of the information." *Id*. § 3729(b)(1)(A).

The question presented is whether and when a defendant's contemporaneous subjective understanding or beliefs about the lawfulness of its conduct are relevant to whether the defendant acted "knowingly" when it presented false or fraudulent claims.

PARTIES TO THE PROCEEDINGS BELOW

No. 21-2136:

Petitioners Tracy Schutte and Michael Yarberry were the appellants below.

The following entities were appellees below, and are respondents before this Court:

SuperValu Inc.

SuperValu Holdings, Inc.

FF Acquisitions, LLC

Foodarama, LLC

Shoppers Food Warehouse Corp.

SuperValu Pharmacies, Inc.

Albertson's, LLC

Jewel Osco Southwest LLC

New Albertson's, Inc.

American Drug Stores, LLC

Acme Markets, Inc.

Shaw's Supermarket, Inc.

Star Market Company, Inc.

Jewel Food Stores, Inc.

AB Acquisition LLC

No. 22-111:

Petitioner Thomas Proctor was the appellant below.

Respondent Safeway, Inc. was the appellee below.

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BRIEF FOR PETITIONERS

Petitioners Tracy Schutte, Michael Yarberry, and Thomas Proctor respectfully urge this Court to reverse the Seventh Circuit's decisions in these consolidated cases.

OPINIONS BELOW

The Seventh Circuit's decisions are reported at 9 F.4th 455 (*Schutte*), and 30 F.4th 649 (*Proctor*). The district court's decision in *Proctor* was reported at 466 F. Supp. 3d 912; the decision in *Schutte* is available at 2020 WL 3577996.

JURISDICTION

This Court has jurisdiction under 28 U.S.C. § 1254(1). The Seventh Circuit decided *Schutte* on August 12, 2021, *Schutte* Pet. App. 1a, and denied a timely petition for rehearing on December 3, 2021, *id*. at 88a-89a. On February 24, 2022, Justice Barrett granted petitioners' timely application to extend the certiorari deadline to April 1, 2022. No. 21A439. Petitioners timely filed their petition.

The Seventh Circuit decided *Proctor* on April 5, 2022. *Proctor* Pet. App. 1a. On June 30, 2022, Justice Barrett granted Proctor's timely application to extend the certiorari deadline to August 3, 2022. No. 21A861. Proctor timely filed his petition.

This Court granted certiorari in both cases on January 13, 2023, consolidating them.

STATUTORY PROVISIONS

Relevant statutory provisions are reproduced fully at *Schutte* Pet. App. 92a-93a. For quick reference to the most relevant parts, the False Claims Act provides that:

> [A]ny person who—
>
> (A) knowingly presents, or causes to be presented, a false or fraudulent claim for payment or approval;
>
> (B) knowingly makes, uses, or causes to be made or used, a false record or statement material to a false or fraudulent claim;
>
> . . .
>
> is liable to the United States Government for a civil penalty . . . plus 3 times the amount of damages which the Government sustains because of the act of that person.

31 U.S.C. § 3729(a)(1).

The statutory definitions provide that:

> [T]he terms "knowing" and "knowingly"—
>
> (A) mean that a person, with respect to information—
>
> (i) has actual knowledge of the information;
>
> (ii) acts in deliberate ignorance of the truth or falsity of the information; or
>
> (iii) acts in reckless disregard of the truth or falsity of the information; and
>
> (B) require no proof of specific intent to defraud.

31 U.S.C. § 3729(b)(1).

STATEMENT OF THE CASE

I. Introduction

Ask anybody the difference between a lie and a mistake, and they will likely say that it turns on what the speaker believed at the time: A person who speaks falsely and believes he is doing so is lying; a person who speaks falsely but sincerely believes he is telling the truth is making a mistake. The common law of fraud tracks that intuition: A misrepresentation made without belief in its truth is fraudulent; a misrepresentation that the maker believes in good faith to be true is not. Under this rule, "knowledge of falsity is not essential"; it is enough that the representation was "made without belief in its truth." Restatement (Second) of Torts § 526 cmt. c & e (Am. L. Inst. 1977, Westlaw Oct. 2022 Update).

The False Claims Act (FCA), which reaches "all fraudulent attempts to cause the Government to pay out sums of money," works the same way. *United States v. Neifert-White Co.*, 390 U.S. 228, 233 (1968). The statute imposes civil liability on any person who "knowingly" presents, or causes somebody else to present, "a false or fraudulent claim." 31 U.S.C. § 3729(a)(1)(A). In 1986, Congress clarified that the term "knowingly" "require[s] no proof of specific intent to defraud," overruling decisions interpreting the word too narrowly. *Id*. § 3729(b)(1)(B). Instead, a defendant acts "knowingly" if he acts with "actual knowledge" of information, or in "deliberate ignorance" or "reckless disregard of the truth or falsity of the information." *Id*. § 3729(b)(1)(A). This standard is at least as broad as common-law fraud. It does not encompass mere negligence, but does reach more culpable mental states.

Here, respondents presented false claims by overcharging the Government for prescription drugs. Ample evidence would allow a reasonable jury to conclude that respondents believed they were overcharging the Government when they presented these claims. But the Seventh Circuit held that this evidence was categorically irrelevant, and that respondents could not have acted "knowingly" as a matter of law. Specifically, the court held that a defendant can present false claims, believing at the time that it is presenting false claims, and yet escape liability by later identifying a wrong-but-reasonable interpretation of the law that would have permitted its conduct.

The Seventh Circuit did not merely misinterpret the FCA's scienter standard; the court turned the law on its head. Under the Seventh Circuit's rule, even a defendant who intentionally defrauds the Government does not act "knowingly," as long as the defendant's attorneys can later rationalize its misconduct.

This Court should reject that rule and hold—consistent with the statutory text, common law, and common sense—that liability attaches to defendants who present false claims without an honest subjective belief in the claims' truth. This includes defendants who present false claims and: (1) subjectively believe the claims are false; (2) recognize a substantial risk that the claims are false but deliberately avoid obtaining clarification; or (3) know or should know that the claims are probably false but recklessly present them as if they are true. This rule appropriately imposes liability on culpable actors, while protecting both the Government and contractors who make innocent mistakes.

II. Factual Background

Petitioners are *qui tam* whistleblowers who learned that respondents,[1] which operate supermarket pharmacies, were overcharging Medicare, Medicaid, and the Federal Employee Health Benefits Program (FEP) for prescription drugs. Under these programs' rules, pharmacies cannot collect more from the Government than the "usual and customary" (U&C) price for a drug, which is defined as the cash price charged to the general public (where "cash" refers to customers paying without insurance). *Proctor* Pet. App. 3a-4a; *Schutte* Pet. App. 6a; *United States ex rel. Garbe v. Kmart Corp.*, 824 F.3d 632, 644-45 (7th Cir. 2016). Thus, federal regulations limit Medicaid prescription reimbursement to U&C price. *See Proctor* Pet. App. 4a; 42 C.F.R. § 447.512(b). The private Pharmacy Benefit Managers (PBMs) that administer Medicare Part D likewise include U&C price ceilings in their pharmacy contracts. *Proctor* Pet. App. 4a-5a; JA37-38.[2]

In 2006, Wal-Mart began offering popular generic drugs for $4, dramatically undercutting its competitors' prices. *Schutte* Pet. App. 33a; JA222 n.1. Shortly thereafter, the Centers for Medicare and Medicaid Services (CMS) issued instructions explaining that

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[1] Petitioners refer to respondents in 21-1326 collectively as "SuperValu" and respondent in 22-111 as "Safeway."

[2] Although the precise definition of U&C varies under state law or contract terms, these definitions generally refer to the cash price charged to the general public. That is the definition the Seventh Circuit used, and petitioners adhere to it here. *Schutte* Pet. App. 6a.

"where a pharmacy offers a lower price to its customers throughout a benefit year" that discount price becomes the pharmacy's U&C price. JA222 n.1. These instructions were then incorporated into CMS's Prescription Drug Benefit Manual. *Proctor* Pet. App. 10a; SJA239-40 n.1. Although the guidance mentioned Wal-Mart's program, it applied to all pharmacies participating in Medicare Part D, including respondents.

Wal-Mart's move placed tremendous pressure on respondents to compete with Wal-Mart's prices. But respondents realized that if they offered discounts to all cash customers, the discount prices would become their U&C prices, and respondents would have to pass those discounts on to insurers and the Government, reducing their profits.

On October 2, 2006 a SuperValu VP drafted a presentation for the Board of Directors stating that PBMs were already "ask[ing] us how we are responding" to Walmart's $4 program and warning that "if we did this, no matter how we packaged the situation, [the PBMs] would consider the $4 our usual and customary price." SJA20. Another SuperValu VP estimated a $40 to $45 million annual gross margin loss if $4 "becomes our U&C." SJA7. Similarly, four days after Wal-Mart introduced its program, a Safeway financial planning executive observed that: "Although we are still making money on the majority of these drugs at $4, we have such a high mark up . . . that the $4/script would force us to take a huge margin hit." SJA221.

Unwilling to cede market share or profits, respondents decided to have their cake and eat it, too. They would compete with Wal-Mart's prices to lure in customers—but not provide the same discounts to the

Government and third-party payors. But there was no legal way to offer discounts to the general public without reporting those prices as U&C, which would then limit Government reimbursement to the discount price. Respondents accordingly devised stealthy ways to dodge their reporting obligations.

SuperValu implemented a nationwide decade-long price-matching program in 2006. *Schutte* Pet. App. 6a-7a; *id.* at 34a-35a (Hamilton, J. dissenting). Under that program, SuperValu would match a competitor's lower price (including Wal-Mart's) and then automatically apply that discount to refills. *Id.* at 7a (majority op.). SuperValu's price matching expanded exponentially after 2006, from 3,813 price matches that year to 1,251,883 in 2011. JA30. By 2012, a majority of cash sales for 44 of SuperValu's 50 top-selling drugs were discounted. For 30 of those drugs, more than 80% of cash sales were at the lower price-matched prices. *Schutte* Pet. App. 8a; *id.* at 35a (Hamilton, J., dissenting). The discounts were substantial, as much as eight to fifteen times less than SuperValu's reported U&C prices. *Id.* at 31a, 35a-36a. Despite widespread price-matching, SuperValu never reported its discount cash prices to Medicare or Medicaid as U&C. *Id.* at 8a (majority op.). Instead, it claimed reimbursement from the Government based on non-discounted prices.

Safeway's initial response to Walmart's $4 discount program was similar to SuperValu's. From 2006 until July 2015, Safeway pharmacies matched competitor prices upon customer request. JA204-05.

