

NATIONAL ASSOCIATION *of*

Professional Employer Organizations

PEOS EXPAND BENEFITS FOR WORKERS

PEO Perspective of a Report by the Center for a Changing Workforce

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The Center for a Changing Workforce report ignores the realities of Professional Employer Organization (PEO) arrangements:

- PEOs enhance statutory rights and protections of worksite employees — often providing protections that do not otherwise exist;
- PEOs, as co-employers, do not displace existing client-employee relationships or responsibilities; and
- PEOs generally increase rather than decrease worker access to employment-related benefits

EXECUTIVE SUMMARY

The Center for a Changing Workforce report “PEOs and Payrolling” is biased and attempts to place a scholarly veneer to an otherwise political position paper. Throughout, the report commingles PEO arrangements with staffing services (temporary, payrolling, contract staffing, and other contingent services) that are unrelated to the PEO co-employment model. The authors ignored significant statutory employee benefits PEOs provide workers in an effort to exaggerate the premise of the report. The report’s selective use of facts, broad assertions of opinion, and omissions of important details, are evidence of the Center’s biased, political agenda.

NAPEO and the PEO industry support improved access to employment-related benefits for working men and women. Legislation (H.R. 2807 /S. 1305) before Congress would advance that goal by codifying the rights of PEOs to sponsor and provide access to 401(k) and other important employee benefits to worksite employees. The legislation is narrowly limited to maintain the integrity of a workforce and promote access to benefits for workers. PEOs certified by the IRS under the legislation would be required to meet significant financial and operating standards beyond those required of other sponsors of federal employee benefit plans. The legislation has strict anti-abuse provisions to ensure workers access to benefits, COBRA rights, and protection under anti-discrimination provisions of existing law.

UNDERSTANDING PEOs

A PEO co-employment arrangement does not involve the type of contingent worker relationship that is the main focus of the CFCW’s report. The report addresses contingent workers, the growth, size and scope of the contingent workforce, and the quality of benefits provided to contingent workers. The report frequently speaks to situations where some of a workforce are employed in a contingent relationship. Workers in professional employer organization (PEO) arrangements are *not* contingent workers. The Bureau of Labor Statistics defines contingent workers as “those who do not have an implicit or explicit contract for ongoing employment.”¹ Workers in a PEO arrangement have a clear implicit or explicit contract for ongoing employment and should not be mislabeled as part of the contingent workforce.

¹ Department of Labor, Bureau of Labor Statistics Report, Contingent and Alternative Employment Arrangements, February 1997.

The report fails to address three important points:

First, under a PEO co-employment arrangement, the worker does not abandon his or her employment relationship with the worksite employer, nor does he or she become a “contingent” worker. The employment relationship with the original employer continues and is expected to continue should the PEO arrangement be terminated.

Second, PEO arrangements do not involve “some” (implying a limited portion) of the workforce. In most such arrangements, all or at least a large majority of the workforce is co-employed.

Third, the PEO arrangement does not insulate the client from its employer obligations as a common law employer.

The CFWC report also failed to disclose the numerous state laws that clearly define the differences between varying types of staffing or contingent services as discussed in the report, and a PEO arrangement. New Jersey defines PEO arrangements as “intended to be, or is ongoing rather than temporary in nature, and not aimed at temporarily supplementing the client company’s workforce.”² South Carolina’s licensing statute makes it clear an employee’s assignment is intended to be of a long-term or continuing nature, rather than temporary or seasonal in nature, and includes a majority of the workforce at a client company worksite.³

The Center’s efforts to label workers in a PEO arrangement as “staffing” or “contingent” is inaccurate and misleading. Just as state statutes define PEO arrangements as “ongoing,” “long-term,” or “continuing,” they also distinguish PEO arrangement and staffing services. For example, the Virginia Workers’ Compensation Act makes it clear “staffing services” means any person, other than a professional employer organization, that hires its own employees and assigns them to a client to support or supplement the client’s workforce.⁴

Professional employer organization arrangements are a relatively new and innovative arrangement providing employer services to existing workforces. PEO arrangements are *not staffing*. The basic PEO arrangement involves all or a majority of worksite employees in a long-term, co-employment relationship. PEOs provide an integrated approach to the management and administration of human resources and employer responsibilities by establishing and maintaining a co-employment relationship with a client’s worksite employees.

