

Christopher v SmithKline Beecham Resolves the Exempt Status of Pharmaceutical Reps

THE SUPREME COURT DELIVERS A DECISION FOR EMPLOYERS

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The Supreme Court's June 18, 2012 decision in the case of *Christopher v SmithKline Beecham* is what the defense bar would call a solid win for employers. The Court squarely held that the Pharmaceutical Sales Representatives (PSR) position is exempt from overtime under the "outside sales" exemption and in doing so refused to give deference to the Department of Labor's (DOL) interpretation of its own regulation as set forth for the first time in its *amicus brief*. The analysis of the case that follows shows how the holding in this case could have wide reaching effects on how the courts will interpret the Fair Labor Standards Act (FLSA) and how much deference the courts will afford regulators' interpretations of their own regulations.

At its most basic level, the FLSA requires employers to pay employees overtime wages for any work done in excess of forty hours a week. Among other exemptions, the Act provides an exemption to this general rule for employees who work as outside salesman. The statute left the definition of "outside salesman" to be determined by the DOL through regulation.

Regulation 29 CFR § 541.500 defines outside salesman as "any employee . . . whose primary duty is . . . making sales within the meaning of 29 U.S.C. §203(k)." Section 203(k) of the FLSA states that the term sale "includes any sale, exchange, contract to sell, consignment for sale, shipment for sale, or other disposition." While the definitions are not perfectly clear, the DOL has previously stressed that an employee meets the exemption if the employee "in some sense, makes a sale."

The question before the Court was whether PSRs fit within the definition of "outside salesman." PSRs' duties involve calling on and meeting with physicians in their assigned sales territories to discuss the features, benefits, and risks of prescription drugs manufactured by their employer. In this case, the PSRs' primary objective was to obtain a nonbinding commitment from the physician to prescribe their employer's drugs in appropriate cases.

The pharmaceutical industry is an extensively regulated industry (a factor which weighed in the Court's analysis) that has treated PSRs as outside salesmen for seventy years. But in 2009, the DOL, in an uninvited *amicus* brief for a pending Second Circuit case, announced that PSRs did not qualify

as outside salesmen. The Second Circuit afforded the DOL's interpretation controlling deference and held accordingly. The Ninth Circuit, however, in deciding the same issue, rejected the DOL's interpretation and held that PSRs did qualify under the exemption. The Supreme Court granted *certiorari* to resolve the split amongst the Circuit courts. The DOL submitted yet another *amicus* brief defending their position before the Supreme Court.

The decision in this case was split 5-4, but it is important that all nine justices agreed that the DOL's interpretation should not be given any special consideration. Both the majority and dissent pointed out that although the DOL came to the same conclusion in all of its briefs, namely that PSRs do not qualify for the exemption, the reasoning behind this conclusion changed. In its briefs to the Second and Ninth Circuits, the DOL took the position that a "sale" requires a "consummated transaction directly involving the employee for whom the exemption is sought." In its brief before the Supreme Court, however, the DOL took the stricter position that a "sale" requires the actual transfer of title.

The Court acknowledged that deference should ordinarily be given to an agency's interpretation of its own regulations even when the interpretation is advanced in a legal brief. However, the interpretation should not be given deference when the interpretation is plainly erroneous, inconsistent with the regulation, or there is reason to suspect that it does not reflect the agency's fair and considered judgment on the matter.

Writing for the majority, Justice Alito explained that adopting the DOL's interpretation would be an "unfair surprise" for the drug companies. The industry has classified PSRs as exempt outside salesmen for decades without any reason to suspect this was a violation of the FLSA, and the agency never initiated any enforcement proceedings against the drug companies. In a particularly strong statement, Justice Alito explained "it is one thing to expect regulated parties to conform their conduct to an agency's interpretations once the agency announces them; it is quite another to require regulated parties to divine the agency's interpretations in advance or else be held liable." Therefore the Supreme Court did not give the agency any special deference.

