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LEGAL ALERT

Pharma Happy With Supreme Court Rx: “No Overtime Pay For Pharma Sales Reps”

In an important wage-hour decision with potential relevance beyond the pharmaceutical industry, the Supreme Court held on June 18, 2012 that pharmaceutical sales reps at GlaxoSmithKline (GSK) were exempt from overtime pay under the Fair Labor Standards Act's exemption for “outside salesmen,” resolving a split among the courts.

Significantly, in reaching that decision, the Court also held that deference was not owed to a U.S. Labor Department (DOL) interpretation of the exemption (an interpretation favoring the employees' claims). The interpretation by DOL was first published only recently in court briefs (not in agency regulations), and DOL had never previously questioned the exempt status of pharmaceutical sales reps who have long been treated as exempt by such companies. *Christopher v. SmithKline Beecham*.

Were The Sales Reps “Making Sales”?

The FLSA exemption for an “outside salesman” applies to an employee if both of the following criteria are met: 1) the employee's primary duty is either “making sales” or “obtaining orders” for his employer; and 2) the employee is customarily and regularly away from the employer's places of business while performing such exempt work.

The main issue before the Court was whether the sales reps were actually “making sales” within the meaning of the exemption under circumstances where the sales reps:

- regularly called on doctors at their offices;
- urged the doctors to prescribe specific drugs of the drug-maker for particular conditions; and
- requested, and often obtained, nonbinding commitments from the doctors that they would prescribe those drugs for their patients when it was medically appropriate.

Sales reps received commissions when those particular doctors did, in fact, prescribe those drugs, as tracked through the records of dispensing pharmacies.

The sales reps (and DOL) contended that the reps were not “making sales” because the reps could not obtain sales orders or binding commitments from the doctors due to drug-industry laws precluding such orders or commitments. The reps and DOL also argued that the reps were engaged only in a non-exempt form of “promotion” work, which refers to promoting sales which will be made by other employees.



GSK (and its supporters, including the U.S. Chamber of Commerce) contended that the sales reps were “making sales” within the meaning of the overtime exemption because the reps obtained nonbinding commitments from the doctors and those doctors did subsequently prescribe those particular drugs. In fact, the more-effective sales reps caused more prescriptions to be written for the drugs by the physicians in those reps' territories. The sales reps also received intensive training in sales techniques and product knowledge, and the reps were highly rewarded. Nationwide such reps commonly earn upwards of \$90,000 per year in combined salary and commissions.

This case and similar cases brought across the country were complicated by the nature of the pharmaceutical industry where such sales reps are barred by law from obtaining actual orders from doctors for any quantity of prescription drugs. Although such sales reps are allowed to give away free samples to doctors, the exchange of payment for any such drugs occurs only when the drug-maker sells to distributors and when patients purchase from pharmacies.

Despite the somewhat unusual nature of the industry, a number of lower courts in other cases (including the U.S. Court of Appeals for the 9th Circuit in this case) previously held that the outside-sales exemption applied to such pharmaceutical sales reps because they were “employees who in some sense make the sales” (quoting from DOL's Preamble to the 2004 revision of the regulations). Some of the courts ruling that way

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noted that the doctor is the “linchpin” to the sales process because the ultimate sales of drugs to patients take place only if the doctor prescribes the particular drug. Those courts found, as one court put it, that the pharmaceutical sales reps “make sales in the sense that sales are made in the pharmaceutical industry.”

On the other hand, several other lower courts (including the U.S. Court of Appeals for the 2nd Circuit) previously ruled the other way and found that such sales reps were not exempt as outside salesmen because, as the 2nd Circuit wrote, “it is reasonable to view what occurs between the physicians and the Reps as less than a ‘sale.’”

In the end, the Supreme Court found that the pharmaceutical sales reps at GSK “qualify as outside salesmen under the most reasonable interpretation of the DOLs regulations.” The sales reps were “making sales” within the meaning of the outside-sales exemption because the reps obtained commitments from the doctors (the relevant decision-makers) to prescribe particular drugs in appropriate circumstances. In sum, the sales reps were exempt because of the nature of this particular industry and because “an employee who functions in all relevant respects as an outside salesman should not be excluded from that category based on technicalities.”

Was DOLs Interpretation Entitled To Deference?

A subsidiary but important issue, which the Supreme Court also agreed to decide, was whether the courts should give deference to DOLs interpretation of the outside-sales exemption in this context, an interpretation first announced in amicus briefs filed by DOL in these cases. DOL filed such amicus briefs in support of the employees in the appeals courts in both the 2nd and 9th Circuit cases (cases which reached opposite conclusions on the question of deference).

In the 9th Circuit’s decision in favor of GSK, that court held that DOLs interpretation of the outside-sales exemption in this context was entitled to “no deference” from the court. By contrast, ruling in favor of the employees in a different case, the 2nd Circuit’s decision was rendered

after the court held that DOLs interpretation was entitled to “controlling deference.” As those cases demonstrate, the issue of whether deference is owed to an agency’s pronouncements can be crucial to the outcome of a case where the employer’s position challenges the agency’s interpretation.

In its decision on the deference issue, the Supreme Court found there were strong reasons for denying the highest level of deference to the DOLs interpretation of the exemption regulation in this case. The Court noted: the DOL offered shifting interpretations during the litigation of the sales rep cases; the DOLs interpretation would impose massive, retroactive liability; the DOLs actions created “unfair surprise”; the DOL had never initiated any enforcement actions regarding such employees in this industry; and the only plausible explanation for the DOLs inaction for decades was that DOL acquiesced in the industry’s treatment of these sales reps as exempt. Applying “traditional tools of interpretation,” the Court then found “DOLs interpretation of its regulations quite unpersuasive.”

Ramifications Of The Supreme Court’s Decision

The Supreme Court’s decision has dramatic, favorable implications for pharmaceutical industry employers who are facing overtime suits across the country by many thousands of pharmaceutical sales reps. This decision makes the outside-sales exemption an option for such employers who can demonstrate similar circumstances.

For employers generally, although DOL interpretations in some situations will not warrant controlling deference from the courts, even in those situations the courts will look into such interpretations to judge whether they are persuasive enough that they should be followed by the courts. You should consider the possible impact of DOLs published interpretations, and court interpretations, on your wage practices governed by the FLSA, including exemption issues and others.

For more information contact your regular Fisher & Phillips attorney or visit our website at www.laborlawyers.com.

This Legal Alert presents an overview of a specific Supreme Court decision. It is not intended to be, and should not be construed as, legal advice for any particular fact situation.

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