

# Clients & Friends Memo

## Two Birds with One Stone: In Action Involving Civil RICO, Second Circuit Provides Defenses Against Mail Fraud and FLSA Allegations

March 6, 2013

On March 1, 2013, in [Lundy v. Catholic Health System of Long Island, Inc.](#), the United States Court of Appeals for the Second Circuit affirmed the dismissal of civil mail fraud claims asserted under the Racketeer Influenced and Corrupt Organizations (“RICO”) statute and alleged violations of the Fair Labor Standards Act (“FLSA”).<sup>1</sup> In doing so, the court reached at least two notable conclusions: (a) mail fraud claims, including under civil RICO, must fail if the alleged mailings made the alleged fraud easier to detect; and (b) the FLSA does not provide a claim for “gap time.”<sup>2</sup> The mail fraud conclusion could have a far-reaching impact; the mail fraud statute has broad reach in federal criminal and civil enforcement including in civil RICO actions, and in other federal civil actions such as those involving the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (“FIRREA”). The FLSA conclusion is also significant because it will make FLSA claims more difficult to pursue in the Second Circuit as it rejects the more expansive view of that statute adopted by the Fourth Circuit and in Department of Labor guidance.

### A. The Second Circuit's Decision in *Lundy*

In *Lundy*, the Plaintiffs, a respiratory therapist and two nurses, alleged that the Catholic Health System of Long Island, Inc., a network of hospitals and other health care providers (collectively, “CHS”), failed to compensate them adequately for time worked during meal breaks, before and after scheduled shifts, and during required training sessions. They sued on behalf of a purported class of similarly situated employees (collectively, the “Plaintiffs”). In particular, the Plaintiffs claimed that CHS used an automatic timekeeping system that deducted time from paychecks for meals and other breaks, even though employees frequently were required to work through their breaks, and that CHS failed to pay for time spent working before and after scheduled shifts, and attending training programs. The district court dismissed the Plaintiffs RICO and FLSA claims with prejudice.

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<sup>1</sup> *Lundy v. Catholic Health System of Long Island Inc.*, 2013 U.S. App. LEXIS 4316 (2d Cir. Mar. 1, 2013).

<sup>2</sup> The court described a gap-time claim as “one in which an employee has not worked 40 hours in a given week but seeks recovery of unpaid time worked, or in which an employee has worked over 40 hours in a given week but seeks recovery for unpaid work under 40 hours.” *Lundy*, 2013 U.S. App. LEXIS, at \*18–19.

## 1. Affirming Dismissal of RICO Claims for Defective Mail Fraud Allegations

As the court explained, to establish a civil RICO claim, a plaintiff must allege (1) conduct (2) of an enterprise (3) through a pattern (4) of racketeering activity, as well as “injury to business or property as a result of the RICO violation.” The pattern of racketeering activity must consist of two or more predicate acts of racketeering.<sup>3</sup>

It is common for plaintiffs suing under RICO to rely on a defendant's use of the mails as the predicate racketeering acts. To satisfy its RICO pleading requirement, Plaintiffs in *Lundy* alleged that CHS violated the federal mail fraud statute<sup>4</sup> which requires, among other things, the existence of a fraudulent scheme and a mailing “in furtherance of the scheme.”<sup>5</sup> Accordingly, Plaintiffs alleged that CHS mailed misleading checks to Plaintiffs because those checks concealed that Plaintiffs “were not being paid for all of their alleged compensable overtime.”<sup>6</sup>

The district court found that Plaintiffs did not sufficiently allege a pattern of racketeering activity. The Second Circuit affirmed. In doing so, the court found that, “fundamentally,” Plaintiffs did not establish that the mailings were “in furtherance of any fraudulent scheme . . . the mailing of pay stubs cannot further the fraudulent scheme because the pay stubs would have revealed (not concealed) that Plaintiffs were not being paid for all of their alleged compensable overtime.”<sup>7</sup> Quoting the United States Supreme Court's decision in *United States v. Maze*, 414 U.S. 395, 403 (1974), the court further explained that “[m]ailings that thus ‘increase[] the probability that [the mailer] would be detected and apprehended’ do not constitute mail fraud.”<sup>8</sup>

## 2. Affirming Dismissal of FLSA Overtime and “Gap-Time” Claims

The Plaintiffs also brought FLSA claims for, among other things, overtime and gap-time for unpaid time they worked “for weeks in which they claim to have worked over 40 hours.”<sup>9</sup> The court stated that the “viability of such a claim ha[d] not yet been settled” in the Second Circuit.<sup>10</sup>

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<sup>3</sup> 18 U.S.C. § 1961(5).

<sup>4</sup> 18 U.S.C. § 1341.

<sup>5</sup> *Lundy*, 2013 U.S. App. LEXIS, at \*28 (internal citations omitted).

<sup>6</sup> *Lundy*, 2013 U.S. App. LEXIS, at \*31.

<sup>7</sup> *Lundy*, 2013 U.S. App. LEXIS, at \*31.

<sup>8</sup> *Lundy*, 2013 U.S. App. LEXIS, at \*31 (quoting *Maze*). The court also reasoned that Plaintiffs did not plead the mail fraud allegations with particularity as required by Federal Rule of Civil Procedure 9(b). *Lundy*, 2013 U.S. App. LEXIS, at \*30. Further, the court noted that courts should be generally wary of transforming civil FLSA claims into RICO actions. *Lundy*, 2013 U.S. App. LEXIS, at \*30, n.12.

<sup>9</sup> *Lundy*, 2013 U.S. App. LEXIS, at \*19.