Beginning in 2008, Safeway also experimented with a discount "club" in some divisions. JA203-04. From March 2008 until July 2015, Safeway offered

members a monthly supply of certain generics for $4 (or two months for $8, or 3 months for $12). To obtain discounts, customers had to pay for prescriptions without using insurance. *Ibid.* This club was very inclusive. Everybody was eligible, and no fee was required to join; instead, customers simply needed to complete an enrollment form by providing basic information that Safeway already had, *i.e.*, contact information, birthdate, and dependents. JA206-07. As the Seventh Circuit recognized, this was, in essence, "a fig leaf to disguise a Wal-Mart-style generics program without reporting those prices as U&C." *Proctor* Pet. App. 17a.[3]

From 2011 to 2015 Safeway's discounted sales constituted a majority of its cash sales. *Proctor* Pet. App. 8a. For example, in 2009, 65% of cash sales of its top 20 generics were at discounted prices. By 2014, that number climbed to 88%. *Id.* at 8a-9a. Nevertheless, Safeway did not report its discounted cash prices to Medicare and Medicaid as its U&C prices. JA204-07; *Proctor* Pet. App. 29a (Hamilton, J., dissenting). Petitioner's expert estimated that this allowed Safeway to improperly receive $127 million from government healthcare programs. *Proctor* Pet. App. 8a (majority op.)

That was by design. Safeway was explicit (internally at least) about the reason for its discount club. As a Safeway Vice President observed: "it seems like

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[3] In other divisions, Safeway experimented with a program that mimicked Wal-Mart's. Safeway properly reported those prices as U&C. *Proctor* Pet. App. 6a. Executives characterized this as a "true" $4 program. JA220; SJA243. Sales under this program are not at issue here—but it did not last long: In July 2010, Safeway replaced it with the free membership club. *Proctor* Pet. App. 6a.

to me this whole thing revolves [around] the insurance angle – to get the $10 per item from them vs the $4 cash price…. am I off?" SJA233-34. Safeway's Director of Finance for Pharmacy responded: "Off the record that is exactly the angle is getting the maximum we can from the insurance." SJA233.

Respondents knew their U&C reporting was inaccurate. Many state Medicaid programs provided guidance stating that discount prices are the pharmacy's U&C price. Safeway's own research showed that multiple States regarded price matches as discounts that must be reported as U&C. *Proctor* Pet. App. 58a. PBMs acting as intermediaries between retail pharmacies and Medicare Part D plans also told pharmacies that U&C prices must account for discounts available to the general public.

On October 27, 2006, for example, the PBM Medco Health Solutions reminded respondents that "by contract," a pharmacy's U&C price is "'the lowest net price a cash patient would have paid on the day that the prescription was dispensed inclusive of all applicable discounts.'" *Schutte* Pet. App. 66a; *see also Proctor* Pet. App. 10a-11a. "These discounts include . . . competitor's matched price, or other discounts offered customers." *Ibid*. SuperValu's VP of Pharmacy Services forwarded the email to the President of Pharmacy Operations stating: "Note the comment about price matching. Theoretically, they could audit." SJA8. Safeway's Director of Managed Care and Marketing circulated Medco's notice among Safeway pharmacy and financial executives, stating "I'm sure this has to do with the Wal-Mart initiatives. There 'are' ramifications to normal 3rd party business. [Medco's] Language is pretty similar in all of our agreements." SJA204.

Medco's notice was the first of many warnings to respondents of their obligation to include discounts in U&C prices. In January 2007, PBM Coventry Health Care notified Safeway that it was required to bill "the lowest possible price," including "any applicable discounts" in U&C. SJA223. The next month, Oregon Medicaid issued a contract amendment stating that Safeway's U&C prices must include discounts. SJA211. Texas Medicaid's April 2008 "Rx Update" also required reporting discounted prices as the U&C price, noting that "pharmacies that use a prescription discount plan (such as the Wal-Mart $4 Rx Program) or who actively match the plan prices, should reflect the discounted prices in their Medicaid prescription claims." SJA207. In September 2008, Colorado issued a bulletin on "Pharmacy Discount Programs" stating that discount program prices must be reported as U&C, and "Pharmacies should not submit higher prices on Medicaid claims than prices offered to the general public." JA225. In October 2008, the Utah Department of Health notified Medicaid providers that: "$4.00 prescriptions offered by pharmacies with low-cost generic programs are being considered as usual and customary by Utah Medicaid. Pharmacies offering these discounts must transmit the $4.00 as the U&C. Medicaid will recoup reimbursement amounts above the $4.00 upon audit." JA36.

The warnings continued for years. In July 2011, Safeway's Director of Managed Care forwarded a notice from Caremark, the PBM for the FEP, to two executives and in-house counsel stating: "Please see the announcement from Caremark. FEP is requiring that we provide our best price to them. This would [include] . . . the $4.00 [membership] program in Dominick's,

Eastern, and Texas. I do not see a way around it." SJA216.

Respondents reacted by concealing their programs from the Government. A SuperValu executive acknowledged that SuperValu had "always taken a 'stealthy' approach" to price matching because once "price matching" is no longer the "exception" and becomes "more 'rule' or routine" that would "begin to affect the integrity of our U&C price . . . as true U&C price is a claim submission requirement for all Medicaid and . . . PBM agreements." *Schutte* Pet. App. 36a-37a, 67a; SJA3.

SuperValu's "stealthy" approach included hiding its cash discount prices from PBMs. In May 2008, PBM Prime Therapeutics emailed a SuperValu executive asking about SuperValu's policy regarding $4 generic programs because "[w]e are seeing that some . . . providers that don't have these types of programs are price matching if the member inquires about it." SJA12. The executive forwarded the email to a SuperValu VP expressing concern "about any response where we acknowledge doing it." SJA11. The VP replied: "We should not respond unless we know what they are going to do with this information," and instructed him to "[m]ake sure [one of SuperValu's attorneys] can defend our price match policy as not being our U and C if they are pressing for a response." *Ibid*.

In June 2008, SuperValu planned advertising that "we match prices EVEN $4 generics." SJA15. SuperValu executives recognized that they would need "a little damage control" if third-party payors saw the ads. *Ibid.* But they took comfort in the fact that it was "[u]nlikely anyone in Managed Care will really see the ad." SJA14.

At least one Safeway executive also described its free membership club as a "stealth Membership Program," SJA201, and Safeway explicitly recognized the need to "keep a low profile" to conceal its discount prices from the Government, SJA228. In April 2008, a Safeway Pharmacy Manager emailed his Pharmacy Division Director stating that Nebraska's Medicaid Program told him that "by matching a price, it becomes our usual & customary and any prescription filled that day has to be priced as such." SJA213. The Division Director forwarded the email to six Safeway executives asking, "FYI Does anyone think we have an issue here? My question is how the state of Nebraska will know that we offered to match any price out there." *Ibid.* A few days later, one of those executives expressed concerns to the Senior VP of Pharmacy: "We may have some issues with U&C and state medicaids with price matching," explaining that according to Safeway's internal legal counsel "if you matcha [sic] price offer, that becomes your usual and customary for that day and that pricing needs to be extended to Medicaid on those drugs that are covered under medicaid." SJA227, 231.

Rather than urge compliance, the executive instead stressed the need to continue to conceal the price-match program from the Government: "If we advertise this price match—it is going to Alert the medicaid programs to start looking . . . Walmart . . . is okay because the $4 is their U and C and is extended to Medicaid—need to keep a low profile." SJA227-28.

Respondents continued offering discounted prices, but not reporting those prices as U&C, until late 2016 (for SuperValu) and 2015 (for Safeway). *Schutte* Pet.

App. 6a; *Proctor* Pet. App. 5a. Over that decade, respondents presented millions of claims reporting inflated U&C prices, improperly claiming many millions of taxpayer dollars. To the best of petitioners' knowledge, respondents have never returned their unlawful gains.

III. Procedural History

1. Petitioners brought these *qui tam* actions to recover money for the federal Government and the affected States, including California, Illinois, Utah, and Washington in *Schutte*, *Schutte* Pet. App. 9a n.4,[4] and California, Delaware, Hawaii, Illinois, Montana, New Jersey, New Mexico, Nevada, Virginia and the District of Columbia in *Proctor*. *Proctor* Pet. App. 106a.[5]

In parallel litigation against Kmart, the Seventh Circuit held in 2016 that a pharmacy presents false claims when it fails to account for widely available discounts in its U&C price reporting. *See Garbe*, 824 F.3d at 645. Like respondents here, "Kmart offered low prices to discount-program cash customers, while submitting higher 'usual and customary' prices for prescriptions reimbursed by third-party insurers and some non-program cash customers." *Id*. at 636. On November 7, 2014, the district court held that "the members of Kmart's generic discount programs are part of the 'general public' (as opposed to a private group or club) because of the open eligibility of the programs, *i.e. anyone* is eligible to join the program," and because

[4] The parties stipulated to the dismissal of claims relating to other States. *Schutte* Pet. App. 9a n.4.

[5] Additional claims on behalf of Colorado, Maryland, and Virginia were dismissed earlier on state-specific grounds, and are not at issue here.

of the minimal barriers to entry. *United States ex rel. Garbe v. Kmart Corp.*, 73 F. Supp. 3d 1002, 1017 (S.D. Ill. 2014). The court accordingly held that by not reporting its discount prices as U&C, Kmart had presented false claims.

The district court certified its order for interlocutory appeal, 2015 WL 11181734, and the Seventh Circuit affirmed, holding that because there was no "meaningful selectivity for the people who joined Kmart's program," they could not "be distinguished in any way from the 'general public,'" *Garbe*, 824 F.3d at 643. Moreover, "the barriers to joining the Kmart 'programs' were almost nonexistent, to the extent they were enforced at all." *Ibid*. The court held that "[r]egulations related to 'usual and customary' price should be read to ensure that where the pharmacy regularly offers a price to its cash purchasers of a particular drug, Medicare Part D receives the benefit of that deal." *Id*. at 644.

After *Garbe*, the district court in *Schutte* granted partial summary judgment to petitioners Schutte and Yarberry on the issue of falsity, concluding that by failing to report its discounted prices as U&C, SuperValu had presented false claims for payment. JA18-19. SuperValu did not contest that holding on appeal. *Schutte* Pet. App. 9a n.5.

