Congressional Research Service
Informing the legislative debate since 1914

Legal Sidebar

Supreme Court Addresses Scope of False Claims Act's Knowledge Requirement

June 13, 2023

On June 1, 2023, the U.S. Supreme Court decided *United States ex rel. Schutte v. SuperValu Inc.*, a case involving the scienter, or mental state, requirement of the False Claims Act (FCA). The FCA prohibits "knowingly" submitting false claims to the government for payment. The Court in *Schutte* ruled unanimously that this knowledge standard encompasses a defendant's subjective beliefs about the accuracy of its claims. The Court rejected the Seventh Circuit's conclusion that a defendant who adopts an objectively reasonable interpretation of an ambiguous legal requirement cannot act "knowingly" within the meaning of the FCA. The *Schutte* decision allows two whistleblower actions against retail pharmacies to proceed to trial. More broadly, it reinforces the Court's earlier admonitions that courts must analyze scienter requirements in the specific context of the statutory framework at issue, including any common-law concepts that Congress incorporated into the statutory text.

Background on the *Schutte* Case

As explained in more detail in an earlier Legal Sidebar, the *Schutte* case involves two separate *qui tam* actions—*United States ex rel. Schutte v. SuperValu Inc.* and *United States ex rel. Proctor v. Safeway, Inc.*—that the Supreme Court consolidated for purposes of its review. Under its *qui tam* provisions, the FCA allows a private individual called a relator to bring a lawsuit in the government's name against a person or company that allegedly violated the act and to retain a portion of the proceeds in any successful action or settlement. In both *Schutte* and *Proctor*, the relators allege that the defendants, operators of retail pharmacies, reported inflated prices when seeking reimbursement for prescription drugs under the federal Medicare and Medicaid programs. Those programs require pharmacies to report their "usual and customary" charges for prescription drugs in certain circumstances. According to the relators, the defendants failed to report their widely offered discounted prices as their usual and customary prices, rendering the defendants' claims for payment under Medicare and Medicaid false. The relators further allege that the defendants submitted these false claims "knowingly."

A defendant who "knowingly" submits false claims under the FCA is liable for civil penalties and treble damages. The statute defines "knowingly" as acting with (1) "actual knowledge of the information," (2) "deliberate ignorance of the truth or falsity of the information," or (3) "reckless disregard of the truth or falsity of the information."

Congressional Research Service
https://crsreports.congress.gov
LSB10978

The district court granted summary judgment in favor of the defendants in each *qui tam* case. On appeal, a divided panel of the Seventh Circuit affirmed in both *Schutte* and *Proctor*, offering similar reasoning in both opinions. Specifically, the Seventh Circuit held that the defendants did not "knowingly" report false prices within the meaning of the FCA because (1) the defendants' interpretation of the usual-and-customary requirement was "objectively reasonable," and (2) no "authoritative guidance" warned them away from that interpretation. The court drew this two-part "test" from the Supreme Court's 2007 opinion in *Safeco Insurance Co. of America v. Burr*, in which the Court interpreted the scienter element of the Fair Credit Reporting Act. In the Seventh Circuit's view, satisfying the *Safeco* test foreclosed FCA liability regardless of what the defendants subjectively knew or believed at the time of submitting their claims.

Summary of the Supreme Court's Opinion in *Schutte*

In the consolidated *Schutte* case, the Supreme Court rejected the Seventh Circuit's interpretation of the FCA's scienter element and its extension of *Safeco* to the FCA context. The Court held that subjective knowledge is a key component of scienter under the FCA. This conclusion aligned with the positions of the relators and the federal government, which filed an amicus brief in support of the relators. Writing for the Court, Justice Thomas observed that the three-pronged definition of "knowingly" in the statute "largely" tracked the "common-law scienter requirement for claims of fraud." The Court cited the interpretive principle that when a federal statute uses common-law terms, courts presume that Congress intended to "incorporate the well-settled meaning" of those terms unless the text suggests otherwise. The Court reasoned that, both as a textual matter and at common law, the standards in the FCA definition "focus primarily" on what the defendants "thought and believed." Although the Court declined to rule on the meaning of "usual and customary," because it did not grant certiorari to review that question, the Court held that the potential ambiguity of that phrase did not foreclose a finding that the defendants knew they were submitting false claims.

