New Jersey Law Journal

VOL. 209 - NO 12 SEPTEMBER 24, 2012 ESTABLISHED 1878

IN PRACTICE

ADMINISTRATIVE LAW

Pharma Sales Reps Are 'Exempt' Employees

U.S. Supreme Court refuses to defer to administrative agency interpretation

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On June 18, the United States Supreme Court resolved a circuit split regarding whether pharmaceutical sales representatives are exempt from overtime compensation as "outside salesm[e]n" pursuant to Department of Labor (DOL) regulations under the Fair Labor Standards Act (FLSA).

In *Christopher v. SmithKline Beecham Corp*., 132 S.Ct. 2156 (2012), a 5-4 decision, the Supreme Court affirmed a Ninth Circuit decision, which held that pharmaceutical sales representatives are exempt from the overtime provisions of the FLSA as "outside salesm[e]n." In so holding, the Supreme Court refused to accord deference to a DOL regulatory interpretation that determined such employees were not exempt. This regulatory interpretation was initially announced by the DOL in an amicus brief filed in a similar action pending in the Second Circuit. In the Second Circuit case, the court accorded deference to the DOL's interpretation and held that pharmaceutical sales representatives were nonexempt under applicable DOL regulations and, therefore, entitled to overtime compensation. See *In re: Novartis Wage & Hour Litig*., 611 F.3d 141, 153-155 (2d Cir. 2010). Therefore, the *Christopher* decision not only resolved a circuit split in favor of the employer defendant but, in so doing, further eroded the deference that courts have traditionally accorded to administrative agency interpretations.

Since at least the 1950s, the pharmaceutical industry has employed pharmaceutical sales representatives, or "detailers," to market their products directly to physicians as this heavily regulated industry only allows prescription medications to be prescribed by licensed physicians. Therefore, legally and ethically, detailers can only obtain nonbinding commitments from physicians that they will prescribe certain pharmaceuticals in appropriate circumstances and cannot transfer them directly to patients.

In *Christopher*, the petitioners were employed by respondent SmithKline Beecham (SKB) as detailers and were responsible for soliciting physicians in assigned sales territories to discuss the features of the respondent's prescription drugs in order to obtain their "nonbinding commitments" to prescribe SKB's products in appropriate cases. The petitioners commenced a lawsuit alleging that SKB violated the FLSA by failing to pay them time-and-a-half wages when they worked in excess of 40 hours per week.

The district court granted SKB's motion for summary judgment, finding that the petitioners were employed in the capacity of "outside salesm[e]n" and were therefore exempt from the FLSA's overtime compensation requirement. Thereafter, the petitioners moved to alter or amend the judgment, contending that the district court erred in failing to accord controlling deference to the DOL's recent pronouncement in the Second Circuit amicus brief that detailers were nonexempt. The district court rejected this argument and denied the motion. On appeal, the Ninth Circuit in *Christopher* agreed with the district court, finding that the DOL's interpretation was not entitled to controlling deference under the circumstances, and affirmed the grant of summary judgment.

The Supreme Court granted certiorari to resolve the conflicting decisions of the Second and Ninth Circuits and to determine whether the petitioners were exempt "outside salesm[e]n" and, therefore, not entitled to overtime compensation. Notably, Congress did not elaborate on the meaning of "outside salesman" under the FLSA and delegated authority to the DOL to issue regulations to define the term. The court examined the statute and regulations and determined that Congress intended to define "sales" broadly under the FLSA to include "those arrangements that are tantamount, in a par-

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ticular industry, to a paradigmatic sale of a commodity." Since the direct transfer of pharmaceuticals by detailers was prohibited by law, the court determined that seeking and obtaining nonbinding commitments from physicians to prescribe such products satisfied the broad definition of "sale" and "other disposition" under the pertinent regulations. Therefore, detailers, who otherwise bore all of the "external indicia of salesmen," were properly classified as "outside salesm[e]n" exempt from the FLSA's overtime compensation requirements.