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The majority went on to explain why the DOL's position was also incorrect. The DOL argued that the term "sale" as used in the outside salesman exemption requires the employee to actually transfer title of goods. The Court found this interpretation to be "flatly inconsistent" with the FLSA's definition of sale found in §203(k), which defines "sale" to include a "consignment for sale." Because a consignment for sale does not require the transfer of title, the Court rejected the DOL's argument that outside salesmen only qualify for the exemption if they transfer title.

The Court employed its own pragmatic approach to analyze whether PSRs qualify for the outside salesmen exemption. The Court first looked to the language of the statute, which exempts anyone employed "in the capacity of [an] outside salesman." Because the statute referred to the "capacity" of the employee, the Court understood that the statute calls for a functional, rather than formal, understanding of what the employee's responsibilities are in determining if the employee qualifies as a salesman.

The Court next turned to the language of the DOL regulations which incorporate the statutory definition of sale found in §203(k). As stated above, under §203(k) "sale" or "sell" "includes any sale, exchange, contract to sell, consignment for sale, shipment for sale, or other disposition." Because the statute uses the terms "includes," "any," and "other disposition" the Court understood the statute as requiring a broad definition of "sale." Finally, the Court noted that the term "other disposition," as used in the §203(k), must include transactions that do not result in a firm commitment to buy product. The Court reasoned that if the salesman offers to sell something and the buyer commits to buy, a formal contract has been made and the term "other disposition" would not add anything to the statute which already accounts for "contracts to sell."

Applying its understanding of the regulations to the PSR context, the Court found that PSRs are exempt outside salesmen. Obtaining a nonbinding commitment from a physician to prescribe one of the company's drugs is the equivalent of a sale in the uniquely regulatory environment of prescription medicine. Furthermore, the PSRs bear all the external indicia of salesmen. They are hired for their sales experience. They are trained to close each sales call by obtaining a commitment. They work away from the office, with minimal supervision, and they are rewarded with incentive based compensation. Also, this interpretation comports with the stated purpose of FLSA's outside salesman exemption because PSRs make well above minimum wage, it is difficult to standardize a time frame for their work, and their responsibilities cannot be easily transferred to other employees after forty hours in a week.

The Majority rejected the argument that PSRs are actually promotional employees who merely stimulate the sales made by others. That argument states that the employees who sell the drugs to the pharmacies are actually the company's outside salesmen. The Court found this argument too formalistic, and analogized it to a car salesman who receives a commitment to buy a car but then asks his or her assistant to process the sale into the computer. Certainly, the assistant is not the one who made the sale. Any other interpretation would be inconsistent with the "realistic approach" the statute calls for.

While the Dissenters agreed that the DOL interpretation should not be afforded any deference, they disagreed with the Majority's broad definition of "sale." The Dissent argued that it is the pharmacist who actually sells the drugs for the drug company; the PSRs are not really involved in any actual sales. PSRs only inform the doctors about the drugs and should fall within the regulation's definition of promoters.

Furthermore, PSRs cannot ethically persuade doctors into "buying" their product. If the drug is the best option for the patient, the doctor should prescribe it without the need for any "selling." If some other drug would be more beneficial, the doctor should prescribe that drug regardless of how hard the PSR has "sold" the product. So, the PSRs main goal cannot be to "sell" the doctor on the drug, rather, the PSRs keep the doctors informed of the up to date data about their drugs. Therefore, PSRs main duty is to keep the doctor informed and they should not qualify as salesmen.

Finally, the Dissent explained that the majority's car salesman analogy is flawed. In the case of a car, the salesman has already obtained a firm commitment from the buyers that a sale is going to ensue. When the assistant enters the data into the computer, he or she is merely carrying out the ministerial tasks of the transaction. PSRs, on the other hand, do not receive a firm commitment to buy when they obtain a nonbinding commitment from a doctor. Because PSRs do not actually sell anything, and because the PSRs job is mostly informational, the dissent argues that they should not qualify for the outside salesman exemption.

The effects of this holding are potentially broad. At a minimum, we do not expect to find courts blindly accepting an agency's interpretation of its own regulations especially in a retroactive context. This holding also indicates that the Court will take a functional, rather than formalistic, approach to interpreting regulations even if it goes against an agency's wishes.

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