Are Pharmaceutical Sales Representatives Exempt from the FLSA Overtime Pay Requirements?

BY IGOR M. BABICHENKO

Second Circuit Says “NO,” Creates Circuit Split

On July 6, the Second Circuit Court of Appeals issued a decision in the Novartis wage and hour litigation.¹ The Second Circuit Court of Appeals reversed a judgment from the United States District Court for the Southern District of New York, which found that Novartis sales representatives (“sales reps”) were exempt from the overtime requirements of the Fair Labor Standards Act (“FLSA”).² The Second Circuit opinion on whether pharmaceutical sales representatives are exempt under either, or both, the administrative and outside sales exemptions is the most decisive appeals court ruling to date. This opinion, however, differs from those of several district courts as well as the Third Circuit Court of Appeals and creates some confusion for major drug companies.

I. Facts of the Case

The Novartis Litigation was a consolidation of two FLSA collective actions, both claiming that approximately 2,500 pharmaceutical sales representatives employed by the company were misclassified as exempt from the overtime requirements of the FLSA.³ The primary function of the sales reps was calling on physicians and giving them information about Novartis’ drugs.⁴ Because Novartis’ products are heavily regulated by the Food and Drug Administration (“FDA”), Novartis provided its sales reps with scripts and prepared promotional materials to which they had to strictly adhere during their discussions with physicians.⁵ Even though sales reps were provided with scripts, they planned their own daily call schedules and decided when to visit each doctor on their target list.⁶ In addition, sales reps organized “lunch-and-learn” presentations and other informational events for the physicians on their lists using a budget provided by Novartis.⁷

Sales reps worked from home and spent most of their day traveling in company-provided vehicles from physician to physician.⁸ Although once every four to six weeks managers would accompany the sales reps on their trips, sales reps generally conducted business on their own.⁹ Because FDA rules prohibit pharmaceutical sales representatives from making direct sales of drugs to physicians, the sales reps’ goal was to persuade physicians to prescribe Novartis’ products to their patients.¹⁰

II. District Court Granted Novartis’ Motion for Summary Judgment

In granting Novartis’ motion for summary judgment, the District Court held that the sales reps were properly classified as either exempt “outside salespersons” or exempt administrative employees under the FLSA.¹¹ Applying what it called the “spirit, purpose, and goals” of the FLSA, the District Court reasoned that outside salespersons “are exempt from overtime pay requirements not because they ‘sell,’ as that term is technically defined, but rather because they (1) generate commissions for themselves through their work and (2) work with minimal supervision, making adherence
to an hours-based compensation scheme impractical.” Even though FDA rules prohibited the sales reps from making direct sales, evidence demonstrated that the sales reps’ so-called “promotional” activities were in fact very successful in increasing the sales of Novartis’ products. In addition, Novartis’ incentive-based pay structure and the sales reps’ relative freedom from supervision contributed to the conclusion that the sales reps were exempt “outside salespersons.”

Turning to the FLSA administrative exemption, the court held that Novartis’ sales reps engaged in work that was directly related to Novartis’ management or general business operations and that they exercised discretion and independent judgment as to matters of significance. Noting the administration/production dichotomy, the District Court reasoned that the sales reps did not play a role in the research, development, and manufacturing of Novartis’ drugs, and that the sales reps’ “promotional” duties were ancillary to Novartis’ production work. In addition, the District Court concluded that the sales reps enjoyed the autonomy traditionally associated with “outside salespersons.” Thus, Novartis properly classified its sales reps as exempt administrative employees.

III. The Department of Labor Weighs-In on Appeal

In an unusual move, the Department of Labor (“DOL”) filed an amicus brief on appeal arguing that, because the sales reps do not actually make sales or obtain orders, they are not “outside salespersons,” and because they do not exercise discretion and independent judgment, they are not administrative employees. The DOL argued that because the sales reps do not sell any drugs or obtain any orders for drugs, and can at most obtain from the physicians a non-binding commitment to prescribe Novartis’ drugs to their patients when appropriate, they do not satisfy the plain and unmistakable requirement under the regulations that their primary duty must be “making sales.” In addition, the DOL maintained that Novartis’ sales reps did not fall under the administrative exemption because, when promoting the drugs to physicians, the sales reps were not permitted to deviate from the “core message” found in the scripts, manuals, brochures, and other materials that Novartis provided them.

IV. The Second Circuit Court of Appeals Sides with Plaintiffs and the DOL

Concluding that the DOL’s interpretation of the relevant FLSA regulations are entitled to “controlling deference,” the Second Circuit Court of Appeals reversed the District Court’s decision in favor of Novartis. The Court of Appeals agreed with the DOL’s position that, “when an employee promotes to a physician a pharmaceutical that may thereafter be purchased by a patient from a pharmacy if the physician—who cannot lawfully give a binding commitment to do so—prescribes it, the employee does not in any sense make a sale” (emphasis added). According to the facts of the case, Novartis’ sales reps received no such binding commitment from the physicians they contacted to buy or even prescribe. Thus, the court held that “where the employee promotes a pharmaceutical product to a physician but can transfer to the physician nothing more than free samples and cannot lawfully transfer ownership of any quantity of the drug in exchange for anything of value, cannot lawfully take an order for its purchase, and cannot lawfully even obtain from the physician a binding commitment to prescribe it,” the employee does not fall under the FLSA “outside salesperson” exemption.

