



ALERTS

U.S. Supreme Court Justices Consider Relevance Of Subjective Knowledge Under False Claims Act

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Highlights

U.S. Supreme Court is considering whether a defendant's subjective beliefs about the meaning of a statute or regulation are relevant under the False Claims Act if the defendant's claim was supported by an objectively reasonable interpretation

During oral argument, the justices questioned whether subjective intent should always be irrelevant to the knowledge standard of the False Claims Act

The justices' questions focused on the scope of the decision required in this case

On April 17, 2023, the U.S. Supreme Court heard oral argument in the consolidated cases of *United States ex rel. Schutte v. SuperValu Inc.* and *United States ex rel. Proctor v. Safeway, Inc.* The dispute concerns the relevance of an actor's subjective knowledge under the False Claims Act (FCA) when the actor adopts an incorrect but nevertheless "objectively reasonable" interpretation of a statute or regulation.

The Court's decision will have a significant impact on a number of industries and, in particular, companies in the healthcare space due to the

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complicated and often ambiguous nature of statutory and regulatory requirements under federal healthcare programs.

Petitioners — *qui tam* whistleblowers — allege respondents — nationwide grocery chains with retail drug pharmacies — knowingly submitted false claims to federal healthcare programs for prescription drugs. In particular, federal law requires pharmacies to report to the government the “usual and customary” prices of their drugs, and petitioners allege respondents violated this requirement by reporting their retail cash prices for prescriptions rather than lower, price-matched amounts charged to qualifying customers under discount programs. Petitioners argue respondents therefore knowingly submitted false claims and overcharged the government by using the higher retail cash price.

The Seventh Circuit’s Adoption of the *Safeco* Objective Knowledge Standard

In both *Schutte* and *Proctor*, split panels of the U.S. Court of Appeals for the Seventh Circuit affirmed grants of summary judgment in favor of the respondents, joining four other circuits in determining that the knowledge standard articulated by the Supreme Court in *Safeco Ins. Co. of Am. v. Burr* for the Fair Credit Reporting Act (FCRA) also applies to the FCA. As the Court held in *Safeco*, where the defendant acted under an incorrect interpretation of the relevant statute or regulation, the FCRA’s scienter requirement cannot be satisfied if the interpretation was objectively reasonable and no authoritative guidance cautioned the defendants against that interpretation.

Applying this standard, the Seventh Circuit held the pharmacies did not “knowingly” submit false claims: It concluded that reporting retail cash prices was supported by an erroneous but objectively reasonable interpretation of federal law and that no authoritative guidance warned the pharmacies away from this view. It further concluded the pharmacies’ subjective knowledge was therefore irrelevant, reasoning that a company “cannot know that its claim is false if the requirements for that claim are unknown.”

The Supreme Court Accepts Petitions for Certiorari

Petitioners contend that the Supreme Court should reverse the Seventh Circuit and rule that the FCA’s knowledge requirement imposes a good-faith subjective intent standard based on common law fraud. Under this standard, to secure summary judgment, defendants would need to show not only that their interpretation of the law was reasonable, but also that they genuinely believed it to be correct. The federal government filed an amicus brief in support of petitioners, arguing that applying *Safeco*’s objective reasonableness standard under the FCA “would allow defendants who *intentionally* submit false claims . . . to escape FCA liability based on concededly incorrect post hoc justifications.”

Respondents counter that the *Safeco* objective standard is appropriate in order to avoid unfairly penalizing providers under the FCA for “failing to ‘divine’ which of multiple reasonable interpretations . . . would ultimately be declared the winner” by the courts.”

The Justices Consider How Subjective Intent May Be

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During the oral argument, the justices pressed all parties regarding the necessary scope of a decision to decide the question presented: the relevance of subjective intent.

Justices Elena Kagan, Sonia Sotomayor, and Ketanji Brown Jackson indicated they believed this was an “easy” case, where the question before the court was simply whether evidence of subjective intent was relevant to the scienter inquiry, and suggested that they would answer that question in the affirmative. Justice Neil Gorsuch seemed to agree; he said the question in this case is “did the Seventh Circuit err when it said that the only evidence that could be admitted against [the defendant] was objective proof?” He explained that he thought “the statute makes that argument pretty hard.”

Although the government stated that it would welcome a holding that evidence of subjective belief could overcome the objective reasonableness standard, both the government and petitioners pushed for a broader ruling that would address the situation where the defendant considered competing interpretations and selected between them prior to submitting the alleged false claims.

The justices seemed to find this a more difficult question. Justice Brett Kavanaugh presented a hypothetical where the defendant contemplates three objectively reasonable interpretations: Option A is “clearly in the safe zone, B is a little more aggressive, and C is [] pushing the envelope.” He pressed petitioners on why there would be liability if the defendant selected Option C and a court later determined that it was an incorrect interpretation. Petitioners and the government answered that, because the defendant in that scenario believes they have not selected the “best” interpretation, any claim submitted subsequent to the issuance of that interpretation would be knowingly false.

Justice Kavanaugh seemed surprised by this answer, responding with “Wow.” Similarly, Justice Samuel Alito and Chief Justice John Roberts presented the “close call” hypothetical where there was a “51-49” split on the reasonableness of two competing interpretations. Each expressed skepticism that choosing the more aggressive interpretation (e.g., the “49”) in such a close case could amount to a knowing violation under the FCA.

In particular, petitioners framed their proposed subjective rule as a reasonable and straightforward alternative to the *Safeco* two-part standard. In rebuttal, petitioners argued the subjective standard accounts for the differences between facts and law by simply asking “Did they believe they were doing the right thing or the wrong thing?” In petitioners’ view, “that could be because of a legal reason or a factual reason,” making the subjective standard a “one-size-fits-all.”

For businesses observing the ultimate outcome of the case, the most significant question will likely center on the scope of the Court’s decision. As Justice Kavanaugh stated, from the business community’s point of view, “it’s a much narrower loss if” the Court limits its opinion to holding that subjective intent is relevant in the face of a post-hoc legal interpretation and “a full-out disaster if it’s the [] broader theory[] that even if you’ve considered it at the time and you guess wrong, legally, you can be held liable for the treble damages.”

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