insurance

How to Evaluate Professional Employer Organizations (PEOs) / Co-Employment Companies

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The annual health insurance evaluation often begs the question, "How do I lower premiums while maintaining benefits?" What is left to do after changing carriers, introducing Health Savings Accounts, Health Reimbursement Arrangements, reducing benefits and raising employee contributions? What are my options?

PEOs, or Co-Employers as they are often called, allow employers to access a level of benefits and competitive pricing not otherwise available to them for a variety of reasons; too few employees, too many claims, "undesirable" industry, etc. A PEO is comprised of numerous groups typically ranging between 5 – 80 employees. The aggregation of employees provides access to benefit levels and pricing that would normally be restricted to much larger organizations than most individual groups could obtain from a prospective carrier.

Different types of organizations may perform similar functions, but they are not the same. For example, a Human Resource Outsourcer (HRO) is a third party provider of common HR services. Single Source Outsourcing companies, also known as Administrative Service Organizations (ASO), also enable businesses to outsource certain HR functions. Because HROs and ASO providers are agents of the Firm, they cannot offer insurance coverage to the employees of the firm.

PEOs can assume multiple HR responsibilities for their co-employers, including, but not limited to, payroll, workers compensation, establishing employee onboarding procedures, creating employee handbooks, creating employee evaluation and review procedures, offering employee benefits, Employment Practices Liability Insurance (EPLI), 401(k) plans, as well as regulatory compliance with various state and federal laws. Contrary to popular beliefs, PEOs do not replace the existing HR department, but rather work in conjunction with them. It enables small employers the ability to provide Fortune 500 caliber HR functions and benefits.

When evaluating a PEO/Co-employer, consider the following:

Are they established in my industry and area?

PEOs usually develop, create and maintain vendor relationships regionally, and are often concentrated in a state or metropolitan area. If a PEO is rooted in a region outside your geographic location, their relationships with health insurance carriers may not be beneficial to your firm, and could be detrimental. For example, a PEO with a strong presence in Philadelphia and limited presence in New York City may not have access to the carriers currently available in the New York City market. If the carrier is the same as your current insurer, networks may be different. Additionally, due to the salary differentials between areas, worker compensation rates, unemployment insurance, and disability insurance may be affected, and your firm could inadvertently subsidize other co-employers.

May I maintain some of my current relationships, benefits and/or procedures?

Flexibility to choose which services you do and do not utilize usually result in longer, mutually beneficial relationships. All PEOs require they provide a

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minimum set of core services, usually consisting of payroll, tax filing, and workers compensation insurance. Many PEOs encourage the group's insurance broker to assist with the transition, as well as maintain their relationship with the employer to provide many of the services they previously did. Ask if you are permitted to continue any procedure(s) you prefer, or do you need to adopt the PEO's protocols, i.e., paper or electronic applications, and review procedures? Reputable PEOs allow you to maintain processes you want, while providing access to processes, functions and assistance you wish to utilize.

Are they a closely held company, or part of a larger organization?

Many PEOs are spin offs or divisions of payroll companies and/or subsidiaries of larger organizations. Often they use the PEO as a strategy to offer additional services to their existing clients. The PEO division reports to, and is held accountable by the parent company. This hierarchal structure may not always benefit the co-employers when downward pressure, or inflexibility, is applied to the subsidiary or PEO.

Many PEOs, however, are closely held private companies, similar to a law firm, and usually understand their co-employers better than a larger organization. They do not engage in a co-employment relationship with every potential company. By underwriting each potential co-employer, the PEO is able to maintain sustainable rates for medical, disability, unemployment, and workers compensation insurance, among others, as well as administrative fees, for all of their co-employers.

What are the fees and how are they calculated?

Administrative fees are usually charged either as a percentage of payroll, or as a flat fee per employee per month. If the fee is based on a percentage of payroll, the PEO intentionally receives a fee increase every time an employee earns a raise.

Each PEO's health insurance plan renews on a date specific to the PEO and not your entry date, i.e., premiums increase at the same time each year regardless of your start date with the PEO. For example, if a PEO's health insurance plan renews on October 1 each year, your health insurance rates increase on October 1, even if you just entered into the plan on September 1. Some PEOs have one premium level for all co-employers, and others have different "buckets" based on their underwriting. You may be placed in a more or less expensive "bucket" than your peers, depending on your risk factors, as determined by the PEO.

Once you become a co-employer, employees are no longer paid under your Federal Employer Identification Number (FEIN). They are paid using the PEO's FEIN. This potentially creates an additional FICA tax liability to the co-employer. If the contract start date is not January 1 and employees earn more than the maximum FICA wage base, you may pay FICA for amounts exceeding the maximum FICA wage. A PEO seeking a long term relationship should create an incentive or offer pricing concessions to recoup this money.

You may or may not be able to maintain your Unemployment and Workers Compensation rate, again, depending on the PEO and their requirements. If unable to keep you current rate(s), you will adopt the PEOs rate(s) for the coverage(s).

Are their benefit programs at least as good, or better, than I can get on my own?

PEOs typically contract with one or two health insurance carriers. Because the PEO acts as one purchaser, carriers usually do not allow the PEO to implement multiple carriers with one co-employer for a specific line, i.e., health. However, most co-employers may offer multiple plans to their employees with the carrier they choose. Depending on the PEO, you may be able to purchase a health plan with out-of-network reimbursement at more generous "usual, customary and reasonable" levels.

PEO Long Term Disability (LTD) and Life/ADD policies are usually not as strong (contractually) as most firms desire. The definition of disability is usually weak for attorneys, often only protecting their "own occupation" for 24 months. Other contractual provisions are less beneficial compared to commercial policies written specifically for law firms.

In summary, PEOs may provide better benefits, additional services, state and federal regulatory compliance, and efficiencies at a significant cost savings. Because PEOs are co-employers with you, seek PEOs that engage groups similar to you. Good PEOs are selective with the groups they co-employ. Similar to a firm interviewing a lateral partner, and vice versa, PEOs and firms should "interview" each other to ensure a long, mutually beneficial relationship. Be cautious of a PEO that is not selective, as the other co-employers may pay for their bad decisions.

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