

Insights, News & Events

ARE PHARMACEUTICAL SALES REPS EXEMPT AS “OUTSIDE SALESMEN?” DIAGNOSIS UNCLEAR

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Just last August, the U.S. Court of Appeals for the 2nd Circuit issued a ruling that sent shock waves through segments of the healthcare industry. Then, as affected employers began responding to that decision, the 9th Circuit reached an apparently contradictory decision that may have raised more questions than it answered.

DUELING DECISIONS

In the first, the 2nd Circuit held that pharmaceutical sales representatives (PSRs) were not exempt from overtime as outside sales persons under the Fair Labor Standards Act (FLSA). *In Re Novartis Wage & Hour Litigation*. In making its decision, the court relied heavily on a Department of Labor (DOL) legal brief, which strongly urged a finding that the PSRs were not exempt as outside sales persons.

The DOL's contention that PSRs were not exempt caught the industry off-guard and seemingly contradicted the position taken by the DOL for over 70 years. Since the inception of the outside-sales exemption in 1938, the DOL had remained silent on the issue and acquiesced to findings that PSRs qualified for the outside sales exemption.

But the more recent 9th Circuit case of *Christopher v. SmithKline Beechman* indicates that the impact of *Novartis* and the DOL's newly-adopted interpretation may be short-lived. In *SmithKline*, PSRs filed a suit contending that they were *not* outside salesmen and should have been paid overtime. SmithKline moved for summary judgment

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contending the PSRs were exempt as outside salespersons and not entitled to overtime. Breaking with both the DOL and the *Novartis* court, the 9th Circuit agreed with *SmithKline* and found that PSRs were outside salespersons exempt from overtime requirements.

THE UNDERLYING PRINCIPAL

To qualify for the exemption from overtime pay under the FLSA's outside sales classification, 1) an employee's primary duty must be making sales or obtaining orders or contracts for services; and 2) the employee must be primarily and regularly engaged away from the employer's place or places of business in performing this primary duty.

The key difference between the *Novartis* and *SmithKline* decisions lies in the evaluation of whether a PSR's primary duty is making sales. The PSRs and DOL take a narrow reading of the exemption and argue that because federal regulations preclude PSRs from making sales directly to physicians, their primary duty is not making sales. Federal regulations preclude PSRs from obtaining anything more than a non-binding purchase commitment from the physician that, if provided with a product, the physician will appropriately prescribe it. In adopting this narrow view, the DOL disregarded the fact that PSRs were hired for their sales experience, and trained in sales methods.

The *SmithKline* court rejected the DOL's interpretation and took a much more reasoned (and more realistic) approach. *SmithKline* found the PSRs' primary duty was making sales. The court reasoned a PSR's non-binding agreement with a physician to appropriately prescribe products provided is, in fact, a sale. The court noted that like all other salespersons, PSRs earned commissions based upon sales commitments and enjoyed a largely autonomous occupation outside the office. In so ruling, the 9th Circuit flatly rejected the DOL's rigid interpretation of the exemption as it applies to PSRs and even stated "deference is not warranted because the Secretary's position is both plainly erroneous and inconsistent with her own regulations and practices...."

In light of the split opinion between the 9th and 2nd Circuits, and varying state laws that may impact the classification of PSRs, employers should be cautious. You should discuss with employment counsel the classification of these individuals under regional, state, and federal laws.

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