By Jonathan M. Horne

# You've Been WARNed

## Private-Equity Liability for Portfolio Company Layoffs

It is no secret that private-equity investments often involve the significant restructuring of portfolio companies, which may require terminating the employment of a number of a portfolio company's employees. While the captive portfolio company might sometimes retain its management team, the private-equity owner will often — if not always — have the final say as to the critical decisions regarding employment termination and the ultimate direction of the portfolio company. Several recent decisions provide a warning to private-equity owners of their potential direct liability under the Worker Adjustment and Retraining Notification (WARN) Act[1] in cases where they exert control over the decision to conduct mass layoffs or plant closings that violate the WARN Act, even where other formalities of corporate separateness are observed.

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### The WARN Act

The WARN Act requires covered employers to give employees at least 60 days' notice, subject to certain exceptions, prior to a plant closing or mass layoff, and provides affected employees with various remedies if their employment is terminated without the requisite notice.[2] The WARN Act is intended to soften the blow to workers affected by plant closings or mass layoffs by providing them time to secure a new job while still being paid through their current, albeit terminating, employment. When workers are discharged without the required notice, they may generally recover "back pay" consisting of up to 60 days of wages and benefits,[3] essentially putting them in the position of having both notice of the termination and a paycheck for a 60-day period. Although this remedy is nice in theory, plant closings and mass layoffs often telegraph an employer's precarious financial condition, and in some instances presage, or are made in conjunction with, a bankruptcy filing. Not surprisingly, downsized employees and their counsel often look to hold the ultimate owner or a solvent affiliate of the direct employer liable for damages under the WARN Act.

### Owner/Affiliate Liability

It is clear that owners and affiliates can be held liable for WARN Act violations if the employing company and its owner or affiliate are adjudged to be a single "employer"[4] for purposes of the WARN Act. While different single-employer tests have been used,[5] courts most often employ the five-factor test promulgated by the U.S. Department of Labor's (DOL) regulations interpreting the WARN Act, which considers whether the employing company and its affiliate exhibit: (1) common ownership; (2) common directors and/or officers; (3) de facto exercise of control by the owner/affiliate; (4) unity of personnel policies emanating from a common source; and (5) the dependency of operations.[6] Under the DOL test, courts analyze each factor and assign appropriate weight based on the facts and circumstances of the case. While in theory no one factor is determinative, in practice the "de facto control" prong is considered the most important and therefore is given the most weight. Indeed, in two of the recent decisions discussed herein, the courts held that the former employees brought valid WARN Act claims against the private-equity owners of their direct employers, even though they failed to allege a majority of the five DOL factors, where the private-equity companies exerted direct control over the decision to conduct the layoffs at issue.

### *Woolery v. Matlin Patterson Global Advisers LLC*[7]

In *Woolery*, Premium Protein Products LLC, a manager of meat-processing plants in Nebraska, was majority-owned by several Matlin Patterson Global Advisers LLC investment funds that also loaned more than $30 million to Premium and an affiliate.[8] Premium allegedly violated the WARN Act when it permanently furloughed its employees in June 2009, then laid them off and declared bankruptcy in November 2009.[9] The employees initiated a putative WARN Act class action against the Matlin funds, alleging that they acted with Premium as a "single

1 29 U.S.C. §§ 2101-2109.

2 The WARN Act applies to employers with 100 or more employees that conduct a "plant closing," which is defined as the permanent or temporary closing of a single site of employment, or a "mass layoff," which is defined as an employment loss of at least 50 employees amounting to at least 33 percent of the employees at a single site, or at least 500 employees in the aggregate. *Id.* at § 2101. In addition, many states have their own iterations of the WARN Act that are generally triggered by a smaller number of layoffs.

3 *Id.* at § 2104(a)(1).

4 *Id.* at § 2101(a).

5 *See* Marisa Anne Pagnattaro, "The Perils of Control: Affiliated Liability under the WARN Act," 41 *Am. Bus. L.J.* 313, 314 (2004) (noting that some circuits apply "business enterprise test" while others apply five-factor test promulgated in U.S. Department of Labor regulations interpreting WARN Act).

6 *See* Worker Adjustment and Retraining Notification Act, 20 C.F.R. § 639.3(a)(2) (2013).

7 No. C.A. 12-726, 2013 WL 1750429 (D. Del. April 23, 2013).

8 *Id.* at *1.

9 *Id.*

employer" in making the decision to conduct layoffs in violation of the WARN Act.

