Staffing Industry Analysts
CWS COUNCIL

Contingent Workforce
Legislative and Regulatory Update

North America

Presented by:

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Moderator:

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December 13, 2012
10 am PT/ 1 pm ET

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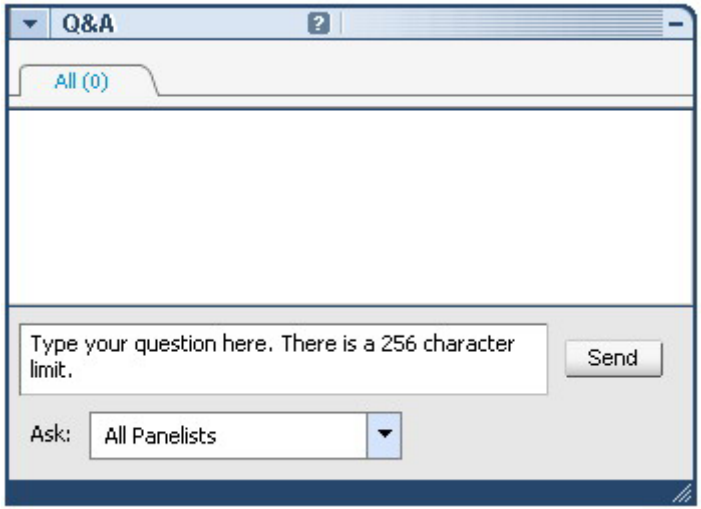

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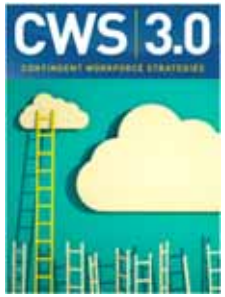
About Staffing Industry Analysts

Staffing Industry Analysts is the global advisor on contingent work

- **Over 700 firms benefit from our international research services**
  - 19 of the world's 25 largest staffing firms are members
  - More than 60 buyers of contingent labor are members of our CWS Council, representing over $100 billion in annual contingent workforce spend
  - Customers in more than 25 countries
- **Founded in 1989**
  - Acquired by Crain Communications ($200M media conglomerate) in 2008
  - Headquartered in Mountain View, California and London, England
  - 80+ years of industry and advisory service experience among executive team



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North America

Our Speakers Today

George Reardon
Special Counsel
Littler Mendelson

Adrianne Nelson
Director, Global Services
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Contingent Workforce Legal, Legislative and Regulatory Update

December 13, 2012

STAFFING INDUSTRY ANALYSTS | Littler Employment & Labor Law Solutions Worldwide™

Overview

- This quarter's webinar is not all breaking news. For two subjects, I will be giving a kind of tutorial on issues that I know that most of you have.

- Here's what we will cover today:
  - How to fix benefit plans and policies to avoid "retrobenefits" risk
  - Update on Affordable Care Act
  - How to fix staffing contracts for the ACA penalties
  - Developments in the co-employment relationship
  - Questions and answers – any subject

Fixing Benefits to Avoid "Retrobenefits" Risk

- **This isn't news, but it is current, since many companies still have not addressed it, and the exposure can be large.**
- **Starting in the 1980s, and reaching a climax with the *Vizcaino v. Microsoft* case in the 1990s, some groups of contingent workers sued their staffing customers for the benefits maintained by those customers for their employees.**
- **After the non-typical *Microsoft* case settled for a large amount in 1999, many staffing customers imposed term limits on contingent workers, believing that such limits would protect them from this "retrobenefits" risk. Those limits do little or nothing to avoid the risk.**
- **What really avoids most of the risk is simply amending the customers' benefit plans and policies to exclude contingent workers.**
- **After *Microsoft*, most private sector employers won these "retrobenefits" cases at an early stage, simply by showing that, even if contingents are assumed to be their common law employees, their plans clearly exclude them.**

Fixing Benefits to Avoid "Retrobenefits" Risk (cont'd)

- The problem with many corporate benefit plans is that they were written to cover everyone and not to exclude anyone.
- Contingents used to be a small part of the workforce, and they had never made any claims against the plans. (The lawyers had not suggested it to them yet.)
- As contingent workforces became bigger and more long-term, the potential value of retrobenefits claims became significant and worth suing over.
- So, how do you ensure that your plans have been fixed to deal with this risk?
- The first thing to do to defend against these claims is to find the actual plan documents – not just the brochures or the summary plan descriptions.
- "Plans" should include, not just the formal, ERISA, insurance and retirement plans, but also the informal plans and policies that are just written up informally and placed in the employee manual.