While this case was watched with interest by the pharmaceutical industry and the plaintiffs' bar, this decision is also significant because it illustrates that not every administrative agency interpretation of its own regulations is entitled to deference and will be rubber stamped by reviewing courts. In reaching its decision, Justice Alito explained that, although an administrative agency's interpretation of its own regulations is ordinarily entitled to deference under *Auer v. Robbins*, 519 U.S. 452 (1997), the court found compelling reasons to reject the DOL's recent interpretation of its regulations as it applied to the status of pharmaceutical sales representatives. In so doing, the court rejected the petitioners' reliance on the "DOL's interpretation of ambiguous regulations to impose potentially massive liability on the respondent for conduct that occurred well before the interpretation was announced." Indeed, to defer to the agency's interpretation under such circumstances would "seriously undermine the principle that agencies should provide regulated parties 'fair warning of the conduct [a regulation] prohibits or requires'… [and] would result in precisely the kind of 'unfair surprise' against which our cases have long warned." The court further explained that to defer to an agency's interpretation of its own ambiguous regulations could create "a risk that agencies will promulgate vague and open-ended regulations that they can later interpret as they see fit, thereby 'frustrat[ing] the notice and predictability of rulemaking.'"

Here, the pharmaceutical industry had no reason to believe that its longstanding practice of treating detailers as exempt "outside salesm[e]n" contravened the FLSA. The statute and regulations did not provide clear notice of the pharmaceutical industries' obligations to the contrary, and, prior to its amicus brief, the DOL never suggested that it thought the industry was violating the FLSA by classifying detailers as exempt employees. The court further noted:

> 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 when the agency announces its interpretations for the first time in an enforcement proceeding and demands deference.

Notably, Justice Breyer's dissent, which was joined by Justices Ginsburg, Sotomayor and Kagan, did not challenge the majority's decision regarding the level of deference to be applied to the agency's interpretation, but rather focused solely on the nonbinding nature of the commitments obtained by the detailers.

The *Christopher* decision is significant because it delivers a clear message to administrative agencies that retroactive changes in its regulatory interpretations, without fair warning to regulated entities, are unacceptable and will not necessarily be accorded deference by reviewing courts. It further confirms that administrative agencies with rulemaking authority should promulgate their positions through regulations, not amicus briefs and other informal methods.

Given the increase in enforcement activity among various administrative agencies, *Christopher* may signal the beginning of the end of the traditional *Auer* deference, due to legitimate concerns about the propriety of sanctioning past conduct without fair warning through the regulatory process. Indeed, this case is likely to have added importance since several administrative agencies have recently provided their interpretation of applicable laws through enforcement activity rather than through the promulgation of regulations. For example, the National Labor Relations Board has been increasingly scrutinizing employers' social media policies and has found that many violate the National Labor Relations Act. Similarly, the Equal Employment Opportunity Commission issued an "enforcement guidance," questioning the legality of pre-employment criminal background investigations in certain instances, which is expected to trigger more charges of disparate impact and investigations by the EEOC against employers who utilize such investigations as part of their pre-employment screening policies.

Furthermore, on July 30, the DOL issued a guidance letter on the applicability of the Worker Adjustment and Retraining Notification Act (WARN) to layoffs by federal contractors that may be required on Jan. 2, 2013, as a result of mandatory sequestration cuts that will be triggered pursuant to the Budget Control Act of 2011 if Congress does not agree on budget cuts. The DOL's recent guidance provides that effected federal contractors need not provide the standard 60-day notice to the displaced workers that WARN typically requires. This guidance is surprising because it diverges from the DOL's longstanding position in favor of providing WARN notice and advising employers that, when in doubt, such notice should be provided. Moreover, the DOL does not have any administrative or enforcement authority under WARN. Some commentators have suggested that the DOL is taking this new, divergent position that WARN notice is not required for politically motivated reasons — namely because WARN notice for layoffs on Jan. 3, 2013, would have to be given by Nov. 3, just three days before a presidential election.

Irrespective of the DOL's motivation and reasoning for its recent WARN guidance, in light of the *Christopher* decision, employers should tread carefully and not necessarily rely on this guidance as it may not be accorded any deference by courts in potential class actions by employees who do not receive the typical WARN notice.

In any event, the Supreme Court's decision in *Christopher v. SmithKline Beecham Corp*., represents a significant erosion of the deference traditionally accorded to administrative agencies and will certainly be relied upon in judicial challenges to agency enforcement actions. ■