

TO PEO...OR NOT: OUTSOURCING OPTIONS FOR YOUR HR NEEDS

Whitepaper

Businesses, especially small businesses, struggle to keep up with the myriad HR compliance requirements and the expense involved in potential liability and employee benefits. Many look to a Professional Employer Organization (PEO) for relief. Although a good option for many businesses, a PEO is not right for every company. This paper outlines options with pros and cons to the various outsourcing alternatives.

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12/1/2014

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Employment laws are many and complex. For many companies, especially small businesses, keeping up with compliance requirements and changes is more than they can realistically handle, even if they want to. Therefore, companies look to various options for ensuring they are in compliance and can access the expertise they need to reduce risk. Many choose to outsource some or all of their HR operations. A popular option is the Professional Employer Organization (PEO.) This paper will look at several options employers have to more effectively operate their HR processes, with a special focus on PEOs.

BEFORE YOU START

It is important to clearly identify what you are trying to do before you begin looking at your options. If you skip this part, or do a poor job identifying your goals, you are likely to go for the easy, rather than the right, option. You should also realize what's right for your friend's business is not necessarily best for yours. So what is it you want to do? You may have multiple objectives. Decide what they are and then prioritize them as you may not be able to get everything you want at the same level with every option. Decide ahead of time what is the most important.

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Here are common issues that companies are trying to address:

- To reduce risk associated with HR programs and policies.
- To access specialized expertise.
- To save money.
- To focus on the core business, not administrative tasks.
- To be able to provide benefits to employees which otherwise are not affordable.

- To ensure employees and managers get timely and accurate services.
- To be sure managers have a “go-to” resource who can help them navigate through decision making.
- To have a sounding board.
- To have someone who can help leverage the competencies of employees for a competitive advantage in the marketplace.

These various wants and needs are not always served best by the same alternative, so it is important to be clear on the objectives and priorities before you begin assessing options.

CHOICES

Companies can choose among several options for HR support or may combine various options:

- They can do it themselves by hiring someone to handle HR, whether as a full-time option or as ancillary to other duties.
- They can purchase software that streamlines administration of HR tasks and provides management reports for better decision making.
- They can outsource one or more functions to a service provider.
- They can engage a PEO.
- They can payroll through a temporary employment service.
- They can purchase specialized expertise on an as-needed basis.
- They can choose to parcel out some of their HR functions to line management.
- They can outsource their entire HR function.

COMPARISONS

Let’s look at some of these options in more detail.

Hire Someone

Initially, most companies assign HR duties to someone who already works for the company. That might be the owner or it could be the administrative assistant. HR is an add-on requirement and usually not the primary purpose or focus for the person in this position. Often the person has no training or experience in HR. As the company grows, the owner at some point may decide to hire someone full-time to fill this role. This often happens by the time the company gets to 50 employees, as by this time, there is just too much work for

someone to do effectively on a part-time basis and the compliance requirements have become too complex. It is not uncommon for this to be the same administrative assistant who previously did the work part-time or the owner may decide to hire someone with some HR experience.

The potential advantages with hiring a person to take care of HR-related issues are:

- You have someone who is familiar with your business, your business objectives and the people who work for you—their strengths and weaknesses.
- You have someone who is immediately accessible.
- You have someone whose only focus is you and your business. You are their priority; they have no other clients to serve.
- You may have greater control over your information (confidentiality.) This may or may not be the case, but your comfort level is important.
- Your managers can get to know and be comfortable with the person, making it more likely they will use their assistance.

The potential disadvantages are:

- The person may not have the knowledge and skills needed.
- You may not get good value for your investment (related to, but not the same as, the above bullet.)

Minimizing risk:

- Pay the freight. If you are going to hire someone, invest in hiring someone with the knowledge and skills you need and ensure they have the tools and resources they need to keep up with the constant changes to requirements.
- Hire outside expertise when needed. Especially in a small company. You may not have the financial resources to hire someone with a lot of experience or you may not choose to pay for training and development in a specialized area you may seldom need. There's nothing wrong with that, but know where your gaps are and purchase additional help when you need it.
- Outsource some of the more demanding and unforgiving high-risk tasks, such as COBRA administration or FMLA administration.

Purchase Software

Purchasing the right software can make a big difference in the timeliness and accuracy of HR processes. You can save as much as 50% of the administrative time for these processes by having and using the right software. In addition, you can have more accurate and timely data for decision making. The issue here is, “the right software.” The HR modules in many enterprise systems are not very robust, although many have the option to purchase more capability, for more money. A lower end solution may be appropriate today, but when you are assessing software, look 5 years down the road. Will it still be effective then? There are many considerations when evaluating software, and that is not the focus on this paper. For now, just be aware that this is an option that can make a huge difference in customer service and manager support.

Outsource One or More Functions to a Service Provider

Generally, most experts will agree this is a good option for administrative tasks or specialized functions that require detailed expertise. It may be possible especially in a very small company, to outsource all of your HR functions. But not all service providers are created equal.