Turning to the FLSA administrative exemption, the Court of Appeals once again deferred to the DOL’s interpretation and agreed with the DOL’s argument that Novartis’ sales reps merely applied well-established techniques or procedures as prescribed by their employer. The Court of Appeals found that the sales reps 1) had no role in planning Novartis’ marketing strategies, 2) played no role in formulating the “core messages” they delivered to physicians, 3) were required to visit a physician a certain number of times per trimester as established by Novartis, 4) were not allowed to deviate from the Novartis established “core messages,” and 5) were forbidden to answer any questions for which they had not been scripted.

V. The Novartis Decision is Inconsistent with Decisions in Other Courts

The Novartis Litigation decision creates confusion for employment lawyers because it is contrary to decisions finding the FLSA “outside salespersons” and administrative exemptions applicable to pharmaceutical sales representatives. For example, the Third Circuit Court of Appeals has found that the administrative exemption applies to sales representatives who travel to various doctors’ offices and hospitals to extol the benefits of their employer’s drugs. In that case, the Third Circuit gave great weight to the plaintiff’s testimony that she was required to form a strategic plan designed to maximize sales in her territory. What is more, the Third Circuit found that the plaintiff exercised the requisite independent judgment and discretion based on the plaintiff’s testimony that she executed nearly all of her duties without direct supervision.

Similarly, several district courts have also concluded that pharmaceutical sales representatives are properly classified as exempt “outside salespersons.” Interestingly, the Christopher court declined to grant the plaintiff’s motion to alter or amend the judgment based on the DOL amicus brief filed in the Novartis Litigation. Unlike the Second Circuit Court of Appeals, the Christopher court refused to give the DOL amicus brief “controlling deference.” More importantly, the Christopher court described the DOL’s position as “inconsistent with the statutory language and its prior pronouncements” and as “defying] common sense.”

VI. What Happens Next?

The inconsistencies created by the Novartis Litigation decision will weigh heavily on drug companies in the near future as legal challenges have been asserted against many of the major drug companies. More unsettling is the fact that the Second Circuit’s decision gives plaintiff’s attorneys the ability to forum shop when suing major drug companies that have sales representatives who operate in numerous states. The issue now is whether other circuit courts will...
give much weight to the Second Circuit’s interpretation of the “outside salesperson” and administrative exemptions. Further, other circuit courts will have to decide whether to give deference to the DOL interpretation and to what degree. How other circuits will settle this conflict is still up in the air. What is certain, however, is that major drug companies have been put on notice that their sales representatives may not be exempt from FLSA overtime pay requirements, and that they will have to keep a keen eye as this issue is litigated in courts across the country.

1 In re Novartis Wage and Hour Litig., 2010 U.S. App. LEXIS 13708 (2d Cir. July 6, 2010) (hereinafter “Novartis Litigation”).
2 In re Novartis Wage and Hour Litig., 593 F. Supp. 2d 637 (S.D.N.Y. 2009).
3 Id. at 640.
4 Id. at 641.
5 Id. at 642.
6 Id.
7 Id.
8 Id.
9 Id.
10 Id.
11 Id. at 640-41.
12 Id. at 649.
13 Id.
14 Id. at 651-53.
15 Id. at 655.
16 Id. at 656 (rejecting as unconvincing the plaintiffs’ argument that modern technology, including e-mail and cellular phones, made the reps subject to constant supervision even while they were in the field).
17 See generally Brief for the Secretary of Labor as Amicus Curiae in Support of Plaintiffs-Appellants, In re Novartis Wage and Hour Litig., 2010 U.S. App. LEXIS 13708 (2d Cir. July 6, 2010).
18 29 C.F.R. §541.500(a)(1)(i).
19 Id.
20 Id.
21 See, Novartis Litigation, supra Note 1.
22 Id. at *31 (rejecting Novartis’ argument that the term “sale” should be read broadly in light of the statement in the Preamble to the 2004 DOL Regulations that “[e]mployees have a primary duty of making sales if they obtain a commitment to buy” from the customer and are credited with the sale”).
23 Id. at *34 (noting that physicians have an ethical obligation to prescribe only the drugs suitable for their patients’ medical needs, meaning that a physician can never make a binding commitment to a sales rep).
24 Id. at *34-35.
25 Id. at *39-40.
26 Id. at *41-42 (rejecting Novartis’ argument that the sales reps exercised discretion because “1) they were free to decide in what order to visit physicians’ offices, 2) free to decide how best to gain access to those offices, 3) free to decide how to allocate their Novartis budgets for promotional events, and 4) free to determine how to allocate their samples”).
27 Smith v. Johnson & Johnson, 593 F.3d 280 (3d Cir. 2010).
28 Id. at 285 (concluding that this requirement satisfied the “directly related to the management or general business operations of the employer” provision of the administrative employee exemption because it involved a high level of planning and foresight”).
29 Id.
32 Id. at *3-4, citing Auer v. Robbins, 519 U.S. 452, 461 (1997).
33 Id. at *5-6.
34 The Second Circuit stated that it was not persuaded by the argument that a number of district courts have held that pharmaceutical sales representatives are exempt from the FLSA overtime requirements.
35 Novartis Litigation