



Is Your Sales Force Exempt or Nonexempt?

Practical Steps To Take In Response to *In re Novartis*

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Agenda

- ▶ **The Legal Landscape: Wage and Hour Litigation on the Rise**
- ▶ **The *Novartis* Decision and Other Key Cases Concerning Sales Employees**
- ▶ **Practical Steps and Potential Solutions**

The Legal Landscape

Wage and Hour Litigation Is On The Rise!

- ▶ Several industries recently have been hit hard:
 - ▶ **Financial Industries** (E.g., Wells Fargo settles class action suit by loan processors for \$6.6 Million; JPMorgan Chase Bank faces misclassification action by loan underwriters)
 - ▶ **Retail Industries** (E.g., Starbucks settles at least 3 misclassification actions by store managers for undisclosed amounts; Wal-Mart announces settling 63 wage and hour suits, including misclassification cases, for up to \$640 Million)
 - ▶ **Healthcare Industries** (E.g., February 22, 2010 DOL press release announced compliance initiative regarding wage and hour violations in New York's health industry; Kaiser settles misclassification class action for \$1.4 Million)

The Legal Landscape: Why?

- ▶ A statutory and regulatory scheme that doesn't match the workforce of the 21st century
- ▶ Technical, vague, and inconsistent legal standards
- ▶ Typically not a management priority until it is too late
- ▶ Attractive cases for plaintiffs' lawyers
 - ▶ A sufficiently large number of employees can generate large damages even if individual damages are small
 - ▶ Attorneys' fees awarded in addition to damages
 - ▶ The attorneys' fees and costs to defend such a suit can be very significant and force a settlement

The Legal Landscape: The 800 lb Gorilla

Uncle Sam Gets In the Game

- ▶ U.S. Department of Labor (DOL) Crackdown:
 - ▶ DOL increased its wage and hour investigators by more than 1/3 in the past year to respond to complaints and to provide more targeted enforcement
 - ▶ “We will not rest until the law is followed by every employer, and each worker is treated and compensated fairly.” (11/19/09 DOL Press Release)
- ▶ DOL has submitted *amicus curiae* briefs in at least two Circuit Court of Appeals cases, opining that certain sales employees were improperly classified as exempt.
- ▶ The public spotlight spurs increased litigation, including increased class actions.

- ▶ **It Seems To Be The Pharmaceutical Industry's Turn:**
 - ▶ Large employers in this industry make for attractive targets (e.g., Johnson & Johnson; Novartis).
 - ▶ A creative and common sense argument: “They can’t be exempt **outside salespeople** if they don’t actually sell anything.”
 - ▶ A corollary argument: “They can’t be exempt **administrative employees** because the employer strictly controls what they can, and cannot, communicate.”
 - ▶ Multiple recent lawsuits, with mixed results.
 - ▶ No binding appellate court decisions, until just recently.

The Legal Landscape: Who's Next?

- ▶ The reasoning behind these cases is not restricted to the pharmaceutical industry – it can be any industry where there is some doubt about whether the employees are actually “selling” anything.
- ▶ Examples of Potentially Risky Positions:
 - ▶ Medical Device Promoters
 - ▶ Software Sales Engineers/Support
 - ▶ Others
- ▶ The practical steps discussed today also would be the same in other industries.

The *Novartis* Decision

- ▶ *In re Novartis Wage and Hour Litigation*
 - ▶ Second Circuit Court of Appeals (July 6, 2010)
(binding precedent on federal courts in Connecticut, New York, and Vermont)
 - ▶ Class of thousands of Novartis "sales representatives" allegedly improperly classified as exempt employees
 - ▶ Court analyzed job positions under **outside salesperson exemption** and **administrative exemption**, and concluded that they did not meet the criteria for either exemption
 - ▶ Court showed deference to Secretary of Labor *amicus* brief supporting the sales representatives

The *Novartis* Decision

▶ **OUTSIDE SALESPERSON EXEMPTION UNDER FEDERAL LAW**

▶ Requirements:

- ▶ Primary duty is (1) ***making “sales”*** or (2) obtaining orders or contracts for services or for the use of facilities for which a consideration will be paid by the client or customer; and
- ▶ Customarily and regularly engaged away from employer's place of business in performing primary duty.

▶ “Sales”

- ▶ “the transfer of title to tangible property, and in certain cases, of tangible and valuable evidences of intangible property”
- ▶ “any sale, exchange, contract to sell, consignment for sale, shipment for sale, or other disposition”

The *Novartis* Decision

- ▶ **Sales Representatives Are *Not* Outside Salespeople**
 - ▶ They only promote pharmaceutical products to physicians
 - ▶ They do not consummate sales
 - ▶ There is no transfer of ownership or other exchange of product (free samples not enough)
 - ▶ They cannot obtain commitments to prescribe

The *Novartis* Decision

▶ ADMINISTRATIVE EXEMPTION UNDER FEDERAL LAW

- ▶ *Compensation*: Employee is compensated on salary/fee basis at a rate of no less than \$455 per week (higher in many states)
- ▶ *Duties*: Primary duty is performance of **office or non-manual work** that is **directly related to the management or general business operations of the employer or its customers**; and
- ▶ *Discretion*: Primary duty includes the exercise of **discretion and independent judgment** with respect to **matters of significance**

The *Novartis* Decision

- ▶ **Sales Representatives *Not* Administrative Exempt Employees**
 - ▶ Visit set list of physicians mandatory number of times
 - ▶ Deliver “core messages” and promotional materials but cannot stray from them
 - ▶ Organize events as required by employer and invite physicians from lists maintained by employer
 - ▶ No role in marketing strategy
 - ▶ No role in creating core messages or promotional materials
- ➔ *Insufficient discretion and independent judgment***

