

Employee Leasing: Implications for State Unemployment Insurance Programs

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**Employee Leasing: Implications for State Unemployment
Insurance Programs**

Final Report

Submitted to:

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All four States provided universe data so that we could vary our identification algorithm. They then provided additional tax and benefit data for the identified leasing firms and client employers.

All States and the District of Columbia participated in the survey, including follow-up phone calls and inquiries of other agencies of the State. This made the reported survey results possible.

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Mr. Rex Ely, Sunmark

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* * * *

Executive Summary

This report presents the results of an exploratory study of the employee leasing industry. It begins with a description of the employee leasing industry, its size and characteristics. It then presents the results of a survey of State Unemployment Insurance (UI) tax administrators on their experience with the industry and their response in terms of administrative handling of leasing companies and taxing and reporting provisions of their laws. It then attempts to determine the implications of the leasing industry on State UI trust funds.

The Nature of the Industry

A leased employee is a worker who is essentially rented on a long-term basis from an agency that is responsible for employing the worker, paying the salary or wages and taxes, and providing benefits for that employee. An employee leasing company is an organization in the business of leasing employees to client firms. Under a typical agreement, an employer contracts with a leasing company and dismisses some or all of its employees. These workers are then hired by the leasing company and leased back to the original employer, now the client company, on a long-term basis. The leasing company pays both the employees' wages and associated payroll taxes, including UI. It also provides the workers with other fringe benefits. This is done for a set fee (usually a percent of payroll) as stipulated in the leasing contract. The contract can be renewed any number of times.

Employee leasing had its origins in the differential pension treatment of different classes of employees, in which one group of employees (generally officers) had a more generous pension program than other employees. Historically, many small business owners have maintained pension plans as a way to defer income for themselves and other employees. Participation in these pension plans was often limited to selected key employees. As these plans were seen as both discriminating against the non-key employees of the business and as a means of deferring or avoiding income taxes, the IRS established a set of guidelines in 1942 to require employers to cover a substantial portion of their employees under the pension plans.

The most recent legislation governing differential treatment was the Tax Reform Act (TRA) of 1986, Public Law 99-514, which amended the tax shelter feature that allowed employers to offer pension plans to partners or high-paid employees with greater tax advantages. To qualify under the safe harbor provision as amended by TRA, leasing companies now are required to offer a pension plan that provides a 10-percent employer contribution to all employees of the leasing firm earning \$1,000 or more annually.

Since TRA, industry growth has been fueled by increases in employee benefit costs, particularly health insurance and workers' compensation premiums, both of which represent a larger share of the nonwage labor cost than UI. Thus, while the impetus for employee leasing may lie elsewhere, the UI system is being affected as a result of these changes in labor market organization. One of the financial incentives motivating employers to use employee leasing is the growing importance of fringe benefits as a component of labor compensation.

Survey of States

The KRA Corporation (KRA) survey was designed to gain an understanding of how States are currently dealing with the employee leasing industry and to obtain a more accurate picture of the impact of employee leasing on State UI systems. In September 1994, KRA initiated a survey of State UI tax administrators that asked questions about definitions of employee leasing, applicable State laws, effects on the UI trust fund, industry size and employment, reported industry classifications, registration requirements, bonding requirements, client firm reporting requirements, failure rates of leasing companies, experience-rating procedures, and associated changes in successor rules.

The mail survey was conducted between September 1 and November 1, 1994. Follow-up telephone calls were made to obtain additional data or clarify responses. Surveys were received from all 50 States and the District of Columbia.

A common feature of many State employee leasing laws is a definition of the employee leasing arrangement or employee leasing company. Twenty-five States have such a definition in their law, with another four States defining employee leasing through regulations. Only 14 States do not have a working definition or a definition of employee leasing in any legislation, regulation, or agency policy. Two primary questions underlie most State laws and policies governing the employee leasing industry: "Who is the employer of leased employees?" and "Who is liable for unemployment contributions?" To answer these two questions, States have regulated the industry in a variety of ways.

According to the survey responses, 27 States consider the employee leasing company the employer of leased employees, while 9 consider the client firm the employer. Of the remaining 14 respondents, 5 indicated that the employer was whoever maintained direction and control of the leased employees. Other States require that the leasing company meet criteria such as the seven-point test to be considered the employer:

Thirty-seven States consider partners/sole proprietors to be owners and therefore not eligible for UI benefits. In these cases, the employee leasing company is most likely serving merely as a payrolling firm for those individuals. Only six States responded that a partner/sole proprietor is considered an employee of the leasing company, whereas one considered those individuals employees of the client firm.

The entity considered the employer of corporate officers varies more significantly than for partners/sole proprietors. Twenty-one States consider corporate officers employees of the leasing company, and 18 consider them employees of the client firm. Two States responded that corporate officers are considered owners and are therefore not eligible for UI benefits, but two others indicated that corporate officers may be considered in dual employment.

Because of the unique nature of an employee leasing arrangement, determining liability for UI contributions and the appropriate amount of contributions can be difficult. In general, 22 States hold the employee leasing company liable for contributions, but 10 States consider the client firm to be liable if contributions are not paid by the leasing company. Nine States consider the client firm jointly and severally liable for contributions, although five States allow relief from liability if a bond is posted by the leasing company.

As a means of assessing UI tax liability, nineteen States reported that they have registration requirements for employee leasing companies. In some cases, the registration is the same as that required of all firms, whereas other States require special registration or licensing of leasing companies.

Some States require employee leasing companies to submit information in addition to a list of client firms, such as addresses and SICs of client firms. The most common information collected, in addition to client lists, is the number of employees leased to client firms. These requirements can be important to proper reporting of employment by industry in the ES 202 reporting system. Absent reporting requirements, employee leasing firms may aggregate all their leased employees in Help Supply Services (SIC 7363) rather than by the industry of their client firms.

Experience rating is a key factor in determining the amount of payroll contributions any company must pay. In the case of leasing companies, it is not always clear how the experience of a leasing company should be computed. Some States consider the experience rate of the client firm when determining the rate for the leasing company, and others maintain different experience rates for each of a leasing company's client firms. However, the overwhelming majority of States (44 of 50 responding) apply a single tax rate to the leasing company based on the overall experience of the leasing company.

Another consideration in determining both tax liability and the appropriate experience rate is the predecessor/successor relationship between a client firm and an employee leasing company. Most States indicated that employee leasing companies may not transfer the experience of client firms under their State's successorship provisions, whereas some States allow the leasing company to be the successor to the client firm. A few States commented that the leasing company is automatically considered the successor to the client firm. Generally, States indicated that employee leasing companies are treated like any other firm when considering potential predecessor/successor relationships.

With regard to the number of leased employees, 25 States provided estimates, ranging from 1 to more than 100,000 leased employees. The average number of leased employees per State is 25,342. Total leased employment in States able to provide estimates was 608,198. The States that require the submission of client lists account for 46 percent of the total (278,888 leased employees).

Twenty-nine States were able to provide estimates of the number of employee leasing companies in their State in 1993. The total estimated number of firms was 2,297. Of the 29 States providing estimates, 19 require that employee leasing companies register or maintain a license to conduct business in that State. These 19 States account for only 757 of the 2,297 firms estimated for 1993 (33 percent).

Nineteen States indicated that they record the SICs of leasing company client firms or their employment in the appropriate SIC. Although leased employment is historically thought to be found in such employment as medical office staff, legal assistants, or office support, the survey responses indicate that leased employment is found in a variety of industries. When the survey asked about the major industry of client firms, the most frequent response (30 respondents) was the service industry.

However, within the service industry, responses varied from Hotels and Motels (SIC 7011) to General Automotive Repair Shops (SIC 7538) to Public Relations Services (SIC 8743). Other common responses of industries of client firms were manufacturing, transportation, and retail trade.

Trust Fund Effects

The third purpose of this study was to estimate the effects the employee leasing industry has on State UI trust funds. These effects are measured using wage-record data from four States to identify firms engaged in employee leasing and their client firms. Using State UI tax rate data, we were then able to analyze the differences in tax rates between the identified leasing and client firms.

Selection of the four States for obtaining detailed wage and administrative data was essentially judgmental and opportunistic. Maryland was selected because we already had access to all of its wage-record data. Therefore, we could test our proposed procedures on this State before approaching other States. Maryland also has voluntary registration for leasing firms and provided an opportunity to test the extent to which we could identify these firms. Florida has extensive experience with the employee leasing industry and has passed a licensing law for employee leasing firms. Oklahoma is concerned about employee leasing, particularly the interstate aspects. Texas also expressed concern about the employee leasing industry, and the Texas Department of Licensing and Regulation maintains a licensing list of employee leasing firms.

One of the greatest difficulties in measuring the effect the employee leasing industry has had on State UI trust funds has been in identifying the employee leasing firms. In this study we address some of the difficulties of identifying employee leasing firms by developing an algorithm that uses State UI wage records to identify firms engaged in employee leasing.

Using all of the UI wage records collected from every employer, it is possible to examine an individual's employment and earnings history. It is a relatively straightforward matter to track an individual's SSN either forward or backward through time to discover from which employers that individual received wages for each year and quarter. It is the ability to track individuals from one employer to the next that makes it possible to use UI wage records to identify employee leasing firms and their client firms.

The number of leasing firms identified by the algorithm varied across the States. In Florida, 101 firms were identified as being engaged in leasing. Texas had the second largest number of identified leasing firms with 93. In Oklahoma, only 18 firms were identified by the criteria as being leasing firms. Finally, Maryland had only 15. The differences in the number of leasing firms are due to the size of the States (in the first quarter of 1994, both Texas and Florida had over 300,000 employers, while Oklahoma had 65,000); the industry mix prevalent in the States and the age of the leasing industry in the State.

As expected, most of the identified leasing firms were large. The mean employment levels for the leasing firms for the first quarter of 1994 for all four States were more than 600 employees.

Oklahoma had the smallest leasing firm mean employment, 636 employees. Also, more than three-quarters of all of the leasing firms in all three States had more than 100 employees in the first quarter of 1994; and in Florida and Texas, more than 60 percent of the identified leasing firms had more than 500 employees in the first quarter of 1994.

The number of identified client firms for each identified leasing firm also varied across the States. The mean number of client firms per identified leasing firm in Oklahoma was approximately five, the lowest of the three States for which the number of separable clients could be identified. Identified leasing firms in Texas had 13.5 clients on average, while the identified leasing firms in Florida had slightly more than 23 clients.

The algorithm identified more leasing firms in Florida than in Texas, and it identified more total client firms in Florida than in Texas. In Florida, 2,350 client firms were identified; in Texas, 1,999 client firms were identified. In Oklahoma, with its much smaller employer and identified leasing firm base, 93 firms were identified as client firms.

The most common two-digit SIC code of identified client firms in Florida was 17 (Special Trade Contractors), in Texas it was 73 (Business Services), and in Oklahoma it was 50 (Wholesale Trade Durable Goods). In all three States, the two-digit SIC codes of 80 (Health Services), 73, and 65 (Real Estate) accounted for more than 5 percent of the identified client firms' SIC codes. In addition, the two-digit SIC codes of 17 and 50 were also relatively common among all three States' 19 identified client firms.

When weighted by the number of employees involved in the leasing occurrence, the mean tax rates for the leasing firms in all three States were lower than the average tax rates for their client firms. The weighted mean tax rates of the leasing firms in both Texas and Florida were approximately 0.40 percent lower than those of their clients (19 and 26 percent reductions, respectively). In Oklahoma the leasing firms' weighted mean tax rate was 0.11 percent lower than their clients' (a 6-percent reduction).

Given that we identified only 747 changeovers in Oklahoma, the fact that the trust fund loss estimate is small (\$8,700) is not surprising. At the other end of the spectrum, the estimates for the State of Texas, with 87,000 changeovers, runs to \$3.2 million. Florida, with 39,800 changeovers has an estimated trust fund loss of over one million dollars. Put in perspective, using 1992 taxable wages as the base, the largest loss, in Texas, amounted to six tenths of a percent of the taxable wages. Thus, it would reduce the average tax rate by that amount. For Florida, it amounts to three tenths of one percent. In Oklahoma, given the small size of the leasing industry, the effect is infinitesimal.

Using data from Florida, we examined the potential for tax rate manipulation by the leasing firms. This involved: establishing a low rate for the firm prior to leasing occurrences; and, shifting employment if the firm has an increase in its experience rated tax rate. We found that only 27 percent of the identified leasing firms in Florida had a beginning tax rate of 2.7 percent at the time of their first leasing occurrence. We also found that 33 out of the 101 identified

¹ For this study, employment was calculated as the number of wage records for a given employer. Although this employment figure may overstate the exact number of employees on a given day, it provides a consistent method of determining employment across firms.

leasing firms experienced a substantial increase in employment in the year after their tax rate declined. Finally, most of the 10 identified leasing firms that went inactive in 1994 or 1995 experienced increases in their tax rates in prior years.

