

August 2005

REGISTRATION OF PROFESSIONAL EMPLOYER ORGANIZATIONS - BACKGROUND MEMORANDUM

Section 7 of House Bill No. 1195 (attached as an appendix) directs a study of the feasibility and desirability of requiring professional employer organizations operating in North Dakota to register with the state. The bill provides that the study must include consideration of how other states address the issue of registration of professional employer organizations. The study directive was included as an amendment to a bill that set forth terms under which a staffing service may be required to pay unemployment insurance taxes and the rate at which the staffing service may be required to pay. The bill also addressed employer restructuring activities and transfers of unemployment insurance tax account reserve history and provided for implementation of the federal anti-SUTA dumping legislation. The testimony from the standing committee indicated that the study provision was included in the bill because professional employer organizations are relatively new to the state and there may be a need for some degree of regulation of the organizations.

PROFESSIONAL EMPLOYER ORGANIZATIONS

A professional employer organization is generally described as a business that provides integrated services to manage critical human resource responsibilities and employer risks for clients by establishing and maintaining an employer relationship with the employees at the client's worksite and by contractually assuming certain employer rights, responsibilities, and risk. The professional employer organization provides services such as management of human resources, employee benefits, payroll, and employment taxes. In general, the Internal Revenue Service recognizes a professional employer organization as the employer of record for federal income tax purposes.

The Legislative Assembly in 2005 adopted House Bill No. 1195, which established guidelines for determining responsibility of professional employer organizations for the purpose of payment of unemployment insurance taxes. The Legislative Assembly adopted similar legislation in 2003 with respect to workers' compensation coverage.

REGISTRATION OF PROFESSIONAL EMPLOYER ORGANIZATIONS IN OTHER STATES

Over one-half of the states require professional employer organizations to be registered, licensed, or

certified. Included among those states are Minnesota and Montana. South Dakota has no law relating to regulation of professional employer organizations.

Minnesota

Under the Minnesota workers' compensation law, a business entity that provides staff, personnel, or employees under a lease arrangement must register with the commissioner of commerce before becoming eligible to be issued a workers' compensation insurance policy. Minnesota Statutes Section 79.255 provides that the registration must:

1. Identify the name of the lessor.
2. Identify the address of the principal place of business of the lessor and the address of each office it maintains within the state.
3. Include the lessor's taxpayer or employer identification number.
4. Include a list by jurisdiction of each name that the lessor has operated under in the preceding five years, including any alternative names and names of predecessors and, if known, successor business entities.
5. Include a list of each person who owns a 5 percent or greater interest in the employee leasing business at the time of application and a list of each person who formerly owned a 5 percent or greater interest in the employee leasing company or its predecessors, successors, or alter egos in the preceding five years.
6. Include a list of each cancellation or nonrenewal of workers' compensation insurance which has been issued to the lessor or any predecessor in the preceding five years.

Minnesota law prohibits a business from registering if its workers' compensation insurance has been terminated within the past five years in any jurisdiction due to a determination that an employee leasing arrangement was being utilized to avoid a premium otherwise payable. The registration fee is \$100. The commissioner of commerce is required to maintain a list of registrants. Minnesota law prohibits a business from referencing its registration in any advertisements, marketing, or publications.

Under Section 79.255, a business that provides personnel supply arrangements or agreements for the purpose of temporarily supporting or supplementing a client's workforce in work situations, such as employee absences, temporary skill shortages, seasonal workloads, and specific functions and projects, may be exempt from the registration

requirements if the arrangements or agreements do not involve the leaseback of the client's employees. To qualify for an exemption, an applicant must obtain a certificate of exemption from registration from the commissioner of commerce. The commissioner is required to issue a certificate of exemption upon the applicant's filing of a letter with the commissioner stating that the applicant meets all of the requirements for obtaining an exemption. If a business operating under the exemption subsequently fails to meet the requirements for the exemption, the business must immediately surrender the exemption certificate and register with the commissioner.

Montana

Under Montana Code Annotated Section 39-8-201, a person acting as a professional employer organization or group must be licensed annually. An applicant for initial licensure is required to file an application with the Department of Labor and Industry. The application fee is \$750 for a resident or nonresident unrestricted license and \$500 for a restricted license. A restricted license may be issued to a nonresident professional employer organization if the applicant's state of residence or domicile provides for licensing of professional employer organizations or groups, the applicant is licensed and in good standing in the state of residence or domicile, and that state grants a similar privilege for restricted licensing to professional employer organizations or groups that are residents of or domiciled in Montana; the applicant does not maintain an office, a sales force, or a sales representative in Montana and does not solicit clients who are residents of or domiciled in Montana; and the applicant does not have more than 100 leased employees working in Montana.

Section 39-8-202 provides that an applicant for a license must meet the following standards:

1. An individual must be 18 years of age or older.
2. A partnership or a limited partnership is required to provide the names and home addresses of all partners, indicate whether each partner is a general or a limited partner, and include a copy of the partnership agreement or an affidavit signed by all partners acknowledging that a written partnership agreement does not exist.
3. A corporation is required to state the names and home addresses of all officers, directors, and shareholders who own a 5 percent or greater interest in the corporation. A domestic or foreign corporation must have filed any required documents with the Secretary of State and must remain in good standing in order to conduct business.
4. A limited liability company is required to state the names and home addresses of those individuals who own a 5 percent or greater

interest in the limited liability company. A domestic or foreign limited liability company must have filed any required documents with the Secretary of State and must remain in good standing in order to conduct business.

5. A group must be authorized to act on behalf of the group; must include for each professional employer organization within the group the information required of other business entities; and must guarantee, on a form provided by the Department of Labor and Industry and executed by each professional employer organization within the group, payment of all financial obligations with respect to wages, payroll-related taxes, insurance premiums, and employee benefits of each other member within the group.

That section also requires an applicant to provide to the Department of Labor and Industry:

1. The trade name or names under which the applicant conducts business, the business's taxpayer or employer identification number, the address of the business's principal place of business in the state, and the addresses of any other offices within the state through which the applicant intends to conduct business as a professional employer organization or group. If the applicant's principal place of business is located in another state, the address must be provided.
2. A list by jurisdiction of each name under which the applicant has operated in the preceding five years, including any alternative names, names of predecessors, and names of related business entities with common majority ownership, and detailed information on the background of each controlling person to the extent required by the department.
3. Other information requested by the department to show that the applicant and each controlling person are of good moral character, have business integrity, and are financially responsible.

Montana law requires an applicant granted a restricted license to maintain a tangible accounting net worth of not less than \$50,000. Montana law also provides procedures for denial of a license application or renewal, suspension or revocation of a license, and disciplinary actions against licensees. Section 39-8-207 requires a professional employer organization to enter written contracts with clients to establish the responsibilities and duties of the parties. That section also establishes disclosure requirements that must be included in the contract.

POSSIBLE STUDY APPROACH

In undertaking this study, the committee should review information regarding registration of professional employer organizations in other states and the

structure and extent of the registration laws in other states and determine the desirability of registration in this state. If the committee determines that it is desirable to require professional employer organizations to register, the committee should determine which state

agency would be the best suited for handling the registration and determine the appropriate type of registration model to adopt.

ATTACH:1