Fixing Benefits to Avoid "Retrobenefits" Risk (cont'd)

- Ideally, the plan documents should resolve every eligibility question or claim.
- Don't let benefit administrators assert that their habitual practices are enough protection.
- What many plans still say – "Employees of Acme are covered ....."
- Saying that "leased employees" are excluded is not enough. That term is defined by the tax code and covers only a small segment of most contingent workforces. You want to exclude all of them.
- Don't rely on terms that could apply both to direct employees and contingent workers. For example "full-time/part-time" doesn't mean the same as "direct/contingent" or the older "permanent/temporary."
- The additional language that you will use in all of these plans, policies, and programs will say:
  - who is covered (in specific detail, like who writes the paychecks)
  - who isn't covered (with detail, like those who are paid by staffing firms)
  - that potential conclusions by courts or agencies won't change the exclusion rules retrospectively

Fixing Benefits to Avoid "Retrobenefits" Risk (cont'd)

- **The plan and policy documents should authorize the plan administrator or some other person or group to interpret the plan when the documents' language is not clear.**
- **Customers and/or their suppliers should obtain waivers of potential benefits from contingent workers.**
- **Customers should urge their suppliers to provide additional periodic reinforcements of the workers' understanding and acceptance of their exclusion from the customer's benefits.**
- **Those reinforcements should also restate the workers' independent contractor status or their employment by the staffing firms.**

Update on Affordable Care Act

- Since the last Legs & Regs quarterly webinar in August, the biggest development in ACA is that, because of the election, the ACA is now clearly here to stay, at least for a while, as the law of the land.
- Most significantly, it will surely be here through January 2014, when the most significant remaining provisions kick in – state insurance exchanges, individual mandate, employer mandate/ penalties, and probably also non-discrimination.
- Some of the key regulations that were held up, pending the election, are now being published.
- The most important regulation of concern to you in your role as staffing customers is the definition of "full-time employee," because of how it may affect the cost of your contingent workforce.

Update on Affordable Care Act (cont'd)

- **The ACA statute says that penalties are measured by each month's tally of full-time employees -- meaning employees who, for the month, work an average of at least 30 hours per week.**
- **However, over the last 19 months, IRS and DOL have issued a series of guidances declaring their intention to allow measurement of full-time status of ongoing employees over longer periods of 3 to 12 months. And there are similar, but slightly different, suggested rules for new, variable hour employees.**
- **It's not clear where the administration's legal authority to substantially change (and not just implement) the statute would come from, but if no one challenges liberalization of the penalties, such a relaxation will probably stand.**

Update on Affordable Care Act (cont'd)