We also attempted to look at the relationship between taxes paid and benefits charged for identified leasing companies and their client firms in Florida and Oklahoma. For this analysis we used the ratio of aggregate taxes paid to benefits charged for leasing companies and their client firms. Although it would appear that the ratio of taxes to benefits was higher for the leasing companies from 1990-1994, we conclude that using the aggregate taxes and benefits is inadequate to measure leasing company effects on State UI trust funds relative to their client firms.

* * * *

Chapter 1

Introduction

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Introduction

This report presents the results of an exploratory study of the employee leasing industry. It begins with a description of the employee leasing industry, its size and characteristics. It then presents the results of a survey of State Unemployment Insurance (UI) tax administrators on their experience with the industry and their response in terms of administrative handling of leasing companies and taxing and reporting provisions of their laws. It then attempts to determine the implications of the leasing industry on State UI trust funds. Finally, it provides a summary of findings and recommendations for States in accommodating employee leasing for administrative and taxing purposes.

1.1 What is Employee Leasing?

A leased employee is a worker who is essentially rented on a long-term basis from an agency that is responsible for employing the worker, paying the salary or wages and taxes, and providing benefits for that employee. An employee leasing company is an organization in the business of leasing employees to client firms. Under a typical agreement, an employer contracts with a leasing company and dismisses some or all of its employees. These workers are then hired by the leasing company and leased back to the original employer, now the client company, on a long-term basis. The leasing company pays both the employees' wages and associated payroll taxes, including UI. It also provides the workers with other fringe benefits. This is done for a set fee (usually a percent of payroll) as stipulated in the leasing contract. The contract can be renewed any number of times.

1.2 Purpose of Study

The growth of employee leasing is a recent phenomenon that has attracted the attention of State and Federal officials. Although employee leasing firms claim to provide numerous benefits for their client firms, government officials have expressed concern that the industry may have a negative impact on certain government programs. However, because of the industry's recent expansion, no comprehensive studies have been done on employee leasing. The purpose of this study is to provide a review of the available data and literature on employee leasing, insight on the industry's effect on State UI systems based on a survey of State UI tax administrators, and analysis of State administrative and tax records to test the effects of employee leasing on State UI systems.

1.2.1 Assess Industry Size, Growth, and Characteristics

Because this study was concerned with the present and future implications of the employee leasing industry on the UI program, information about the size of the industry and State efforts to regulate the industry also were necessary. The first objective was to review available data on the industry and assemble estimates of the size of the industry. Contact with State government officials and existing surveys provided insight into the efforts that have been made to regulate the leasing industry.

The second major research objective of this study was to estimate the size of the industry, both nationally and by State. Although a consensus exists that the industry has grown considerably during the last 10 years, it is difficult to obtain reliable national estimates of the industry's size because data collected on the national level aggregates data on employee leasing firms with data on other types of temporary help firms. Alternative data sources, on the other hand, were either incomplete or unreliable.

To obtain more reliable estimates on industry size, four data sources were used. First, the study reviewed available data sources and the difficulties encountered in trying to obtain estimates on the size of the employee leasing industry when using these sources. The project then assembled estimates of the size of the employee leasing industry, as well as of industry employment. Data on the characteristics of employee leasing firms were also collected.

1.2.2 Determine State Legislative and Administrative Responses

The third major research objective of this study was to determine the State legislative and administrative responses to the growth of the employee leasing industry. To accomplish this objective, a survey of State UI tax administrators was undertaken. A number of informal studies have previously been done by various State UI tax offices and the Interstate Conference of Employment Security Administrators (ICESA). The survey undertaken for this study both updates data obtained in previous studies and provides additional data on State legislative and administrative initiatives.

Three tasks were undertaken to accomplish this objective. First, the study reviewed previous surveys on State responses to employee leasing. This involved contacting relevant government officials and researchers to obtain copies of previous surveys and reviewing the surveys. Second, a new survey was prepared and mailed to all State UI tax administrators. Third, the results were tabulated and compared with the findings of earlier surveys to analyze what strategies, if any, State UI agencies have pursued to regulate and monitor the growth of the industry and how these strategies have changed over time.

1.2.3 Evaluate the Impact on State UI Trust Funds

The fourth major research objective of the study was to evaluate the impact of the employee leasing industry on State UI funds. Considerable concern has been raised that employee leasing has had an adverse effect on State UI trust funds. In particular, there is concern about the following issues:

- **Aggregation-** Shifting payroll reporting from the client employer to the leasing company can result in several problems. First, State trust funds may lose revenue if employee leasing reduces employee turnover. Each firm that an employee works for in a given calendar year must pay payroll taxes on the worker's wages up to a taxable maximum; however, if workers who previously had worked for more than one employer are employed only by an employee leasing company during the year, this tax collection may be reduced. Taxes will be reduced even if the employee works for two or more client firms during the course of the year. Second, aggregation into the employee leasing company may result in apparent

changes in reported industry employment, such as the decline in manufacturing and the rapid rise in employment services.¹

- **Reduced Experience-Rating**- Shifting employees from a client firm with a high experience-rated tax rate to the tax rate of the employee leasing firm (a professional services firm) may have a negative effect on payroll tax revenues if the tax rate of the leasing firm is lower than that of the client firm and does not accurately reflect the client firm's layoff experience.
- **Tax Rate Manipulation**- Employee leasing companies may shift employees through successive corporate entities to avoid paying increases in UI payroll taxes when their tax rates increase as the result of the experience-rating system in the State.
- **Bankruptcy**- Financial failure of the employee leasing company may leave outstanding delinquent payroll taxes. It also may mean that any future claims by employees of the leasing company will become ineffective charges.

To assess the impact of employee leasing on the UI system, the project conducted several indepth, State-level analyses. Several States were targeted for indepth data collection and analysis. Tax rates (and benefit-tax ratios) of firms with groups of leased employees were compared with tax rates (and benefit-tax ratios) of the client firms to assess whether these rates (and ratios) increase or decrease under employee leasing.

* * * *

¹ "Where Are the Jobs?" *The Wall Street Journal*, October 19, 1993, p. A-1.

Chapter 2

Literature Review

Chapter 2

Literature Review

This chapter provides background on the rise and growth of the employee leasing industry as well as early responses to the increased presence of the industry within the contingent worker segment of the labor force.

2.1 Historical Origins of Employee Leasing

Employee leasing had its origins in the differential pension treatment of different classes of employees, in which one group of employees (generally officers) had a more generous pension program than other employees. Because the higher pretax contribution to the pension fund represents tax avoidance, the Internal Revenue Service (IRS) generally requires that all "employees" be eligible for the same pension plan. If, however, one group of workers could be considered employees of the firm and another group employees of the leasing company, this could accomplish the same end.

2.1.1 Pre-1982

The first leasing firm was said to have opened in California in 1972,¹ although others cite the leasing of Pinkerton security guards in the 19th century as the origins of employee leasing. Although its origins may be disputed, the growth in employee leasing is consistently linked to employee pensions.

Historically, many small business owners have maintained pension plans as a way to defer income for themselves and other employees. Participation in these pension plans was often limited to selected key employees. As these plans were seen as both discriminating against the nonkey employees of the business and as a means of deferring or avoiding income taxes, the IRS established a set of guidelines in 1982 to require employers to cover a substantial portion of their employees under the pension plans.

Many methods were used by employers to avoid the antidiscrimination laws. For example, some small business owners instituted lengthy vesting schedules in order to exclude all but long-term employees from becoming vested in their pension plan. Another tactic undertaken by small employers was to separate employment of highly compensated employees from that of the rest of the firm. One way that this was accomplished was by firing the firm's rank-and-file employees and then leasing them back from a leasing firm.

In order to stem these abuses, Congress passed the Employee Retirement Income Security Act (ERISA) in 1974 Public Law 93-406. ERISA instituted the test of common control. Under this test, if two organizations had substantial common ownership, then the employees of both organizations were to be treated as if they were employed by one employer. In the

¹Howard Potter. "Getting a New Lease," *Management Review*." April 1989, p. 30.

case of leasing companies, however, if the common control test was not violated, the leasing company was considered the employer for pension purposes.

2.1.2 The Tax Equity and Fiscal Responsibility Act of 1982

The next major piece of legislation to try to deal with employee leasing was the Tax Equity and Fiscal Responsibility Act (TEFRA) of 1982, Public Law 97-248. TEFRA was the first piece of Federal legislation that specifically referenced leased employees. It stated that employers, partners, or other high-paid employees of a company could not be provided a different pension plan than other employees and further clarified that leased employees were to be treated as employees of the client company unless safe harbor provisions were met.

TEFRA's safe harbor provisions² provided an escape route for employers desiring different pension plans. This section stated that leased employees are not subject to the same pension rules if the leased employee is covered by a plan maintained by the leasing organization that allows for immediate participation, full and immediate vesting, and employer contributions of at least 7.5 percent of the employee's salary. By meeting the provisions of the safe harbor section, employers could turn their employees over to a leasing company and provide pension plans with larger tax advantages to partners and other high-paid employees. These pension tax advantages, coupled with the savings in personnel management costs, proved to be very attractive and are often attributed with the growth of the employee leasing industry from only 5 firms³ with fewer than 5,000 employees prior to the enactment of TEFRA⁴ to an industry where 75,000 people worked under leasing arrangements in 1985.⁵

2.1.3 The Tax Reform Act of 1986

The Tax Reform Act (TRA) of 1986, Public Law 99-514, amended this tax shelter feature that allowed employers to offer pension plans to partners or high-paid employees with greater tax advantages. To qualify under the safe harbor provision as amended by TRA, leasing companies now are required to offer a pension plan that provides a 10-percent employer contribution to all employees of the leasing firm earning \$1,000 or more annually.

Additionally, IRC§414(n)(5)(A) states that the safe harbor provisions do not apply if leased employees constitute more than 20 percent of the recipient's nonhighly compensated workforce.⁶

²IRC§ 414 (n)(5).

³James R. Redeker and James O. Castagnera. "The Legal Nightmares of Employee Leasing." *Personnel Journal*. February 1985, pp. 58-62.

⁴Thomas A. Ulrich and Charles J. Hollon. *Business*; October to December 1988, p.44.

⁵ Kenneth Traynor and James G. Pesek. "Implications of Employee Leasing for Small Business," *Journal of Small Business Management*: October 1987, p. 10.

⁶Nonhighly compensated employee is defined

The changes enacted by TRA have virtually curtailed the use of safe harbor provisions to achieve the tax advantages previously associated with employee leasing. The leasing industry, however, continues to grow.

2.2 Reasons for Continued Growth of the Employee Leasing Industry

Since TRA, industry growth has been fueled by increases in employee benefit costs, particularly health insurance and workers' compensation premiums, both of which represent a larger share of the nonwage labor cost than UI. Thus, it should be kept in mind that the impetus for employee leasing may lie elsewhere, but the UI system is being affected as a result of these changes in labor market organization.

2.2.1 The Growth of Fringe Benefits

One of the financial incentives motivating employers to use employee leasing is the growing importance of fringe benefits as a component of labor compensation. This trend is apparent in data from the National Income Accounts (NIA) and in data from the Employment Cost Index (ECI) survey. In the NIA data, fringe benefits (employer contributions for social insurance and other non-labor compensation) grew from 5.0 percent of employee compensation in the year 1950 to 17.3 percent in 1992.

The ECI, an establishment-occupation based survey, has tracked wage and fringe benefit growth among private nonfarm employers since 1980. Fringe benefit costs grew faster than wages in every year between 1980 and 1992 except 1985. Over these 13 years, the annual average growth rates were 5.2 percent for wages and salaries and 6.6 percent for fringe benefits a 27-percent higher growth rate for fringe benefits. From 1993 to 1995, fringe benefits as a percent of total compensation declined by 1 percent to 28.4 percent of total compensation.

Within the detailed categories of fringe benefit costs, the employer costs of both Federal and State UI payroll taxes are identified. Combined, these UI taxes decreased from 1.1 percent of total compensation in March 1987 to 0.9 percent in March 1995. Thus, UI payroll taxes have not been growing as a share of employee compensation among private industry employers.

Exhibit 2-1 indicates that the six categories of fringe benefits representing the largest costs to employers in March 1995 were (in descending order) health insurance (6.2 percent), Social Security taxes (6.0 percent), vacation pay (3.1 percent), pensions and workers' compensation (each 2.3 percent), and holiday pay (2.2 percent). Combined Federal and State UI taxes among private industry employers (0.9 percent) were similar in magnitude to nonproduction bonuses (1.3 percent), premium (mainly overtime) pay (1.1 percent), and sick leave (0.8 percent).

