

## **Third Circuit Affirms That NutriSystem's Call Center Sales Associates Are Exempt Under the FLSA**

**September 15, 2010**

On September 7, the Third Circuit Court of Appeals affirmed a district court grant of summary judgment on behalf of NutriSystem, Inc. (NutriSystem) in *Parker v. NutriSystem, Inc.*<sup>1</sup> The Third Circuit held that NutriSystem's call center sales associates, who sell the company's weight loss programs, were not entitled to overtime pay under the Fair Labor Standards Act (FLSA) because they are exempt employees under the retail services exemption of Section 7(i) of the FLSA. The Third Circuit declined to give deference to the Department of Labor's (DOL's) interpretation of its regulations.

Under Section 7(i), a retail employer that pays its sales force pursuant to a bona fide commission plan is not required to pay overtime. The issue before the Third Circuit was whether NutriSystem's compensation plan was a bona fide commission; neither the FLSA nor the regulations define the term.

Under NutriSystem's compensation plan, its sales associates are paid a flat payment that is determined by the time of the sale and kind of sale, but does not fluctuate based on the price paid by the customer. According to the plaintiffs, this compensation plan was not a commission because it did not tie their payments directly to the revenue generated per sale. NutriSystem, in turn, argued that commissions did not have to be a strict percentage of the revenue generated from the sale to be a commission plan, provided that the commissions were proportional and de-linked from the number of hours a sales associate worked.

The Third Circuit, in a 2-1 opinion, agreed with NutriSystem and the district court, and affirmed that NutriSystem's compensation plan was a bona fide commission pursuant to Section 7(i). The Third Circuit held that the flat-rate payments were proportional to the revenue generated by a sale because they fluctuated only slightly for legitimate business purposes, such as changes to the weight loss programs' costs based on customers' dietary needs or sales promotions.

The Third Circuit noted that it was illogical and unnecessary to strictly link a sales associate's pay with the price paid by a customer because NutriSystem should be able to offer its customers discounts or allow for minor differences in prices of its various programs. The Third Circuit further noted that the compensation plan was a commission because the sales associates did not have to work long hours to generate high commissions, i.e., they could be just as successful in selling programs to customers in eight hours as they could be in 12 hours.

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<sup>1</sup> *Parker v. NutriSystem, Inc.*, No. 09-3545 (Sept. 8, 2010).

Finally, the Third Circuit held that NutriSystem’s compensation plan was consistent with the purpose of the FLSA in that the sales associates were well compensated and were unlikely to have increased health risks due to hours worked. In reaching its decision, the Third Circuit relied on the limited case law in this area and noted that the DOL’s regulations did not define the term “commission.”

This opinion is significant in several respects. First, the Third Circuit clarified that employers can compensate sales representatives through commissions without having to provide overtime payments, provided that the commission payments bear some proportionality to the price paid by the customers. Although the Third Circuit did not set the outer limits of the proportionality required, it made clear that an employee could receive the same commission payment for differently priced products so long as the price range was not significant.

This holding gives retail employers greater flexibility in how it compensates and incentivizes their sales forces. Although retail employers contemplating a switch to a commission-based compensation structure should give careful consideration to the terms of their commission plans before implementation, they can now cite to appellate authority in support of such a business decision.

Second, the Third Circuit declined to grant any deference to the DOL, which had filed an amicus brief on behalf of the employees and participated at oral argument. The DOL argued that the Third Circuit should defer to its amicus and several opinion letters, which it claimed supported the interpretation that a commission must be linked to the cost of the product sold or service provided for purposes of the 7(i) exemption. The Third Circuit disagreed, and concluded that the applicable regulations did not specifically define what constitutes a commission for 7(i) purposes. A court, therefore, would have to look beyond the letter of the regulations in reaching its decision.

Although the Third Circuit conceded that the “Department may have more ‘specialized experience’ . . . in the day-to-day administration of the FLSA,” it found that the DOL and its opinion letters lacked “sufficiently thorough reasoning, consistency, or factual similarities . . . to warrant deference.” Accordingly, in reaching its holding, the Third Circuit did not give *any* weight to the DOL’s position.

Judicial deference to the DOL’s interpretation of its regulations is particularly relevant to all employers in all industries. Recently, the DOL has been more active in interpreting its regulations expansively in ways that are adverse to employers and sometimes inconsistent with prior agency interpretations. If courts, and particularly appellate courts, defer to these more expansive interpretations by the DOL, then the landscape of labor and employment law would significantly change for employers. It is important for employers to monitor the level of deference appellate courts grant the DOL in future litigation in order to remain aware of these trends. The Third Circuit, it appears, will examine the DOL’s positions carefully to determine what, if any, deference the DOL is entitled.

NutriSystem was represented in the court of appeals and district court by Morgan Lewis.

If you have any questions or would like more information on any of the issues discussed in this LawFlash, please speak with any of the members of the firm’s Labor and Employment Practice, or with one of the following attorneys:

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