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Supreme Court Rules FCA Scienter Is a Subjective Inquiry

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In a closely watched case, the Supreme Court of the United States has reversed a Seventh Circuit decision applying a defendant-friendly test for evaluating False Claims Act (FCA) scienter. The decision in *United States ex rel. Schutte v. SuperValu Inc.*, No. 21-1326 (June 1, 2023) instead squarely held that the FCA's scienter element refers to a defendant's subjective knowledge and beliefs at the time the claims in question were submitted. However, the Court confined its decision to the discrete issue before it, declining invitations made during oral argument to issue a broader ruling.

The pharmacy defendants in the case were alleged to have violated Medicare and Medicaid regulations capping reimbursements at a retailer's "usual and customary" prices when they failed to give the government the benefit of the discounted prices provided to club members and as part of a price-matching promotion. Although the defendants allegedly were informed and understood that "usual and customary" meant the discounted price, defendants allegedly attempted to hide their discounted prices from regulators and requested reimbursement at the higher retail rate, knowing that such a request was improper.

The defendants prevailed on summary judgment in the trial court, as affirmed by the Seventh Circuit, by relying on the "Safeco defense" to FCA scienter. In *Safeco Ins. Co. of America v. Burr*, 551 U.S. 47 (2007) the Supreme Court interpreted the term "willfully" in the Fair Credit Reporting Act to require courts to use a two-step test for evaluating scienter—first asking whether the defendant acted consistently with any objectively reasonable interpretation of the law, and if (and only if) they did not, then evaluating the defendant's subjective intent. The Seventh Circuit applied this scienter test to the FCA claims in *Schutte* and found that the pharmacy defendants' conduct was consistent with an objectively reasonable interpretation of the phrase "usual and customary," regardless of the defendants' actual intent at the time they requested reimbursement.

The Supreme Court flatly rejected application of the *Safeco* scienter test to FCA claims, calling it a “straightforward” issue. First, the text of the FCA defining scienter to mean actual knowledge, deliberate ignorance, or reckless disregard closely tracks common-law scienter requirements for fraud claims, which focuses on a subjective inquiry into what the defendant thought and believed at the time of the alleged conduct. Objective interpretations of the law formulated after the fact are not relevant to the scienter analysis. The Supreme Court also noted that *Safeco* involved a different statute, and interpreted a word (willful) not found in the FCA.

Although the Court rejected the viability of this “objectively reasonable” defense to scienter, the Court was careful to note that its ruling was limited to the narrow legal issue of whether FCA scienter is judged under an objective or subjective standard. The Court emphasized it was not resolving any factual issues, and remanded the case for further proceedings instead of issuing a final ruling. The Court issued this narrow decision despite requests from petitioners and the government during oral argument for a broad ruling on whether or how, for example, an incorrect interpretation of a statute or regulation could give rise to FCA scienter. In light of the narrow scope of the decision, such issues will continue to be litigated in the lower courts on a case by case basis.

Vorys has deep experience, across multiple different industries, with the FCA. We will continue to monitor this and other developments. In the meantime, please do not hesitate to contact your Vorys attorney with any FCA issues that you may have.