

March 2012

Supreme Court to Decide Significant Case on the Outside Sales Overtime Exemption

By Richard Black and Bradley Strawn

Earlier this week, GlaxoSmithKline PLC (Glaxo), formerly known as SmithKline Beecham Corporation, filed its brief in the U.S. Supreme Court in *Christopher v. SmithKline Beecham Corporation*, one of the only Supreme Court cases to address the overtime exemptions under the Fair Labor Standards Act (FLSA), and the first to address the criteria for the outside sales exemption. At issue is whether pharmaceutical sales representatives (PSRs) qualify for the outside sales exemption because pharmaceuticals are generally purchased by end-users at pharmacies, which purchase from wholesale distributors. The Court's decision may have far-reaching implications, not only for the pharmaceutical industry, but also for other industries that depend on representatives to call on customers at their place of business to generate sales, although the actual sales orders are placed by customers through a centralized order and distribution center or similar process. The case is also significant because it may determine the extent to which courts are required to defer to U.S. Department of Labor's (DOL) changing interpretations of federal employment statutes and regulations.

Petitioners' Position

Petitioners Michael Shane Christopher and Frank Buchanan (Petitioners), former SmithKline PSRs, are seeking to reverse the Ninth Circuit Court of Appeals' decision¹ holding that: (1) Glaxo's PSRs were properly classified as exempt under the "outside sales" exemption, and (2) the court was not required to defer to the DOL's *amicus brief*, on behalf of petitioners, interpreting the exemption.

PSRs Do Not Actually Sell

First, as to the outside sales exemption, Petitioners argue that PSRs are not engaged in sales because they do not actually sell Glaxo products to anyone. Rather, Petitioners argue, PSRs "promote" Glaxo products to healthcare providers. Petitioners claim that PSRs "provide medical professionals who prescribe pharmaceuticals with the 'details' of pharmaceutical products, seeking to educate the prescribers with the ultimate goal of influencing their prescribing decisions." Petitioners also rely heavily on the fact that PSRs are prohibited by federal law from actually selling pharmaceuticals. Moreover, Petitioners attempt to set the theme for their argument by throughout their brief repeatedly referring to PSRs as "detailers" (an antiquated term in the industry with far fewer sales-related connotations).

Courts Should Defer to the DOL's Position

Second, Petitioners argue that the Ninth Circuit erred by not deferring to the DOL's regulations, and actually "usurped the role that Congress assigned to the Department of Labor." Petitioners argue that, in its regulations, the DOL expressly defined an "outside salesman" as an "employee with the 'primary duty' of 'making sales,'" and that the DOL purposefully drew a sharp distinction between employees who sell something themselves and those who "promote" products to stimulate sales of others. According to Petitioners, PRSs fit cleanly into the category of those who undertake "promotional work that is incidental to sales made, or to be made, by someone else."² Throughout their argument, Petitioners sound a common theme – that any question or ambiguity surrounding the outside sales regulations should be read narrowly and afforded great deference.

Petitioners further argue that the DOL's *interpretations* of its regulations, in *amicus* briefs in this case and others, are also binding on the courts. They claim that assessing the outside sales exemption is a "classic" case for deference because Congress "created the Department of Labor precisely in order to administer the nation's labor laws, particularly the FLSA." The courts, argue Petitioners, lack the experience or knowledge the DOL possesses to define and set parameters around the meaning of "outside sales." Taking particular aim at the Ninth Circuit, Petitioners state: "No member of the Ninth Circuit spent a career studying the labor markets and developing rules for their orderly administration, much less a career undertaken on the basis of a congressional assignment to develop a special expertise in that field."

Finally, Petitioners argue that the Ninth Circuit erred when it "buttressed" its conclusions with the fact that for more than 70 years the DOL "did not challenge the conventional wisdom that detailing is the functional equivalent of selling pharmaceutical products" asserting that "[t]here is no indication that the Department of Labor previously was aware of and considered whether pharmaceutical detailers are outside salesmen." At the same time, Petitioners argue that the DOL is entitled to "change its views" so long as the change is reasoned.

The Employer's Position

In its brief to the Supreme Court, Glaxo argues for affirmance of the Ninth Circuit's decision asserting that the DOL's position in *amicus* briefs in *Christopher* and other recent PSR cases is not entitled to deference under any Supreme Court precedent. Glaxo asserts that Petitioners and the DOL interpret the outside sales exemption much more restrictively than required by the broad and flexible language of the FLSA and the DOL's implementing regulations. Glaxo further argues that the DOL's current position is a radical change that would abrogate regulatory rulemaking procedures and reverse over 70 years of acceptance of PSRs as exempt from overtime. Glaxo asserts that the DOL's interpretation of the exemption ignores the language of the statute itself, Congressional intent, and the DOL's own prior interpretations of its regulations. Glaxo also disputes Petitioners' characterization of the work PSRs perform.

PSRs' Primary Duty Is Sales

While Petitioners characterize PSRs' duties as merely promoting Glaxo's products to physicians and not actually consummating sales to wholesalers or pharmacies, Glaxo emphasizes that physicians, who are the only people authorized under federal law to write prescriptions, are the real "customers" and the focus of Glaxo's sales efforts. When hiring PSRs the company prefers candidates with prior sales experience. In fact, the PSR job announcement states that PSRs' "key responsibility" is to "[s]ell products to [a] specific customer market according to the business plan." PSRs are expected to use "customer-focused selling techniques" and to develop and deliver informative "sales presentations based on customer needs," and to "[p]ositively impact sales in [their] territory." Glaxo trains PSRs in specialized sales skills, and "closing the sale" by asking for a commitment from customer-physicians to prescribe Glaxo products for patients when medically appropriate. On the job, PSRs visit physician-customers at the physicians' locations. They target physicians they believe can appropriately prescribe more Glaxo products and thus increase Glaxo's sales in their territories, and then tailor their sales approach for those physicians. PSRs are evaluated on sales techniques: planning for each sales call; executing an effective sales presentation; and obtaining commitments from physicians to prescribe Glaxo products for appropriate patients. In addition to salary, a significant portion of the PSRs' total pay is commission contingent upon convincing physicians on whom they call to write more prescriptions for Glaxo drugs for appropriate patients, thereby directly increasing sales within the territory.

