The Dangers of Staffing Agencies That Promise Lower Workers' Comp Premiums

Many employers receive aggressive sales calls from employee leasing firms or their brokers telling them they can not only get rid of the administrative headache of handling payroll and compliance, but also reduce their workers' comp costs.

These organizations вЂ” known as professional employer organizations (PEOs) вЂ” promise to assume various employer human resources responsibilities by becoming the employer on record for the client business's workers.

Besides touting the benefit of having someone else handle your HR responsibilities, the big selling point that they push is that they can save you money on your workers' compensation program.

PEOs do this by essentially becoming the employer of record, and handling everything from payroll and benefits administration, to paying payroll taxes and purchasing workers' compensation coverage.

While many PEOs are legitimate, some underreport payroll and misclassify employees so that the workers' comp premium is lower than what you pay. Some especially unscrupulous players have been jailed for not paying workers' comp premiums and payroll taxes, leaving their clients in a bind.

In those cases, the employer is often left holding the bag for workers' compensation claims they thought were covered, or for unpaid tax bills.

The danger of PEOs

When an employer outsources its workers' compensation coverage responsibility to a PEO, it is entrusting that all insurance requirements will be fulfilled by that organization.

This means that the PEO will be responsible for classifying employees, communicating payroll to insurers, selecting appropriate coverage and paying premiums. This also presupposes that the PEO is familiar with your state's workers' compensation statutes and regulations.

Some employers shift this burden to the PEO without securing contractual evidence of the PEO's rights and duties. What's worse, these employers may rely on an ambiguous contract that fails to protect their interests.

These poorly written contracts can lead to fraud or misrepresentation by the PEO, which in turn can backfire on the employer.

Take the following examples:

- A San Francisco jury found that two PEOs, Onvoi Business Solutions and Select Staffing, had run a scheme to defraud an insurance company and avoid paying $30 million in workers' compensation premiums.

  The two PEOs were accused of piggybacking an arrangement where one PEO with a high X-Mod obtains coverage through another PEO with a lower X-Mod so that it can take advantage of better rates.

- Six executives from three PEOs were given varying prison sentences and probation for swindling insurance companies and small businesses that had signed up for their services out of more than $100 million.

  The men ran a series of PEOs that piggybacked on each other, while collecting payroll and other taxes, as well as workers' comp premiums from their small business clients.

  Rather than use the money the defendants were paid by the small businesses to submit payroll taxes and provide workers' compensation insurance, they spent it on vacations, girlfriends, gambling trips to Las Vegas, a private jet, real estate (including a 551-acre horse-training ranch) and other personal expenses.

Both of these failures affected thousands of businesses, and many were forced to purchase new workers' compensation policies since the PEOs had failed to remit premiums to insurers.

In addition, they were forced to pay the IRS for the failed remittances of payroll taxes, even though the employers had paid the PEO for the taxes.

The takeaway

While there are many legitimate PEOs operating across the country, employers still have to take a leap of faith and assume that the PEO will pay the bills on their behalf. If it doesn't, the burden falls back on the employer.

And there is a big difference between a PEO failing and an insurance company failing. If the PEO fails, you could be on the hook for any workers' comp claims that were incurred or premium that wasn't paid. If your insurer goes belly up, the policy will be guaranteed through its expiration and all claims will be paid by a state-run insurance guaranty fund.

If you have questions about PEOs, feel free to call us. We can answer any queries you may have about them.

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