Exhibit 2-1
Unemployment Insurance Service
Department of Labor

Employer Costs Per Hour Worked
for Employee Compensation and Costs
as a Percent of Total Compensation,
Private Industry, March 1995

Compensation Component	Total Private		1-99 Workers		100 workers or more	
	Cost	Percent	Cost	Percent	Cost	Percent
Total compensation	\$17.10	100.00%	\$14.58	100.00%	\$19.44	100.00%
Wages and salaries	12.25	71.6	10.81	74.1	13.58	69.9
Total benefits	4.85	28.4	3.77	25.9	5.85	30.1
Paid leave	1.09	6.4	0.77	5.3	1.36	7.2
Vacations	0.54	3.1	0.37	2.5	0.69	3.6
Holidays	0.37	2.2	0.27	1.9	0.47	2.4
Sick leave	0.14	0.8	0.1	0.7	0.17	0.9
Other leave	0.05	0.3	0.03	0.2	0.06	0.3
Supplemental pay	0.47	2.8	0.35	2.4	0.58	3
Premium pay	0.19	1.1	0.12	0.9	0.25	1.3
Shift pay	0.05	0.3	*	*	0.1	0.5
Nonproduction bonuses	0.23	1.3	0.22	1.5	0.24	1.2
Insurance	1.15	6.7	0.82	5.7	1.45	7.5
Life	0.04	0.3	0.03	0.2	0.05	0.3
Health	1.06	6.2	0.77	5.3	1.34	6.9
Sickness and accident	0.04	0.3	0.03	0.2	0.06	0.3
Retirement and savings	0.52	3	0.33	2.3	0.69	3.5
Pensions	0.39	2.3	0.25	1.7	0.51	2.6
Savings and thrift	0.13	0.7	0.08	0.6	0.17	0.9
Legally required	1.59	9.3	1.48	10.2	1.69	8.7
Social Security	1.02	6	0.91	6.2	1.13	5.8
Federal unemployment	0.03	0.2	0.03	0.2	0.03	0.2
State unemployment	0.12	0.7	0.12	0.8	0.12	0.6
Worker's compensation	0.39	2.3	0.42	2.8	0.37	1.9
Other benefits	0.03	0.2	*	*	0.05	0.3

*Cost per hour worked is \$0.01 or less.

SOURCE: Bureau of Labor Statistics. Employer Cost Indexes and Levels, 1975-95. October 1995, Bulletin 2466, Table 18.

For small employers (those with 1 to 99 employees in published ECI tabulations), the legally required payments represent a larger share of total compensation: 10.1 percent in March 1995 compared to the all-employer average of 9.3 percent. The higher percentage for small employers is probably due to their below-average wages (coupled with a fixed tax base for UI and Social Security taxes) as well as higher average rates for workers' compensation. Health insurance costs are actually a below-average percentage of payroll for small employers, but the explanation here is undoubtedly that many do not provide any health insurance. Among those who provide it, health insurance is an above-average share of employer costs. Unfortunately, this cannot be discerned from the survey results.

From the preceding, it is apparent that fringe benefits have come to constitute a very large component of employer labor costs. Fringe benefit costs as a whole have been growing more rapidly than wages and salaries. A sizable share of fringe benefit costs are mandated payroll taxes. These taxes are more important in the cost structure of small employers than other employers. Finally, UI taxes represent only a modest share of fringe benefit costs. Health insurance and workers' compensation premiums represent a larger share of nonwage labor costs than UI. However, although the impetus for employee leasing may lie elsewhere, the UI system is being affected as a result of these changes in labor market organization.

2.2.2 Growth of Nonstandard Employment

Leased employees traditionally have been considered within the larger category of contingent workers, a group that is broadly defined by employment arrangements that differ from regular full-time, permanent, wage-and-salary positions.⁷ Corporate downsizing and worker dislocation have increased the use of nontraditional employment arrangements. Workers who usually fall into this category include part-time, temporary, and contract employees; those who are self-employed; workers from the business services sector; and leased employees⁸. Based on a supplement to the February 1995 Current Population Survey (CPS) questionnaire, there were 6.034 million contingent workers under the definition that would include leased employees out of a total workforce of 123 million workers over the age of 16.⁹ Leased employees, however, should be considered a unique subset of contingent workers: they usually have full-time positions, are more likely to have long-term employment arrangements, and receive higher wages and more complete benefits than other contingent workers. Measured differently, an estimated 652,000 workers in the CPS supplement were

⁷Richard S. Belous. *The Contingent Economy: The Growth of the Temporary, Part-time and Subcontracted Workforce*. National Planning Association, Washington, D.C. 1989.

⁸U.S. Congress. Senate. Committee on Labor and Human Resources. Subcommittee on Labor. Hearing on *Toward a Disposable Workforce: The Increasing Use of "Contingent Labor."* 103d Cong., 1st sess., 1993. S.Hrg. 103-620.

⁹U.S. Bureau of Labor Statistics. *Contingent and Alternative Employment Arrangements*, Report No. 900, USDL 95-318, August 1995, Table 1.

provided by contract firms.¹⁰ For a number of reasons, this may be expected to be both an overestimate and underestimate of leased workers.

2.3 Public and Private Responses to Industry Growth

2.3.1 County Business Patterns

Leasing firms were classified in Standard Industrial Classification (SIC) 7369 (Personnel Services, Not Elsewhere Classified) in County Business Patterns (CBP) data under the 1972 industrial classification system.¹¹ In March 1979, this industry had 450 establishments and 47,285 workers. The number of workers dropped from 45,137 in 1982 to 31,359 in 1983, and the number of establishments decreased from 438 to 383, presumably the result of changing ERISA regulations governing safe harbor leasing under TEFRA.

After 1983, the number of employees again grew and reached 45,122 in 1987, the last year firms were classified under 1972 SIC codes. This estimate is lower than suggested by the tone of public discussions about employee leasing from the early to mid-1980's. These low national totals in CBP data could be partially due to the misclassification of some leasing companies into SIC 7362 (Temporary Help Services). During the 1979 to 1987 period, average employment of establishments in SIC 7369 (Personnel Services, Not Elsewhere Classified) remained in the 105,000 to 115,000 range.

After 1987, leasing firms were reported along with temporary help agencies within SIC 7363 of the revised SIC system. SIC 7363 (Help Supply Services) had 1,075,730 workers in 1988, compared to 800,227 for the temporary help industry alone in 1987. Although it is not known what percentage of the additional 275,503 employees worked for employee leasing firms, it is possible to estimate the proportion based on data on the growth of temporary workers. Temporary help employment grew by more than 100,000 in the 3 years prior to 1987. Thus, it seems likely that more than half of the 275,503 increment from 1987 to 1988 is due to growth in temporary help employment.

The combined SIC 7363 (Help Supply Services) has continued to show employment growth since 1988. By 1990, the latest year of available CBP data covering all States, the national total was 1,210,312.

2.3.2 ES 202

A recent estimate of employment available using the Employment Service (ES) 202 data is for employment during 1994. During this period, 23,531 Help Supply Firms (SIC 7363) reported activity. They reported aggregate employment of approximately 2 million

¹⁰Ibid., Table 5.

¹¹It is more accurate to state that most leasing firms are classified in this four-digit industry. When 1972 SICs were first assigned in the early 1970s, there were no leasing firms. When leasing came into existence, the firms were encouraged to report in SIC 7369, but many may have reported in SIC 7362 along with Temporary Help agencies.

workers. BLS currently has a project underway to distinguish temporary help agencies from Employee Leasing firms within SIC 7363 (Help Supply Services). The BLS project had separated most of the reporting units into the two categories by late November 1993. In June 1992, there were 20,408 reporting units in SIC 7363. The breakdown by type of firm was as follows: 2,006 leasing companies, 11,332 temporary help firms, 6,922 not yet classified, and 148 not leasing companies or temporary help firms. The latter are apparently reporting units with inappropriate industrial classifications. The associated employment counts were as follows: 1,469,559 total, 188,593 leased employees, 1,024,753 temporary help employees, 238,882 not classified, and 17,331 employees in firms not classified appropriately. Thus, of the workers classified as either leased or temporary help, leased employees made up 15.5 percent of the total (188,593 of 1,213,346).

The ES 202 reporting system adopted the 1987 SIC codes in 1988. Therefore employees in leasing firms are classified in SIC 7369 prior to 1988 and in SIC 7363 from 1988 to the present. A tabulation of ES 202 data showed that in March 1987 (under 1972 SIC codes), there were 879,220 workers in Temporary Help Services and 71,329 in Personnel Supply Services, Not Elsewhere Classified (SIC 7369). This count in SIC 7369 exceeds by 58 percent the corresponding count in CBP data.

Under current SIC codes, total employment in SIC 7363 was 1,065,919 in March 1988. This combined total for the temporary help and leased employment classification had grown to 1,293,091 by March 1992. For March 1990, where national totals can be compared with CBP data, the two data sources showed very similar employment totals: 1,247,432 in ES 202 data and 1,210,312 in CBP data, a difference of 3.0 percent.

The ES 202 reporting system requests that employee leasing firms report employment in each of its client firms using a Multiple Worksite Report form, as well as total employment and central office employment. Compliance with this requirement is spotty. Another outcome expected from the BLS project mentioned above is to generate estimates of the number of leasing firms and the associated employment that is reported solely in SIC 7363 (Help Supply Services).

2.3.3 Leasing Company Registration Lists

In States that have special registration requirements for leasing companies (for example, Florida), the universe of actual and potential leasing companies among active employers is known, making the problem of identifying employee leasing firms and employees greatly simplified. Unfortunately, not all States compile these lists. This makes it impossible to generate reliable national estimates based only on this source of data.

As a result of the inability to produce reliable estimates of the size and characteristics of the employee leasing industry, one of the objectives of this study was to attempt to do this utilizing a survey of State UI Agencies. The results of this survey are provided in the next section of this report.

* * * *

Chapter 3

Survey of State Unemployment Insurance Agencies

Chapter 3

Survey of State Unemployment Insurance Agencies

Only two other surveys have been conducted on the topic of employee leasing. In 1989, the State of Louisiana conducted an informal survey of States to determine the extent to which employee leasing is permissible within States and sought applicable State laws. In 1990, the Interstate Conference of Employment Security Administrators (ICESA) surveyed the States and obtained information about State laws governing employee leasing and problems encountered with the leasing industry. However, neither survey produced definitive information because of low response rates and other methodological issues.

The KRA Corporation (KRA) survey was designed to gain an understanding of how States are currently dealing with the employee leasing industry and to obtain a more accurate picture of the impact of employee leasing on State UI systems. In September 1994, KRA initiated a survey of State UI tax administrators that asked questions about definitions of employee leasing, applicable State laws, effects on the UI trust fund, industry size and employment, reported industry classifications, registration requirements, bonding requirements, client firm reporting requirements, failure rates of leasing companies, experience-rating procedures, and associated changes in successor rules. The survey instrument is found in Appendix A.

The mail survey was conducted between September 1 and November 1, 1994. Follow-up telephone calls were made to obtain additional data or clarify responses. Surveys were received from all 50 States and the District of Columbia. Data cleaning and database construction were completed as surveys were received, and data analysis was conducted during January 1995. The remaining sections of this chapter present the data collected through the survey.

3.1 State Statutes on Employee Leasing

As more States have experience with the employee leasing industry, the number of States with legislation governing the industry has increased. The ICESA survey of 1990 indicated that 13 States had laws governing coverage of employee leasing companies, with another 17 States having a rule or policy governing employee leasing. The results of the KRA survey show that 25 States now have laws governing the operation of employee leasing companies, and 35 States have at least a working definition of employee leasing or a definition in legislation, regulation, or agency policy. Appendix B contains a State-by-State summary of laws and regulations pertaining to employee leasing. This information was obtained through the survey and supplemented by a review of State UI laws. Citations of workers' compensation laws and regulations may be incomplete.

3.1.1 Reasons for and Effects of Employee Leasing Legislation

Responses to the survey question on the reasons for enacting employee leasing legislation varied. Some States reported that legislation was passed in reaction to problems encountered and concerns about abuse, whereas others reported that legislation was precautionary and

intended to avoid problems encountered in other States. Other reasons given for the passage of State legislation were the following:

- To support agency rulings, such as the determination of who the employer is.
- To regulate such issues as tax liability and experience rating.
- To clarify the rights and responsibilities of client firms.
- To clarify the rights and responsibilities of leasing companies. (In some States, legislation was encouraged by the leasing industry.)

Given the different reasons for employee leasing legislation and the fact that the growth of the leasing industry has been fueled by increases in employee benefit costs, it is not surprising that State laws addressing employee leasing are found in various sections of State statutes. Some are contained within the UI section of the statutes, whereas others exist in the general business regulation, taxation, or workers' compensation sections. This inconsistency contributes to the variation in the provisions of the laws and also leads to situations where, for purposes of UI, no provisions exist, but for workers' compensation, extensive guidelines are contained in legislation.

