

Third Circuit Embraces "Lower Bar" for Successor Liability under the FLSA (Fair Labor Standards Act)

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In *Thompson v. Real Estate Mortgage Network*, No. 12-3828, 2014 WL 1317137 (3d Cir. Apr. 3, 2014), the Third Circuit adopted a standard of successor liability that will lower the bar for whether an employer can be held accountable under the Fair Labor Standards Act ("FLSA") for the wage and hour violations of its predecessor. This alert discusses the implications of the decision for employers that acquire or merge with another business.

Background

Patricia Thompson and her colleagues worked for Security Atlantic Mortgage Company ("Security Atlantic"). During the course of their employment, they were asked by their supervisors to fill out new job applications to work for Real Estate Mortgage Network ("REMN"). Upon completion of this request, Thompson's paychecks were issued by REMN instead of the now "defunct" Security Atlantic. Despite this "transfer,"^[1] Thompson and her colleagues continued to work at the same location, perform the same job responsibilities, and retain the same supervisors, rate of pay, and work email addresses.

Thompson subsequently filed a lawsuit in the District of New Jersey against Security Atlantic and REMN (and individuals of these entities) for wage and hour violations under the FLSA and the New Jersey Wage and Hour Law. Among her allegations, Thompson claimed that REMN was liable for the violations of Security Atlantic under theories of joint liability and successor liability. REMN moved to dismiss Thompson's complaint on the pleadings and the lower court granted the motion. The Third Circuit reversed, finding, among other things, that REMN could be held liable under the FLSA as both a joint employer^[2] and successor of Security Atlantic.

Holding

To determine whether REMN could qualify as the successor of Security Atlantic under the FLSA, the Third Circuit embraced for the first time the federal common law standard for successor liability as articulated by the Seventh and Ninth Circuits. Under the federal standard, which is less stringent than its state law counterpart,^[3] an employer may be liable for the conduct of its predecessors "when necessary to protect important employment-related policies." To make this assessment, courts must consider the: (1) "continuity in operations and work force of the successor and predecessor employers"; (2) "notice to the successor-employer of its predecessor's legal obligation"; and (3) "ability of the predecessor to provide adequate relief directly."

Applying the three-factor test, the Third Circuit first stressed that, on the face of the complaint, "essentially all facets of the business at issue, including operations, staffing, office space, email addresses, employment conditions, and work in progress, remained the same" following the transfer. Second, although it was "unclear" from the allegations whether REMN had knowledge of Security Atlantic's purported wage and hour violations prior to the transfer, the court maintained that such "detailed proof" was not necessary at this stage in the litigation. And, third, the court emphasized that Security Atlantic was "defunct" and "likely incapable of satisfying any award of damages." Concluding that REMN could qualify as a successor employer under the FLSA, the Third Circuit vacated the lower court dismissal.

Takeaway



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Given that the Third Circuit has adopted a lower standard of successor liability for claims under the FLSA, before acquiring or merging with another business, employers should make careful assessment of potential wage and hour violations a routine part of the pre-transaction due diligence process.

[1] The Third Circuit opinion does little to elaborate on the specifics of the transfer.

[2] Applying the so-called "*Enterprise* test" the Third Circuit refused to dismiss Thompson's claims against REMN on the grounds that it could qualify as a "joint employer" with Security Atlantic, though the court noted that a "full factual record" may demonstrate otherwise.

[3] To no avail, REMN argued that the Third Circuit should have applied the more rigorous New Jersey state law standard, which holds that successor corporations are legally distinct from their predecessors and do not assume any of the debts or liabilities of the prior entity, except where: "(1) the purchasing corporation expressly or impliedly agreed to assume such debts and liabilities; (2) the transaction amounts to a consolidation or merger of the seller and purchaser; (3) the purchasing corporation is merely a continuation of the selling corporation, or (4) the transaction is entered into fraudulently in order to escape responsibility for such debts and liabilities." *Ramirez v. Amsted Indus., Inc.*, 431 A.2d 811, 815 (N.J. 1981).

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