CLIENT ALERT: United States Supreme Court Holds Pharmaceutical Sales Representatives Are Exempt Outside Sales Employees

On June 18, 2012, the United States Supreme Court held that pharmaceutical sales representatives are exempt "outside salesmen" and therefore not entitled to overtime under federal law. The *Christopher v. Smithkline Beecham* decision is significant in that the Court (a) clarified the Fair Labor Standards Act ("FLSA") "outside sales" exemption is applicable to pharmaceutical sales representatives despite their lack of a traditional sales role, and (b) declined to follow regulatory guidance from the Department of Labor ("DOL") that was directly on point.

Background

Under the FLSA, employers must pay overtime to their employees for any hours worked over 40 in a workweek. However, employees who work "in the capacity of outside salesmen" (among others) are exempt from this overtime provision. According to DOL regulations, for an "outside salesman" to be exempt, the employee's primary duty must be "making sales" (as the FLSA defines the term) and he or she must be "customarily and regularly engaged away from the employer's place or places of business" when performing this duty. The primary question in the *Christopher* case was whether this outside sales exemption applied to pharmaceutical sales representatives – specifically, whether or not their job involved "making sales."

Pharmaceutical sales representatives are responsible for trying to persuade physicians to write prescriptions for their company's products in appropriate cases. The plaintiffs in the *Christopher* case were responsible for securing non-binding commitments from physicians to prescribe Smithkline Beecham products and they frequently spent more than 40 hours per week doing so, but were never paid overtime.

Plaintiffs alleged that the failure to pay overtime was a violation of the FLSA and Smithkline defended on the basis that the plaintiffs were exempt as outside salespeople. Plaintiffs argued that they were not salespeople because they *promoted* products, they did not *sell* anything; they simply obtained non-binding commitments. (Doctors do not purchase drugs for distribution from sales representatives; patients purchase drugs from pharmacies.) Smithkline Beecham prevailed on summary judgment and the decision was affirmed by the Ninth Circuit, which created a Circuit split. (In 2010 the Second Circuit reached the opposite conclusion and held that pharmaceutical sales representatives were not exempt because they did not perform "sales.")

Department of Labor Interpretation – "Sales vs. Promotion"

The DOL submitted an *amicus* brief supporting the Plaintiffs. According to the DOL, pharmaceutical sales representatives are not exempt because their "primary duty" (obtaining non-binding commitments from physicians) is akin to "promotion" not "making sales" as defined in the relevant FLSA regulations (regulations that were drafted and promulgated by the DOL). Under the DOL's interpretation, a "sale" is not made unless the employee "actually transfers title to the property at issue."

Generally, courts will defer to an agency's interpretation of its own regulations under a principle known as "*Auer* deference" after a 1997 Supreme Court case of the same name (also dealing with DOL interpretation of the FLSA, coincidentally). However in this case, the Court refused to defer to the DOL interpretation in part because the interpretation had only existed since 2009 (announced during the aforementioned Second Circuit case) and would impose massive liability on the pharmaceutical industry for conduct that occurred well before the interpretation was announced.

This, said Justice Alito, writing for the majority, would constitute an "unfair surprise" to the industry. Moreover, treating sales representatives as exempt was a "decades-long practice" in the pharmaceutical industry, yet the DOL had never initiated any enforcement actions or suggested the practice was illegal. To the Court, this constituted "acquiescence."

After refusing to defer to the DOL's interpretation of what constitutes a "sale," the Court then closely evaluated that interpretation and rejected it altogether, describing it as unpersuasive and inconsistent with the FLSA. According to the Court, determining what constitutes a "sale" might vary by industry and, at least in the pharmaceutical industry, obtaining non-binding commitments from physicians "comfortably" fit the FLSA's broad definition of "sale." As such, the Court ruled that the pharmaceutical sales representatives were exempt outside sales people.

Significance

Employers with an outside sales force should periodically review their employees' actual job duties (not merely job descriptions) – especially those businesses that are currently treating outside employees as exempt under the federal outside sales exemption. Applying the exemption too broadly is a common and potentially expensive mistake. Although the *Christopher* case appears to expand the outside sales exemption by broadening what constitutes a "sale" under the FLSA, employers should not interpret this case as carte blanche from the Courts to treat outside employees as exempt. All decisions should be made with the assistance of counsel – particularly in light of the "industry-by-industry" language Justice Alito and the majority chose to use.

Employers should also bear in mind this decision is based upon federal law. Several states have their own versions of various exemptions and deciding which exemption will apply (if any) should be done with careful guidance from employment counsel.

Finally, from a broader standpoint, this case should serve as a reminder to employers that administrative decisions and interpretations will not always be adopted by the courts. However, identifying when judges will defer to administrative agencies and when they will not, is difficult to predict.

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