PEO CLIENTS REMAIN EMPLOYERS

The Center suggests that PEO services are used by clients to avoid recognition as employers to discriminate in providing 401(k) retirement benefits. They inappropriately cite Metropolitan Water District of Southern California (MWD) as support. The Center fails to note that this California appellate decision is limited to a determination of the statutory eligibility under the California Public Employees Retirement System (PERS) of certain temporary, contract staffing employees. This selective use of the authority ignores other case law supporting the concept that there can in fact be more than one employer or the fact that the court in MWD acknowledged in that opinion that there are “other statutory schemes which expressly recognize co-employment between two employers.”⁵

In an arrangement among a PEO, a worksite employee, and a client company, there exists a co-employment relationship in which a PEO and client company are both employers of the worksite employees and share and allocate employer responsibilities. It is pivotal to understand that a PEO arrangement does not change a client company’s status as an employer.

Furthermore, Section 414(n) of the Internal Revenue Code⁶ provides that for the purpose of determining whether a client discriminates in providing retirement benefits to its employees, a “leased employee” is treated as

2 New Jersey Senate Bill 1466 to be codified at Title 34, Chapter 8.

3 South Carolina Licensing Statute Title 40, Chapter 68.

4 Virginia Workers’ Compensation Act at § 65.2-101.

5 Metropolitan Water District of Southern California v. Superior Court of Los Angeles County, 2001 WL1230457 (Cal. App. 2d Dist. 2001).

an employee of the client and benefits provided by the PEO are treated as being provided by the client for that purpose. Section 414(n) also applies to cafeteria plans, group term life insurance plans, dependent care assistance programs, group legal service plans, qualified tuition reduction programs, and employer-sponsored health plans. While Section 414(n) does not require a client to provide benefits, it requires that the client take “leased” employees into account for discrimination testing purposes.

PEOS PROVIDE BENEFITS

The average client in a PEO arrangement is a small business with just 15 worksite employees.⁷ Workers at small businesses are most likely not to have access to quality employee benefits. The Small Business Administration reports that workers at small businesses have only a 38% chance of having access to employer-sponsored health benefits. A small business worker’s access to a 401(k) retirement savings plan is even less. The SBA reported that last year the opportunity for workers at a small business to have access to a 401(k) retirement savings plan dropped to 19% from 28% the year before.

PEOs provide workers access to employee benefits. In one analysis by Alex. Brown & Sons, it was estimated that 40% of companies in a PEO co-employment relationship upgraded their total employee benefit package as a result of the PEO relationship and further, that 25% of the companies upgrading their benefit offering are providing health care and other benefits to their workers for the first time.

While the CFCW raises the red herring of employer matches, it ignores the reality that in the vast majority of situations there was no access to any plan at all before the presence of the PEO. When NAPEO surveyed its members in 1998, the response indicated that only 4% of clients had offered any 401(k) retirement plan before the PEO arrangement. Over 90% of the PEOs responding provided access for the worksite employees to such a plan. The Center fails to acknowledge that without the PEO and its focus on the human resource side of business, hundreds of thousands of American workers would be without any access to benefits or would receive only minimal benefits.

Equally importantly, the Center completely failed to acknowledge the access PEOs provide worksite employees to important federal statutory benefits and protections such as the Family and Medical Leave Act (FMLA) and COBRA. Because most PEO clients have worksites with fewer than 15 employees, workers at these sites are often not protected by federal employment laws or benefits absent the PEO relationship. Because a PEO’s worksite employees are included in the larger workforce of the PEO for purposes of determining statutory coverage, they are in many cases covered by employment laws that would otherwise not apply (Title VII, ADEA, COBRA, ADA, FMLA, WARN).

PEOS INTRODUCE FEDERAL LEGISLATION

The current legislation before Congress (H.R. 2807 & S. 1305) strengthens worker protections by clarifying and codifying the rights of PEOs for collection and remittance of employment taxes and sponsorship of employee benefit plans. As stated by IRS Commissioner Rossotti, “the bill can provide invaluable clarification of the federal employment tax and employee benefit obligations of professional employer organizations and their clients.”

The Center’s report is factually wrong to imply the legislation “weakens” the link between an employer and a worker. The legislation does absolutely nothing to weaken the link between an existing employer and a worker.

⁶ See I.R.C. § 414(n).

⁷ NAPEO 2000 Financial Ratio Survey©

The legislation simply opens new opportunities for a worker to receive benefits from a PEO by codifying the right of a PEO to sponsor and make available qualified benefits to worksite employees.

