

Wage-and-Hour Challenges in Drug Sales



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In the recent movie, “Love and Other Drugs,” the lead character Jamie (Jake Gyllenhaal) gets a job as a pharmaceutical sales representative (PSR). At a family dinner, Gyllenhaal’s messy, overweight, but very business-savvy brother, played by Josh Gad, explains the appeal of his brother’s job to their parents. As Gad explains to them, PSR positions are the only entry-level jobs in America that can pay “a hundred grand a year.” (And there was no mention of overtime pay in the movie dialogue!)

Under this comic setup lurks a serious and complex wage-and-hour issue that has produced a dramatic conflict in the courts. In cases filed all over the nation, PSRs have argued that their positions are nonexempt, the claimed exemptions do not withstand analysis, and they should be paid by the hour for the long hours worked. The drug companies have argued that, consistent with decades of such treatment, the PSRs are exempt from the overtime pay laws pursuant to the outside sales and/or administrative exemptions.

The typical job duties of a PSR are depicted in “Love and Other Drugs,” as Gyllenhaal, with his engaging smile and blatantly flirtatious manner, successfully

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charms receptionists, nurses and doctors and encourages doctors to prescribe the products he is promoting. (He does have the extraordinary good luck to be assigned the drug Viagra.)

According to the various factual recitations of PSR job duties as described in the cases, PSRs are typically in the field from 8 a.m. to 5 p.m. on work days — sometimes showing up at hospitals early in the morning, calling on as many as 10 physicians a day, taking doctors to lunch, driving to appointments, checking emails and filling out reports, and organizing events that often last into the evening.

Drug companies train the PSRs how to tailor their presentations to certain doctors’ social styles, how to maximize the impact of a five-minute meeting with a doctor, how to take doctors out for breakfast, lunch or dinner, and how to bring gifts of food or coffee to the doctor’s offices.

In the cases, the drug companies rely on the “outside sales” exemption and/or the “administrative” exemption to argue that no overtime pay is due. The cases are filed as class actions and the potential exposure is large. The spate of lawsuits has come as a shock to the pharmaceutical companies because they have, for more than 70 years, routinely treated PSRs as exempt pursuant to the exemptions provided by the federal Fair Labor Standards Act of 1938 and similar state laws.

Courts have reached widely varying conclusions in the current cases. The contrast between the Second Circuit and the Ninth Circuit appeals courts is particularly startling, with the Second Circuit siding with the PSRs and the Ninth coming down on the side of the pharmaceutical companies.

SECOND CIRCUIT HOLDS PSRS ARE NOT EXEMPT

The Second Circuit weighed in on the

treatment of PSRs in the case *In re Novartis Wage and Hour Litigation*. In that case, Novartis Pharmaceuticals Corp.’s current and former PSRs (who earned an average compensation of \$91,539 per year) alleged they were not truly exempt employees under the FLSA and thus were entitled to overtime pay for hours worked in excess of 40 in a week. The district court had granted summary judgment to Novartis on the grounds that the PSRs were exempt under both the outside sales and administrative exemptions.

The PSRs appealed to the Second Circuit, contending that the lower court did not properly apply the exemption standards set out in the regulations promulgated by the secretary of labor pursuant to the FLSA. The secretary of labor appeared as amicus curiae and supported the position of the PSRs, contending that the PSRs were nonexempt because they did not make sales nor exercised sufficient discretion and independent judgment.

In its ruling, the Second Circuit analyzed the functions served by the PSRs under both the outside sales and administrative exemptions and agreed with the secretary of labor. The court noted that when a PSR calls on a doctor, “The meetings are brief — generally less than five minutes — and the physicians neither buy pharmaceuticals from the reps nor commit to buying anything from the reps.” The *Novartis* court concluded that the PSR has not in any sense made a sale, and therefore the outside sales exemption does not apply.

The administrative exemption also failed, in this court’s view, because the claimed discretion and independent judgment that PSRs supposedly exercise was insufficient. For example, the ability to “develop a rapport with a physician who has a certain social style” or the “ability to remember past conversations

with a given physician” are skills gained through Novartis training sessions, and applying these skills does not demonstrate the necessary independence and discretion required for the administrative exemption.

Novartis subsequently appealed the matter to the U.S. Supreme Court. On Feb. 28, the Supreme Court denied *certiorari*, despite the conflict among the circuit courts in the interpretation of the exemptions as they relate to PSRs.

NINTH CIRCUIT HOLDS PSRS ARE EXEMPT

A few months after the Second Circuit’s opinion, the Ninth Circuit reached the exact opposite conclusion in *Christopher v. SmithKline Beecham*. The *SmithKline* case involved a potential class action by PSRs who were well-compensated and had job functions virtually identical to those of the Novartis PSRs.

The Ninth Circuit reached a conclusion that conflicts directly with the Second Circuit and reasoned that when the PSRs make “calls” on doctors, and obtain vague nonbinding commitments to prescribe, the reps are making “sales” as much as sales can be made in the highly regulated world of drugs as products. The court pointed out that PSRs can earn salaries well above minimum wage — up to \$100,000 a year.

In addressing the issue of an absence of a clear sale when the PSR leaves the doctor’s office, the Ninth Circuit stated that “the fact that commitments are nonbinding is irrelevant; the record reveals that binding or nonbinding, a physician’s commitment to a PSR is nevertheless a meaningful exchange because pharmaceutical manufacturers value these commitments enough to reward a PSR with increased commissions when a physician increases his or her use of a drug in the PSR’s bag.”