2. In both *Schutte* and *Proctor*, however, the district court granted summary judgment to respondents on the issue of scienter. The court found that the reasoning of *Safeco Insurance Co. of America v. Burr*, 551 U.S. 47 (2007)—which held that "willful" violations of the Fair Credit Reporting Act (FCRA) include reckless violations, but that a party does not act recklessly if it merely followed a reasonable interpretation of the

FCRA and no authoritative guidance warned the party away from that interpretation (*Schutte* Pet. App. 88a-105a)—"applies to the FCA and its scienter requirement." *Id.* at 74a; *Proctor* Pet. App. 2a. Applying that standard, the court held that respondents had not acted "knowingly" as a matter of law.

3. In separate appeals, sharply divided panels of the Seventh Circuit affirmed. The court of appeals decided *Schutte* first, holding that *Safeco* is controlling precedent in the FCA context. *Schutte* Pet. App. 20a. The court thus held that if the defendant's conduct falls within a reasonable interpretation of the law it broke (*e.g.*, the definition of U&C), a court cannot hold that the defendant acted "knowingly" unless the Government had issued authoritative guidance warning the defendant away from that interpretation. *Id*. at 22a. The Seventh Circuit reasoned that if the law is unclear, then a defendant cannot be found to have acted knowingly under any of the FCA's definitions. *Id*. at 20a-21a. In the court's view, "if relators cannot establish the *Safeco* scienter standard," then "[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." *Id*. at 21a.

To reach that conclusion, the court brushed aside common-law fraud principles, which provide that when a defendant makes false statements without belief in their truth, the defendant has fraudulent scienter. *Schutte* Pet. App. 16a-18a. Instead, the court held that the FCA's scienter provisions are informed by the distinct standard for recklessness that applies to torts relating to physical safety. *See id.* at 17a. Under this standard, as the Seventh Circuit interpreted it, "it is

not enough that a defendant suspect or believe that its claim was false." *Id*. at 26a-27a.

Under the Seventh Circuit's rule, whether an interpretation is "objectively reasonable" is determined solely by looking to the relevant legal text. *Schutte* Pet. App. 22a-23a (explaining that the inquiry "hinges on the text of the statute or regulation that the defendant allegedly violated"). Other interpretive tools do not matter; the plaintiff must show that "the plain language of the statute precludes the erroneous interpretation." *Id*. at 23a.

What is more, the court rejected the argument that "the defendant must have held [its wrong-but-reasonable interpretation] at the time that it submitted its false claim." *Schutte* Pet. App. 26a. Although the court recognized the possibility that defendants could "avoid liability by concocting 'post-hoc arguments' to justify their conduct under an objectively reasonable reading of the applicable regulation—even if they acted in bad faith," the Seventh Circuit deemed this point "irrelevant" under *Safeco*. *Ibid*.

Analyzing the second prong of the *Safeco* inquiry, the Seventh Circuit held that a wrong-but-reasonable interpretation can only be negated by "authoritative guidance." *Schutte* Pet. App. 27a. Such guidance "must come from a source with authority to interpret the relevant text," *i.e.*, circuit-level precedent or an executive agency, and "must be sufficiently specific to the defendant's incorrect interpretation." *Ibid*.

Applying these standards, the Seventh Circuit held that SuperValu had not acted knowingly as a matter of law. That was because, in the Seventh Circuit's view, the regulatory definition of U&C "is open

to multiple interpretations," potentially meaning "that discount prices qualify only if applied to all consumers," and not only if they are merely "*offered* to the public, regardless of whether all consumers take advantage of it." *Schutte* Pet. App. 24a. The court then held that no authoritative guidance warned SuperValu away from the first interpretation. The court refused to consider the views of PBMs because it limited authoritative guidance to "governmental source[s]." *Id*. at 28a. And it held that even though CMS's policy memo and manual "clarifies that a pharmacy's consistent, lower-price offers are included within U&C prices," that guidance was not sufficiently specific because "it says nothing about price-match programs" in particular. *Id*. at 30a. The court thus affirmed the grant of summary judgment to SuperValu.

In *Proctor*, the Seventh Circuit followed *Schutte* to hold that Safeway could not have acted knowingly with respect to its price-matching program. *See Proctor* Pet. App. 17a, 20a. The court then considered Safeway's discount-club program. The court acknowledged that the barriers to entry were minimal: "The only thing separating club members from 'the general public' was the fact that they took an affirmative step to enroll." *Proctor* Pet. App. 17a. But "[t]here was no fee to enroll, and the enrollment form collected information that Safeway often already had, including a customer's address, birthdate, dependents, and phone number." *Id*. at 7a. Thus, the Seventh Circuit held 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." *Id*. at 17a.

Nevertheless, the court concluded that Safeway's conduct fell within an objectively reasonable interpretation of the law. *Id*. at 18a.

The court then turned to whether authoritative guidance compelled reporting discount-club prices as U&C. It recognized that "the CMS manual may have been specific enough to put Safeway on notice that it should have reported its membership-club prices as its U&C prices," but it concluded that the manual was not sufficiently "authoritative" because the relevant guidance was located in "a single footnote in a fifty-seven page chapter" of a manual, and because subsequent versions of the manual did not include the same footnote. *Proctor* Pet. App. 21a-23a. The court thus again affirmed summary judgment.

Judge Hamilton dissented in both cases. He explained in *Schutte* that *Safeco*'s analysis of the FCRA's scienter provision does not make sense in FCA cases and contradicts the statute's text and history. *Schutte* Pet. App. 48a-49a, 52a-53a. Judge Hamilton pointed to the FCA's three-pronged definition of "knowledge," explaining that the majority's grafting-on of *Safeco*'s rule "effectively nullifies two-thirds of the statutory definition of 'knowing'" by reducing the requirement to recklessness alone. *Id*. at 49a. He explained in *Proctor* that the majority had "misinterpret[ed] the standard of fraudulent intent set forth in the False Claims Act," creating "a deep and basic anomaly in the law" because the majority's rule requires it to "turn its back on the evidence of Safeway's fraudulent intent at the time it was submitting false claims to the Government to keep its drug reimbursements inflated by tens of millions of dollars." *Proctor* Pet. App. 28a.

The dissent drew heavily on history, noting how "state of mind is critical" in the "common law of fraud." *Schutte* Pet. App. 54a (emphasis omitted). Furthermore, the dissent warned that preventing judges from considering subjective intent—particularly given the vast permutations of fraudulent conduct for which clever lawyers "can concoct a post hoc legal rationale that can pass a laugh test"—could open the door to widespread fraudulent conduct. *Id.* at 32a.

4. Petitioners, supported by the United States, sought rehearing *en banc* in *Schutte*, which the Seventh Circuit denied. *Schutte* Pet. App. 89a.

5. Petitioners then filed timely petitions for certiorari in both *Schutte* and *Proctor*.

In *Schutte*, this Court called for the views of the Solicitor General, who urged the Court to grant certiorari. The Government's brief explained that "the court of appeals' decision is contrary to the FCA's text, history, and common-law antecedents," and "could significantly disrupt government programs involving everything from medical insurance to military equipment." U.S. Cert. *Amicus* Br. 8, 22.

6. On January 13, 2023, this Court granted the petitions in *Schutte* and *Proctor*, consolidating the cases.

SUMMARY OF ARGUMENT

In this appeal, there is no meaningful dispute that respondents presented false or fraudulent claims, wrongfully claiming public money that was not due to them. The question before the Court is whether respondents' subjective understanding and beliefs when they presented those claims are relevant to whether

they acted "knowingly," such that the FCA applies to those wrongful acts.

I. The answer is "yes." Liability attaches to a defendant who presents a false claim without an honest subjective belief in its truth, meaning a sincerely held belief based on a prudent inquiry. This standard imposes liability on anybody who presents a false claim and: (1) subjectively believes the claim is false; (2) recognizes a substantial risk that the claim is false but deliberately avoids obtaining clarification; or (3) knows or should know that the claim is probably false but recklessly presents it as true. On the other hand, a defendant who makes a reasonably prudent inquiry and honestly believes its claims were true is not liable—even if that belief is mistaken. In all cases, however, the defendant's lack of honest belief when it presented false claims is sufficient to support a finding of scienter.

The FCA's text makes this clear in two independent ways.

A. First, the text imposes liability for knowingly presenting "false or fraudulent" claims. This Court's precedents establish that the word "fraudulent" takes its common-law meaning, which provides that when a defendant lacks an honest belief in the truth of its statements, any misrepresentation is fraudulent—even if the defendant was not sure that the statement was false. The FCA imposes liability on any defendant who knowingly presents a claim meeting that common-law standard.

B. Second, the FCA's three-part definition of "knowingly" makes clear that a defendant who presents a false claim without belief in its truth has acted

with actual knowledge, in deliberate ignorance, or in reckless disregard—depending on the facts of the case. In this context, actual knowledge can be satisfied by a correct belief in the claims' falsity; deliberate ignorance occurs when the defendant is subjectively aware of a risk that the claims are false but does not make reasonable inquiries to address that risk; and recklessness occurs when the defendant either knows or should know that a claim is probably false, but presents it as if it is true. Under any of these standards, the defendant's subjective understanding and beliefs when it presented the claim can establish scienter.

II. The Seventh Circuit deviated from the correct rule by establishing a special exception when the falsity of a claim turns on the defendant's violation of a legal requirement. In that situation, the court turned the law upside down, holding that the defendant's subjective understanding and beliefs stop being the core of the inquiry, and instead become "irrelevant." *Schutte* Pet. App. 26a. According to the Seventh Circuit, the relevant question is whether the defendant's conduct can be shoehorned into a textually permissible interpretation of the law the defendant broke, in which case the defendant wins unless the Government previously issued hyper-specific authoritative guidance foreclosing that interpretation.

The Seventh Circuit reached this result via multiple legal errors, each independently fatal to its analysis. In a nutshell, the lower court improperly added arbitrary qualifiers to the FCA's clear text that effectively unravel Congress's 1986 amendments; deviated from the common law of fraud; and adopted an interpretation that threatens to undermine the statute's efficacy by jettisoning all incentives for defendants to

comply with the law and replacing them with incentives to pillage the public fisc whenever a clever attorney can rationalize the move. Under the Seventh Circuit's rule, intentional fraudsters will thrive while the rest of us foot the bill. This Court should reject that radical rule and hold that ordinary fraud rules govern the FCA's scienter requirement, including when the falsity of a defendant's claim results from violation of a legal requirement.

III. Under the correct rule, the decisions below must be reversed. Based on the record, a reasonable jury could find that respondents believed they were misreporting their U&C prices by omitting their widely available discounts. At a minimum, the evidence would permit a reasonable jury to conclude that respondents were aware of a high risk that their U&C prices were inflated, and yet reported those prices anyway, thus knowingly claiming government funds they should not have claimed. Petitioners are accordingly entitled to present their case to a jury—where respondents may argue that they made an honest mistake.