But *Novartis* Isn't the Only Decision

▶ ***Smith v. Johnson & Johnson***

- ▶ Third Circuit Court of Appeals (February 2, 2010) (binding precedent on federal courts in Delaware, New Jersey and Pennsylvania)
- ▶ Found sales rep had sufficient discretion and independent judgment to satisfy **administrative exemption**
- ▶ **Key duties:**
 - ▶ Rep received budgets and lists of doctors to visit, but chose itinerary, order of visits, number of extra visits beyond company-required ones, methods for persuading doctors, and how to spend budgeted funds
 - ▶ Rep planned/prioritized responsibilities to maximize results and was self-proclaimed manager of her own business in running her territory
 - ▶ Rep developed strategic plan to achieve higher sales
 - ▶ Rep completed pre-visit strategy reports and post-visit summary reports
- ➔ **Note Court limited decision to the facts of *Smith* case only**

But *Novartis* Isn't the Only Case

- ▶ ***Baum v. AstraZeneca LP*** (March 24, 2010)
 - ▶ Third Circuit Court of Appeals
 - ▶ Citing very similar duties of reps to those described in *Smith v. J&J*, found reps to be exempt under administrative exemption
- ▶ Several federal district court decisions with varying results (Arizona, Connecticut, Indiana, New Jersey, Texas)

But *Novartis* Isn't the Only Case

- ▶ **Cases in Central District of California and District of Arizona found pharmaceutical reps were exempt outside salespeople**
 - ▶ Courts considered the industry, stating reps' positions are within the "spirit and purpose" of the exemption
 - ▶ Pending review by Ninth Circuit Court of Appeals (binding precedent on federal courts in Alaska, Arizona, California, Hawaii, Idaho, Montana, Nevada, Oregon and Washington)
 - ▶ Secretary of Labor submitted *amicus* brief in Arizona case, supporting reps (*Christopher v. SmithKlein Beecham Corp.*)
- ➔ ***Exemption determination may depend upon the jurisdiction that decides the case!***

Practical Steps and Potential Solutions

Introduction

- ▶ **Consider whether *Novartis* could affect any of your company's job positions**
- ▶ **If so, conduct an exempt classification analysis** (protected by the attorney/client and work product privileges if at all possible)
- ▶ **Or, consider doing nothing until the legal dust settles (a risky strategy)**

Consider Potential Solutions If You've Got a Problem:

- ▶ Determine if another exemption could apply
- ▶ Modify duties/compensation to attempt to satisfy exemptions
- ▶ Convert employees to nonexempt status (carefully)
- ▶ Work to change the law

1. Increase/Guarantee Annual Comp to Meet Highly Compensated E'ee Exemption

▶ HIGHLY COMPENSATED EMPLOYEE EXEMPTION

- ▶ Employee whose total ***annual compensation is at least \$100,000*** (including salary of at least \$455 per week plus any *nondiscretionary* bonuses, commissions and other nondiscretionary compensation); and
- ▶ Employee customarily and regularly performs any **one or more of the exempt duties** or responsibilities of an executive, administrative or professional employee.
- ▶ ***Be careful!*** Some states require stricter standards than those in this exemption (e.g., California)

2. Modify Duties to Meet Administrative Exemption

- ▶ Increase discretion and independent judgment, where possible
- ▶ Consider job responsibilities outside the regulated areas
- ▶ *There is precedent for this! (E.g., Smith v. J&J and Baum v. AstraZeneca LP)*

2. Factors to Consider – Duties to Meet Administrative Exemption

▶ **Potential Duties to Add**

- ▶ Pre- and post- visit reports or strategic plans to create/follow
- ▶ Input into creation/development of “core messages”
- ▶ Input regarding sales aids and promotional materials
- ▶ Discretion in choosing who to visit and the number of visits, including potential for adding new physicians or pharmacies to Company lists
- ▶ Discretion in the conversation with physician, including various methods of persuasion
- ▶ Other events to organize – discretion, budget, number of events, invitee lists

2. Factors to Consider – Duties to Meet Administrative Exemption

▶ **Other Job Factors**

- ▶ **Training** – knowledge needed for positions, information taught by the Company, skills given and required
- ▶ **Supervision** – what must be reported to managers and in what format, in what manner work is reviewed by managers, and how ride-alongs are conducted

▶ **Create Tiers of Sales Representative Positions**

- ▶ Increased input/involvement with more experience
- ▶ Increased training/supervision
- ▶ Could help to reduce likelihood of a class action or lessen the effect of one

▶ **But There is No Silver Bullet – Each Case is Decided On Its Own Facts**

3. Modify Duties to Meet Outside Sales Exemption

- ▶ Consider whether employees can sell other Company products outside the regulated ones
- ▶ Consider whether workforce can perform dual functions (promotion and sales)
- ▶ **Remember:** Sales duties will need to be “primary” and promotion duties secondary

4. Convert Employees to Nonexempt Status

- ▶ Nonexempt employment is always permissible
- ▶ Key considerations
 - ▶ Pay for actual work time (not personal time or errands)
 - ▶ Time card system
 - ▶ Overtime compensation
 - ▶ Meal and rest periods (where applicable)
 - ▶ Pay stubs
- ➔ ***WARNING!! Conversion can be tricky and create suspicion of previous misclassification. Messaging and process are key.***

5. Change the Law!

- ▶ **Lobby together as an industry to make legislatures recognize pharmaceutical sales representatives as exempt outside salespeople**