The varying reasons for enacting legislation also contribute to varying effects. Fifteen respondents indicated that legislation increased regulation of the industry; however, only one respondent reported slowed industry growth or a reduction of industry size due to legislation. Eleven respondents indicated that the legislation resulted in increased reporting requirements, in some cases due to a provision in the law that requires employee leasing companies to provide additional data or lists of client firms. Nine respondents reported an increase in financial entry requirements that are often associated with licensing fees or bonding requirements. When asked about the effect of legislation, the most common response was that it was too early to tell. Many State statutes were passed in the late 1980's or early 1990's, and, States have not had adequate time to assess the effects of the legislation.

3.2 Defining Employee Leasing

A common feature of many State employee leasing laws is a definition of the employee leasing arrangement or employee leasing company. Twenty-five States have such a definition in their law, with another four States defining employee leasing through regulations. Only 14 States do not have a working definition or a definition of employee leasing in any legislation, regulation, or agency policy. State definitions are contained in Appendix C.

3.2.1 Provisions Contained in Definitions

The determination of the employing unit is a common provision in State definitions. Some States consider the employee leasing company the employer under all circumstances, but others consider the leasing company the employer of leased employees only if the firm meets certain criteria. Other provisions contained in legislated definitions include the requirement

that a leasing company maintain "direction and control" to be considered the employer of leased employees. Further discussion of determining the employer of leased employees is contained in Section 3.3.1.

State definitions utilize a variety of criteria to distinguish employee leasing from other types of firms or employment relationships. Twelve States specify that to be an employee leasing arrangement, staff placement must be ongoing or long-term in nature (although only one State specifies the period that meets the ongoing or long-term requirement). Other criteria used to distinguish employee leasing from other types of firms include the receipt of a fee (seven States) and requirements that the lease arrangement cover all or a significant portion of a client firm's staff (three States).

3.2.2 Distinguishing Between Employee Leasing and Temporary Help Firms

One purpose of legislated definitions is to distinguish employee leasing from temporary help firms. Distinguishing between employee leasing and temporary help firms is no small matter. First, both are included in SIC 7363 Help Supply Services. Further, employee leasing firms may also provide temporary help (and vice versa). BLS is trying to encourage different reporting standards for employee leasing and temporary help firms, with temporary help firms reporting all of their employment in SIC 7363 and employee leasing firms reporting their leased employees according to the SIC of their client firms.¹

The extent to which States attempt to distinguish between employee leasing and temporary help firms varies. Five States do not attempt to distinguish between the two types of firms or use a single definition for both. In addition to (or in place of) legislated definitions, States use other characteristics to distinguish between leasing and temporary help firms. Thirty States indicated they have discussions with leasing company managers to determine the type of business being conducted. Another common distinguishing characteristic is the word "leasing" in the firm's name (18 States). Other ways State staff distinguish employee leasing from temporary help firms is by requiring special licensing of leasing companies, by assessing the length of placements made by the firm, and by legislative registration requirements for leasing companies.

3.3 Other Regulation of the Industry

Two primary questions underlie most State laws and policies governing the employee leasing industry: "Who is the employer of leased employees?" and "Who is liable for unemployment contributions?" To answer these two questions, States have regulated the industry in a variety of ways. The methods for determining the employer of leased employees and regulation of the industry including registration requirements, bonding, reporting requirements, experience rating procedures, and successorship determination are discussed below.

¹BLS currently has a project underway to try to distinguish between employee leasing and temporary help firms in its ES 202 data, with employee leasing firms being requested to file Multiple Worksite Reports.

3.3.1 Determining Employer Status

Determining the employer or the employing unit is a key factor in understanding who is responsible for reporting and making contributions as required by the UI system. Historically, considerations such as who maintains "direction and control" of the employees, who has the right to hire and fire, and who pays the employee have led to determinations of who is the employer. Many of the same factors are considered when determining whether the employee leasing company or the client firm is the employer of leased employees. However, because of the nature of employee leasing, determining who has direction and control or the authority to hire and fire is often difficult.

3.3.1.1 Methods for Determining Employer Status

According to the survey responses, 27 States consider the employee leasing company the employer of leased employees, while 9 consider the client firm the employer. Of the remaining 14 respondents, 5 indicated that the employer was whoever maintained direction and control of the leased employees. Other States require that the leasing company meet criteria such as the seven-point test below to be considered the employer:

1. Negotiates with clients or customers for such matters as time, place, type of work, working conditions, quality, and price of services
2. Determines assignments or reassignments of workers, even though workers retain the right to refuse specific assignments
3. Retains the authority to assign or reassign a worker to other clients or customers when a worker is determined unacceptable by a specific client or customer
4. Assigns or reassigns the worker to perform services for a client or customer
5. Sets the rate of pay for the worker, whether or not through negotiation
6. Pays the worker from its own account or accounts
7. Retains the right to hire and terminate workers

Some States do not require that all seven criteria be met; rather, they use some combination of three or five of the criteria. Other reported State considerations include who benefits most from the leased employment, whether or not the employee leasing company has posted a bond, and the provisions of the contract between the leasing company and the client firm. Four States indicated that each case is reviewed separately but did not specify the criteria used to determine the employing unit.

3.3.1.2 The Employer of Partners/Sole Proprietors and Corporate Officers

In some States, special considerations are made when determining the employer of partners/sole proprietors and corporate officers. Most State laws prohibit payment of UI benefits to sole proprietors or partners, the theory being that they are self-employed and, therefore, cannot be laid off. If the leasing company pays their salaries and UI contributions, they may be monetarily eligible for benefits, should they be separated from the firm (the leasing company). The other side of the situation is that it would, in most cases, represent a windfall to the UI trust fund, because these individuals would be very unlikely to actually collect benefits.

Thirty-seven States consider partners/sole proprietors to be owners and therefore not eligible for UI benefits. In these cases, the employee leasing company is most likely serving merely as a payrolling firm for those individuals. Only six States responded that a partner/sole proprietor is considered an employee of the leasing company, whereas one considered those individuals employees of the client firm. Some States determine the employer of partners/sole proprietors based on who reports wages, whereas others make case-by-case determinations. Based on the premise that an individual cannot be leased to him or herself, one State does not allow owners to be part of a lease arrangement.

The entity considered the employer of corporate officers varies more significantly than for partners/sole proprietors. Twenty-one States consider corporate officers employees of the leasing company, and 18 consider them employees of the client firm. Two States responded that corporate officers are considered owners and are therefore not eligible for UI benefits, but two others indicated that corporate officers may be considered in dual employment.

3.4 Determining Tax Liability

Because of the unique nature of an employee leasing arrangement, determining liability for UI contributions and the appropriate amount of contributions can be difficult. In general, 22 States hold the employee leasing company liable for contributions, but 10 States consider the client firm to be liable if contributions are not paid by the leasing company. Nine States consider the client firm jointly and severally liable for contributions, although five States allow relief from liability if a bond is posted by the leasing company. Other States consider issues of direction and control and who is, by definition, the employer of leased employees when determining tax liability. Determining tax liability and recovering contributions are aided by reporting and registration or licensing requirements. Both of these topics, as well as bonding, experience rating, and successorship provisions, are discussed in more detail below.

3.4.1 Registration Requirements

Registration requirements are one way States identify employee leasing companies for purposes of assessing UI tax liability. As shown in Exhibit 3-1, 19 States reported that they have registration requirements for employee leasing companies. In some cases, the registration is the same as that required of all firms, whereas other States require special registration or licensing of leasing companies. Registration requirements have been recently

Exhibit 3-1

Unemployment Insurance Service
 Department of Labor
 Registration Requirements by State
 and Reason

STATE	Registration Requirement	Year Required	Reasons for Registration Requirement			
			To track Industry Growth	To ensure UI Taxes Are paid properly	To distinguish employee leasing from temporary help	To ensure proper SICs of client firms are reported
AK	N					
AL	N					
AR	Y	1987				
AZ	N					
CA	N					
CO	N					
CT	Y	1989	Y	Y	Y	Y
DC	N					
DE	N					
FL	Y	1992	Y	N	Y	N
GA	Y	1992	N	Y	Y	N
HI	Y	1987	N	Y	N	Y
IA	N					
ID	N					
IL	N					
IN	N					
KS	Y	1990	N	Y	N	N
KY	N					
LA	N					
MA	Y	1993	Y	Y	Y	Y
MD	N					
ME	Y	1991	N	Y	Y	N
MI	N					
MN	Y	1992	Y	N	Y	N
MO	N					
MS	N					
MT	N					
NC	N					
ND	N					
NE	N					
NH	Y	1994	Y	Y	Y	Y
NJ	N					
NM	Y	1994				
NV	Y	1994	Y	Y	Y	N
NY	N					
OH	N					
OK	N					
OR	N					
PA	N					
RI	Y	1992	N	Y	N	N
SC	Y	1994	N	N	N	N
SD						
TN	Y	1996	N	N	Y	N
TX	Y	1994	N	Y	Y	N
UT	Y					
VA						
VT	Y	1989	Y	Y	N	Y
WA	N					
WI	N					
WV	N					
WY	Y	1989	N	Y	N	N
Affirmative Responses	19		7	12	10	5

implemented, with 11 States requiring registration as recently as 1992. When asked about the reasons registration is required of employee leasing companies, the most frequent response was to ensure that UI taxes are paid properly. Other common reasons were to distinguish employee leasing from temporary help firms, to track industry growth, and to ensure proper SIC reporting of client firms. Additional reasons include the following:

- To ensure adequate coverage for leased workers
- To identify joint and several liability
- To prevent leasing companies from circumventing proper workers' compensation rate computations
- To ensure that experience rating is uniform
- To identify a client firm's entry in an employee leasing arrangement, as well as its exit

Because registration or a licensing requirement is often a recent addition to policy governing employee leasing, most States are not sure if it has accomplished its goals. Twelve of 13 States responding indicated that registration has helped ensure that all UI taxes are paid properly, whereas 8 States noted registration has assisted in distinguishing employee leasing from temporary help firms. Eight States also reported that registration has helped track industry growth, whereas five States indicated proper SIC reporting has been assisted by registration. Some States commented that although registration requirements are in place, they are not sure that all firms required to register actually do so.

3.4.2 Reporting Requirements

Another way States track employee leasing companies and their clients is through submitting lists of client firms. Currently, 24 States require the submission of a list of client firms, with 1 State requiring client lists as of 1995 and another State having such a requirement pending legislative approval. Lists of client firms are required in some States so that client firms can be considered the employer and held liable for contributions unpaid by the leasing company. Other States use such lists to ensure correct reporting by the leasing company, and still others use the lists to ensure proper predecessor/successor designations and experience-rated tax rate computation.

Some States require employee leasing companies to submit information in addition to a list of client firms, such as addresses and SICs of client firms. Exhibit 3-2 shows States with client firm reporting requirements and the additional information collected. The most common information collected, in addition to client lists, is the number of employees leased to client firms. These requirements can be important to proper reporting of employment by industry in the ES 202 reporting system. Absent reporting requirements, employee leasing firms may aggregate all their leased employees in Help Supply Services (SIC 7363) rather than by the industry of their client firms.

Exhibit 3.2

Unemployment Insurance Service
Department of Labor

Client List Requirements by State and
Type of Information

STATE	Client List Required	Year Required	Additional Information Required			
			Leased Employment at Client Firm	SIC Codes of Client Firms	Multiple Worksite Reports	Employer IDs of Client Firm
AK	N					
AL	N					
AR	Y					
AZ	N					
CA	N					
CO	Y	1993	N	Y	Y	N
CT	Y	1989	N	N	N	Y
DC	N					
DE	N					
FL	Y	1987	Y	N	N	N
GA	Y	1992	N	N	N	N
HI	N					
IA	Y	1990	Y	Y	Y	N
ID	Y	1994	Y	Y	Y	N
IL	N					
IN	N					
KS	Y	1990	Y	Y	Y	N
KY	N					
LA	Y	1994	Y	Y	Y	Y
MA	Y	1993	Y	N	N	Y
MD	Y		N	N	N	Y
ME	Y	1991	Y	N	Y	N
MI	N					
MN	Y	1995				
MO	Y	1992	Y	N	Y	N
MS	N					
MT	N					
NC						
ND	N					
NE	Y	1992	Y	N	N	Y
NH	Y	1994	Y	N	Y	N
NJ	Y	proposed	Y	N	N	Y
NM	N					
NV	Y	1994	Y	N	Y	Y
NY	N					
OH	N					
OK	N					
OR	N					
PA	N					
RI	N					
SC	Y	1994	Y	N	N	N
SD						
TN	N					
TX	Y	1994	Y	Y	Y	Y
UT	Y	1991	Y	N	Y	N
VA	N					
VT	Y	1989	Y	Y	N	N
WA	N	1993	N	N	N	Y
WI	N					
WV	N		N	N	Y	N
WY	Y	1989	Y	N	Y	N
Affirmative Responses	24		17	7	13	9

3.4.3 Bonding

Bonding requirements are used in two ways relative to leasing arrangements. First, some States require that employee leasing companies post a bond to ensure that the firm is financially solvent. Presumably, the bond ensures that if a leasing company goes out of business with delinquent contributions, the company has a sufficient net worth to allow for the recovery of amounts owed. Employee leasing companies are not generally considered to have significant material assets (i.e., buildings and equipment) that can be liquidated to pay delinquent contributions or wages owed to employees. Second, some States require that employee leasing companies post a bond to cover delinquent contributions or to relieve client firms of joint and several liability for contributions. The concern is to avoid having client firms paying UI contributions twice, once to the leasing company and again when the leasing company fails to pay.