ARGUMENT

I. The False Claims Act Imposes Liability on Defendants Who Present False Claims Without an Honest Subjective Belief in the Claims' Truth

A. A False Claim Presented Without Honest Belief in its Truth Is a "Fraudulent" Claim Presented With "Actual Knowledge"

The FCA imposes liability on any person who "knowingly presents, or causes to be presented, a false

or fraudulent claim." 31 U.S.C. § 3729(a)(1)(A). One easy way to resolve this case is to focus on what it means for claims to be "false or fraudulent."

In *Universal Health Services, Inc. v. United States ex rel. Escobar*, 579 U.S. 176 (2016), this Court interpreted the phrase "false or fraudulent," noting that "[i]t is a settled principle of interpretation that, absent other indication, Congress intends to incorporate the well-settled meaning of the common-law terms it uses," and holding that "the term 'fraudulent' is a paradigmatic example of a statutory term that incorporates the common-law meaning of fraud." *Id.* at 187 (quotation marks omitted). Thus, although "[t]he False Claims Act abrogates the common law in certain respects," the Court "presume[s] that Congress retained all other elements of common-law fraud that are consistent with the statutory text because there are no textual indicia to the contrary." *Id.* at 187 n.2.[6]

For a claim to be "fraudulent," the claim must be: (i) tainted by a misrepresentation or omission that renders the claim ineligible for payment in full; and (ii) presented with fraudulent scienter. The first component covers a wide range of claims. As Congress explained, the FCA "is intended to reach all fraudulent attempts to cause the Government to pay out sums of

[6] The FCA differs from common-law fraud in that it imposes liability for the presentment of false or fraudulent claims—meaning the claim need not be accepted or paid for liability to attach. In other words, the FCA "lacks the [common-law] elements of reliance and damages." *United States ex rel. Grubbs v. Kanneganti*, 565 F.3d 180, 189 (5th Cir. 2009). Similarly, by explicitly providing that no proof of intent to defraud is required to establish scienter, 31 U.S.C. § 3729(b)(1)(B), the FCA makes clear that its cause of action is broader than common-law fraud.

money or to deliver property or services." S. Rep. No. 99-345, at 9 (1986). Such claims "may take many forms, the most common being a claim for goods or services not provided, or provided in violation of contract terms, specification, statute, or regulation." *Ibid*. Other examples include claims to a government program when "the claimant is ineligible to participate in the program," or claims "submitted under a contract, loan guarantee, or other agreement which was originally obtained by means of false statements or other corrupt or fraudulent conduct, or in violation of any statute or applicable regulation." *Ibid*.[7]

The common-law definition of "fraudulent" also includes a mental component. In general, a misrepresentation is fraudulent if the maker does not believe it to be true. This rule encompasses a variety of specific circumstances. Thus, the Restatement of Torts, which this Court routinely cites as an authoritative reference for the common law,[8] explains that:

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[7] In *Universal Health Services*, this Court held that when the defendant billed Medicaid using codes corresponding to certain services, it implicitly represented that the services were provided by staff that were appropriately qualified and trained—and the falsity of that implicit representation rendered the claims fraudulent under the "implied false certification" theory. 579 U.S. at 189-90. To reach that result, the Court reasoned that "common-law fraud has long encompassed certain misrepresentations by omission," and it found that the particular misrepresentations in that case fell "squarely within the [common-law] rule that half-truths . . . can be actionable misrepresentations." *Id*. at 187-88 (citing Restatement (Second) of Torts § 529 (Am. L. Inst. 1976)).

[8] *See, e.g.*, *Universal Health Servs.*, 579 U.S. at 190 n.4, 193 (citing Restatement of Torts in FCA case to hold that omissions

> A misrepresentation is fraudulent if the maker
>
> (a) knows or believes that the matter is not as he represents it to be,
>
> (b) does not have the confidence in the accuracy of his representation that he states or implies, or
>
> (c) knows that he does not have the basis for his representation that he states or implies.

Restatement (Second) of Torts § 526 (Am. L. Inst. 1977, Westlaw Oct. 2022 update).[9] The test is venerable: the Reporter's Note explains that it "adopts, in general effect, the opinion of Lord Herschell in *Derry v. Peek*, 14 A.C. 337, 374 (1889)," which "has been accepted and followed in numerous American cases." Restatement (Second) of Torts § 526, Reporter's Note.

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can render claims fraudulent, and to explain materiality requirement); *Omnicare, Inc. v. Laborers Dist. Council Const. Indus. Pension Fund*, 575 U.S. 175, 191 (2015) (citing Restatement to explain when statements of opinion may be deemed fraudulent); *see also, e.g.*, *Cedar Point Nursery v. Hassid*, 141 S. Ct. 2063, 2079 (2021) (citing Restatement as authority regarding common-law privileges to access private property); *Torres v. Madrid*, 141 S. Ct. 989, 1000 (2021) (citing Restatement for the elements of common-law false imprisonment); *Nieves v. Bartlett*, 139 S. Ct. 1715, 1726 (2019) (citing Restatement for the proposition that arrests based on probable cause were privileged at common law); *Air & Liquid Sys. Corp. v. DeVries*, 139 S. Ct. 986, 993 (2019) (citing Restatement for the elements of products liability claims).

[9] The American Law Institute published the Restatement (Third) of Torts: Liability for Economic Harm, in 2020. Petitioners cite the Restatement (Second), which was the definitive resource when the FCA's operative text was amended in 1986. Substantively, the standards are essentially the same. *See* Restatement (Third) of Torts: Liab. for Econ. Harm § 10 (Am. L. Inst. 2020).

Lord Herschell's opinion in *Derry* holds that "fraud is proved when it is shewn that a false representation has been made (1) knowingly, or (2) without belief in its truth, or (3) recklessly, careless whether it be true or false." *Derry*, 14 A.C. at 374. On the other hand, "[t]o prevent a false statement being fraudulent, there must . . . always be an honest belief in its truth." *Ibid*.

Under this test, the question is not whether the false statement had a reasonable basis. Instead, the statement's basis is merely evidence as to whether the defendant subjectively believed the statement to be true. Often, "the fact that an alleged belief was destitute of all reasonable foundation would suffice of itself to convince the Court that it was not really entertained, and that the representation was a fraudulent one." *Derry*, 14 A.C. at 375-76. Moreover, if the court "thought that a person making a false statement had shut his eyes to the facts, or purposely abstained from inquiring into them, [it] should hold that honest belief was absent, and that he was just as fraudulent as if he had knowingly stated that which was false." *Id*. at 376. But the mere fact that a false statement is reasonable does not negate a defendant's lack of belief in its truth.

Leading American treatises confirm that the defendant's lack of belief can, by itself, make a misstatement fraudulent. Thus, Justice Story's Commentaries on Equity Jurisprudence explains that whether the defendant who makes a misrepresentation:

> knew it to be false, or made the assertion without knowing whether it were true or false, is wholly immaterial; for the affirmation of what one does not know or believe to

> be true is equally, in morals and law, as unjustifiable as the affirmation of what is known to be positively false.

1 Joseph Story, Commentaries on Equity Jurisprudence § 193, p.117 (1st English ed. 1884) (footnote omitted).

Professor Dobbs similarly explains that a false statement is fraudulent where it was made with knowledge; without belief in its truth; or recklessly, careless whether it be true or false. *See* Dan B. Dobbs et al., The Law of Torts § 665 (Westlaw July 2022 Update). In this taxonomy, "the key principle is expressed in the second category—a statement made without belief in its truth," because that category "really includes both the first and the third" as well. *Ibid*. After all, "[i]f the defendant represents a fact knowing it to be false he is making a representation without belief in the truth of his statement"—and "if he falsely asserts a fact without caring whether it is true or not he probably if not certainly lacks a belief in its truth and it is entirely fair to treat the case as an intentional fraud." *Ibid*. In other words, all roads lead back to whether the defendant believed the statement to be true. Without that honest belief, a false statement is fraudulent.

Prosser and Keeton confirm that the key "must be a matter of belief, or of absence of belief, that the representation is true." W. Page Keeton et al., Prosser & Keeton on the Law of Torts § 107, p.741 (5th ed. 1984). Thus, liability is appropriate "where it appears that the speaker believes his statement to be false," "when a representation is made without any belief as to its truth, or with reckless disregard whether it be true or false," and as to "representations made by one who is

conscious that he has no sufficient basis of information to justify them." *Id*. at 741-42.

The commentary in Section 526 of the Restatement elucidates what the subsidiary clauses mean. Under Clause (a), which applies if a speaker "knows or believes that the matter is not as he represents it to be," the authors explain that "knowledge of falsity is not essential; it is enough that [the speaker] believes his representation to be false." Restatement (Second) of Torts § 526(a) & cmt. c. That accords with more than a century of understanding that "[b]elief" that a representation is false "is undoubtedly enough" to make the representation fraudulent. *E.g.*, Henry T. Terry, *Intent to Defraud*, 25 Yale L.J. 87, 94 (1911). Indeed, even before *Derry v. Peek*, American courts recognized that "[a] false affirmation, not believed to be true, is fraudulent; and the question of the liability of the person making it must depend upon the sincerity of his belief as to its truth, which will of course be for the jury to pass upon." *Howard v. Gould*, 28 Vt. 523, 526 (Vt. 1856).

The commentary on Section 526, Clause (b), which deems a false statement fraudulent if the maker "does not have the confidence in the accuracy of his representation that he states or implies," explains that:

> In order that a misrepresentation may be fraudulent it is not necessary that the maker know the matter is not as represented. Indeed, it is not necessary that he should even believe this to be so. It is enough that being conscious that he has neither knowledge nor belief in the existence of the matter he chooses to assert it as a fact. . . . This is often expressed by saying that fraud is proved if it is

> shown that a false representation has been made without belief in its truth or recklessly, careless of whether it is true or false.

Restatement (Second) of Torts § 526(b) & cmt. e. Under this portion of the rule, a defendant who has doubts about whether a statement is true but asserts it anyway is liable for fraud if the statement is false.

The commentary on Clause (c), which deems a false statement fraudulent if the maker "knows that he does not have the basis for his representation that he states or implies," explains that if a representation is "based upon the maker's personal knowledge of the fact in question or even upon his personal investigation of the matter"—whether expressly or implicitly—a "misrepresentation so made is fraudulent even though the maker is honestly convinced of its truth from hearsay or other sources that he believes to be reliable." Restatement (Second) of Torts § 526(c) & cmt. f. In other words, if the speaker of a false statement knows that the recipient would believe—based on the statement or its context—that the speaker has carried out an appropriate inquiry or investigation before making the statement, then the speaker commits fraud if the statement is false and the appropriate inquiry has not been made.