The Outside Sales Regulations Have Historically Been Interpreted Broadly

Explaining the DOL's recent "abrupt about-face" toward a much more restrictive meaning of outside sales, requiring a transfer of title, Glaxo

takes the Court through the broad, flexible language and interpretations that have historically been applied to the definitions of “sale.” Glaxo emphasizes that Section 3(k) of the FLSA defined “sale” in broad and flexible terms to “include[] any sale, exchange, contract to sell, consignment for sale, shipment for sale, or other disposition.”³ Glaxo notes that a consignment, which is included as an example of a sale, does not involve a transfer of title. Glaxo also cites the 1940 Congressional Committee Stein Report, which emphasized the flexible, nonrestrictive manner in which Congress defined “sales” in Section 3(k), and explained that an employee engages in “sales” whenever he has “in some sense ma[d]e a sale.”⁴ The Stein Report explained that “[i]n borderline cases, the test is whether the person is actually engaged in activities directed toward the consummation of his own sales, at least to the extent of obtaining a commitment to buy from the person to whom he is selling.”⁵ Glaxo emphasizes that, consistent with this test, PSRs’ “core responsibility” is to meet with customer-physicians to “obtain a commitment” to write more prescriptions for Glaxo products, where medically appropriate. Another DOL regulation – entitled “Selling” – emphasizes the flexible approach to sales by providing that as long as the employee *in any way participates* in the sale of the goods he will be considered to be “selling” the goods, whether he physically handles them or not.⁶ Thus, if an employee performs any work that, *in a practical sense*, is an essential part of consummating a “sale” of the particular goods, he will be considered to be “selling” the goods.

Glaxo argues that the current regulations remain flexible, defining an “outside salesman,” as one whose “primary duty” is “making sales within the meaning of section 3(k) of the Act” and “[w]ho is customarily and regularly engaged away from the employer’s place or places of business in performing such primary duty.”⁷ In explaining its current regulations when they were adopted in 2004, the DOL emphasized that it “did not intend any substantive changes” and it in fact did not change its interpretation of the term “sales.”⁸ The DOL specifically reiterated its statement from the Stein Report that all that is required for the exemption to apply is that the employee “in some sense make the sales.”⁹ Over the years the DOL has also provided other guidance and has approvingly quoted judicial decisions for the proposition that “the term ‘sale’ does not always have a fixed or invariable meaning.”¹⁰ Thus, until recently, Glaxo argues, the DOL has consistently construed the term “sale” in a flexible, pragmatic, rather than a technical or restrictive, manner.

No Deference Should Be Given to the DOL’s New Interpretation

Glaxo argues that the DOL’s new, sharply constrained interpretation of the term “sales” in its uninvited *amicus* briefs amounts to a “reinterpretation” of its regulation resulting in an “unfair surprise” to the regulated parties and an “end-run” around the rulemaking process. Thus, the DOL’s reinterpretation in its *amicus* briefs is not entitled to controlling deference because granting deference in such circumstances would circumvent the procedural safeguards of the agency rulemaking process. Finally, Glaxo argues that deference is inapplicable here because the DOL’s regulations simply incorporate and parrot the statutory definition of “sale” and, pursuant to the Supreme Court’s decision in *Gonzales v. Oregon*,¹¹ deference is not warranted when a regulation does little more than restate the terms of the statute.

In sum, Glaxo asks the Supreme Court to decline to defer to the DOL’s about-face regulatory interpretations, expressed only in uninvited *amicus* filings, and instead find that PSRs do in fact make “sales” and that the “sale” in the pharmaceutical industry is the exchange of nonbinding commitments between the PSRs and physicians. This flexible, pragmatic approach is supported by the text of Section 3(k), which defines the word “sale” to include “consignment” and “other dispositions” that do not necessarily require a transfer of title, and by the DOL’s own usage and regulations, which as recently as 2004 reaffirmed the concept that a salesmen is someone who “in some sense” sells.

The parties, the pharmaceutical industry, and the thousands of companies that employ outside sales representatives are awaiting the Supreme Court’s decision with hope that it will provide guidance in interpreting the outside sales exemption. All employers are looking to the Court to provide clarity as to the DOL’s role in employment litigation regarding federal employment laws and regulations.

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¹ *Christopher v. SmithKline Beecham Corp.*, 635 F.3d 383 (9th Cir. 2011).

² 29 C.F.R. § 541.503(a).

³ 29 U.S.C. § 203(k) (emphasis added).

⁴ United States Department of Labor, “Executive, Administrative, Professional . . . Outside Salesman” Redefined: Report and Recommendation 46 (1940) (“Stein Report”).

⁵ *Id.*

⁶ 29 C.F.R. § 779.241 (1970) (emphasis added).

⁷ 29 C.F.R. § 541.500(a).

⁸ See Defining and Delimiting the Exemption for Executive, Administrative, Professional, Outside Sales, and Computer Employees. 69 Fed. Reg. 22,122, 22,161-22,162 (Apr. 23, 2004).

⁹ *Id.* at 22,162.

¹⁰ See Wage and Hour Opinion Letter FLSA 2005-6, 2005 WL 330605 (Dep't of Labor Jan. 7, 2005).

¹¹ 516 U.S. 213 (2006).