Currently, only two States require that employee leasing companies post a bond; however, five other States have provisions for optional bonding as a method of proving financial solvency or relieving client firm liability. Bond amounts in most States are flat amounts specified in legislation or regulation. The bond amounts vary from \$10,000 to \$100,000. One State requires a flat amount or the amount equivalent to 2.7 percent of the leasing company's payroll, whichever is greater. Another State requires a bond equal to \$100,000 or the amount of UI contributions the leasing company was liable for in the last year, whichever is greater. Some States have provisions that reduce the size of the bond if the leasing company pays required contributions, usually for 3 consecutive years.

Few responses to questions about liabilities covered by the bond were received. State legislation pertaining to bonding indicates that most bonds are to ensure the prompt payment of contributions, interest, and penalties for which the leasing company is liable. In some cases, the bond is to cover wages and benefits for which the leasing company is liable, although "benefits" is not defined and it is unclear if benefits includes unemployment contributions.

3.4.4 Experience Rating

Experience rating is a key factor in determining the amount of payroll contributions any company must pay. In the case of leasing companies, it is not always clear how the experience of a leasing company should be computed. For example, some States consider the experience rate of the client firm when determining the rate for the leasing company, and others maintain different experience rates for each of a leasing company's client firms. However, the overwhelming majority of States (44 of 50 responding) apply a single tax rate to the leasing company based on the overall experience of the leasing company. Only in those States that consider the client firm's experience when determining the leasing company's rate does the method of establishing experience rates differ from the method used for temporary help firms. Generally, temporary help firms have a single experience rate, and their client firms' rates are not considered in any way.

3.4.5 Successorship

Another consideration in determining both tax liability and the appropriate experience rate is the predecessor/successor relationship between a client firm and an employee leasing company. Some States do not consider the employee leasing company the successor to the client firm because the leasing company only takes over the employees and human resource functions from the client, not the assets or production function. Exhibit 3-3 shows each State's successorship provision as it pertains to employee leasing. Most States indicated that employee leasing companies may not transfer the experience of client firms under their State's successorship provisions, whereas some States allow the leasing company to be the successor to the client firm. A few States commented that the leasing company is automatically considered the successor to the client firm. Generally, States indicated that employee leasing companies are treated like any other firm when considering potential predecessor/successor relationships. Only two States responded that the growth of the employee leasing industry has resulted in the altering of State successorship provisions.

3.5 Industry Estimates

The 1987 revisions to the Standard Industrial Classification Manual include employee leasing in the 7363 Help Supply Services category. That classification also includes temporary help services, office help supply services, labor pools, and manpower pools. Because of the variety of services included in the 7363 classification, determining the size of the employee leasing industry separate from other 7363 activities is difficult. In States where leasing companies are required to register or obtain a license, an estimate of the leasing industry separate from the other 7363 activities may be more accurate. However, as stated previously, only 19 States have such a requirement.

Further complicating industry estimates is the method by which firms are classified by industry. Industry classifications are based on the firm's principal economic activity, although many firms engage in several activities. This assignment is particularly important in reference to employee leasing companies because they may supply employees to client firms conducting several different activities. Therefore, the potential for misclassifying leased employees is greater than for other firms. In addition, in States where lists of client firms are not required, it is possible that not all leased employment is reported in the appropriate SIC.

3.5.1 Estimates of Leased Employment

Exhibit 3-4 shows the geographic distribution of estimates of leased employment in 1993. Twenty-four States provided estimates, ranging from 1 to more than 100,000 leased employees. The average number of leased employees per State is 25,342. Total leased employment in States able to provide estimates was 608,198. The States that require the submission of client lists account for 46 percent of the total (278,888 leased employees). State estimates of the leasing industry show variable growth between 1989 and 1993. Estimates of leased employment for previous years were also requested and are provided in Exhibit 3-5.

Exhibit 3-3

**Unemployment Insurance Service
Department of Labor**

Successorship Provisions by State

STATE	May not transfer Client experience record	Must maintain client experience record and tax rate	Treated like any other firm
AK	x		x
AL	x		
AR	x		x
AZ	x		x
CA			x
CO	x		
CT		x	
DC			x
DE			
FL	x		x
GA	x		x
HI			x
IA			x
ID	x		x
IL			x
IN			x
KS	x		x
KY		x	
LA			x
MA			x
MD			x
ME			x
MI			x
MN	x		x
MO			x
MS	x		x
MT	x		
NC	x		
ND			x
NE	x		
NH	x		
NJ			
NM			x
NV			x
NY			x
OH	x		x
OK			x
OR			x
PA			x
RI			x
SC	x	x	
SD			
TN	x		x
TX	x		
UT	x		
VA	x		x
VT	x		x
WA	x		x
WI	x		x
WV	x		
WY	x		x
TOTAL	26	3	36

Exhibit 3-4

Unemployment Insurance Service
Department of Labor

State Estimates of Leased Employment, 1993

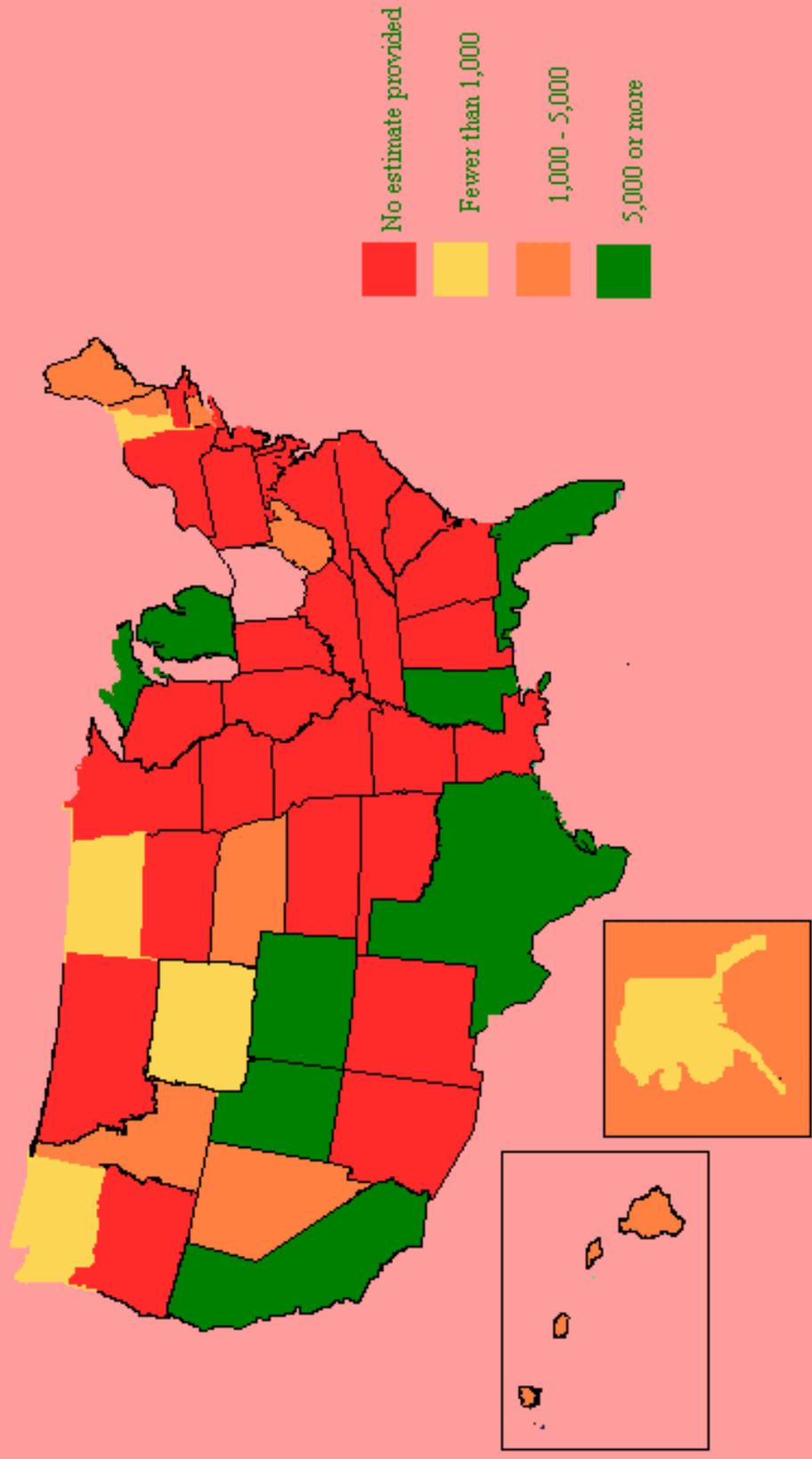


Exhibit 3-5
Unemployment Insurance Service
Department of Labor
State Estimates of Leased Employment,
1989-1993

STATE	Client firm Reporting Requirement	Year Reporting Required	1989	1990	1991	1992	1993
AK	N						817
AL	N		12,142	14,358	18,372	24,982	28,941
AR	Y						
AZ	N						
CA	N						260,000
CO	Y	1993					9,173
CT	Y	1989	827	1,004	1,050	1,153	1,214
DC	N						
DE	N						1
FL	Y	1987	35,106	68,739	84,907	90,056	113,773
GA	Y	1992					
HI	N		1,800		2,055		2,600
IA	Y	1990					
ID	Y	1994	2,187	2,210	1,971	2,534	3,681
IL	N						
IN	N						
KS	Y	1990					
KY	N						
LA	Y	1994					
MA	Y	1993					
MD	Y					942	1,215
ME	Y	1991	833	1,733	2,650	4,850	3,849
MI	N		500	1,600	3,200	7,200	11,000
MN	Y	1995					
MO	Y	1992					
MS	N						15,000
MT	N						
NC							
ND	N		200	200	200	200	200
NE	Y	1992					1,000
NH	Y	1994	1,500	1,500	2,500	3,000	3,507
NJ	Y	Proposed					
NM	N						
NV	Y	1994					3,500
NY	N						
OH	N						
OK	N						
OR	N						
PA	N						
RI	N					4,000	6,200
SC	Y	1994					
SD							
TN	N						
TX	Y	1994	40,000	60,000	85,000	100,000	125,000
UT	Y	1991			6,257	6,741	11,958
VA	N						
VT	Y	1989	50	300	400	500	668
WA	N	Requested				500	700
WI	N						
WV	N		2,497	2,776	2,635	3,064	3,851
WY	Y	1989					350
Total	24		97,642	154,420	211,197	249,722	608,198
Total of States Requiring Client List Reporting			80,503	135,486	184,735	209,776	278,888

3.5.2 Estimates of Leasing Companies

Exhibit 3-6 shows the geographic distribution of estimates of employee leasing companies. Twenty-nine States were able to provide estimates of the number of employee leasing companies in their State in 1993. The total estimated number of firms was 2,297. Of the 29 States providing estimates, 19 require that employee leasing companies register or maintain a license to conduct business in that State. These 19 States account for only 757 of the 2,297 firms estimated for 1993 (33 percent). Growth in the number of employee leasing companies has also been variable. The estimated number of companies increased by only 25 percent between 1991 and 1992, although the period 1992 to 1993 showed a 56-percent increase.

This higher growth rate in recent years may be due to recent registration requirements as opposed to actual industry growth. Estimates of the number of leasing companies for previous years are shown in Exhibit 3-7.

3.6 Standard Industrial Classification of Client Firms

Nineteen States indicated that they record the SICs of leasing company client firms or their employment in the appropriate SIC. Although leased employment is historically thought to be found in such employment as medical office staff, legal assistants, or office support, the survey responses indicate that leased employment is found in a variety of industries. When the survey asked about the major industry of client firms, the most frequent response (30 respondents) was the service industry. However, within the service industry, responses varied from Hotels and Motels (SIC 7011) to General Automotive Repair Shops (SIC 7538) to Public Relations Services (SIC 8743). Other common responses of industries of client firms were manufacturing, transportation, and retail trade. A complete list of the reported industries of client firms is found in Exhibit 3-8.

Because so few States require reporting of client firms' SICs, it is difficult to determine if there have been shifts in the reporting of the workforce from one industry category to another. When queried on this topic, 15 States indicated that the growth of the industry has resulted in shifts in reported employment. However, 25 States indicated they could not determine whether such shifts have occurred.