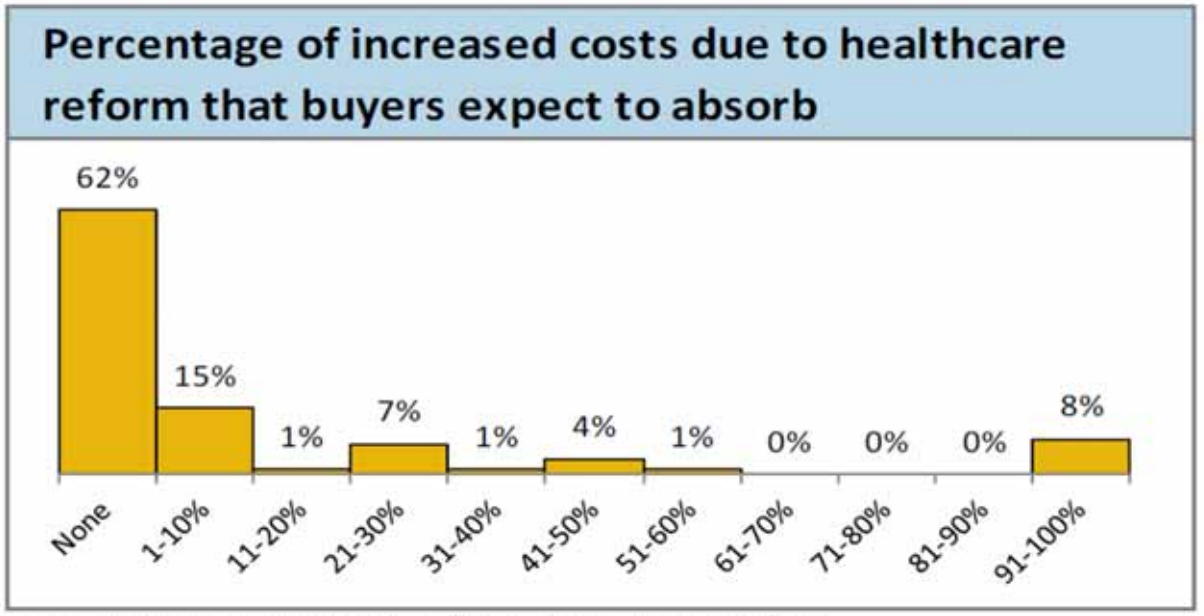
- IRS isn't trying to reduce penalties (and its lookback proposal has not yet survived the budgetary scoring process.) It just wants to prevent frequent changes in "full-time" status, to make insurance plan eligibility more stable and penalty obligations more predictable.
- The politics of this regulation is odd.
- When agency notices are published, they invite comments from interested parties. Associations, unions, employers, academics, think tanks, and others submit comments, some of which are published on the Internet.
- The Administration's traditional antagonists on health care reform (like the US Chamber of Commerce) loved the idea of a lookback system and suggested additional ways that it could be "improved."

Update on Affordable Care Act (cont'd)

- Yet the Administration's traditional allies (the SEIU, AFSCME, and academics) disapproved of any lookback system, arguing that such a system would sharply reduce government penalty revenue and defeat the main purposes of the law by allowing workers to be employed for over a year before being considered full-time and eligible for health insurance.
- If the IRS suggestion is ultimately implemented, the staffing industry's penalties would be significantly lower than the statute would otherwise require, and some of the problem of the ultimate cost increase to you would go away.
- Like other delayed regulations, this one may have been held up in order to be published only after the election. Significantly, it was a White House spokesperson who announced that the regulation would not be out before the election but would be out "this fall." If that promise is fulfilled, the regulation should be out within the next week or so (counting December 21 as the last day of fall).

How to Fix Staffing Contracts for the ACA Penalties

- **No matter what the final regulations say on full-time status, many or most staffing firms will be incurring some amount of ACA penalties for the employees they assign to you.**
- **Staffing Industry Analysts did separate surveys of staffing providers and staffing customers to determine what their respective expectations are regarding who will pay these penalties.**
- **Here is what buyers expected to pay:**