The court concluded that the plaintiffs had not sufficiently alleged the existence of three of the five DOL factors: namely, the existence of common officers or directors, a unity of personnel policies emanating from a common source, or a dependency of operations.[10] Nevertheless, the court held that the plaintiffs brought a WARN Act claim against Matlin based on their allegations of common ownership and de facto control, the latter of which was particularly striking.[11] Indeed, the court noted that the employees had alleged that "Matlin personnel ran roughshod over Premium management, independently made the decision to conduct layoffs, and scoffed at the WARN Act's requirements."[12] Ultimately, this alleged conduct went well beyond a parent company's standard exercise of control pursuant to the ordinary incidents of stock ownership and stated a valid claim against Matlin for single-employer liability under the WARN Act.[13]

## Young v. Fortis Plastics LLC[14]

The *Young* case involved the closing of an Arkansas plastics component manufacturing facility owned by Fortis Plastics LLC, the sole owner of which was Monomoy Capital Partners LP, a New York private-equity company.[15] Following the closing of the facility and the termination of their employment, employees of Fortis initiated a class action against both Fortis and Monomoy for WARN Act violations allegedly committed in conjunction with the plant's closing.[16] While Fortis was their direct employer, the plaintiffs alleged that Monomoy was a single employer that was also subject to liability. In applying the five DOL factors, the court noted that "[w]here a closely related entity exists and was partially responsible for the decisions leading to WARN Act liability, it is reasonable to require it to assume certain of those obligations, which is what the DOL has done with its interpretation."[17] As in *Woolery*, the court found that the plaintiffs had stated a valid WARN Act claim against the private-equity investor (in this case, Monomoy) even though they had similarly failed to alleged three of the five DOL factors.

The court characterized the plaintiffs' allegations regarding Monomoy's exercise of control over Fortis in making the decision to close the Arkansas facility as "the issue of highest importance," which supported their WARN Act claim under the single-employer doctrine.[18] Among the specific allegations were that Monomoy maintained a continuous presence at the Arkansas facility and exercised de facto control over Fortis's labor practices, including allegedly ordering the plant's closing.[19] As a result of common ownership and de facto control, the plaintiffs brought a valid WARN Act claim against Monomoy.

10 *Id.* at *5-6.
11 *Id.* at *6.
12 *Id.*
13 *Id.*; *see also Pearson v. Component Tech. Corp.*, 247 F.3d 471, 505 (3d Cir. 2001) (noting that where de facto control is particularly striking, liability may be warranted even in absence of other factors).
14 No. 12-CV-364, 2013 WL 5406276 (N.D. Ind. Sept. 24, 2013).
15 *Id.* at *1.
16 *Id.*
17 *Id.* at *4.
18 *Id.* at *7.
19 *Id.* at *6.

## Guippone v. BH S&B Holdings LLC[20]

*Guippone* involved a WARN Act class action against private-equity owners and affiliates of chain apparel retailer Steve & Barry's.[21] On appeal to the Second Circuit, the court affirmed the district court's dismissal of WARN Act claims against the private-equity investors while reversing dismissal of claims against the holding company (the "HoldCo"); the HoldCo was wholly owned by the private-equity investors, and was the parent and sole managing member of the plaintiff's direct employer.[22] The court concluded that under the DOL test, the complaint raised a question of fact whether HoldCo was a single employer under the WARN Act by exercising de facto control over the subsidiary's decision to conduct layoffs, where its board passed a resolution authorizing the subsidiary to effectuate the reduction in force, and where HoldCo's board of directors chose the subsidiary's management and negotiated its financing.[23] As a result, "[t]he record evidence would allow a jury to conclude that [the subsidiary] was so controlled by HoldCo that it lacked the ability to make any decisions independently, and that the resolution passed by HoldCo ... was, in fact, direction from HoldCo ... to undertake the layoffs."[24] On the other hand, the court affirmed the district court's determination that the plaintiff had failed to state a claim against the private-equity owner because "there are no allegations that the defendant entities *controlled* the day-to-day personnel policies of daily labor operations" of the employer, notwithstanding the fact that the owners' representatives discussed operations with management and the owners participated indirectly in the employer's management structure by vetting certain programs.[25]

## Conclusion

Based on these recent decisions and given other decisions reaching similar results, it is clear that owners and affiliates that exert control over a subsidiary's personnel decisions simply cannot rely on notions of corporate separateness in defending WARN Act claims brought by former employees. It is safe to assume that those claims will survive a motion to dismiss where the owner or affiliate exercised de facto control over the specific decision giving rise to the plaintiffs' claim, even in the absence of some or all of the remaining DOL factors. However, as the *Guippone* decision illustrates, owners are still entitled to some degree of oversight and general control over their portfolio company's policies without opening the door to direct WARN Act liability. The line is not a bright one, though, and as a result, private-equity decision-makers must be fully cognizant of the WARN Act's implications when making personnel decisions affecting their portfolio companies. **abi**

20 No. 12-183-cv, (2d Cir. Dec. 10, 2013).
21 *Id.* at *1.
22 *Id.* at *5.
23 *Id.*
24 *Id.* at *5.
25 *Guippone v. BH S & B Holdings LLC*, No. 09-1029(CM), 2010 WL 2077189, at *5 (S.D.N.Y. May 18, 2010).

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