

# *U.S. ex rel. Proctor v. Safeway, Inc.*: When “Subjective Intent Is Legally Irrelevant” to Proving Scierter Under the FCA

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False Claims Act

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The False Claims Act (FCA) only imposes liability on those who “knowingly” cause the submission of false claims. 31 U.S.C. § 3729. “Knowingly” is defined as having “actual knowledge,” acting “in deliberate ignorance of the truth or falsity of the information,” or, at minimum, acting “in reckless disregard of the truth or falsity of the information.” To establish scierter under this standard, *qui tam* relators frequently invoke evidence, such as internal emails and policy documents, to show that the defendant was subjectively aware of legal requirements but did not follow them. However, courts are applying increased scrutiny when relators premise a defendant’s alleged liability on noncompliance with an ambiguous statute or regulation, as they frequently do. Under a framework first set forth by the Supreme Court in *Safeco Insurance Co. of America v. Burr*, 551 U.S. 47 (2007), if a defendant follows an “objectively reasonable” interpretation of the law, the defendant’s subjective intent is irrelevant. As illustrated by a recent decision from the Central District of Illinois, relators who seek to use vague regulatory standards as the foundation for FCA liability should expect to be met with “[s]trict enforcement of the FCA’s knowledge requirement.”

## Case Summary & Ruling

In *United States ex rel. Proctor v. Safeway, Inc.*, the relator alleged that Safeway violated the FCA by failing to treat certain discount prices provided to customers as its “usual and customary price” for government programs, thereby overbilling those programs for prescription drugs. Safeway moved for summary judgment, arguing that during the time in question it reported “usual and customary pricing” in a manner that was “objectively reasonable, and the FCA prohibits only knowing violations of clearly established law.” To support its argument, Safeway relied on the Supreme Court’s decision in *Safeco*, a case that addressed the scierter requirement of the Fair Credit Reporting Act. In *Safeco*, the Supreme Court held that a defendant who follows an objectively reasonable, but erroneous, interpretation of an ambiguous legal standard is not reckless as a matter of law.

In response, the relator argued that the *Safeco* standard does not apply to the FCA, and that recklessness was demonstrated by evidence of Safeway’s subjective understanding of the rule. The relator also argued that even if *Safeco* does apply in the FCA context, it only applies to the “reckless disregard” formulation of the FCA’s scierter requirement, and it did not affect the relator’s ability to demonstrate that Safeway acted with actual knowledge, or at least deliberate ignorance. Finally, the relator argued that the *Safeco* standard could not save Safeway from liability because its treatment of the “usual and customary pricing” standard had not been

“objectively reasonable” in light of guidance that warned Safeway away from its approach.

The court granted summary judgment in favor of Safeway, holding that “*Safeco’s* objective scienter standard applies to the FCA.” *United States ex rel. Proctor v. Safeway, Inc.*, no. 11-cv-3406 (June 12, 2020). Applying that standard, the court found that Safeway’s application of “usual and customary pricing” – though later determined to be incorrect – had been objectively reasonable at the time the claims were submitted, irrespective of any subjective intent. The court also found that there had been “no guidance from the courts of appeals or binding authority from the applicable agency” to conclusively warn Safeway away from that interpretation.

### Key Takeaways

*Safeway* is the latest in a long line of decisions to confirm that the *Safeco* standard applies with equal force in the context of the FCA. See, e.g., *U.S. ex rel. Streck v. Allergan Inc.*, 746 F. App’x 101 (3d Cir. 2018); *U.S. ex rel. McGrath v. Microsemi Corp.*, 690 F. App’x 551, 552 (9th Cir. 2017); *U.S. ex rel. Donegan v. Anesthesia Associates of Kansas City, PC*, 833 F.3d 874, 879-80 (8th Cir. 2016); *U.S. ex rel. Purcell v. MWI Corp.*, 807 F.3d 281 (D.C. Cir. 2015). In so doing, the court continued an important trend of emphasizing “[s]trict enforcement of the FCA’s knowledge requirement.” The court’s application of the *Safeco* standard is exemplary of two critical elements of this enforcement, both of which demonstrate increasingly important arguments to rebut allegations of wrongdoing based on ambiguous standards.

**First**, the *Safeway* court refused to entertain the relator’s argument that subjective intent can establish knowledge under the FCA when the defendant’s actions were consistent with an objectively reasonable interpretation of an ambiguous rule. Citing internal emails between Safeway executives, corporate policy documents, and communications from regulators, the relator argued that it did not matter whether Safeway had adopted an objectively reasonable interpretation of the term “usual and customary,” because Safeway had acted with “actual knowledge” that its interpretation was wrong. The court rejected this argument, holding that the defendant’s “‘subjective intent’ is legally irrelevant if [it adopts] ‘an interpretation that could reasonably have found support in the courts.’” As the court explained, “if there is more than one reasonable interpretation of the applicable legal standard and no authoritative guidance, a party may think it knows what the law requires,” but, without “authoritative guidance,” a party “cannot know what is required or deliberately or recklessly ignore what is required.” “Otherwise, two actors could engage in the same conduct on the exact same facts and be subject to different liability under the FCA based on how they subjectively interpret the law. Such a result is not permitted under *Safeco*.” In sum, “[s]ubjective intent is ‘irrelevant’ if a defendant has a reasonable interpretation.”

**Second**, the court carefully examined whether the defendant was “warned away” from its course of action by authoritative guidance, placing particular emphasis on the clarity and authority of the guidance that existed at the time the alleged false claims were made. Applying *Safeco*, the court explained that the fundamental rule is that “[i]n order for the conduct to be ‘knowingly’ or ‘recklessly’ illegal . . . an authoritative interpretation must exist stating that it is.” Order at 42. If such authoritative guidance exists, a defendant cannot be objectively reasonable in taking a contrary approach.

Relying on “informal guidance documents” published by the governing regulatory agencies, statements excerpted from prior judicial decisions, and evidence of industry practices that were

contrary to Safeway's approach, the relator argued that Safeway was warned away from its application of the "usual and customary pricing" rule. The court disagreed, emphasizing two key failures in the relator's argument:

- The guidance must be "authoritative": Although there were agency guidance documents that supported the relator's interpretation, the court found that "[g]uidance documents alone [are] not [] sufficiently authoritative" to "show there was a clear rule forbidding Safeway's position at the time of the conduct," especially in light of the other guidance materials that were either ambiguous or supported Safeway's approach. The court specifically noted that the guidance materials at issue had not undergone notice and comment rulemaking, and therefore were "not binding" and did "not constitute authoritative guidance."
- The guidance must have existed in the time-period of the defendant's alleged conduct: The court also emphasized that in determining whether defendant's actions were objectively reasonable in light of existing guidance, the relevant time period is the time when the claims were submitted. Although a Seventh Circuit decision that post-dated the submission of the alleged false claims provided a clearer definition of "usual and customary pricing," this decision had no bearing on the objective reasonableness of the defendant's interpretation of the law *before* that decision was issued. A relator cannot use hindsight to impute knowledge to a defendant who did not have the benefit of the relevant guidance at the time.

As the Supreme Court said in *Safeco*, if "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." *Safeway* is just the most recent application of this sensible rule in the FCA context. It provides a valuable example of how courts may apply the *Safeco* standard and how defendants can rebut allegations of wrongdoing based on post-hoc interpretations of ambiguous statutes and regulations. Moreover, although this case was decided at summary judgment, by adopting an objective rather than subjective standard, it provides a blueprint to dispose of these types of cases at the motion to dismiss stage.

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