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WARN Liability: Who's in Control?

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Last month, **we wrote about *Young v. Fortis Plastics***, where an Indiana District Court found that a private equity firm could be on the hook for the WARN Act liabilities of one of its portfolio companies under the "single employer" doctrine. We noted that the court there focused on the allegations that the private equity firm had de facto control over the portfolio company because it was closely involved in management decisions that resulted in the plant closure. The court held that, even in the absence of other factors that could give rise to single employer liability, such de facto control alone could result in single employer liability. Recently, another federal court, this time the Second Circuit Court of Appeals, in ***Guippone v. BH S&B Holdings***, again focused on the locus of control of the employment decisions to find parent WARN liability for the mass layoff at a partially owned subsidiary.

The plaintiff in the Guippone case was an employee of Steve & Barry's, a retail apparel chain. Guippone' s direct employer was BH S&B Holdings, LLC ("Holdings"), which was in turn owned, in part, by BHY S&B HoldCo, LLC ("HoldCo"). HoldCo was the sole managing member of Holdings. Holdings did not have a board of directors. In or about October 2008, Holdings faced a downturn in its finances and the HoldCo board determined to liquidate the company. HoldCo hired a management firm to manage the liquidation, and terminated the President and the Chief Financial Officer of HoldCo. The HoldCo board also decided to terminate Holdings' employees and Holdings issued termination notices to the affected employees, but did not do so in the time required by WARN.

As we wrote before, in the event of a mass layoff or plant closing, the federal Worker Adjustment and Retraining Notification Act or "WARN" requires covered employers to give terminated employees at least 60 days advance notice of termination. If the employer fails to do so, the employer may be liable for the wages and benefits that the affected employees would have received if they had been given proper notice. Many states have similar laws. Under the "single employer" doctrine, certain affiliated companies, including parent companies, even when not the direct employer, can be deemed the "employer" and therefore responsible for WARN Act liabilities.

Addressing an open issue in the Second Circuit as to what test governs whether a related parent entity can be considered an "employer" for purposes of the WARN Act, the Second Circuit, like the Indiana District Court, adopted the five non-exclusive factors set forth in the U.S. Department of Labor's regulations. The DOL regulations provide that subsidiaries which are partially or wholly owned by a parent company are treated as separate employers or as part of the parent depending on the degree of independence from the parent. The five factors to be considered in making the determination are (1) common ownership, (2) common directors/or officers, (3) de facto exercise of control, (4) unity of personnel policies emanating from a common source, and (5) dependency of operations. The Second Circuit held that these factors were "useful for courts in determining whether the nominally separate corporations actually functioned as a single entity with respect to [the decision to terminate the employment of a significant part of the work force]." Notably, the Second Circuit stated that the same factors could be used in determining whether WARN Act liability should be imposed on an equity investor who similarly exercises control over a termination decision.

Here, the Second Circuit found, there were sufficient questions of fact as to whether HoldCo exercised de facto control over Holdings. The Court focused on the "control" element of the test, noting that the factor is particularly important when the parent was the decision-maker responsible for the employment decision. Similar to the Indiana District Court, the Second Circuit concluding by stating "Because the balancing of factors is not a mechanical exercise, if the de facto exercise of control was particularly striking – for instance, were it effectuated by disregarding the separate legal personality of its subsidiary, then liability might be warranted even in the absence of other factors."

While the case is still pending, the Second Circuit has definitively adopted the U.S. DOL's five factor test for determining WARN Act liability. Parent companies should be aware that the more it exercises control over its subsidiaries, particularly around employment related policies, the more likely it could be responsible for liabilities under WARN, similar state laws, as well as other employment statues under

which entities other than the direct employer can have liability for violations.

Authors