For the States that do require reporting of employment by client SICs, only three indicated that there has been a noticeable change in the industry mix in the last 5 years. Again, the low response may be caused by limited collection and monitoring of such data.

Improper reporting of employment by SICs could have significant effects on the data reported at both the Federal and State levels. Nonetheless, few States collect information that allows them to determine the frequency of improper reporting. Of the States collecting SICs of client firms, only nine indicated that there have been instances of improper reporting, with six of the nine states categorizing those instances as infrequent (5 percent to 10 percent of leasing companies misclassifying their leased employees).

Exhibit 3-7

Unemployment Insurance Service
Department of Labor

State Estimates of Employee Leasing Companies
1989-1993

STATE	Registration Requirement	Year Reporting Required	1989	1990	1991	1992	1993
AK	N		15	19	25	28	40
AL	N		229	260	280	310	319
AR	Y	1987					
AZ	N						
CA	N						1,368
CO	N						152
CT	Y	1989	22	24	28	32	43
DC	N						
DE	N		0	0	0	0	1
FL	Y	1992	138	153	171	151	147
GA	Y	1992					60
HI	Y	1987	9		8		6
IA	N						
ID	N		90	100	102	117	133
IL	N						
IN	N						
KS	Y	1990	32	29	19	16	5
KY	N						
LA	N						
MA	Y	1993					
MD	N		4	11	13	14	17
ME	Y	1991	8	12	19	23	19
MI	N				50	175	400
MN	Y	1992					
MO	N					25	60
MS	N						100
MT	N						
NC	N						
ND	N		5	5	7	7	7
NE	N		10	20	30	40	50
NH	Y	1994	6	8	9	10	12
NJ	N						10
NM	Y	1994					
NV	Y	1994					40
NY	N						
OH	N						
OK	N		9	27	27	50	50
OR	N						22
PA	N						
RI	Y	1992			3	18	20
SC	Y	1994					
SD							
TN	Y	1996					
TX	Y	1994	100	150	200	250	300
UT	Y				40	41	50
VA							
VT	Y	1989	2	8	10	12	14
WA	N						
WI	N						
WV	N		107	109	129	150	179
WY	Y	1989	0	0	0	0	41
Total	19		786	935	1,170	1,469	3,665
Total of States With Registration Requirements Reporting			317	384	507	553	757

Exhibit 3-8**Unemployment Insurance Service
Department of Labor****Reported Standard Industrial Classifications
of Client Firms**

Construction		
	15	Construction
	1522	General Contractors - Residential Buildings, Other Than Single-Family
	1731	Electrical Work
	1761	Roofing, Siding, and Sheet Metal Work
Manufacturing		
	20	Meat Products
	28	Chemicals and Allied Products
	2452	Prefabricated Wood Buildings and Components
	2752	Commercial Printing, Lithographic
	3444	Sheet Metal Work
	3484	Small Arms
	3944	Games, Toys, and Children's Vehicles, Except Dolls and Bicycles
	3999	Manufacturing Industries, nec.
Transportation		
	42	Trucking
	4212	Local Trucking Without Storage
	4213	Trucking, Except Local
	4215	Courier Services, Except by Air
	4724	Travel Agencies
Wholesale Trade		
	5049	Professional Equipment and Supplies, nec.
	5099	Durable Goods, nec.
	5112	Stationery and Office Supplies
Retail Trade		
	53	General Merchandise Stores
	5541	Gasoline Service Stations
	5734	Computer and Computer Software Stores
	5736	Musical Instrument Stores
	5812	Eating Places
	5813	Drinking Places (Alcoholic Beverages)
	5943	Stationery Stores
Finance, Insurance, and Real Estate		
	63	Insurance Carriers
	6411	Insurance Agents, Brokers, and Service
	6531	Real Estate Agents and Managers

Exhibit 3-8(2)

Services		
7011		Hotels and Motels
7216		Drycleaning Plants, Except Rug Cleaning
7331		Direct Mail Advertising Services
7342		Disinfecting and Pest Control Services
7349		Building Cleaning and Maintenance Services, nec.
7363		Help Supply Services
7371		Computer Programming Services
7379		Computer Related Services, nec.
7389		Business Services, nec.
7513		Truck Rental and Leasing, Without Drivers
7534		Tire Retreading and Repair Shops
7538		General Automotive Repair Shops
7542		Carwashes
8011		Offices and Clinics of Doctors of Medicine
8051		Skilled Nursing Care Facilities
8052		Intermediate Care Facilities
8059		Nursing and Personal Care Facilities, nec.
8062		General Medical and Surgical Hospitals
8072		Dental Laboratories
8111		Legal Services
8721		Accounting, Auditing, and Bookkeeping Services
8731		Commercial Physical and Biological Research
8743		Public Relations Services
8748		Business Consulting Services, nec.
Miscellaneous		
1381		Drilling Oil and Gas Wells
781		Landscape Counseling and Planning
913		Commercial Fishing-Shellfish

3.7 Problems Encountered

Most employee leasing problems encountered by States are identified through industry monitoring. However, because the employee leasing industry is relatively new, State efforts to monitor the industry vary. In some States, monitoring efforts are driven by encountered problems, although other States conduct consistent monitoring of employee leasing companies because they are considered prone to high turnover of firms. Only a small number of States can identify failures of leasing companies. Although survey results indicate that the frequency of failures is low, the associated cost to the trust fund for some cases may be high.

3.7.1 Monitoring the Employee Leasing Industry

Only 26 States indicated that the employee leasing industry is monitored by UI staff, and the level of effort across these 26 States varies widely. For example, one State with extensive registration and reporting requirements dedicates 1« positions within the Tax Department for full-time monitoring, yet another State without registration requirements reported that monitoring is minimal because of the difficulty of identifying leasing companies. Other responses to questions about the level of effort dedicated to monitoring the employee leasing industry include the following:

- A total of 30 hours per quarter to review delinquent accounts and reporting requirements
- Periodic review of leasing companies' master tax files, including review of tax rates, delinquencies (monetary and reporting), covered workers, and benefit charges
- No monitoring for the leasing industry that would not be conducted for any industry prone to rate manipulation and high turnover of firms
- Annual contacting of leasing companies to ensure proper reporting of clients
- Limited monitoring through ES 202
- Periodic monitoring by random checks to ensure compliance with State law

3.7.2 Types of Problems Encountered

States reported a variety of problems encountered with employee leasing companies. The most commonly reported problem was employee leasing companies with delinquent payroll taxes (35 States). In addition, 27 States reported they had problems with firms with unpaid UI trust fund contributions that filed for bankruptcy, and 24 States indicated they had identified instances of payroll tax manipulation. The following problems were also reported:

- Leasing companies reporting employees to other States with lower tax rates

-
- Not knowing an employer with delinquent payments has signed on with a leasing company and wages for the delinquent quarter being reported by the leasing company
 - Knowing whether all employees are reported if leasing companies do not provide client lists or a list of job sites
 - Firms setting up a leasing company to circumvent worker's compensation and UI rates and charges
 - Previously uncovered services being reported under leasing
 - Leasing companies acquiring another entity and transferring clients to obtain a lower tax rate
 - Collecting delinquent payments from leasing companies located out of State
 - Corruption of statistical information on types of employers (employment by appropriate SIC)

3.7.3 Failure Rates

Because of variations in registration and reporting requirements, only 15 States could identify the number of employee leasing companies inactivated with delinquent account balances. Of these 15 States, 54 such occurrences were identified in 1993, with a total associated dollar value of \$787,286. It should be noted, however, that most States reported fewer than five occurrences²; and the dollar values per State range, on average, from \$1,351 to \$222,535.

When asked to compare the occurrences and dollar values of delinquencies in the leasing industry with other industries, most States were unable to respond. Only four States responded that the number of occurrences and dollar amounts were higher than the temporary help industry, and only two States reported that the incidence was higher than those in all other industries. One State reported that the dollar amounts were higher than in other industries but that there were fewer occurrences.

3.8 Effects of the Employee Leasing Industry

Because of the limited data available on employee leasing companies, the effects of the industry remain difficult to determine. Given what is known about the industry, however, the potential effects are significant. For example, the large number of States holding employee leasing companies liable for payroll contributions, coupled with the small number of States securing bonds and lists of client firms, leaves the potential for losses to the State trust fund when employee leasing companies with delinquent contributions go bankrupt. Additionally, without registration and reporting requirements, States may not have a complete understanding of the

²The total results from one State reporting 27 companies inactivated with delinquent account balances.

size of the employee leasing industry and the composition of client firms. This lack of information could result in lower levels of contributions than should be collected.

3.8.1 Tax Rate Effects

Because most States do not have reporting systems in place to track employee leasing companies and their client firms, tax rate effects remain difficult to determine. Although most States indicated there had been no significant tax rate effects caused by the employee leasing industry, three States did respond that employee leasing had raised tax rates statewide because of ineffective charges. One State specified that although the effect could not be determined, it was not insignificant. However, several States indicated that the effect could not be determined.

3.8.2 Trust Fund Effects

As discussed above, liability for payroll contributions and recovery from employee leasing companies that default have potential effects on the UI trust fund. Once again, however, because of the limited data collected on the employee leasing industry, specific effects are difficult to determine. Responses from States that commented on trust fund effects are contained in Exhibit 3-9. Thirteen States indicated that the effects of the employee leasing industry on the State trust fund is unknown because the necessary data are not collected or monitored. Others reported that employee leasing has reduced contributions because employee leasing companies now report as professional services firms, which have lower rates than the averages of their client firms. A few States indicated that contributions have increased because leasing companies now report employment and wages of client firms that were not previously reported by those firms. Additionally, some States reported that taxable wages have decreased because employees who previously worked for more than one client company now report wages from one employer only. Finally, 17 States answered that employee leasing has reduced the number of covered employers because of aggregate reporting by the leasing company.

The most frequent response was that the industry has had no significant effect on the State's trust fund. This high response may also be due to limited data collection or monitoring and, therefore, be based on presumption. Additional explanations for small trust fund effects may be that, in some States, the number of leasing company defaults is small, although the one-time cost is large, and the incidents leave a greater impression of trust fund effects than may actually exist.

3.9 Summary and Conclusions

It is clear that the growth of the employee leasing industry has prompted responses from some State UI agencies. The responses have been through legislation that defines employee leasing and determines the employer, as well as through industry regulation. States have employed a variety of methods for regulating the industry, including reporting, bonding, and registration

Exhibit 3-9
Unemployment Insurance Service
Department of Labor

Trust Fund Effects of Employee Leasing

STATE	Reduced Trust Fund Contributions	Increased Trust Fund Contributions	Reduced Taxable Wages	Reduced Covered Employers	No Significant Trust Fund Effect
AK					X
AL	X		X	X	
AR					X
AZ					
CA					
CO					
CT				X	
DC					X
DE					X
FL				X	X
GA				X	X
HI					X
IA					
ID				X	X
IL					
IN					X
KS		X		X	X
KY				X	
LA					
MA				X	
MD				X	
ME					
MI			X	X	
MN		X		X	
MO			X	X	
MS					
MT	X				
NC			X		
ND					X
NE					X
NH					
NJ					X
NM				X	
NV					X
NY					
OH					X
OK	X				
OR					
PA					
RI					X
SC					X
SD					
TN					
TX			X	X	
UT	X			X	
VA					
VT	X			X	
WA					
WI					X
WV	X		X	X	
WY					X
TOTAL	6	2	6	17	19

requirements. However, the current size and impact of the industry remain difficult to determine, primarily due to the lack of data collection by all States on issues specific to employee leasing. For States that do attempt to collect data on the leasing industry, reporting requirements (such as the inclusion of employee leasing in SIC 7363) make it difficult to separate the effects of the leasing industry from other activities. Although survey results on questions of tax rate and trust fund effects were sketchy, the potential for losses to State trust funds remains substantial as long as leasing firms are not held accountable for contributions through registration and bonding requirements and data are not collected and monitored by all States.

* * * *

Chapter 4

Effects on State UI Trust Funds

Chapter 4

Effects on State UI Trust Funds

This chapter examines the effects the employee leasing industry has on State Unemployment Insurance (UI) trust funds. To measure these effects, we used wage-record data from four States to identify firms engaged in employee leasing and their client firms. Using State UI tax data, we were then able to analyze the differences in tax rates between the identified leasing and client firms. The chapter begins by detailing the States selected for the study. It then describes the methodology used in the analysis, the characteristics of both the identified leasing firms and the identified client firms, and then presents the results of the tax rate analysis.