This Court's precedents have long recognized the foregoing common-law rule. For example, in *Cooper v. Schlesinger*, 111 U.S. 148 (1884), the Court considered the accuracy of a jury charge as to fraud. The charge itself stated the general rule:

> It is not necessary, to constitute a fraud, that a man who makes a false statement should know precisely that it is false. It is enough if

> it be false, and if he made it recklessly, and without an honest belief in its truth, or without reasonable ground for believing it to be true, and be made deliberately and in such a way as to give the person to whom it is made reasonable ground for supposing that it was meant to be acted upon and has been acted upon by him accordingly.

Id. at 152. Evaluating this charge, the Court held that "the jury were properly instructed that a statement recklessly made, without knowledge of its truth, was a false statement knowingly made, within the settled rule." *Id*. at 155. More than a century later, in *Universal Health Services*, this Court affirmed that fraudulent claims under the FCA include claims that were fraudulent under the common law, and admonished against "adopting a circumscribed view of what it means for a claim to be false or fraudulent." 579 U.S. at 192 (quotation marks omitted).

Applying that common-law definition of "fraudulent" to the FCA, a claim is fraudulent if two conditions are met. *First*, the claim is actually improper, *i.e.*, it seeks money that is not rightfully due. *Second*, the defendant does not, at the time he presents the claim, subjectively believe the claim to be proper (either because he knows it is improper, believes it to be improper, is indifferent to whether it is improper, or has not taken the requisite steps to determine its propriety). If a claim meets these conditions, it is "fraudulent" under the common law, and therefore under the FCA.

This matters because even under the narrowest interpretation of the FCA's definition of "knowingly"—

i.e., requiring actual awareness that a claim is fraudulent, *see Intel Corp. Inv. Pol'y Comm. v. Sulyma*, 140 S. Ct. 768, 776 (2020)—a defendant who presents a false claim with actual awareness that he lacks belief in the claim's truth is "knowingly" presenting a "fraudulent" claim, and therefore falls squarely within the FCA's liability provision, 31 U.S.C. § 3729(a)(1)(A). The Court can accordingly hold that such a defendant is liable for knowingly presenting a fraudulent claim without even parsing the FCA's definition of knowledge.

B. A Defendant Who Presents a False Claim Without Honest Belief in its Truth Is Acting "Knowingly" Under the False Claims Act's Three-Part Scienter Standard

The foregoing establishes that the Court can reverse by relying solely on the terms "actual knowledge" and "fraudulent." Another path to that result is to hold that the FCA's three-part scienter definition reaches defendants who present false claims without belief in those claims' truth. The three prongs—actual knowledge, deliberate ignorance, and reckless disregard—all support liability in that circumstance.

1. A defendant that correctly believes that it is presenting a false claim has "actual knowledge." The premise of this argument is that belief in a true fact is tantamount to knowledge for scienter purposes.

The understanding of "knowledge" as a true belief dates back to Plato, and has been the predominant understanding in the field of epistemology since then. *See* Joseph Blocher, *Free Speech & Justified True Belief*,

133 Harv. L. Rev. 439, 444 (2019). In the law of scienter, commentators have embraced the principle that subjective belief in a true fact is the same as having knowledge of that fact. *See, e.g.*, Rollin M. Perkins, *A Rationale of Mens Rea*, 52 Harv. L. Rev. 905, 919 (1939) (explaining that "a belief which corresponds with the facts . . . is 'knowledge' as the word is used in regard to *mens rea*"); Warren A. Seavey, *Negligence - Subjective or Objective?*, 41 Harv. L. Rev. 1, 17 (1927) ("Describing knowledge as belief in the existence of a fact, belief is the mental element which if coincident with truth creates knowledge.").

When the FCA was amended in 1986, legal dictionaries defined "knowledge" to include a "state of mind that one considers that he knows." *Knowledge*, Black's Law Dictionary (5th ed. 1979). The same dictionary explains that when knowledge "is an element of an offense, such knowledge is established if a person is aware of a high probability of [a fact's] existence, unless he actually believes it does not exist." *Ibid*. Courts have similarly recognized, in a variety of contexts, that true beliefs qualify as knowledge. *See, e.g.*, *Viacom Int'l, Inc. v. YouTube, Inc.*, 676 F.3d 19, 31 (2d Cir. 2012); *United States v. Nektalov*, 461 F.3d 309, 315 (7th Cir. 2006); *United States v. One 1973 Rolls Royce*, 43 F.3d 794, 813 (3d Cir. 1994). In other words, a "knowledge" standard does not necessarily require *absolute certainty*—and in general, subjective belief of a true fact is sufficient to establish knowledge.

This understanding of knowledge coheres with the common law of fraud, which treats a subjective belief in a statement's falsity as being tantamount to knowledge. *See* Restatement (Second) of Torts § 526 cmt. c. And it accords with the purpose of scienter and

mens rea, which is to distinguish innocent actors from culpable ones. Somebody who correctly believes he is making a false statement and makes it anyway has no claim to innocence—and is therefore appropriately held liable as a knowing violator.[10]

This refutes the Seventh Circuit's suggestion 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." *Schutte* Pet. App. 21a. That holding rests on the flawed premise that knowledge in this context requires epistemic certainty. The better view is that if a defendant presents a false claim, correctly believing it to be false, the defendant has presented a false claim with actual knowledge.

2. The FCA's constructive scienter provisions—deliberate ignorance and reckless disregard—cover situations in which the defendant may not actually believe that its claims are false, but instead either knows or

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[10] Among epistemology scholars, knowledge is sometimes defined as "justified true belief," where "justification" distinguishes knowledge from mere lucky guesses. But in the scienter context, justification is unnecessary absent a specific intent requirement because knowledge here serves as "a gauge of culpability," which can be satisfied by showing that the defendant correctly believed he was doing wrong—even if that belief was founded on incorrect assumptions. Gregory M. Gilchrist, *Willful Blindness as Mere Evidence*, 54 Loy. L.A. L. Rev. 405, 431 (2021). For example, a defendant who believes he is smuggling cocaine is not innocent because he is actually smuggling methamphetamine. In any event, even if justification were required to establish actual knowledge, justification is not certainty; it is merely a reasoned basis (*i.e.*, something other than a lucky guess). Here, a jury could easily find that respondents had reason to believe their claims false. *See* Part III, *infra*.

should know that the claims are probably false, and yet presents them anyway.

The constructive scienter provisions were added in 1986 to overturn judicial decisions requiring "the Government to prove the defendant had actual knowledge of fraud, and even to establish that the defendant had specific intent to submit the false claim." S. Rep. No. 99-345, at 7. Congress believed "this standard is inappropriate in a civil remedy and presently prohibits the filing of many civil actions to recover taxpayer funds lost to fraud." *Ibid*. Although Congress did not want "to punish honest mistakes or incorrect claims submitted through mere negligence," it was equally clear 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." *Ibid*. Congress accordingly added the constructive knowledge provisions to ensure that anybody who fails to make such inquiries can be held liable for presenting false claims.

On the House floor, Congressman Berman, who sponsored the bill, explained that:

> [P]ersons and entities doing business with the government must be made to understand that they have an affirmative obligation to ascertain the truthfulness of the claims they submit. No longer will Federal contractors be able to bury their heads in the sand to insulate themselves from the knowledge a prudent person should have before submitting a claim to the Government. Contractors who ignore or fail to inquire about red flags that should alert them to the fact that false claims

> are being submitted will be liable for those false claims.

132 Cong. Rec. H6482 (daily ed. Sept. 9, 1986). In the Senate, Senator Grassley, the architect of the amendments, explained that "under this act, reckless disregard does not require any proof of an intentional, deliberate, or willful act." 132 Cong. Rec. S11244 (daily ed. Aug. 11, 1986).

Against that backdrop, the Court should interpret the FCA's constructive knowledge standards to impose liability when a defendant presents false claims despite subjective awareness of a probability that the claims are false, or when the truth of a claim is so questionable that a reasonable person would inquire before presenting it.

a. In *Global-Tech Appliances, Inc. v. SEB S.A.*, 563 U.S. 754 (2011), this Court explained the elements of deliberate ignorance (which the Court referred to as "willful blindness"[11]): "(1) The defendant must subjectively believe that there is a high probability that a fact exists and (2) the defendant must take deliberate actions to avoid learning of that fact." *Id*. at 769. The defendant's subjective beliefs form the crux of the first step of the inquiry. Thus, if a defendant subjectively believes that there is a high probability that its claims are false, and avoids learning the truth (*e.g.*, by refus-

[11] Courts treat deliberate ignorance and willful blindness as synonyms. *See, e.g.*, *Tantchev v. Garland*, 46 F.4th 431, 437 (6th Cir. 2022); *United States v. Hong*, 938 F.3d 1040, 1046 (9th Cir. 2019); *S.E.C. v. Big Apple Consulting USA, Inc.*, 783 F.3d 786, 804 (11th Cir. 2015); *United States v. One 1989 Jeep Wagoneer*, 976 F.2d 1172, 1175 (8th Cir. 1992).

ing to take advantage of opportunities to obtain clarification, or by ignoring available guidance), the defendant is deliberately ignorant.

b. The "reckless disregard" standard can be satisfied using both subjective and objective tests. On the subjective side, "a false representation has been made . . . recklessly" when the maker "has merely a belief in its existence and recognizes that there is a chance, more or less great, that the fact may not be as it is represented." Restatement (Second) of Torts § 526, cmt. e. If the defendant holds such a belief and offers a false statement without qualification, he is acting recklessly.

Congress also intended recklessness in the objective sense of gross negligence. If a high risk of falsity would be obvious to a reasonable person in the defendant's position, but the defendant ignores that risk and presents the false claim anyway, the defendant has acted recklessly. *See, e.g.*, *Universal Health Servs.*, 579 U.S. at 191 (providing a hypothetical example involving a contractor supplying malfunctioning guns, and explaining that "because a reasonable person would realize the imperative of a functioning firearm, a defendant's failure to appreciate the materiality of that condition would amount to 'deliberate ignorance' or 'reckless disregard' of the 'truth or falsity of the information' even if the Government did not spell this out").