In addition to clarifying the FCA's scienter requirement, the *Schutte* decision limited the reach of the *Safeco* opinion. While acknowledging that *Safeco* included a discussion of the common-law concepts of "knowing" and "reckless" acts, the Court cautioned that lower courts should not read *Safeco* as "establishing categorical rules for those terms." The Court reminded readers that *Safeco* involved a different statute (the Fair Credit Reporting Act) and a different scienter standard ("willfully") and urged lower courts to consider the specific statutory context in which a scienter requirement appears. The Court also explained that *Safeco* did not establish a general "safe harbor" whereby a defendant's actual, subjective beliefs about the accuracy of its statements at the time of submitting a claim are irrelevant if the defendant can later advance an objectively reasonable interpretation of the law in question.

Additionally, the Court addressed the defendants' argument that FCA liability turns only on misrepresentations of *fact*, not of *law*. The Court reasoned that even if the FCA incorporated such a rule and the defendants' reported prices reflected their (incorrect) legal analysis of the usual-and-customary requirement, those statements also represented something about the prices the defendants charged to the public, which is factual in nature.

Based on these holdings, the Court vacated the Seventh Circuit's judgments and remanded the cases for further proceedings.

Considerations for Congress

The most immediate consequences of the *Schutte* decision are for the parties to these two and other pending FCA *qui tam* actions. On remand, the parties in *Schutte* and its companion case could decide to settle the actions or proceed to trial, in which case a jury might have to decide what the defendants knew or believed about their usual and customary prices at the time they submitted their claims for reimbursement. Although the federal government has not intervened in these *qui tam* actions to date

(participating as amicus curiae before the Supreme Court), the FCA would permit it to do so upon a showing of "good cause." Whether the government could move to dismiss these cases at this stage, and under what circumstances, could depend on the result of another FCA case that is pending before the Supreme Court.

Beyond the effects on this and related litigation, the *Schutte* decision clarifies that the FCA's scienter requirement focuses on a defendant's subjective knowledge and beliefs at the time of submitting a claim, thereby settling a question that had started to divide the lower courts. The defendants in *Schutte* had urged the Court to adopt the Seventh Circuit's objective standard in order to provide "fair notice" to federal contractors who try in good faith to understand ambiguous legal requirements. By contrast, at least one Member of Congress who sponsored significant amendments to the FCA viewed the Seventh Circuit's decisions as part of "a growing misinterpretation of the language of the FCA that threatens to undermine its critical role in policing those who do business with the government." If Congress were to disagree with the Court's interpretation of the FCA in *Schutte*, it could amend the statute to adopt a different scienter standard or definition of knowledge. Congress also has the option of amending the FCA to expressly adopt the Court's interpretation if it agrees with the *Schutte* decision. The Court's ruling binds lower courts even in the absence of congressional action unless the Court were to overturn or modify its decision in a later case.

The effects of the *Schutte* decision on other laws may be more limited. Although other statutes authorizing civil penalties use the term "knowingly," the *Schutte* decision suggests that each statute's scienter requirement must be interpreted in the context of the specific language and history of that statute. Even so, the Court's conclusion that the terms "actual knowledge," "deliberate ignorance," and "reckless disregard" encompass a defendant's subjective beliefs "*[o]n their face and at common law*," could provide a basis for lower courts to interpret the same terms in other statutes consistently with *Schutte*, especially if courts consider those laws to likewise incorporate the common law of fraud.

Author Information

Victoria L. Killion
Legislative Attorney

Disclaimer