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Supreme Court rejects effort to narrow scope of False Claims Act liability | White Collar Corner

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On June 1, 2023, the Supreme Court issued a unanimous decision in *United States ex rel. Schutte v. SuperValu Inc.*, rejecting efforts to redefine the knowledge prong of the False Claims Act to disregard a defendant's subjective knowledge or belief. The decision will have far-reaching impacts for companies dealing with ambiguous regulatory regimes or government contract provisions.


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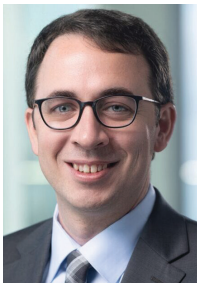
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The False Claims Act and its scienter provision

The False Claims Act (FCA), codified by 31 U.S.C. §§ 3729–3733, imposes civil liability on anyone who, among other things, knowingly presents to the federal government a false or fraudulent claim for payment. The FCA's "scienter" requirement ensures that punishment only be meted out to defendants who present false claims *knowingly*, which is defined to cover actual knowledge, "deliberate ignorance" of the truth or falsity of information, and "reckless disregard" of the truth or falsity of information.

The FCA is frequently employed in the area of health care reimbursement and defense contracting. The FCA has been described as a "quasi-criminal" statute because it imposes damages that the Supreme Court has described as "essentially punitive in nature": treble damages awards, per-claim civil penalties (currently $13,507 to $27,018 per violation) and attorney's fees.

The statute allows private citizens to bring civil actions in the name of the United States for enforcement of the FCA and provides that such "qui tam" litigants ("qui tam" is short for a Latin phrase that means "who as well for the king as for himself sues in this matter") will receive a percentage of the government's recovery — typically between 15% and 30%. Qui tam plaintiffs, also known as relators, are often whistleblowers who are incentivized by the prospect of a lucrative payout.

In *Schutte*, the Supreme Court addressed an open question about the FCA's scienter requirement: Can a defendant "knowingly" submit a false claim, where the truth or falsity of the claim turns on the interpretation of an ambiguous statute or regulation for which no court or government agency has provided authoritative guidance?

The facts and history of *Schutte*

The relators in Schutte (and a companion case, *United States ex rel. Proctor v. Safeway, Inc.*) are former pharmacists for respondents, supermarket chains SuperValu and Safeway. The relators accuse the companies of overcharging Medicare and Medicaid for generic drugs. Whether the companies actually overcharged the government turns on the meaning of a federal regulation authorizing pharmacies to seek reimbursement for the "usual and customary" charge to the general public.

SuperValu and Safeway had price-matching programs and discount programs under which they would match competitors' prices or provide widespread discounts. The companies did not report these discounted prices as their "usual and customary" prices for purposes of reimbursement, but instead reported their undiscounted cash prices.

The relators argued that respondents subjectively knew that they were overcharging the government, or submitted claims with deliberate ignorance or reckless disregard for the truth or falsity of their claims as to their "usual and customary" drug prices.

The respondents countered that "usual and customary" was nowhere clearly defined and that the government had failed to provide clarification. They argued that their interpretation of "usual and customary" to be the base, undiscounted price was at least objectively reasonable such that they could not have knowingly presented false claims to the government, regardless of what they subjectively believed. The U.S. Court of Appeals for the Seventh Circuit agreed.

The Supreme Court's decision

The court unanimously held that where the falsity of a claim turns on the meaning of a facially ambiguous legal standard, the defendant's subjective understanding is relevant. Thus, a defendant may submit a false claim if they correctly understand the meaning of the applicable legal standard and thinks that its claim is false, regardless of whether a hypothetical person could reasonably but incorrectly believe the claim is true.

In reaching this conclusion, the court (in an opinion by Justice Thomas) first reasoned that the FCA's scienter standard "largely tracks the traditional common-law scienter requirement for claims of fraud" and that traditionally, common-law fraud has depended on a subjective rather than objective test.

From that standpoint, the court rejected three arguments in support of a rule under which a defendant's subjective beliefs would be irrelevant, where a hypothetical person could have reasonably made an honest mistake as to falsity:

- The first argument was that, since the phrase "usual and customary" is ambiguous, respondents could not have known whether their claims were true or false. The court disagreed, noting that the ambiguity did not "preclude respondents from … learn[ing] their correct meaning — or, at least, becoming aware of a substantial likelihood of the terms' correct meaning." The court gave an example: "[C]onsider a hypothetical driver who sees a road sign that says 'Drive Only Reasonable Speeds.' … But then assume that the same driver was informed earlier in the day by a police officer that speeds over 50 mph are unreasonable and then noticed that all the other cars around him are going only 48 mph. … [I]f the same police officer later pulled the driver over, we imagine that he would be hard pressed to argue that some other person might have understood the sign to allow driving at 80 mph."
- Similarly, the court rejected the respondents' efforts to rely on a holding in another case, *Safeco Insurance Company of America v. Burr*, 551 U.S. 47 (2007), where the court had interpreted the Fair Credit Reporting Act to provide a safe harbor for defendants whose acts were consistent with an objectively reasonable interpretation of the relevant law that had not been ruled out by definitive legal authority or guidance. The court distinguished Safeco by noting that the statute at issue in that case had a different *mens rea* standard ("willfully") than the False Claims Act's ("knowingly"), and that the FCA's history and purpose did not support applying the *Safeco* rule in the context of the FCA.
- The third argument was that at common law, misrepresentations of law are not actionable; thus, a claim cannot be false if its truth depends on the meaning of the legal phrase "usual and customary." But the court, assuming without deciding that the False Claims Act incorporates this idea, concluded that the argument still fails because "statements involving some legal analysis remain actionable if they 'carry with [them] by implication' an assertion about 'facts that justify' the speaker's statement" (quoting Restatement (Second) of Torts § 545 c).

The Supreme Court thus concluded:

Under the FCA, petitioners may establish scienter by showing that respondents (1) actually knew that their reported prices were not their "usual and customary" prices when they reported those prices, (2) were aware of a substantial risk that their higher, retail prices were not their "usual and customary" prices and intentionally avoided learning whether their reports were accurate, or (3) were aware of such a substantial and unjustifiable risk but submitted the claims anyway. [31 U.S.C.] § 3729(b)(1)(A). If petitioners can make that showing, then it does not matter whether some other, objectively reasonable interpretation of "usual and customary" would point to respondents' higher prices. For scienter, it is enough if respondents believed that their claims were not accurate.

The court's decision in *Schutte* will have tremendous implications for FCA litigation moving forward. A defendant who intends to rely on a defense that a statute, regulation or contract term was ambiguous must demonstrate its *subjective* knowledge and belief as to the meaning of the at-issue requirement, rather than simply pointing to an objective ambiguity. A defendant's subjective knowledge and belief is not capable of resolution on a motion to dismiss or for summary judgment; a defendant relying on such a defense would have to accept the risk of trial — a daunting proposition given the extremely punitive nature of the FCA's treble damages and civil penalty provisions.

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