

Professional Employer Organizations FAQ*

**Frequently Asked Questions*

1. What is a Professional Employer Organization (PEO)?

Also commonly called “Employee Leasing”, PEOs are companies that specialize in providing employee administration services to businesses. They typically offer payroll services in combination with workers compensation coverage. Optionally, some PEOs also offer group health and other employee benefits as well as Human Resource (HR) services to their clients.

The PEO sells this service to individual businesses and becomes a “co-employer” of the employees. The PEO issues paychecks and handles any workers compensation claims that arise. They typically bill each business once a month for the costs incurred or use a banking account funded by the business.

Employees end up with two employers, called co-employment: the business is their “workplace employer” and manages their day-to-day activities and operations as they always have. The PEO becomes the “administrative employer”, handling payroll and the other services noted above.

2. Why would a business join a PEO?

A PEO can relieve the business owner of payroll, injured worker claim issues and other human resources administrative duties. The business essentially issues one check each month to the PEO to handle all of these matters.

Some businesses may have workers compensation challenges – their NCCI experience modifier may be high due to claim issues. PEOs usually buy a single master workers compensation policy for all of their clients – by joining a large group that shares a common experience modifier, a business may be able to decrease their modifier and/or premium costs. If the PEO also offers other employee benefits, a similar group advantage may be available.

3. Are there any disadvantages?

As with any situation in which aspects of a business are outsourced, PEO arrangements can be complicated and legalistic. A business needs to carefully look at all of the implications that may arise. Some of these issues are:

- Gaps in workers compensation coverage may be created. When a business buys their own WC policy, it provides coverage for any worker they employ in that state. However, the PEO is only responsible for the specific employees covered by the contract. If the business hires a worker outside of the PEO contract, the PEO won't give them coverage for a claim that arises. Besides the uninsured claim, state fines and penalties may also apply
- The business is trusting the PEO to responsibly handle payroll, workers compensation premium payments and other fiduciary obligations. If the PEO runs into financial problems or mismanages their responsibility, it could create big problems for the business. For example, in a September 25, 2016 article in the

St. Louis Post Dispatch, one cause of a nursing home closure was, unbeknownst to the business, the PEO had failed to pay over \$1 million in withholding taxes to the IRS.

- Administrative errors by the PEO could also drag the business into an Employment Practices lawsuit or EEOC claim. Even if the PEO has Employment Practices Liability Insurance (EPLI) coverage for such situations (and many don't), it may only protect the PEO, not their clients. Even if it does extend to the businesses they administer, keep in mind this limit is shared by you and dozens or perhaps hundreds of their other clients. They could quickly run out of insurance limits, leaving you holding the bag.
- Having a common “administrative employer” with many other businesses can subject the “worksite employer” to employment law obligations such as FMLA, WARN, FLSA and various other laws that previously may not have applied to them as an individual business.
- Once in a PEO arrangement, it can be messy to go back to your prior setup with the business taking back responsibility for their payroll, workers compensation and other benefits. For example, the PEO may not properly report the business's individual payroll and claim history information to the NCCI, resulting in an incorrect experience modifier for the business after the split.
- The PEO's workers compensation policy may not include all of the endorsements needed to properly cover all of the business's exposures – all states coverage, USL&H or other Federal Act programs, foreign, voluntary compensation, etc.
- The business should keep in mind that they are now sharing the Employers Liability coverage limits with all of the other businesses insured by the PEO. As with the EPLI situation, claims involving other businesses covered by the PEO could significantly dilute the limits available to your business, leaving you underinsured or even uninsured.
- The legal contract with the PEO may contain requirements and obligations that are not to the business's advantage. Insurance and indemnification clauses in particular should be carefully reviewed.

4. How do I decide if a PEO is right for my business?

As with any business decision, that is a choice only you can make. The most important thing is to carefully read the proposed contract with the PEO – have your attorney and other professionals knowledgeable in this area review the contract. Check how the various issues noted in this FAQ apply to your business, making sure you weigh all of the various advantages and disadvantages as they relate to your operations.