The Ninth Circuit also considered the current view of the secretary of labor, as laid out in the amicus brief filed in the *Novartis* case, and refused to give deference to the secretary’s views as to what constitutes a true sale. The *SmithKline* panel regarded the PSRs as highly paid workers, clearly exempt, in accordance with the way they have been categorized for decades: “PSRs are driven by their own ambition and rewarded with commissions

when their efforts generate new sales. They receive their commissions in lieu of overtime and enjoy a largely autonomous work-life outside of an office.”

On March 24, in the *SmithKline* case, the secretary of labor filed an amicus brief in support of plaintiffs-appellants’ petition for a rehearing *en banc*, noting that the case is one of exceptional importance, that it is in direct conflict with a decision of the Second Circuit, that cases turning on the same issues are pending in the Fifth and Seventh circuits, and that the case “affects a rule of national application in which there is a need for national uniformity.”

MORE CONFUSION — OTHER CASES AND OTHER COURTS

Two opinions from the Third Circuit issued in 2010 and an opinion from the U.S. District Court for the Southern District of Florida issued in July demonstrate the logical challenges faced by courts when considering the outside sales and administrative exemptions for PSRs.

In *Smith v. Johnson & Johnson*, (3d Cir. 2010), a potential class action brought by a former PSR of a subsidiary of Johnson & Johnson, plaintiff was found to be exempt under the administrative exemption only, and the Third Circuit affirmed that the outside salesman exemption did not apply. The former PSR had a base salary of \$66,000 plus the potential for bonuses.

The Third Circuit panel focused on the administrative exemption and did not provide any analysis of the outside sales exemption that had been rejected by the lower court. The court laid out the administrative exemption requirements, namely that the employee: 1) be compensated on a salary or fee basis at a weekly rate of \$455 or more; 2) have a primary duty that is the performance of office or nonmanual work directly related to the management or general business operations of the employer or its customers; and 3) exercise discretion and independent judgment with respect to matters of significance.

Plaintiff’s compensation was obviously adequate, but the parties disagreed on the other two requirements. Finding that the position involved a “high level of planning and foresight” and that she developed a strategic plan to maximize her sales, the court concluded that the second requirement was met.

As to the third requirement, the court found that the PSR performed almost all of her functions (including traveling to doctors’ offices and hospitals where she extolled the benefit of J&J pharmaceuticals) without direct oversight and ran her territory as she saw fit, according to her own testimony. As a result, the court held that she was exempt from the overtime requirements pursuant to the administrative exemption.

In another Third Circuit case, *Baum v. AstraZeneca LP*, a former PSR of the company, with a base salary of \$63,000, had been found to be exempt by the district court pursuant to the outside sales exemption under Pennsylvania law.

Plaintiff appealed to the Third Circuit, which dodged the tricky “sales” issue and affirmed “on different grounds,” finding that her job with AstraZeneca had very similar duties to those of the plaintiff in *Smith*. The court reviewed the duties and responsibilities of the PSR and concluded that she “exercised discretion and independent judgment in her day-to-day activities” and that she was involved in the marketing and advertising of the company’s products.

The court determined that she had significant discretion in how and where she approached physicians, used innovative themes in making approaches, and spent the majority of her time in the field unsupervised. This matter was also appealed to the U.S. Supreme Court. As with *Novartis*, the court denied *certiorari*.

In *Palacios v. Boehringer Ingelheim Pharmaceuticals*, (S.D. Fla. 2011) the district court was asked to rule on competing motions for summary judgment on the applicability of the outside sales and administrative exemptions to PSRs. In considering the outside sales exemption, the court analyzed the rulings in the *Novartis* (Second Circuit) and *SmithKline* (Ninth Circuit) in great detail. Ultimately, the court sided with the Second Circuit in finding the outside sales exemption inapplicable to PSRs, stating that:

“Plaintiff’s inability to transfer ownership of any one of the drugs she was responsible for in exchange for money, her inability to take a purchase order for any of the drugs, and her inability to obtain a binding commitment from physicians to prescribe a drug, renders her unable to

make a 'sale' as defined under the FLSA and its implementing regulations."

In ruling that the administrative exemption likewise did not apply, the court expressly distinguished the ruling in the Third Circuit case of *Smith*, finding that the work of plaintiff was not related to the management or general business operations of Boehringer Ingelheim, and that plaintiff did not exercise discretion or independent judgment in matters of significance as required to be exempt under the administrative exemption.

OVERVIEW — THE MURKY FUTURE

The dueling decisions percolating throughout the courts leave the pharmaceutical industry in a quandary as to the correct classification of their PSRs. While the Ninth and Third circuits concluded that PSRs are properly treated as exempt employees, these courts used different exemptions to justify their conclusions. The Ninth Circuit relied on the "outside sales" exemption and the Third Circuit used the "administrative" exemption.

The Second Circuit, the Southern Dis-

trict of Florida and the secretary of labor argue strenuously that PSRs should not be treated as exempt employees. Eventually, the U.S. Supreme Court may well clear up the confusion.

The only conclusion that can be drawn at this point is all employers, not only pharmaceutical companies, should re-examine the classification of their employees. Periodic review of classifications of employees, especially those who spend a great deal of work time out of the office, would serve employers well.