4.1 States Selected for Study

Selection of the four States for obtaining detailed wage and administrative data was essentially judgmental and opportunistic. Maryland was selected because we already had access to all of its wage-record data and could test our proposed procedures before approaching other States. Maryland also has voluntary registration for leasing firms and provided an opportunity to test the extent to which we could identify these firms.¹ Florida has extensive experience with the employee leasing industry and has passed a licensing law for employee leasing firms. Oklahoma is concerned about employee leasing, particularly the interstate aspects. Texas also expressed concern about the employee leasing industry, and the Texas Department of Licensing and Regulation maintains a licensing list of employee leasing firms. All these States were most cooperative in providing data and dealing with KRA staff.

Massachusetts and New York expressed interest in participating early on in the study. However, limited wage-record histories prevented their inclusion in the analysis. For example, Massachusetts had only 1 year of archived wage-record data at the time the study began.

4.2 Methodology

One of the greatest difficulties in measuring the effect the employee leasing industry has had on State UI trust funds has been in identifying the employee leasing firms. Difficulty in defining the difference between leased employees and other members of the contingent (or temporary) workforce, coupled with a lack of a clear distinction in the help supply services industry (SIC code 7363), makes isolating employee leasing firms difficult. In addition, some State laws provide disincentives in the form of licensing fees, bonds, or additional taxes for employee leasing firms to identify themselves.

In this study we address some of the difficulties of identifying employee leasing firms by developing an algorithm that uses State UI wage records to identify firms engaged in employee leasing. Appendix D addresses the methodology of the analysis. The appendix begins with a brief description of the State UI wage records. Then, it describes in detail the two-step process

¹Unfortunately, we could not obtain additional tax rate and benefit data from Maryland. Therefore, we have not included Maryland in the analysis of tax rates.

used to identify leasing firms and their client firms. Finally, it discusses some of the limitations of using State UI wage records to monitor the employee leasing industry. In the remainder of this chapter, we discuss the results of the analysis of the data on the potential leasing companies identified and the implications for State UI trust funds.

4.3 Characteristics of Identified Leasing and Client Firms

Using State UI wage-record data and the algorithm described above, this study identified firms engaged in leasing arrangements, including the leasing firms and their client firms (i.e., those firms to which the employees were leased). This section describes general characteristics of the firms identified by the study and examines characteristics of the leasing occurrences identified by the criteria.

4.3.1 Characteristics of Identified Leasing Firms

The number of leasing firms identified by the algorithm varied across the States. In Florida, 101 firms were identified as being engaged in leasing. Texas had the second largest number of identified leasing firms with 93. In Oklahoma, only 18 firms were identified by the criteria as being leasing firms. Maryland had 15 firms identified. The differences in the number of leasing firms are due to the size of the States (e.g., in the first quarter of 1994, both Texas and Florida had more than 300,000 employers, while Oklahoma had 65,000); the industry mix prevalent in the States; and the age of the leasing industry in the State.

As expected, most of the identified leasing firms were large. The mean employment levels for the leasing firms for the first quarter of 1994 for all four States were more than 600 employees. Oklahoma was first with 1,996 employees. Maryland had the smallest leasing firm mean employment, 633 employees². Also, more than three-quarters of all leasing firms in all four States had more than 100 employees in the first quarter of 1994; and in Florida and Texas, more than 60 percent of the identified leasing firms had more than 500 employees in the first quarter of 1994.

The number of identified client firms for each identified leasing firm also varied across the States. The mean number of client firms per identified leasing firm in Oklahoma was approximately five, the lowest of the three States for which the number of separable clients could be identified. Identified leasing firms in Texas had 13.5 clients on average, while the identified leasing firms in Florida had slightly more than 23 clients.

The most common SIC code for the identified leasing firms was 7363. Given both the criteria used to identify the leasing firms and the classification procedures of most States, this result is not surprising. Roughly one-fourth of the identified leasing firms in both Texas and Florida had a SIC code of 7363, while 8 of the 18 (44 percent) leasing firms in Oklahoma had a SIC code of 7363. Of Maryland's 15 identified leasing firms, 6 had a SIC code of 7363

²For the study, employment was calculated as the number of wage records for a given employer. Although this employment figure may overstate the exact number of employees on a given day, it provides a consistent method of determining employment across firms.

(40 percent), and another 7 were in the specialized services series (8700). The other SIC codes of the leasing firms varied across the States, although a number of the leasing firms in each State had a two-digit SIC code of 80 (Health Services). Exhibit 4-1 displays the number, size distribution, mean number of client firms, and major SIC codes for the leasing firms identified in each of the four States.

4.3.2 SIC Codes of Identified Client Firms

The algorithm identified more leasing firms in Florida than in Texas, and it identified more total client firms in Florida than in Texas. In Florida, 2,350 client firms were identified; in Texas, 1,999 client firms were identified. In Oklahoma, with its much smaller employer and identified leasing firm base, 93 firms were identified as client firms.

The most common two-digit SIC code of identified client firms in Florida was 17 (Special Trade Contractors); in Texas, it was 73 (Business Services); and in Oklahoma, it was 50 (Wholesale Trade Durable Goods). In all three of these States, the two-digit SIC codes of 80 (Health Services), 73, and 65 (Real Estate) accounted for more than 5 percent of the identified client firms' SIC codes. In addition, the two-digit SIC codes of 17 and 50 were also relatively common among all three States' identified client firms. Exhibit 4-2 displays the most commonly occurring two-digit SIC codes for the identified client firms in all three States. To the extent that the identified leasing firm list includes cases that are, in fact, successorship, this may affect the distribution of SICs of "client" firms. This may help explain the ranking of Real Estate firms in Exhibit 4-2.

The differences in the identified client firms' SIC codes and the identified leasing firms' SIC codes indicate substantial shifts of employment from client SICs to leasing company SIC categories as a result of employee leasing. This can be misleading in terms of reported employment by industry categories. It is this shift that the earlier described BLS study is attempting to rectify in the ES 202 program.

4.3.3 Characteristics of Leasing Occurrences

The number of leasing occurrences increased each year in all four States. This is due primarily to the fact that leasing occurrences are harder to identify as time passes using the criteria established for this study because of employee turnover. The increases may also be the result of increased activity by leasing firms in the States in more recent years, reflecting industry growth.

An example of the pattern of leasing occurrences over time is shown in Exhibit 4-3 for Texas. The first three columns display information about the identified leasing firm: the first column displays its scrambled EIN, the second column lists its SIC code, and the third column shows its number of employees as of the first quarter of 1994. The fourth and fifth columns display information about the identified client firm: its scrambled EIN and its SIC code, respectively. The remaining columns provide information about the leasing occurrences identified for that particular leasing firm/client firm combination for the preceding years (the first quarter of 1993 back to the first quarter of 1990).

Exhibit 4-1

**Unemployment Insurance Service
Department of Labor**

**Characteristics of Identified Leasing Firms
By State**

Florida

Number of Estimated Leasing Firms, 1994	101
Average Employment, 1994:1	1,996
Average Number of Client Firms, 1994:1	23.3
Size of Leasing Firms	

<u>Employees</u>	<u>Firms</u>
6 – 25	2
26 – 100	8
101 – 500	25
501+	66

Major SIC Codes	7363	Help Supply Services	26
	87	Engineering and Mgt.	9
	80	Health Services	8

Maryland

Number of Estimated Leasing Firms, 1994	15
Average Employment, 1994:1	633
Average Number of Client Firms, 1994:1	n/a

Size of Leasing firms

<u>Employees</u>	<u>Firms</u>
6 - 25	0
26 - 100	1
101 - 500	8
501+	6

Major SIC Codes	7363	Help Supply Services	6
	87	Engineering and Mgt.	7

Exhibit 4-1 (2)

Unemployment Insurance Service
Department of Labor

Characteristics of Identified Leasing Firms
By State

Oklahoma

Number of Estimated Leasing Firms, 1994 18
Average Employment, 1994:1 636
Average Number of Client Firms, 1994:1 5.2
Size of Leasing Firms

<u>Employees</u>	<u>Firms</u>
6 - 25	1
26 - 100	3
101 - 500	10
501+	4

Major SIC Codes	7363	Help Supply Services	8
	1389	Oil and Gas Field Services, NEC	2

Texas

Number of Estimated Leasing Firms, 1994 93
Average Employment, 1994:1 1,582
Average Number of Client Firms, 1994:1 13.5

Size of Leasing firms

<u>Employees</u>	<u>Firms</u>
6 - 25	3
26 - 100	15
101 - 500	38
501+	93

Major SIC Codes	80	Help Supply Services	10
	13	Engineering and Mgt.	9

Exhibit 4.2

**Unemployment Insurance Service
Department of Labor**

**Most Frequent Two-Digit SIC Codes of Client
Firms in Florida, Oklahoma, and Texas**

Florida				Oklahoma				Texas			
<i>SIC</i>	<i>Description</i>	<i>Freq.</i>	<i>Pct.</i>	<i>SIC</i>	<i>Description</i>	<i>Freq.</i>	<i>Pct.</i>	<i>SIC</i>	<i>Description</i>	<i>Freq.</i>	<i>Pct.</i>
17	Special Trade Contractors	208	8.85%	50	Wholesale Trade--Durable Goods	8	8.60%	73	Business Services	150	7.50%
80	Health Services	147	6.26%	73	Business Services	6	6.45%	80	Health Services	150	7.50%
73	Business Services	132	5.62%	49	Electric, Gas, and Sanitary Services	5	5.38%	50	Wholesale Trade-- Durable Goods	147	7.35%
58	Eating & Drinking Places	115	4.89%	65	Real Estate	5	5.38%	17	Special Trade Contractors	146	7.30%
65	Real Estate	107	4.55%	80	Health Services	5	5.38%	65	Real Estate	127	6.35%
50	Wholesale Trade—Durable Goods	102	4.34%	42	Trucking & Warehousing	4	4.30%	87	Engineering & Mgmt. Services	81	4.05%
72	Personal Services	69	2.94%	55	Automotive Dealers & Services Stations	4	4.30%	60	Depository Institutions	73	3.65%
87	Engineering & Mgmt. Services	69	2.94%	17	Special Trade Contractors	3	3.23%	42	Trucking & Warehousing	68	3.40%
7	Agricultural Services	65	2.77%	27	Printing & Publishing	3	3.23%	64	Insurance Agents, Brokers & Srvs.	62	3.10%
75	Auto Repair, Services, & Parking	64	2.72%	34	Fabricated Metal Products	3	3.23%	51	Wholesale Trade-- Durable Goods	61	3.05%
55	Automotive Dealers & Service Station	60	2.55%	56	Apparel & Accessory Stores	3	3.23%	13	Oil & Gas Extraction	58	2.90%
59	Miscellaneous Retail	57	2.43%	72	Personal Services	3	3.23%	59	Miscellaneous Retail	54	2.70%
15	General Building Contractors	54	2.30%	95	Environmental Quality & Housing	3	3.23%	15	General Building Contractors	52	2.60%
99	Nonclassifiable Establishments	54	2.30%					88	Private Households	47	2.35%
51	Wholesale Trade-Nondurable Goods	53	2.26%					72	Personal Services	38	1.90%
86	Membership Organizations	46	1.96%					55	Automotive Dealers & Service Stations	37	1.85%
57	Furniture & Homefurnishings Stores	44	1.87%					49	Electric, Gas & Sanitary Services	36	1.80%
88	Private Households	44	1.87%					81	Legal Services	36	1.80%
42	Trucking & Warehousing	33	1.40%					47	Transportation Services	34	1.70%
70	Hotels & Other Lodging Places	33	1.40%					76	Miscellaneous Repair Services	33	1.65%

Exhibit 4.3

**Unemployment Insurance Service
Department of Labor**

**Leasing Occurrences by Year
for Sample Texas Employer**

Leasing Firm Information			Client Firm Information		1993: First Quarter		1992: First Quarter		1991: First Quarters		1990: First Quarters			
<i>EIN</i>	<i>SIC</i>	<i>1994:1 Emp.</i>	<i>EIN</i>	<i>SIC</i>	<i>No. in Changeover</i>	<i>Client Firm Emp.</i>								
224621663	7363	1,050	202728876	5541							1	2		
			203032964	6510							10	53		
			204549212	1799							1	1		
			205425130	3089							9	21		
			205425156	3089							7	17		
			206585383	2339					8	22				
			206632451	5810							11	30		
			207105319	7622			7	8						
			207440048	5810					1	2				
			221995842	5148					2	3				
			222406896	5064			11	25						
229535365	6553			1	2									

In Texas, the average number of employees involved in leasing occurrences increased between 1990 and 1992 and then decreased between 1992 and 1993. In Florida, the average number of employees involved in leasing occurrences increased between 1990 and 1991 but then fell between 1991 and 1993. For both States, increases in the average number of employees involved in leasing occurrences were always accompanied by increases in the average employment level of the identified client firms; likewise, decreases in the average number of employees involved in leasing occurrences were accompanied by decreases in the average employment level of the client firms. As a result, the percentage of an identified client firm's workforce changing employers (to an identified leasing firm) remained somewhat consistent. The only anomaly occurred in Texas in 1992 when, on average, 45 percent of the identified client firms' workforces were involved in leasing occurrences.

