Employment Law: Wage and Hour

Second Circuit Strips Pharmaceutical Sales Reps Of Their Exempt Status

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Case Returned To Lower Court To Determine Company’s Overtime Liability

A federal appellate court recently held that pharmaceutical sales representatives did not fall under either the “outside sales” or “administrative” exemptions to the Fair Labor Standards Act (FLSA), and that, accordingly, they had been misclassified and are entitled to unpaid overtime. The overtime to which the workers could be entitled is significant, because they typically work 12-hour days, travel for their jobs, and attend after-hours events as part of their marketing efforts. In re Novartis Wage and Hour Litigation, 09-0437-cv, Second Circuit Court of Appeals (July 6, 2010).

Factual Background

Sales representatives at two pharmaceutical companies brought separate overtime class actions in which they claimed that their employer had misclassified them as exempt employees (who are not entitled to overtime pay). The reps claimed that they are not covered by either the “outside sales” or “administrative employee” exemptions.

Legal Analysis

In a consolidated opinion addressing both cases, the Second Circuit Court of Appeals considered Novartis’ position that their reps are covered by either the outside sales exemption (because they are marketing and selling products), or the administrative employee exemption (because they are highly compensated and exercise sufficient discretion and independent judgment in their jobs). The court first decided that the reps did not qualify for the outside sales exemption because they never actually sell product; rather they provide information about the product and encourage doctors to prescribe it. Without selling their product (by making a deal that results in the transfer of the item in exchange for money), the reps cannot qualify for the outside sales exemption.

Novartis asked the court to focus on the fact that physicians are asked to “commit” to prescribing a specific drug. But the court noted that, by definition, physicians do not commit to buying a Novartis product. Rather, physicians must prescribe drugs appropriate for their patients and cannot make binding commitments. The court was further influenced by the fact that it is difficult to tie the reps’ compensation directly to the results of their marketing efforts. After considering these factors, the court held that the reps do not qualify for the outside sales exemption.

The Second Circuit also considered whether the reps are exempt administrative employees and found that they have little discretion over their sales strategy or methods. Rather, the sales reps are trained in how to question physicians to
determine why they may be hesitant to prescribe certain drugs, are taught four "social styles" to use depending on a physician's response to a sales call, and are provided with specific "core messages" to convey during each sales call.

The court also found that the reps play no role in formulating the company's core messages, written marketing materials, or advertising messages. In fact, they are specifically instructed not to deviate from the core message or company-provided written materials. The court was particularly persuaded by one rep's testimony that Novartis expects the reps to act like "robots." Given those indicators that the rep's jobs are highly formulaic and lack independent discretion, the court rejected the claim that they are covered by the administrative exemption.

Based on the court's ruling that the reps are not covered by either exemption, the cases will now be remanded to the lower courts to determine the appropriate damages.

**Practical Impact**

The Second Circuit is only the second federal appellate court to address the classification of sales reps under the FLSA. The Third Circuit Court of Appeals ruled earlier this year that reps exercise sufficient discretion and independent judgment to qualify for the administrative exemption. There is currently a rep classification case pending in the Ninth Circuit, and other appellate courts may be asked to consider the question as well. The disagreement among the courts may bring the issue before the U.S. Supreme Court.

In the meantime, the Second Circuit's decision poses a serious challenge for pharmaceutical companies classifying reps as exempt. Pharmaceutical companies, particularly those doing business in New York, Connecticut, and Vermont, should closely examine the classification of their reps and the basis for any exemptions. In addition, the federal Department of Labor (DOL) made it clear through the Novartis case that it does not think reps working for pharmaceutical companies are exempt, so the DOL may increase enforcement of overtime payments to reps in the wake of this decision.

While the court held that neither exemption applies to the Novartis reps, there may be more flexibility in applying the administrative exemption to reps at other companies that may allow more latitude and independent discretion. Companies should examine the duties of their reps and work with counsel to assess their level of independent discretion.

A shareholder in Ogletree Deakins' Boston office, notes that "pharmaceutical companies likely face a unique challenge in allowing reps to exercise autonomy while still complying with strict federal regulations regarding pharmaceutical marketing. Companies should consider working with their counsel to develop a plan that is consistent with both wage and hour law and other industry regulations." If it is not feasible to allow reps a greater level of discretion and autonomy, companies should carefully consider reclassifying reps as nonexempt, and may need to limit their travel time and after hours work.

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