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SuperValu & the False Claims Act's Common-Law Roots

By Caleb Hayes-Deats
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The Supreme Court's decision in *United States ex rel. Schutte v. SuperValu Inc.* has been heralded as a win for whistleblowers, and rightly so. The court unanimously held that a defendant who subjectively believes it has submitted a false claim to the government can face False Claims Act liability, even if an objectively reasonable interpretation of relevant legal requirements would have supported the claim. That holding reversed rulings by the Seventh Circuit that would have immunized any claims that could, with the benefit of hindsight and creative litigation counsel, qualify as objectively reasonable.

As a practical matter, *SuperValu* will often preclude adjudication of whether a defendant "knowingly" submitted a false claim on a motion to dismiss or summary judgment: After *SuperValu*, the inquiry will focus on factual questions about what the defendant actually believed, rather than legal questions about what might have been objectively reasonable.

But another aspect of the opinion might give rise to new legal defenses. Specifically, the Supreme Court held that the FCA incorporates common-law doctrines, echoing its earlier decision in *Universal Health Services v. United States ex rel. Escobar*. The common law may prove fertile ground for new interpretations of the FCA, particularly in cases involving government contracts.

The *SuperValu* Decision

SuperValu involved a requirement that pharmacies and medical providers charge the government their "usual and customary price." The defendants—two retail pharmacies—had adopted price-match programs, and many customers asked them to match a competitor's prices. Those requests raised questions about whether and when discounted rates became the pharmacies' "usual and customary" prices, such that the defendants had to extend them to the government.

Caleb Hayes of MoloLamken (Courtesy photo)

The Seventh Circuit granted summary judgment for the defendants. It found that it was objectively reasonable to believe that the defendants' undiscounted retail rates were their "usual and customary prices" because no definitive legal authority had rejected that interpretation. The objective reasonableness of that interpretation immunized the defendants from FCA liability, regardless of what they subjectively believed about the "usual and customary price" requirement.

The Supreme Court reversed, holding that the FCA's knowledge element required assessment of the defen-

dants' subjective beliefs. The court traced that requirement to both the FCA's text and the common law, both of which focused "primarily" on what defendants "thought and believed." The whistleblower had produced evidence showing that defendants made most of their sales at steeply discounted prices, expressing concern internally about how the volume of such sales affected the "integrity" of their usual and customary price. That evidence, the court held, had to be considered when adjudicating defendants' scienter.

The False Claims Act and the Common Law

The Supreme Court based its holding in substantial part on common law. The court observed that the "text of the FCA tracks the common law" because the "FCA is largely a fraud statute," originally passed to stop "massive frauds perpetrated by large contractors during the Civil War." Given that history, the court deemed the FCA to incorporate the "well-settled meaning" of common-law terms absent "statutory text to the contrary."

SuperValu's discussion of common law echoes and amplifies past statements. It cited common-law sources, such as the *Restatement of Torts*, in support of its determination that the FCA requires a "subjective test" for knowledge. Similarly, in *Escobar*, the Supreme Court described the FCA's materiality requirement as "demanding" based in substantial part on state court common-law decisions.

Implications

The incorporation of common-law doctrines into the FCA may create new defenses in the future. The potential impact can be seen in *SuperValu* itself. The defendants argued that they could not face liability for statements about their "usual and customary price" because, at common law, misrepresentations about the law (as opposed to facts) were not actionable. That argument had no obvious foothold in the FCA's text, which by its terms prohibits all material false statements regardless of subject matter. But the Supreme Court "assume[d] without deciding that the FCA incorporates" some version of the common-law rule, finding that the whistleblower had pleaded a factual (or nonlaw) misrepresentation.

Perhaps the most significant questions arise in the field of government contracts, a historical hotbed for FCA litigation. At common law, courts strictly distinguished tort and contract claims. They held that even intentional or malicious contractual breaches could not support a fraud claim unless the plaintiff proved intent to commit such a breach at the time the parties entered the contract. In 2016, the Second Circuit applied that common-law principle to erase a $1 billion judgment in favor of the government under a different statute. Although a jury found the defendant had, during the financial crisis, intentionally sold government-sponsored entities mortgages that violated contractual requirements, the government had not shown that fraudulent intent existed years earlier, when the parties entered the contract. Incorporating this same common-law doctrine into the FCA could unsettle other cases involving government contracts. And that is only one of many historical common-law rules that courts might incorporate.

The impact of *SuperValu* may take years to fully understand. But as the Supreme Court closed the door on one potential defense to FCA liability, it may have opened the door to others. The decision promises potential rewards for deep historical research and legal creativity. Given the amounts often at issue in FCA cases, few stones will remain unturned.

Caleb Hayes-Deats *is a partner at MoloLamken LLP, where he represents companies and individuals in False Claims Act and other types of whistleblower litigation. Previously, he served as an assistant U.S. attorney in the Southern District of New York.*

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