The Center's assertion that it will weaken "enforcement of numerous federal laws designed to protect workers, including laws addressing discrimination, wage and hour, and workplace safety" is completely mistaken. In reality, the legislation expressly does not create any inference as to who is the employer for any other legal purpose except certain federal taxes. The legislation does not override the common law determination of an individual employer and has no implication as to any other provision of federal or state law, including EEOC, NRLA, or FLSA.

On the other hand, for PEOs to receive the right to sponsor benefits, they must be certified by the IRS and meet bonding and other financial reporting requirements. The legislation requires certified PEOs to maintain a qualified retirement plan for the benefit of 95% of its non-highly compensated worksite employees – a requirement not found under any other federal benefit law. Commissioner Rossotti has commented, "the certification, bonding, and financial reporting requirements in the bill create a strong probability that certified professional employer organizations will be responsible, compliance-oriented organizations."

The legislation has been carefully and narrowly drawn to improve and not detract from employee benefits and protections. The legislation requires a PEO to have a written contract with a client that assumes responsibility for the wages of workers; the reporting, withholding, and payment of employment taxes of workers; the responsibility of any benefits required under the service contract; the maintenance of employee records; and a shared responsibility with the client for firing and hiring worksite employees. The legislation's definition of a PEO is very similar to legal definitions already adopted under state laws.

This narrow definition avoids confusion with temporary or staffing firms by requiring a PEO contract to cover at least 85% of a client's worksite employees. The narrow definition also avoids confusion with outsourcing services, such as payrolling firms that are at the main focus of the Center's report. Unlike payrolling firms, the legislation requires PEOs to assume substantial employer responsibilities, including the responsibility for the wages of workers. The Center's concern about firms that assert to be a PEO without assuming substantial employer responsibilities highlight the importance of adopting the federal legislation. The narrow PEO definition and requirement of substantial employer responsibilities would clearly address the Center's concerns.

Finally, the legislation provides clarity as to important COBRA rights for workers. As addressed earlier, the Center failed to acknowledge the access PEOs provide workers to important federal statutory benefits and protections. It is only because of a PEO arrangement that millions of working men and women could obtain the benefits of these statutory rights. This legislation ensures that COBRA continues to be among the many additional statutory benefits worksite employees of PEOs are eligible for because of the co-employment relationship. The legislation provides important clarity as to how COBRA protections are administered by PEOs.

CONCLUSIONS

The Center for a Changing Workforce report, "PEOs and Payrolling," selectively uses facts, broad assertions of opinion, and omissions of important details in an attempt to place a scholarly veneer to an otherwise slanted position paper. The report commingles PEO arrangements with staffing services that are unrelated to the PEO co-employment model. A PEO co-employment arrangement is not a contingent relationship and does not involve contingent workers. The report fails to disclose numerous laws that clearly define the differences between varying types of staffing or contingent services and PEO arrangements.

The Center's selective use of facts and omissions of important details hides the reality that a PEO arrangement

does not change a client company's status as an employer or important anti-abuse provisions of existing federal laws that prohibit the type of practices alluded to in the report.

The Center raises the red herring of employer matches and ignores the reality that in the vast majority of small business worksites there is no access to an employer retirement savings plans. The Center also failed to disclose that in addition to providing access to retirement savings plan, PEOs provide worksite employees important federal statutory benefits (FMLA, COBRA, etc.) that would not be available absent the PEO arrangement.

The Center's unsupported assertion that federal legislation (H.R. 2807 & S. 1305) weaken the link between an employer and a worker or changes enforcement of numerous federal laws is factually wrong. The legislation does not in any way diminish the client as an employer. In fact, it does not create *any* inference to any other legal purpose except federal taxes.

Finally, the federal legislation was carefully and narrowly drawn to improve and expand access to employee benefits and protections of federal law. The legislation differentiates PEOs from other outsourcing and contingent services and establishes substantial bonding and financial reporting requirements for certified PEOs. The legislation addresses the concerns of the Center's report by requiring certified PEOs contract to cover all or a substantial portion of a worksite's employees and to guarantee access for these workers to a qualified employer-sponsored retirement plan.

- NAPEO and the PEO industry have long supported changes in federal law to increase access to employee benefits for workers (H.R. 2807 & S. 1305).
- NAPEO and the PEO industry do not support changes to the employer status of client companies.
- NAPEO and the PEO industry support anti-abuse provisions of federal law, including IRC § 414(n) to protect a workers' right and access to employee benefits.
- NAPEO and the PEO industry have long supported the policy objectives and employer responsibilities as embodied in Title VII, ADA, HIPAA, COBRA, and FMLA.