Do you want to bundle services to a single provider? That means you only have to deal with one vendor, which can save you time. Often, you will also save money. However, sometimes when you bundle, your provider may not have the same level of service and expertise across the spectrum of services.

It may be that you are better off breaking up your services with different companies for the expertise or services needed. However, that should be balanced against administrative time and costs.

The most important part of the process is a clear statement of work of precisely what a service provider will do for you. It is important to be clear and to be thorough as there is often a disconnect between what the company thinks is it purchasing and the supplier thinks they agreed to. Once the contract is signed, extras cost extra.

Also consider the market the provider services. Choose providers that specialize in companies of your size and/or industry whenever possible.

Engage a PEO

A Professional Employer Organization (PEO) is a good choice for many small companies. Employers often turn to a PEO for certain reasons:

- To reduce or eliminate the work and worry associated with compliance.
- To reduce liability related to the employment relationship. However, there is less reduction than most business owners realize—keep reading.
- To reduce workers compensation costs. This is especially true if the company has a high experience rating—for companies with a good experience rating, this may not be the case.
- To provide benefits to employees the company may not be able to provide on their own due to the expense related to small group plans.
- To have access to HR expertise and legal advice to a greater extent than they have on their own.

However, there are some potential pitfalls.

- What may make good financial sense when you sign up with a PEO may not be the case after a couple of years. This is especially true in the case of workers compensation.
- PEO salespeople sometimes represent that the PEO has all of the liability relating to employment practices. If your salesperson tells you that, look for another PEO. Regardless of the fact that the employees work for the PEO, they are in your facilities, following instructions from your managers. You have very real co-employer liability. Do not rush out to cancel your Employment Practices Liability Insurance (EPLI). If you can get your PEO to write a contract indemnifying you from all financial risks relating to employment practices, then you might consider cancelling your EPLI—but you won't get indemnification.
- If you have a retirement plan such as a 401(k) currently, you may end up with a “wrap” plan, which costs your employees more in fees in the long run. This is an important concern from a fiduciary point of view and needs to be carefully considered.

Payroll Through a Temporary Services Agency

An intermediate step that may be a good choice, especially for new or very small companies, is to payroll staff through a temporary services company. In other words, the employee belongs to the temporary staffing agency that provides workers compensation insurance and pays the payroll and unemployment taxes. Of course, those costs are passed on to the employer, but sometimes that may still be less expensive, especially if you have a high experience rating for worker's compensation. Some staffing companies also have some benefits available to the employee. There can be wide variation in the benefits available, so ask. It is also possible, that the employee may have options with the staffing agency you would be too small to be required to provide, such as Family Medical Leave.

However, like PEOs, payroll your employees through a staffing company is not a panacea for liability. Your company must include work-related injuries and illnesses on your OSHA Log. You should still carry Employment Practices Liability Insurance (EPLI) as you are a co-employer for the purposes of most employment statutes.

Purchase Specialized Expertise as Needed

Many times a company has the expertise it needs for day-to-day operations, but doesn't have the knowledge or experience in areas that they don't need every day. Some common examples might be compensation, benefits design, affirmative action, workplace investigations, and mediation. Training in these areas can be expensive and time consuming and if not used on a regular basis, the knowledge can become obsolete. In cases where the organization only needs specialized support on an irregular basis, buy it.

For some specialized services, time may be of the essence and shopping for a vendor can eat up valuable time. Knowledge of the company can be useful in many cases. It is a good idea to establish a relationship with a consultant and to cultivate a long-term relationship, as long as you receive the level of service you expect. Generally, the consultant can do a better job as they become more familiar with the organization and its employees.

Parcel Out HR Functions to Line Management

Several companies have taken the approach to outsource much of the benefits management, payroll and other specialized functions to a service

provider and then shift the interface between the employee and the company for many processes to the line managers. This can work for some companies if:

- Supervisors are well-trained in areas in which they normally rely upon HR to assist.
- The company has robust supporting technology that supports the supervisor's increased administrative responsibilities.
- The employees handle most benefits issues on their own through a self-help system with the vendor.

The advantage of such an arrangement are that companies may reduce or eliminate positions in HR, potentially saving money. The disadvantage of the arrangement is that line managers, who have more than enough on their plate have additional responsibilities that detract from their primary focus—getting the work done. Absent proper training, the legal risks also increase.

In some cases companies revert to at least some HR support for employment law related issues. Companies who choose this option should have a good working relationship with an employment law attorney and/or HR consultant for unusual or sensitive situations with high risk (sexual harassment/discrimination complaints, etc.)

Outsource Entire HR Function

All of the same issues apply as when you outsource only some HR processes. This is usually what companies are trying to do when they choose a PEO. But a PEO arrangement is not the only option. It is possible to outsource your entire HR function, while keeping control over your employees. This is not something that is done often now, but has been mentioned as a possible emerging trend, especially for smaller companies.

Summary

Companies have many options for performing their HR functions. Every company is different and no one model works best for every organization. It is crucial for the company to identify the objectives they seek and to set up appropriate measures to determine success before sorting through the various options available to them.

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