A common real-world example of recklessness is when a defendant has received warnings about likely falsity from attorneys, compliance officers, the Government, or the Government's contractors—and yet chose to present claims that are contrary to those warnings. In that situation, courts routinely find FCA claims viable. *See, e.g.*, *United States ex rel. Prather v.*

Brookdale Senior Living Communities, 892 F.3d 822, 837-38 (6th Cir. 2018); *United States v. Chen*, 402 F. App'x 185, 187 (9th Cir. 2010); *United States ex rel. Walker v. R&F Props. of Lake Cnty., Inc.*, 433 F.3d 1349, 1358 (11th Cir. 2005); *United States ex rel. Lynch v. Univ. of Cincinnati Med. Ctr., LLC*, 2020 WL 1322790, at *31 (S.D. Ohio Mar. 20, 2020); *United States ex rel. Decesare v. Americare in Home Nursing*, 2011 WL 607390, at *6-7 (E.D. Va. Feb. 10, 2011).

Another common example—sometimes described as recklessness, and sometimes as deliberate ignorance—is that courts permit claims against defendants who presented false claims without first making an appropriate inquiry into whether the claims are truthful. *See, e.g.*, *Prather*, 892 F.3d at 838; *United States ex rel. Swoben v. United Healthcare Ins. Co.*, 848 F.3d 1161, 1174 (9th Cir. 2016); *United States v. Bourseau*, 531 F.3d 1159, 1168 (9th Cir. 2008); *Com. Contractors, Inc. v. United States*, 154 F.3d 1357, 1366, 1369 (Fed. Cir. 1998); *United States ex rel. Ormsby v. Sutter Health*, 444 F. Supp. 3d 1010, 1082 (N.D. Cal. 2020); *United States v. Outreach Diagnostic Clinic LLP*, 2020 WL 1272609, at *4 (S.D. Tex. Mar. 16, 2020); *United States v. Raymond & Whitcomb Co.*, 53 F. Supp. 2d 436, 447 (S.D.N.Y. 1999).

In these cases, the amount of diligence a claimant must exercise before presenting a claim may vary by circumstance. Congress intended to reach those who have "failed to make simple inquiries which would alert [them] that false claims are being submitted." S. Rep. No. 99-345, at 21. A contractor's subjective belief that its claims are likely invalid triggers a duty to inquire. And a sophisticated business that plans to present a large number of claims for millions of dollars

over many years—and also has open lines of communication with the Government and its agents—certainly should ask about doubtful questions before claiming public funds.

* * *

Based on the foregoing, this Court should hold that a defendant who presents a false claim without an honest subjective belief in the claim's truth has knowingly violated the FCA. The Court may do so by holding that such a defendant presents a "fraudulent" claim with "actual knowledge," or by applying the appropriate component of the FCA's three-part scienter definition. Under either approach, the defendant's subjective understanding and beliefs suffice to establish scienter.

II. The Seventh Circuit Erroneously Created a Novel and Unfounded Exception to the False Claims Act's Scienter Standard

The Seventh Circuit held that the foregoing legal principles—honed over centuries of common law and codified into the FCA by Congress—are irrelevant. Instead, the court of appeals held that under *Safeco Insurance Co. of America v. Burr*, 551 U.S. 47 (2007), courts must apply a special rule when the falsity of a defendant's claim arises because of noncompliance with a legal requirement. In that situation, the court of appeals held that the defendant's subjective understanding and beliefs are categorically "irrelevant" to the scienter inquiry. *Schutte* Pet. App. 26a. Instead, what matters is whether: (1) the defendant's conduct falls within an "objectively reasonable" interpretation of the relevant requirement; and, if so, (2) whether the Government foreclosed that interpretation using

highly specific "authoritative guidance." *Proctor* Pet. App. 2a. The Seventh Circuit erred by importing *Safeco*'s context-specific rule to the distinct context of the FCA, and then erred again by misapplying *Safeco*.

1. In *Safeco*, an insurer failed to notify consumers that the insurer had taken "adverse action[s]" based on the consumers' credit reports, including "an increase in any charge for . . . any insurance." 551 U.S. at 52 (quoting 15 U.S.C. 1681m(a)). A provision of the FCRA imposed additional penalties for willful violations. 15 U.S.C. § 1681n(a). This Court granted review to decide whether the undefined term "willfully" encompassed "reckless disregard of" the FCRA's requirements and, if so, whether the insurer's violations had been "reckless." *Safeco*, 551 U.S. at 52, 56.

The Court concluded that reckless misconduct is "willful" under the FCRA, but that the defendant's conduct was not willful because it was "not objectively unreasonable." *Safeco*, 551 U.S. at 59, 69. To reach that result, the Court borrowed the standard for "reckless disregard of a person's physical safety" in Section 500 of the Restatement (Second) of Torts, which describes when a defendant's "conduct is in reckless disregard of the safety of another." *Id.* at 69. The Court used this standard for recklessness for want of any "indication that Congress had something different in mind." *Ibid.*

Applying that standard, the Court held that the insurer had not been reckless. Although the Court rejected the insurer's interpretation of the FCRA, it recognized that the insurer's reading had "a foundation in the statutory text, and a sufficiently convincing justification to have persuaded the District Court to adopt

it"; moreover, the insurer lacked "the benefit of guidance from courts of appeals or the Federal Trade Commission (FTC) that might have warned it away from the view it took." *Safeco*, 551 U.S. at 69-70 (citation omitted). "Given this dearth of guidance and the less-than-pellucid statutory text, [the insurer's] reading was not objectively unreasonable, and so falls well short of raising the 'unjustifiably high risk' of violating the statute necessary for reckless liability." *Id*. at 70.

In a footnote, the Court rejected an argument that, "for purposes of [Section] 1681n(a)," "evidence of subjective bad faith must be taken into account." *Safeco*, 551 U.S. at 70 n.20. The Court reasoned that "[w]here, as here, the statutory text and relevant court and agency guidance allow for more than one reasonable interpretation, it would defy history and current thinking to treat a defendant who merely adopts one such interpretation as a knowing or reckless violator" of the FCRA. *Ibid*. The Court believed that "Congress could not have intended such a result for those who followed an interpretation that could reasonably have found support in the courts." *Ibid*.

2. In the decisions below, the Seventh Circuit held that: (a) *Safeco*'s articulation of the recklessness standard applies to the FCA; (b) under *Safeco*, it does not matter whether a defendant actually held its purported "reasonable interpretation" of the law at the time it acted; (c) if a defendant is not liable for recklessness, it cannot be liable under the FCA's other scienter standards, either; and (d) the reasonableness of a defendant's interpretation is evaluated only by considering the relevant statutory or regulatory text, and only a narrow subset of on-point guidance from governmental sources may warn the defendant away from

that interpretation. Each of those propositions is wrong, and an error in any one of them suffices to reject the Seventh Circuit's rule.

a. First, *Safeco*'s holding, which is a judicial gloss on the recklessness standard applicable to torts relating to physical safety, does not govern the FCA's cause of action for fraud. This Court has taken care "to construe such words" as "knowing," "intentional," and "willful" "in their particular statutory context"—as opposed to ascribing a one-size-fits-all meaning to them. *Jerman v. Carlisle, McNellie, Rini, Kramer & Ulrich LPA*, 559 U.S. 573, 585 (2010). Indeed, in *Safeco* itself, this Court recognized that "the term recklessness is not self-defining," and takes different meanings depending on context. 551 U.S. at 68 (quoting *Farmer v. Brennan*, 511 U.S. 825, 836 (1994)). Consistent with that admonition, this Court has recognized that in some contexts, a defendant who commits a wrongful act "in the face of a perceived risk that its actions will violate federal law" is acting recklessly. *Kolstad v. Am. Dental Ass'n*, 527 U.S. 526, 536 (1999). And in other contexts, the Court has held that "subjective willfulness . . . may warrant enhanced damages" even when the defendant's conduct was not "objectively reckless." *Halo Elecs., Inc. v. Pulse Elecs., Inc.*, 579 U.S. 93, 105 (2016).

The FCA's text and context dictate a scienter standard under which the defendant's subjective understanding and beliefs are always relevant—and under which a defendant who presents claims without a subjective belief in their truth can be liable. Three important distinctions between the FCRA and the FCA compel this outcome.

i. Textually, the two statutes contain different scienter standards. The FCRA imposes penalties on those who "willfully fail[] to comply" with the statute, 15 U.S.C. § 1681n(a), while the FCA imposes liability on anybody who "knowingly" presents a "false or fraudulent" claim. 31 U.S.C. § 3729(a)(1)(A). And while the FCRA does not define "willfully," the FCA provides a three-part definition of "knowingly," which focuses on the defendant's subjective mental state at the time it acts. *See* 31 U.S.C. § 3729(b)(1)(A).

The FCA's definition was enacted in response to judicial decisions that interpreted the scienter requirement too narrowly—and was designed to ensure that the FCA's standard was broader than common-law fraud by eliminating the specific intent requirement and ensuring that liability would fall on defendants who fail to make reasonable inquiries before presenting claims. *See* S. Rep. No. 99-345, at 6-7; *see also Schutte* Pet. App. 44a-45a (Hamilton, J., dissenting). Applying the Seventh Circuit's version of *Safeco*, however, would make the FCA's standard narrower than common-law fraud, turning the amendments upside down.

ii. The background legal rules are different. The FCA draws from the common law of fraud—whereas the FCRA draws from general tort principles unrelated to fraud. As explained in Part I.A, *supra*, both the "actual knowledge" component of the FCA's definition of "knowingly" *and* the word "fraudulent" point squarely towards a defendant's subjective understanding and beliefs in determining whether the defendant acted with scienter. And as explained in Part I.B., *supra*, recklessness in fraud cases is not limited to situations involving an objectively high risk of falsity; it

also includes situations in which "a false representation has been made without belief in its truth," Restatement (Second) of Torts § 526, cmt. e. This includes any situation in which the maker of a misrepresentation "does not have the confidence in the accuracy of his representation that he states or implies." *Id*. § 526(b). Thus, in the fraud context, recklessness can be established by looking to the defendant's contemporaneous subjective beliefs.

The Seventh Circuit recognized that Section 526 "makes subjective intent relevant to the scienter inquiry." *Schutte* Pet. App. 17a. But the court held that Section 526 was irrelevant because it "defines 'conditions under which misrepresentation is fraudulent,'" but "does not define 'knowingly' (or any of the common law scienter terms listed in § 3729(b)(1)(A))." *Schutte* Pet. App. 17a. Indeed, the court went so far as to claim that "nothing in the language of the FCA suggests that a defendant's subjective intent is relevant." *Ibid*. In reaching this conclusion, the Seventh Circuit acted as if the word "fraudulent" is irrelevant to FCA liability—which is plainly wrong because "fraudulent" is *right there* in the operative text. *See* Part I.A, *supra.* The word is not surplusage, either; this Court expressly relied on it to find that the FCA reaches "more than just claims containing express falsehoods." *Universal Health Servs.*, 579 U.S. at 187.