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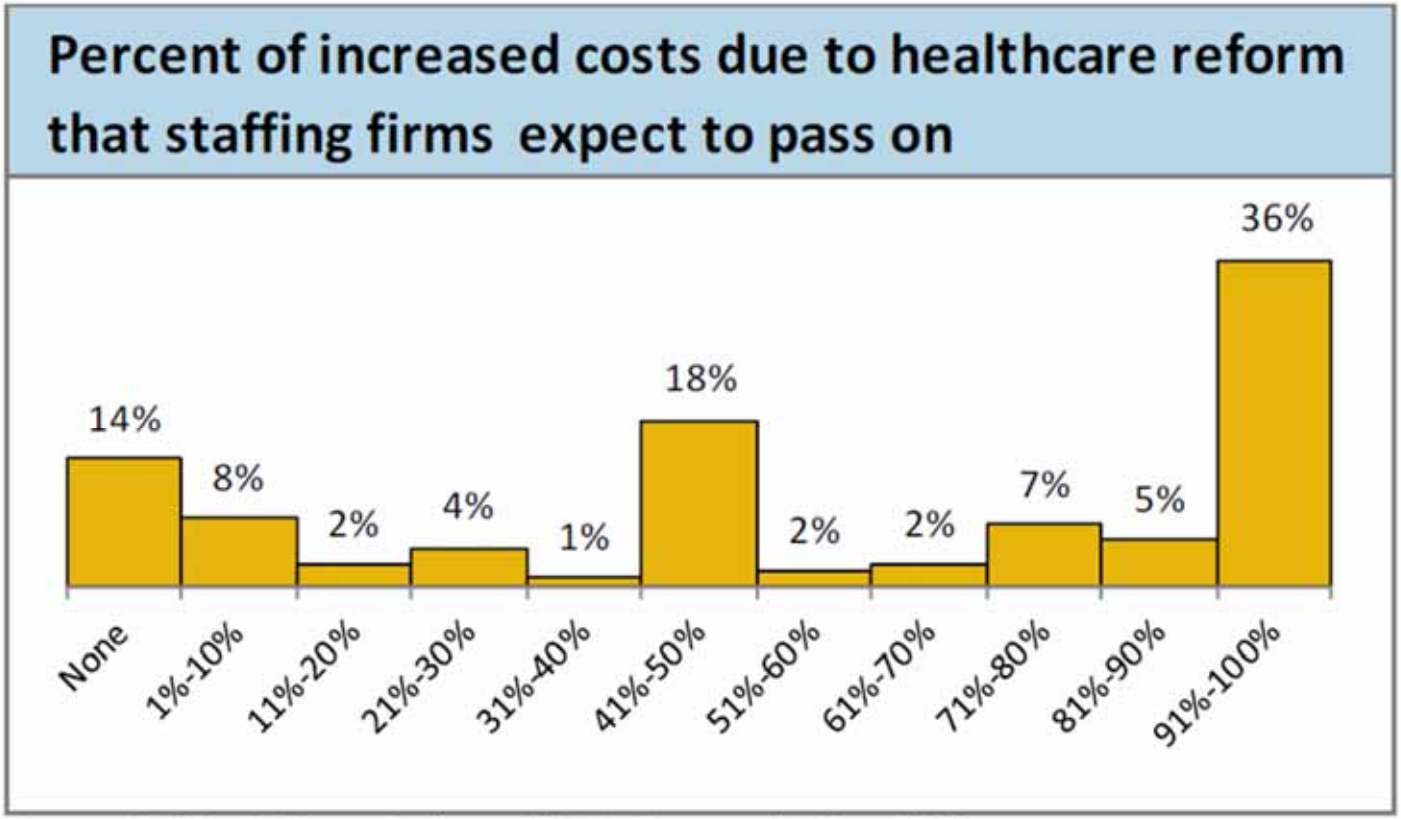
How to Fix Staffing Contracts for the ACA Penalties (cont'd)

Here is the chart showing what staffing suppliers expect to pay:



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How to Fix Staffing Contracts for the ACA Penalties (cont'd)

- There is a huge disconnect in these expectations. If staffing firms bill you for these penalties starting in 2014 without any prior discussions about it, there may be disruptive disputes between staffing firms and their customers. That would be bad for everyone.
- The delay in the calculation of the penalties also causes a doubling of the accounting and invoicing processes. And your accounting people won't like being billed in one accounting period for work that was performed in an earlier period.
- So this item should be discussed and resolved now.

How to Fix Staffing Contracts for the ACA Penalties (cont'd)

- **Most staffing contracts quote prices as a percentage markup from the pay rate to the bill rate or a flat dollar bill rate. When rate contracts are binding for several years, they leave the staffing firms vulnerable to increases in "burden" -- the sum of the payroll taxes, worker's compensation and unemployment insurance, other government-mandated costs, and other direct labor costs.**
- **To avoid the risk of having government mandates turn their rates unprofitable, many staffing firms have put "burden increase passthrough" clauses into their agreements.**
- **Usually, these provisions say that, when the government increases or introduces new burdens, the staffing firm will bill the customer for the actual cost of those changes (without any markup) until the contract rates are renegotiated.**

How to Fix Staffing Contracts for the ACA Penalties (cont'd)

- **Here is an example of a "burden increase passthrough" clause:**

"If any government-mandated cost (such as a required wage, minimum wage, payroll tax, insurance premium, assessment, contribution, benefit, or fee) is imposed, increased, adjusted, or newly introduced with respect to Associates assigned to Client, Staffing Firm will notify Client and add it, without markup, to Client's invoices until Client and Staffing Firm adopt a new Rate Schedule."

