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SafeCo No More: The Changing Landscape of Scienter under the False Claims Act

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By Noam B. Fischman and Ayman Rizkalla

Yesterday, the United States Supreme Court held that a False Claims Act (FCA) defendant cannot rely on an objectively reasonable interpretation of a law, regulation, or rule to negate the scienter element of the FCA. In *United States ex rel. Schutte v. SuperValu Inc.*, the Court emphasized the importance of a defendant's subjective belief in resolving the scienter element. [1] In so doing, the Court has removed a valuable argument from the FCA defense toolkit.

The FCA imposes liability on those who "knowingly presen[t]...a false or fraudulent claim for payment or approval." [2] Companies that regularly submit claims to the federal government are familiar with the complex maze of rules and regulations that often govern them. At times, those rules and regulations are drafted in a manner that renders them subject to reasonable alternative interpretations. Ambiguity was particularly relevant for healthcare and healthcare adjacent companies—in this particular case, pharmacies.

The Prior SafeCo Standard

Until yesterday, defendants could seek dismissal of fraud claims based on the absence of scienter by relying on the two-part test codified by the Court

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in *SafeCo Ins. Co. of America v. Burr*. [3] That test posed two questions. Did the defendant act consistent with an objectively reasonable interpretation of the law? If "yes," then the inquiry ended. A dispositive motion could be granted and the defendant could avoid the threat of a jury verdict and the accompanying trebling of damages, plus the prospect of draconian statutory penalties (for additional information on FCA damages, see Akerman's Health Law Rx Blog Post titled, "The Trebling Effect of (Some) False Claims Act Trials."). If "no," then the inquiry shifted to a more fact intensive question. Did the defendant subjectively believe that its actions were consistent with the law? [4] Now, this *Safeco* standard, contrived by the Court in response to a Fair Credit Reporting Act challenge almost sixteen years ago, [5] is no longer relevant.

The Court's *Supervalu* Decision

Supervalu involved two combined FCA cases, both brought against supermarkets (Supervalu and Safeway) that house internal pharmacies and that participate with Medicare and Medicaid. [6] These government payor programs limit the amount pharmacies can charge for generic medications to the "usual and customary" price. [7] Relators in these respective cases alleged that pharmacy operators knowingly filed inflated reports of the "usual and customary" drug prices when seeking reimbursement from Medicare and Medicaid. [8]

During the pertinent time period, each defendant offered discount programs to its non-government payor clients, which significantly lowered the typical cost of certain medications (in some cases to $4.00 per 30-day supply). [9] Based on an objectively reasonable interpretation of the "usual and customary" price standard, these pharmacies would charge Medicare and Medicaid for the same medications at standard retail rates (that were exponentially higher than $4.00 per 30-day supply). [10] The delta hinged on the interpretation of what is the "usual and customary" price. [11] Both Supervalu and Safeway won summary judgment at the district

court level by arguing that this standard is facially ambiguous and that their respective interpretations —essentially that "usual and customary" means the retail prices—is just as plausible as any other interpretation. [12]

The Court unanimously disagreed. It emphasized the three bases for establishing scienter under the FCA —actual knowledge, deliberate ignorance of, or a reckless disregard for the truth. [13] Relying on common law fraud principles, the Court emphasized that scienter (at common law and for the FCA) focuses on what a person believes or has reason to believe, not whether a mistaken belief is objectively reasonable. To be clear—this decision did not displace longstanding precedent establishing that mistakes alone are not actionable under the FCA. A mistake is still a mistake, not fraud. The Court took great pains to explain that someone can believe that a certain tact is legally appropriate at one moment in time, and then learn later that it is not. [14] The former conduct (depending on the facts) could constitute a non-actionable (or highly defendable) mistake. But, the continuation of that conduct after learning of its impropriety can no longer can be credibly defended under the theory of objective reasonableness. "For scienter, it is enough if respondents believed that their claims were not accurate." [15]

Ultimately, the Court emphasized that this decision should be narrowly construed. Nevertheless, it will not be without consequences to the FCA defense bar.

The Impact of this Decision

1. **Impact on summary judgment**: As mentioned above, defendants can no longer rely on the concept of an objectively reasonable interpretation of the law to defend against an FCA matter. This issue is most frequently raised pre-trial at the summary judgment stage. It is unlikely to be successful moving forward. Moving forward, the Court's focus on the distinction

between mistakes and subjectively understood violations of the law will likely become a court's focus.

2. **Impact on preliminary dispositive motions**: The Court did not displace the application of Rule 9(b) pleading standards to elements of an FCA case. Consequently, generic pleading of subjective intent likely will not suffice to permit an FCA case to progress. Accordingly, this decision should not result in a greater percentage of FCA claims surviving initial pleading deformities.
3. **Impact on clients**: Petitioners in the *Supervalu* had, allegedly, developed evidence to suggest that one or both respondents came to learn that "usual and customary" price meant the discounted price frequently offered to certain customers. Given the now enhanced role that evidence of subjective knowledge will play in defending FCA claims, clients should take this opportunity to evaluate the role that counsel plays in compliance decisions. Protecting these conversations by having them in an exclusively privileged environment would enhance the defense options available to a client in the event of an FCA claim.

Akerman has a sophisticated Healthcare Litigation team available to answer any questions that you might have regarding the impact of the *Supervalu* decision on your business.

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[1] *United States ex rel. Schutte v. SuperValu Inc.*, No. 21-111, 2023 WL 3742577 (U.S. June 1, 2023).

[2] 31 U.S.C.A. § 3729.

[3] *Safeco Ins. Co. of America v. Burr*, 551 U.S. 47 (U.S.,2007).

[4] *See SuperValu Inc.*, No. 21-111, 2023 WL 3742577, at *5.

[5] The Court in part seized on the statutory distinction between the Fair Credit Reporting Act (which bases liability on willful violations) and the FCA (which predicates liability on knowing violations). *Id.* at *8.

[6] *Id.* at *1.

[7] *Id.*

[8] *Id.*

[9] *Id.* at *4.

[10] *Id.*

[11] *Id.*

[12] *Id.* at *5 (“What mattered, instead, was that someone else, standing in respondents’ shoes, may have reasonably thought that the retail prices were what counted.”).

[13] *Id.*

[14] *Id.* at *8 (proffering a “reasonable speed” analogy).

[15] *Id.* at *10.