Instead of looking to Section 526 of the Restatement, the Seventh Circuit relied on Section 500 (discussing reckless disregard of safety), which this Court analyzed in *Safeco*. The Seventh Circuit's justification was that Section 500 uses the phrase "reckless disregard," while Section 526 does not. *Schutte* Pet. App. 17a. In the Seventh Circuit's view, this made Section

500 a closer match with the FCA's text. *Ibid*. But that argument misses the forest for the trees. The Seventh Circuit picked the words "reckless disregard" out of the phrase "reckless disregard of safety," located in a section of the Restatement that has nothing to do with fraud. It then privileged that cherry-picked fragment over the section "Conditions Under Which Misrepresentation Is Fraudulent (Scienter)," which discusses making a false statement "recklessly, careless of whether it is true or false." Compare those phrases to the FCA's scienter standard—"acts in reckless disregard of the truth or falsity of the information," 31 U.S.C. § 3729(b)(1)(A)(iii)—and the inference that Congress intended to incorporate Section 500—but not Section 526—into the FCA's text is obviously wrong.

iii. The FCA protects the Government from false claims—and the law has always placed the onus on claimants seeking public funds to know the law and to ensure that their conduct conforms to it before presenting claims for payment. Thus, two years before Congress amended the FCA's scienter definition, this Court explained that Justice Holmes's observation that "Men must turn square corners when they deal with the Government . . . has its greatest force when a private party seeks to spend the Government's money." *Heckler v. Cmty. Health Servs. of Crawford Cnty., Inc.*, 467 U.S. 51, 63 (1984) (quotation marks omitted). "Protection of the public fisc requires that those who seek public funds act with scrupulous regard for the requirements of law," and should "expect no less than to be held to the most demanding standards in [their] quest for public funds. This is consistent with the general rule that those who deal with the Government are expected to know the law." *Ibid*.

Heckler was about a provider that overbilled Medicare, and the Court was clear that "[a]s a participant in the Medicare program, [the provider] had a duty to familiarize itself with the legal requirements for cost reimbursement," which included "obtain[ing] an interpretation of the applicable regulations" when facing "a doubtful question not clearly covered by existing policy statements." 467 U.S. at 64. The Court specifically disclaimed any "requirement that the Government anticipate every problem that may arise in the administration of a complex program such as Medicare." *Ibid*. Instead, the Court recognized that the law places the burden on claimants seeking public funds to ensure that their claims are not false.

The Court's rule in *Heckler* embodies a "general rule that those who deal with the Government are expected to know the law." 467 U.S. at 63. That duty is incompatible with a rule that would require the Government to anticipate every violation and issue preemptive authoritative guidance to prohibit it. And it weighs against a scienter standard that would permit a contractor to claim public funds pursuant to interpretations of the law that the contractor does not believe to be correct.

For the foregoing reasons, this Court should hold that *Safeco* does not govern the FCA's scienter element.

b. Even if the Court holds that *Safeco* is relevant in FCA cases, it should reject the Seventh Circuit's extreme holding that if *Safeco*'s criteria are satisfied, the defendant's subjective understanding and beliefs are irrelevant. At a minimum, the Court should hold that for a defendant to seek refuge in an "objectively rea-

sonable" interpretation of the law it broke, the defendant must have been relying on that interpretation at the time it acted.

The only part of the *Safeco* opinion that could even arguably be read to support the decisions below is footnote 20. There, the Court rejected the plaintiffs' argument that "evidence of subjective bad faith must be taken into account in determining whether a company acted knowingly or recklessly for purposes of § 1681n(a)." *Safeco*, 551 U.S. at 70 n.20. There are two problems with relying on this footnote here.

First, the footnote referred specifically to scienter "for purposes of § 1681n(a)," *i.e.*, the FCRA, referencing the "history and current thinking" surrounding that statute. *Safeco*, 551 U.S. at 70 n.20. The Court did not purport to establish a general scienter rule applicable in all cases. Second, the text of the footnote itself strongly implies that the defendant contemporaneously held its interpretation at the time it acted. Thus, the Court referred to "the company's reading of the statute," described the defendant as an entity that "merely adopt[ed] one such [reasonable] interpretation," and explained that the company had "followed an interpretation that could reasonably have found support in the courts." *Ibid*. Whatever the footnote said about bad faith, it does not clearly support the Seventh Circuit's holding that a defendant need not have held its purported interpretation at the time it presented false claims.

Indeed, this Court distinguished *Safeco* on those bases in *Halo Electronics*. There, the Federal Circuit, relying on *Safeco*, held that to award enhanced damages for the willful infringement of a patent, a court had to find that the infringement was both objectively

reckless and done with subjective knowledge. *See Halo*, 579 U.S. at 100-01. This Court rejected that standard, holding that "[t]he subjective willfulness of a patent infringer, intentional or knowing, may warrant enhanced damages, without regard to whether his infringement was objectively reckless." 579 U.S. at 105. The Court was particularly skeptical of a rule that would make "dispositive the ability of the infringer to muster a reasonable (even though unsuccessful) defense at the infringement trial . . . even if he did not act on the basis of the defense or was even aware of it." *Ibid*. The Court did not think it right that such an infringer could "escape any comeuppance . . . solely on the strength of his attorney's ingenuity." *Ibid*.

Instead of adopting that novel rule, the Court followed the ordinary rule, under which "culpability is generally measured against the knowledge of the actor at the time of the challenged conduct." *Halo*, 579 U.S. at 105. The Court then explained that "[n]othing in *Safeco* suggests that we should look to facts that the defendant neither knew nor had reason to know at the time he acted." *Id*. at 106. The Court addressed *Safeco*'s footnote 20 by effectively cabining the statements therein to determining "whether there had been a knowing or reckless violation of the Fair Credit Reporting Act." *Id*. at 106 n.*. Because the Court's "precedents make clear that 'bad-faith infringement' *is* an independent basis for enhancing patent damages," *Safeco*'s footnote was not controlling. *Ibid*.

So too here. More than a century of precedent establishes that a defendant's subjective beliefs at the time it acted are sufficient to establish scienter in fraud cases. *See* Part I.A, *supra*. Nothing in *Safeco* suggests that precedent should be set aside.

Indeed, the parallels between this situation and the circumstances that moved the Court in *Halo* are striking. Here, too, history and precedent hold that a defendant's subjective lack of belief in the truth of his statement is sufficient to support an action for fraud. And here, too, the Seventh Circuit's rule would provide a defense to a person who "might suspect, believe, or intend to file a false claim," as long as he was able to hire lawyers who could later assert that his conduct fell within a reasonable interpretation. *Schutte* Pet. App. 21a. Again, it would be lawyers' ingenuity, and not the defendant's culpability, that would improperly determine whether the Government could recover for false claims.

c. A third error in the Seventh Circuit's analysis is that it collapses the FCA's three distinct scienter standards. Even if the court below were correct that recklessness is purely objective (which it is not, because it can be satisfied by subjective indifference to whether a claim is true or false), the same is not true of actual knowledge and deliberate ignorance, which are necessarily subjective.

The Seventh Circuit rejected that logic, reasoning that because reckless disregard is the loosest of the FCA's standards, any conduct that fails to meet it necessarily fails to meet the others, too. *Schutte* Pet. App. 21a. This erroneously treats the three standards as steps on a ladder, such that meeting the most permissive is a prerequisite to meeting the others. In reality, the FCA's three scienter provisions are separate targets, each with its own requirements. Accordingly, even if the Court believes that *Safeco* might inform the "recklessness" inquiry, it does not follow that *Safeco*'s rule is controlling vis-à-vis those other standards, too.

Nor would any other logic compel that conclusion. As explained in Part I.B, *supra*, actual knowledge is properly understood as subjective belief in a true fact; and the first prong of deliberate ignorance requires a subjective awareness of a high risk of falsity. Subjective beliefs are accordingly pivotal to the application of those standards—and neither standard requires knowledge in the sense of epistemic certainty; either can be satisfied by belief.

In fact, the Seventh Circuit's rule effectively renders the knowledge and deliberate ignorance prongs of the scienter inquiry surplusage. Under the Seventh Circuit's rule, a plaintiff who cannot show recklessness cannot rely on the other prongs, either—and a plaintiff who can show recklessness derives no additional benefit from proving alternatives. They become meaningless in both directions. That outcome discredits the Seventh Circuit's interpretation of the statute.

d. Finally, the Seventh Circuit's interpretation of the *Safeco* rule imposes arbitrary limitations on recklessness by holding that a defendant's interpretation is reasonable unless "the plain language of the statute precludes the erroneous interpretation," *Schutte* Pet. App. 23a, and that such a reasonable interpretation is conclusively exculpatory unless it has been negated by authoritative guidance "from a governmental source," *id*. at 28a, with "a high level of specificity," *id*. at 29a. These limitations create multiple problems.

First, none of these limitations has any basis in the statutory text. When Congress amended the FCA, it did not create a special scienter standard for claims where falsity is predicated on violations of a legal requirement. The Seventh Circuit was wrong to create a

bespoke rule for this circumstance, and this Court can reject its rule for that reason alone.

Second, neither *Safeco* nor the common law support the Seventh Circuit's rule. *Safeco* did not hold that any textually permissible interpretation is automatically reasonable, nor delineate with any precision which sources count as authoritative; it merely held, in the context of that case, that those factors weighed against a finding that the defendant's conduct was willful. Nor does the common law of fraud support the Seventh Circuit's efforts to allow defendants who present false claims to don blinders. Instead, as explained *supra*, the common law holds that defendants who make false statements are at risk unless they honestly believed in the truth of their statements.

Third, the Seventh Circuit's adaptation of *Safeco* makes no sense in the FCA context because it encourages exactly the sort of behavior the FCA was enacted to prevent. By holding that any textually permissible interpretation is automatically an "objectively reasonable" choice, the Seventh Circuit has conflated being able to shoehorn one's conduct into a textually permissible interpretation of the law with acting objectively reasonably under the circumstances. But the two aren't the same. Among textually permissible interpretations, some will always be better than others—and deliberately choosing a worse interpretation isn't a reasonable thing to do. Or if the question is close, and clarification is available, then failing to seek guidance isn't reasonable either. The FCA seeks to prevent such behavior through its broad understanding of "false or fraudulent," as well as its constructive knowledge standards.