How to Fix Staffing Contracts for the ACA Penalties (cont'd)

- **But ACA penalties are so different from the usual burden items that these contract provisions probably won't clearly indicate who pays for them, how much is to be paid, and how and when they are to be paid.**
- **ACA penalties may be taxes, but they aren't really payroll taxes. They aren't computed as a function of pay or of hours, and they aren't necessarily directly related to the work that is performed for you.**
- **ACA penalties also aren't insurance premiums, since they don't buy coverage directly for anyone. They're just penalties payable to the government.**
- **ACA penalties are also different by being non-deductible. That means that the real cost of penalties to staffing firms will be larger than the penalties – an amount calculated by grossing up for income taxes. That calculation requires the staffing firm's marginal income tax rate as an input. The disclosure and verification of that tax rate are tricky tasks.**

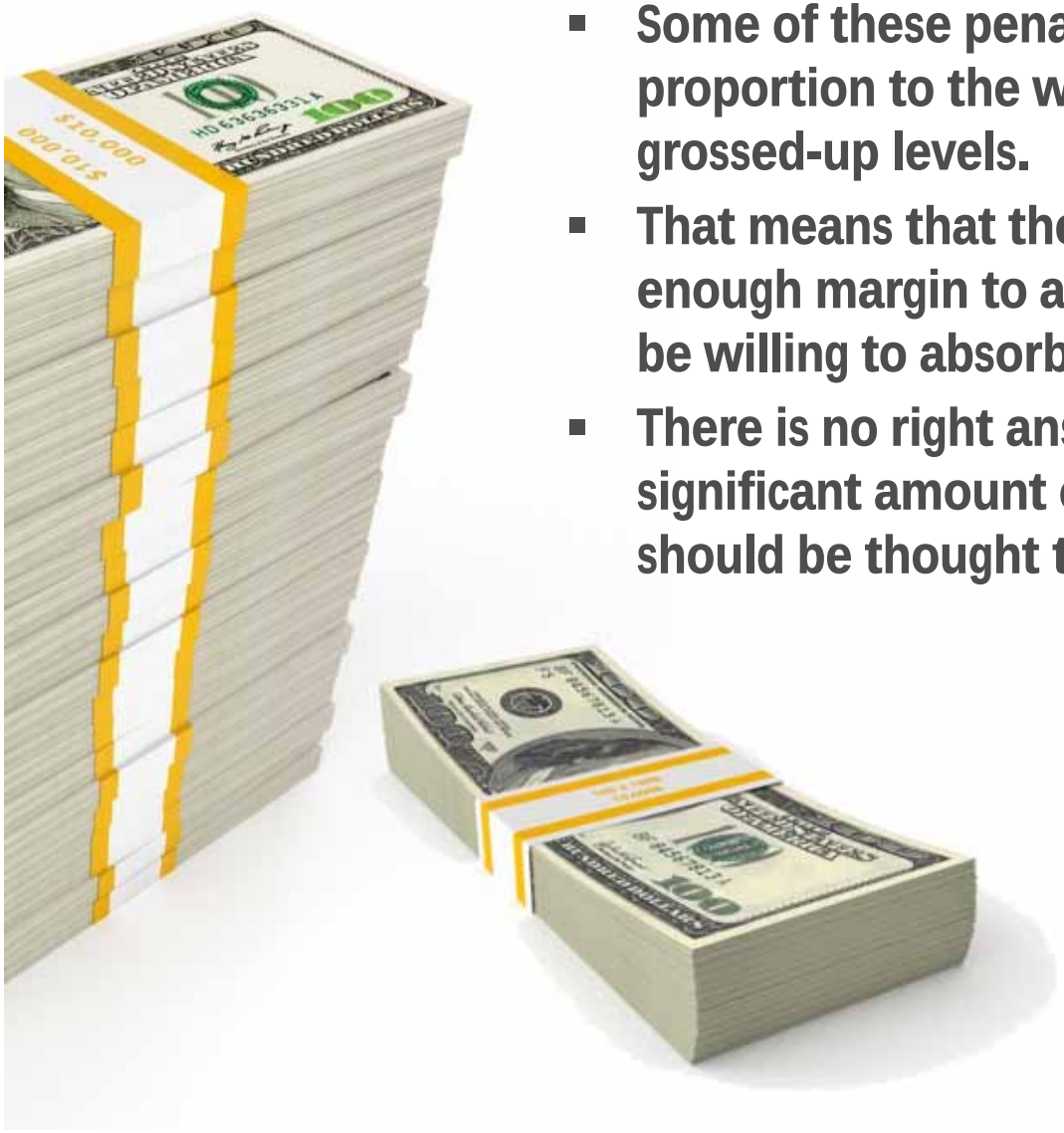
How to Fix Staffing Contracts for the ACA Penalties (cont'd)