Affirming the district court's dismissal of Plaintiffs' FLSA overtime and gap-time claims, the court first concluded that the Plaintiffs failed to allege a "plausible" FLSA overtime claim. Allegations that a nurse and other care staff may have been asked or required on occasion to work during a portion of a scheduled break or lunch or beyond his or her work shift – not uncommon in a health care facility – does not support an FLSA overtime claim where the complaint insufficiently alleges uncompensated work time in excess of 40 hours a week.

Having disposed of Plaintiffs' FLSA overtime claim, the court next turned to the viability of their FLSA "gap-time" claim. The court held that the "FLSA does not provide for a gap-time claim even when an employee has worked overtime."<sup>11</sup> The court reasoned that the text of the FLSA requires only payment of the minimum wage and overtime wages. In light of the express language of the FLSA, the court concluded that the FLSA "does not provide recourse for unpaid hours below the 40-hour threshold" and that the FLSA "simply does not consider or afford a recovery for gap-time hours."<sup>12</sup> In other words, even counting gap-time hours, there is no FLSA claim if an employee's average weekly wage satisfies minimum wage requirements.

## **B. The Significance of the *Lundy* RICO Mail Fraud and FLSA Gap-Time Holdings**

### **1. Mail Fraud Under RICO**

The *Lundy* court's RICO mail fraud conclusion reaffirms an important potential defense in any civil or criminal action involving the federal mail fraud statute, one of the broadest and most powerful statutes on the books. That is, a plaintiff must plead and prove that the mail itself helped to perpetrate or conceal a fraud.

Just as private plaintiffs may rely on an alleged violation of the federal mail fraud statute under civil RICO, the Department of Justice (the "DOJ") may predicate civil – in addition to criminal – liability on an alleged violation of the same statute. For instance, the DOJ has recently used FIRREA with greater frequency to pursue financial institutions and others involved in the financial markets for alleged frauds arising out of the financial crisis. As we have written about previously, FIRREA is a potent statute for several reasons, including because it permits the DOJ to pursue onerous civil remedies by a mere preponderance of the evidence instead of the more difficult to prove beyond a reasonable doubt standard that applies in criminal prosecutions or the clear and convincing evidence standard that may apply in other civil fraud contexts.<sup>13</sup> Similarly, the DOJ can and does

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<sup>10</sup> *Lundy*, 2013 U.S. App. LEXIS, at \*19.

<sup>11</sup> *Lundy*, 2013 U.S. App. LEXIS, at \*19.

<sup>12</sup> *Lundy*, 2013 U.S. App. LEXIS, at \*19–20.

<sup>13</sup> See "[FIRREA: Expect Substantial Anti-fraud Enforcement and Compliance Issues](#)," *Compliance and Ethics Professional*, Adam S. Lurie, Jason Jurgens, Douglas P. Cohan (August 2012).

pursue, through a civil action, the forfeiture of property for alleged violations of the federal mail fraud statute.<sup>14</sup>

Accordingly, those facing potential criminal or civil liability for mail fraud should assess carefully whether they can credibly argue that the alleged mailings at issue made detection of the alleged fraud more difficult, as in *Lundy*. For instance, where private plaintiffs or the DOJ allege that a defendant mailed account statements, pricing information or other material to a plaintiff, a defendant may be able to argue – again as in *Lundy* – that such mailings arguably revealed the fraudulent scheme, not concealed it. Indeed, private plaintiffs and the DOJ may be unable to allege or prove that the mailings at issue concealed fraud.

## 2. FLSA Gap-Time

The *Lundy* court's rejection of Plaintiffs' FLSA gap-time theory makes FLSA claims more difficult to pursue in the Second Circuit. Significantly, the court disagreed with the Fourth Circuit in *Monahan v. County of Chesterfield, Virginia*, 95 F.3d 1263, 1279 (4th Cir. 1996) and declined to give any deference to Department of Labor (the "DOL") "interpretive guidance" found in 29 C.F.R. §§ 778.315, 317, 322 which suggested that gap-time claims were actionable under the FLSA. The court explained that, unlike regulations, interpretive guidance is not binding as it does not have the force of law.

In *Monahan*, the Fourth Circuit relied on the DOL guidance in explaining that, depending on the facts and circumstances, the FLSA requires an employer to pay an employee for all non-overtime gap-hours worked in a period in which the employee also worked overtime.<sup>15</sup> The Second Circuit in *Lundy* rejected this view, however, stating that the DOL's "interpretive guidance on which *Monahan* relied, insofar as it might be read to recognize gap-time claims under FLSA, is owed deference only to the extent it is persuasive: it is not."<sup>16</sup> Thus, defendants may now argue that *Lundy* created a complete bar to FLSA gap-time claims in the Second Circuit.

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<sup>14</sup> See 18 U.S.C. § 981.

<sup>15</sup> *Monahan*, 95 F.3d at 1273. Other courts have reached similar conclusions. See, e.g., *Koelker v. Mayor and City Council of Cumberland*, 599 F. Supp. 2d 624, 634-35 (D. Md. 2009) (collecting cases).

<sup>16</sup> *Lundy*, 2013 U.S. App. LEXIS, at \*21.

Please contact any of the following Cadwalader attorneys if you have any questions about this memorandum.

Adam S. Lurie	+1 202 862 2461	<a href="mailto:adam.lurie@cwt.com">adam.lurie@cwt.com</a>
Brian T. McGovern	+1 212 504 6117	<a href="mailto:brian.mcgovern@cwt.com">brian.mcgovern@cwt.com</a>
Jason Jurgens	+1 212 504 6102	<a href="mailto:jason.jurgens@cwt.com">jason.jurgens@cwt.com</a>
Brian Wallach	+1 202 862 2332	<a href="mailto:brian.wallach@cwt.com">brian.wallach@cwt.com</a>