By treating every wrong-but-textually-possible reading as "reasonable," the Seventh Circuit has invited bad-faith actors to flyspeck every government program for ambiguities, and then plunder each such ambiguity for maximum gain. That is the opposite of what is supposed to happen: Contractors are supposed to engage with the Government in good faith, attempt to conform their conduct to the correct interpretation of the law, and only claim public funds that are actually owed.

The Seventh Circuit's "authoritative guidance" rule is equally problematic. By limiting authoritative guidance to government sources, the rule encourages contractors to ignore warnings from everywhere else—including their own employees, attorneys, industry experts, and even the Government's agents—even if all of them reject the incorrect interpretation. That is how the Seventh Circuit justified ignoring evidence that PBMs, who administer the Medicare program on CMS's behalf, had advised respondents to report discount prices as U&C.

With respect to government sources, the Seventh Circuit imposed made-up "authoritativeness" and "specificity" requirements that arbitrarily limit the universe of relevant guidance. The court of appeals held that only circuit courts of appeals and the relevant government agency can issue authoritative guidance—and that any guidance must be specific to the issue at hand to qualify.

Thus, in *Schutte*, the court of appeals held that CMS's manual—which stated that "in cases where a pharmacy offers a lower price to its customers throughout a benefit year," the pharmacy should treat

that discount price as its U&C price—was not sufficiently specific because "it says nothing about price-match programs." *Schutte* Pet. App. 30a. Pointing to superficial distinctions between price-matching and Wal-Mart's program, the Seventh Circuit held that "[t]he manual did not put SuperValu on notice that this type of discount program fell within the definition of U&C—at least, not with the specificity required to be authoritative guidance." *Id*. at 30a-31a.

In *Proctor*, the Seventh Circuit reiterated that holding, and then considered the same manual vis-à-vis Safeway's discount clubs. There, the court found the guidance in the manual sufficiently specific, but insufficiently "authoritative" because the relevant passage was in a footnote, and the footnote was not included in every version of the manual during the relevant time period. *Proctor* Pet. App. 22a-23a.

The Seventh Circuit's application of its made-up rule shows how mushy, unpredictable, and untethered from reality the rule is. In the real world, contractors do not seek advisory opinions from circuit courts or request that agencies undertake notice-and-comment rulemaking about every question. Instead, much guidance about what the law means comes from sources other than the Government. That is especially the case for programs, like Medicare Part D, that are principally administered by private actors. The Government also resolves many ambiguities by issuing informal guidance, *e.g.*, responding to questions by phone, letter, or on websites—in addition to manuals, bulletins, and other general guidance. But the Seventh Circuit treats all such guidance as irrelevant.

Instead, the Seventh Circuit's rule allows a court to decide, on an ad hoc basis, that guidance was not

firm, prominent, or clear enough to put a defendant on notice of the likely falsity of its claims—while simultaneously prohibiting any inquiry into whether the defendant *was actually on notice*. Because the contours of what constitutes "authoritative guidance" are so narrow and so poorly defined, this judge-made rule is an open invitation to mischief.

3. Finally, only petitioners' rule achieves the purpose of the FCA's scienter requirement, which is to separate culpable from innocent behavior when the defendant has presented a false claim. This Court should hesitate to adopt an interpretation that merges culpable and innocent behavior, leaving a large number of false claims unremedied.

Petitioners' rule strikes the correct balance by providing a defense to any person who makes a false statement but made an honest inquiry and believed he was being truthful. On the other hand, it imposes liability on those who intentionally present false claims, correctly believe they are presenting false claims, or present false claims indifferent to their verity. Petitioners' rule thus incentivizes contractors to try to understand and follow the law by protecting those who do, and punishing those who don't.

The Seventh Circuit's rule, by contrast, extends a defense to people Congress plainly did not want to protect: Those who present false claims and simultaneously "suspect, believe, or intend to file a false claim." *Schutte* Pet. App. 21a. It creates disincentives to seek clarity, and instead rewards those who devise the most clever frauds or hire the most clever counsel after the fact. It is impossible to square those incentives with the text Congress enacted.

Indeed, it is hard to square the Seventh Circuit's rule with any reasonable anti-fraud regime. As this Court explained in *Jerman*, "even in the criminal context, reference to a 'knowing' or 'intentional' 'violation' or cognate terms has not necessarily implied a defense for legal errors." 559 U.S. at 585. Instead, the ordinary rule is that ignorance of the law is no excuse for wrongdoing. Against that benchmark, petitioners' rule is generous to defendants because petitioners acknowledge that honest mistakes of law, made after appropriate inquiry, are not culpable. But the Seventh Circuit's rule goes much further: It not only grants a defense based on mistakes of law; it grants such a defense *even when no mistake has actually occurred, allowing the defendant to keep public funds that it improperly claimed*. Such solicitude for false claims makes no sense.

III. Under the Correct Legal Standard, This Court Should Reverse the Decisions Below

Neither the district court nor the Seventh Circuit applied the correct scienter standard in these cases, and this Court could remand for the lower courts to apply it in the first instance. In the alternative, if the Court reaches the question, it should hold that a reasonable jury could find that respondents acted with the requisite scienter for FCA liability, because a reasonable jury could find that respondents did not believe in the truth of the claims they presented. The Court could then remand the cases to the district court for trial.

Scienter is ordinarily a jury question because it can be proved solely using "inference from circumstantial evidence," and at summary judgment all "facts

must be viewed in the light most favorable to the nonmoving party." *Intel*, 140 S. Ct. at 779; *see also Farmer*, 511 U.S. at 842 (describing such inferences as among "the usual ways" that scienter is proved). Under this standard, respondents are not entitled to summary judgment because the evidence, viewed in the light most favorable to petitioners, would allow a reasonable jury to conclude that respondents did not believe that they were accurately reporting their U&C prices vis-à-vis drugs for which the majority of cash sales occurred at discount prices.

In SuperValu's case, the evidence showed that SuperValu had received notifications from CMS, PBMs, and certain States explaining that widely available discounts had to be reported as U&C. SuperValu intentionally ducked that obligation by taking a "stealthy" approach to price-matching—precisely because it understood that once "price matching" is no longer the "exception" and becomes "more 'rule' or routine"—which it did—that would "affect the integrity of our U&C price" reported to Medicare and Medicaid. *Schutte* Pet. App. 36a-37a, 67a. And when a PBM asked SuperValu directly about price matching, executives expressed "concern[] about any response where we acknowledge doing it," and resolved not to "respond unless we know what they are going to do with this information." SJA11.

Consistent with that stealthy approach, SuperValu did not report its discount prices as U&C even when the majority of its cash sales for particular drugs were discounted. *See Schutte* Pet. App. 8a. For example, in 2012, a majority of the non-insurance sales for 44 of the top 50 drugs were discounted; and for 30 of those drugs, more than 80% of sales were discounted—

often steeply, with customers paying eight to fifteen times less than the prices SuperValu claimed were U&C. *Id*. at 35a (Hamilton, J., dissenting). SuperValu thus made millions of extra dollars at the Government's expense—and the district court found those claims false as a matter of law. A reasonable jury could find that SuperValu's conduct was "knowing."

The evidence against Safeway is comparable. It, too, received communications from CMS, States, and PBMs. But Safeway did not respond with candor. For example, in 2008 Nebraska's Medicaid program told a Safeway pharmacy manager that discounts had to be included as U&C prices—and a Safeway executive responded not by suggesting that Safeway report those prices properly, but instead by asking his colleagues "how the state of Nebraska will know that we offered to match any price out there." SJA213. A few days later, an executive told a senior vice president that price-matched discounts "become[] your usual and customary for that day and that pricing needs to be extended to medicaid." SJA227. But the solution was not to accurately report the prices; instead, it was to "keep a low profile" to avoid "[a]lert[ing] the medicaid programs to start looking." *Ibid*. That's because, as Safeway executives understood, "the angle" here was always about "getting the maximum we can from insurance." SJA233. And they did: Petitioner's expert "estimated that Safeway received $127 million more in reimbursements from government health programs" than it should have. *Proctor* Pet. App. 8a.

Respondents also knew their reporting was dishonest for a more fundamental reason. These discount programs were concocted specifically to compete with Wal-Mart while evading U&C reporting requirements.

In other words, the programs were deceptive at their core: They aimed to offer deep discounts to the general public, but to create an illusion of deniability—or, as the Seventh Circuit candidly acknowledged, "a fig leaf to disguise a Wal-Mart-style generics program without reporting those prices as U&C." *Proctor* Pet. App. 17a. Any reasonable company implementing such a program would have been concerned that its U&C price reports were dishonest—especially for drugs where discounts accounted for the majority of cash sales. That is enough for a reasonable jury to find scienter.

This Court should accordingly reverse the grant of summary judgment. Instead, petitioners should present their case to a jury, where respondents will have every opportunity to show that they conducted an appropriate inquiry and honestly believed their U&C reporting was accurate. If a jury credits those arguments, respondents will prevail under petitioners' rule.

CONCLUSION

The decisions below should be reversed.

Respectfully submitted,

Tejinder Singh
Counsel of Record
SPARACINO PLLC
1920 L Street, NW
Suite 835
Washington, DC 20036
(202) 629-3530
tejinder@sparacinopllc.com

Rand J. Riklin
GOODE CASSEB JONES RIKLIN CHOATE & WATSON
2122 North Main Avenue
P.O. Box 120480
San Antonio, TX 78212
(210) 733-6030

Gary M. Grossenbacher
ATTORNEY AT LAW
402 Vale Street
Rollingwood, TX 78746
(512) 699-5436

Glenn Grossenbacher
LAW OFFICE OF GLENN GROSSENBACHER
24165 IwH-10 W.
Ste 217-766
San Antonio, TX 78257
(210) 271-3888

John Timothy Keller
Dale J. Aschemann
ASCHEMANN KELLER LLC
300 North Monroe St.
Marion, IL 62959-2326
(618) 998-9988

Paul B. Martins
Julie Webster Popham
James A. Tate
HELMER, MARTINS, TATE & GARRETT CO., LPA
1745 Madison Road
Cincinnati, OH 45206
(513) 421-2400

Jason M. Idell
IDELL PLLC
6800 Westgate Blvd.
Ste 132 #301
Austin, TX 78745
(512) 689-3081

C. Jarrett Anderson
ANDERSON LLC
1409 Wathen Avenue
Austin, TX 78703-2527
(512) 619-4549

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