- Another practical problem is that, at the time that a temporary employee's work is performed, no one will know for sure whether that worker will qualify as full-time in order to generate an ACA penalty.
- That answer could be determined as late as 13 months after the work is performed.
- Yet another problem is that a full-time temporary may earn that status by working for several staffing customers. It is likely that none of the customers will feel that they have received the benefit of a long-term, full-time worker and won't want to pay penalty money, but the cost to the staffing firm and the need to recover it are just as real.

How to Fix Staffing Contracts for the ACA Penalties (cont'd)

- **Many staffing firms are contemplating spreading the penalties generated by some assigned workers over the rates charged for all assigned workers.**
- **This spreaded cost may simply be added to their quoted rates, in which case regular economic competition will determine whether customers continue to do business at the higher rates. Some firms may show a small "spread" penalty cost as a separate item. I think that it is likely that purchasing departments and VMS vendors will ban this kind of add-on charge.**
- **Staffing customers may also demand that the workers assigned to them not have accumulated prior service with the staffing firm, thus making them less likely to achieve full-time penalty-generating status during the new assignment.**

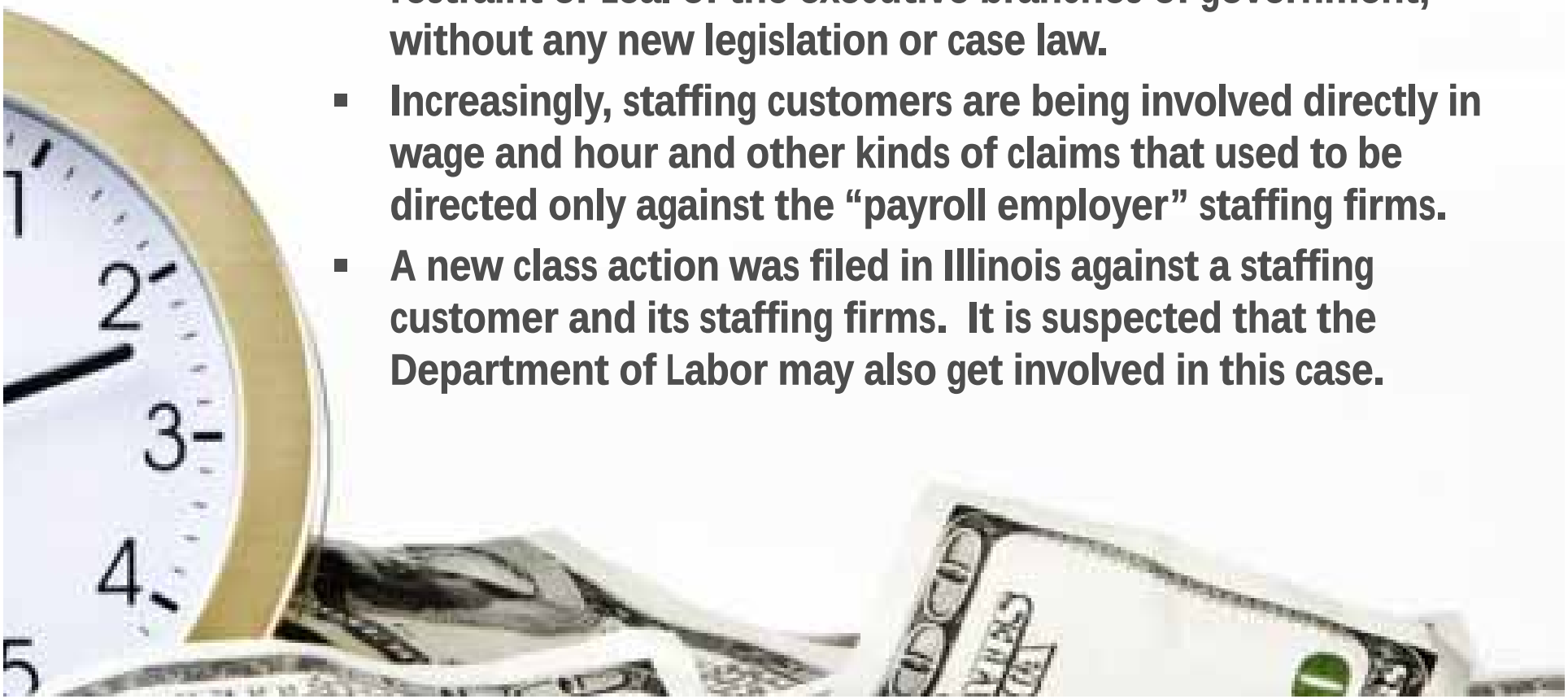
How to Fix Staffing Contracts for the ACA Penalties (cont'd)



- **Some of these penalties will be very large in proportion to the workers' wages, especially at grossed-up levels.**
- **That means that the staffing firms may not have enough margin to absorb them, even if they would be willing to absorb them.**
- **There is no right answer to this issue, but a significant amount of money may be involved, so it should be thought through carefully and in advance.**

Developments in Co-employment

- The consensus among employment lawyers is that, following the election, federal agencies will be moving very aggressively to increase enforcement of numerous employment laws. The legal environment can change dramatically through the restraint or zeal of the executive branches of government, without any new legislation or case law.
- Increasingly, staffing customers are being involved directly in wage and hour and other kinds of claims that used to be directed only against the "payroll employer" staffing firms.
- A new class action was filed in Illinois against a staffing customer and its staffing firms. It is suspected that the Department of Labor may also get involved in this case.



5-MINUTE WARNING

PLEASE PREPARE YOUR QUESTIONS

Developments in Co-employment (cont'd)

- **In New Jersey, the U.S. Department of Labor has reported that a wholesale produce broker is having to pay $650,000 in back wages to more than 500 temporary workers under the Fair Labor Standards Act. The broker is suing its staffing supplier and may recover some of its payments, but it has already taken the front-line hit as a joint employer.**
- **Recently, when a temporary nurse worked overtime in violation of the policies of her staffing companies and their customer, the nurse nevertheless recovered overtime premium pay, liquidated damages, and attorney's fees from the customer.**
- **In a case of administrative review by the U.S. Department of Labor, a PEO customer was found to solely liable for purposes of liability under the Occupational Safety and Health Act. The case turned on the actual control exercised by the employer rather than the allocation of control prescribed by the leasing agreement.**

Developments in Co-employment (cont'd)

- An executive order signed by President Obama in 2009 has finally received the implementing rules required for it to take effect. The order requires successor contractors on federal service contracts to hire the workforces of their predecessor contractors. This could be described, in staffing industry slang terms, as "mandatory tempnapping," which will make such accounts less attractive to staffing firms and may make it harder for staffing customers to get the staffing firms' best personnel.
- Other likely areas of ramped-up federal enforcement include:
  - targeted industries (like construction, hotels, and restaurants)
  - targeted, rather than complaint-driven, project-wide investigations
  - more frequent assessment of liquidated damages
  - heightened litigation threats
  - more ready use of penalties, debarment from government contracts, and criminal prosecutions

Developments in Co-employment (cont'd)

- **In California and Massachusetts, new laws require staffing firms to make detailed disclosures to their employees. The disclosures are of information that staffing firms already routinely give, as a matter of operational necessity, to their assigned employees. Civil, and sometimes criminal, penalties may be imposed for violations of the laws. While there is nothing wrong with such disclosure requirements in principle, the laws impose very inconvenient rules about how and when the disclosures must be made.**

Developments in Co-employment (cont'd)

- **Under an unusual Ohio law, staffing services are subject to sales tax, but the tax isn't payable when the assigned employees are "permanently" assigned to the customer. That leaves a lot of room for factual disputes. In a recent case, a mechanical contractor contracted to obtain assigned employees from two staffing firms. Although the staffing contracts declared that the assignments were to be for at least a year and on an indefinite basis, the taxing agency required further evidence of the actual facts and circumstances of the employment relationships with the workers. Because the contractor didn't produce such evidence, the sales tax on the services was upheld.**
- **Not all of the news is bad. In Louisiana, a court ruled (against the position of the state workforce agency) that nurses can work at hospitals and nursing homes as independent contractors on assignment from staffing firms.**

Thank You

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January 23, 2013
Introduction to the Contingent Workforce in Asia

February 21, 2013
Term Limits and Other Contingent Workforce Risks

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