In Oklahoma, the average percentage of the identified client firms' workforces that changed over increased each year with the number of leasing occurrences, from 12 percent in 1991 to 17 percent in 1992, to 25 percent in 1993. Somewhat surprisingly, the average number of employees involved in the leasing occurrences declined between 1991 and 1992 but then rose again between 1992 and 1993. Exhibit 4-4 displays the number of leasing occurrences, the average number of employees involved in each leasing occurrence, the average number of employees in the client firms' workforces, and the average percentage of the client firms' workforces involved in the leasing occurrences for the years 1990 through 1993 for these three States.

4.4 Effect on State UI Trust Funds

Some UI administrators contend that the employee leasing industry has had an adverse effect on State UI trust funds. As noted earlier in this report, this can occur in a number of ways: changes in the experience rated tax rate; turnover of the corporate identity of the firm; and, delinquency/default on tax payments. Using the leasing firms and client firms identified by the process described in this report, this study examined the differences between the UI tax rates of the leasing and client firms. By comparing the tax rates of both types of firms, it is possible to determine whether leasing arrangements adversely affect State UI trust funds and to estimate the total effect on the trust fund. This section describes the analysis of the UI firm tax-rate data and the results of that analysis.

4.4.1 Measuring the Effects on State UI Tax Rates

Measuring the effects the leasing industry has on State UI trust funds using UI wage records is not a straightforward task. Ideally, one would want to calculate the taxes paid by and benefits charged to the client firm for the year of the leasing arrangement and the taxes paid by and benefits charged to the leasing firm for the year after the leasing arrangement for only those employees who were leased. This is impractical because of the difficulty involved in accurately identifying the leased employees who collected benefits charged to either the leasing or client firms. This is particularly the case because, by virtue of the algorithm used to identify leased employees, those employees who changed over to an identified leasing firm had to remain employed by that firm until the first quarter of 1994. Instead, a more practical approach is to compare the UI tax rates paid by both the leasing and client firms in the year in which the changeover occurred.

Exhibit 4-4

**Unemployment Insurance Service
Department of Labor**

**Leasing Occurrence Characteristics
by State and Year**

State	Year	Number	Avg. No. Of Employees	Avg. Client Firm Employment	Pct. of Client Workforce
Florida	1990	80	45.8	184	25%
	1991	176	54.9	202	27%
	1992	370	23.1	106	22%
	1993	1743	14.9	50	30%
Oklahoma	1991	7	15.9	133	12%
	1992	12	6.8	39	17%
	1993	75	35.3	141	25%
Texas	1990	240	29.3	100	29%
	1991	260	60.2	204	30%
	1992	477	92.3	207	45%
	1993	1098	30.8	90	34%

Upon first consideration, it would appear that the best comparison of tax rates would be the client firm's tax rate the year in which the leasing arrangement occurred, as compared with the leasing firm's tax rate the year after the leasing arrangement. However, because of changes in State tax schedules from one year to the next, this may not be an accurate measurement in the differences between the leasing firms' and client firms' tax rates. For example, if the State trust fund were to experience an increase in its balance from one year to the next, it is possible that nearly all firms would experience a decrease in their tax rates as a result of a shift in the tax schedules for the following year.

To eliminate the effects of shifts in schedules, it is best to compare tax rates for the same year for both the client and the leasing firms. Because many client firms lease their entire workforce, many client firms cease to have UI covered employees (and thus a UI tax rate) in years subsequent to the leasing. To maximize the number of leasing firm/client firm combinations analyzed, this study compares tax rates for the leasing and client firms for the year of the leasing occurrence. This analysis will not reflect changes in the tax rates of the leasing firms brought about by the States' experience-rating systems, but it will provide a measure of the change in the tax rate (and hence payroll taxes) for the leased employees as a result of leasing. Because most States use multiple years' (generally, 3 to 5) worth of payroll taxes and charged benefits to calculate their experience-rated tax rate, an analysis of the effects of leasing arrangements on leasing firms' experience rating would require the use of data taken over an extended period of time. However, such an analysis would be unsatisfactory because, with the passage of time, it would be difficult to attribute such experience-rating changes only to the leasing arrangements.

4.4.2 Results of the Tax Rate Analysis

The analysis consists of the comparison of the mean tax rates for the leasing firms and client firms in each of the three States. We first calculate the unweighted mean tax rates of the leasing and client firms. Because occurrences involving a greater number of employees changing firms (and thus tax rates) would have a greater effect on the trust funds, a second component of the analysis calculates the mean tax rates for the leasing and client firms, weighted by the number of employees involved in each leasing occurrence. Thus, a leasing occurrence involving 500 employees would have a greater effect on the weighted mean tax rates for the leasing and client firms than one involving 50 employees. Using these weighted mean tax rates, we then estimate the total effect, in dollar amounts, the identified leasing arrangements had on the State trust funds.

Some States, including Florida, regulate the employee leasing industry within their State boundaries. To do so, they maintain lists of licensed employee leasing firms. Florida identified both their licensed leasing firms and their licensed client firms for this study, and additional analyses were conducted comparing the mean tax rates of the licensed firms (both leasing and client), with those firms identified using Florida UI wage records. These results make up the fourth component of this analysis.

³Both the client firm and leasing firm were required to have a tax rate for the year of the leasing occurrence for that particular leasing occurrence to be included in both the weighted and unweighted analyses.

4.4.2.1 Unweighted Mean Tax Rates

In all three States (Florida, Texas, and Oklahoma) the average tax rates over the 4 years for the identified leasing firms were lower than the average tax rates for their client firms. The greatest disparity was in Florida, where the leasing firms' average rate was 0.90 percent lower than that of their clients. Texas had the least difference, with the mean tax rate of the identified leasing firms being only 0.28 percent lower than that of their clients (a 16-percent reduction). Oklahoma had a 0.40-percent difference between the mean rates of the leasing firms and client firms against an average tax rate for the client firms of 1.94 percent (a reduction in the rate of 21 percent). Exhibit 4-5 displays the unweighted mean tax rates for both the leasing firms and their clients for all three States.

4.4.2.2 Weighted Mean Tax Rates

When weighted by the number of employees involved in the leasing occurrence, the mean tax rates for the leasing firms in all three States were lower than the average tax rates for their client firms. The weighted mean tax rates of the leasing firms in both Texas and Florida were approximately 0.40 percent lower than those of their clients (19 and 26 percent reductions, respectively). In Oklahoma the leasing firms' weighted mean tax rate was 0.11 percent lower than their clients' (a 6-percent reduction). Exhibit 4-6 displays the weighted mean tax rates for the leasing and client firms for the three States.

4.4.2.3 Effects on State Trust Funds

The differences in the weighted average tax rates were created based on the actual tax rates of the leasing and client firms in the same year the year in which the changeover of employees from the client firm to the leasing firm occurred. This avoids the issue of the effects of changes in tax schedules from year to year based on overall trust fund effects.

The elements of the analysis are shown in Exhibit 4-7. Because leased employees are generally full-time workers, we assume that each employee who changes over to a leasing company receives at least the maximum taxable wage in the State in that year. Given that the highest, Oklahoma, is \$10,700, this seems plausible. We then calculate the per-employee annual tax using the tax rate of the client firm and the leasing company applicable to each employee that changed over in the year they changed over. The difference in the average annual tax per employee is shown in column 6 of the exhibit. This amount, multiplied by the number of employees involved in the changeovers in each State yields an estimate of the loss to the State trust fund over the period of the analysis as the result of employee leasing. This is shown in column 7 of the exhibit.

To the extent that the employee who changed over did not earn at least the maximum taxable amount of wages in the State in each year, these estimates of loss to the trust fund are overestimates. However, more importantly, the estimates are generated only for the year in which the changeover occurred. By definition, once a worker changed over to the leasing company, that worker remained employed by the leasing company through the first quarter of 1994. Thus, to the extent that the workers remain with the same leasing company and client firms, the estimates presented here may be thought of as 1-year losses to the State trust fund.

Exhibit 4-5

**Unemployment Insurance Service
Department of Labor**

**Unweighted Mean Tax Rates of Identified
Leasing Firms and Their Clients**

State	Leasing Firms' Mean Tax Rate	Client Firms' Mean Tax Rate	Difference	Percent Reduction
Florida	0.97%	1.86%	-0.89%	-47.85%
Oklahoma	1.54%	1.94%	-0.40%	-20.62%
Texas	1.47%	1.75%	-0.28%	-16.00%

Exhibit 4-6

**Unemployment Insurance Service
Department of Labor**

**Mean Tax Rates of Identified Leasing Firms
and Their Clients Weighed by Employees
Involved in Leasing Occurrence**

State	Leasing Firms' Mean Tax Rate	Client Firms' Mean Tax Rate	Difference	Percent Reduction
Florida	1.16%	1.56%	-0.40%	-25.64%
Oklahoma	1.65%	1.76%	-0.11%	-6.25%
Texas	1.78%	2.19%	-0.41%	-18.72%

Exhibit 4-7

**Unemployment Insurance Service
Department of Labor**

Estimates of Trust Fund Loss

State	Maximum Taxable Wage	Total Employees in Changeovers	Annual Client Firm Taxes per Employee	Annual Leasing Firm Taxes per Employee	Annual Tax Difference per Employee	Estimated Annual Trust Fund Loss
Florida	\$7,000	39,851	\$109.20	\$81.20	\$28.00	\$1,115,828
Oklahoma	\$10,700	747	\$188.32	\$176.55	\$11.77	\$8,792
Texas	\$8,500	87,552	\$197.10	\$160.20	\$36.90	\$3,230,669

Because we identified only 747 changeovers in Oklahoma, the fact that the trust fund loss estimate is small (\$8,700) is not surprising. At the other end of the spectrum, the estimates for Texas, with 87,000 changeovers, runs to \$3.2 million. Florida, with 39,800 changeovers has an estimated trust fund loss of more than one million dollars. Put in perspective, using 1992 taxable wages as the base, the largest loss was six tenths of a percent of the taxable wages in Texas. Thus, it would reduce the average tax rate by that amount.⁴ For Florida, it amounts to three tenths of 1-percent. In Oklahoma, the small size of the leasing industry had infinitesimal effect.

4.4.2.4 Effects of Licensing

As noted earlier, Florida provided both their licensed leasing firms and those firms' licensed clients, coupled with the firms (both leasing and client) identified by using Florida's UI wage records, which allows comparison between the following combinations of leasing and client firms:

- Identified unlicensed leasing firms and their identified client firms
- Unidentified licensed leasing firms and their licensed client firms
- Identified licensed leasing firms and their identified client firms
- Identified licensed leasing firms and their licensed client firms

Only unweighted means were calculated for those leasing/client firm combinations involving unidentified licensed clients, because the licensed clients were not identified using the UI wage records and thus had no leasing occurrences and, therefore, no weighting variable.

For all four leasing/client groups examined, the unweighted mean tax rate was lower for the leasing firms. The identified licensed leasing firms had lower unweighted tax rates than both the identified unlicensed leasing firms and the unidentified licensed leasing firms.

For those licensed leasing firms identified by the UI wage-record algorithm, the unlicensed client firms (i.e., those identified by the algorithm but not by Florida) had a higher unweighted mean tax rate than the licensed clients. Furthermore, the difference between the leasing firms' and unlicensed client firms' unweighted mean tax rates was greater than that between the leasing firms' and licensed client firms' unweighted mean tax rates.

Even though the identified unlicensed leasing firms' unweighted mean tax rate is lower than their (identified) client firms' unweighted mean tax rate, the weighted mean tax rates of the client firms are lower than those of the leasing firms. This suggests that, although the identified leasing firms' tax rates are generally lower than their client firms', the larger leasing occurrences that occurred for the identified, yet unlicensed, leasing firms took place with those clients that had lower tax rates. Exhibit 4-8 displays the mean tax rates,

⁴Committee on Ways and Means, U.S. House of Representatives, 1994. *Overview of Entitlement Programs*, July, Table 7-12, p. 297.

Exhibit 4-8

**Unemployment Insurance Service
Department of Labor**

**Mean Tax rates of Licensed
and Unlicensed Florida Leasing
and Client Firms**

	Leasing Firms' Weighted Mean Tax Rate	Client Firms' Weighted Mean Tax Rate	Diff.	Leasing Firms' Unweighted Mean Tax Rate	Client Firms' Unweighted Mean Tax Rate	Diff.	Pct. Reduction
Unidentified Licensed Leasing Firms and Licensed Client Firms	n/a	n/a	n/a	1.48%	1.82%	-0.34%	-19%
Identified Licensed Leasing Firms and Licensed Client Firms	n/a	n/a	n/a	0.99%	1.78%	-0.79%	-44%
Identified Licensed Leasing Firms And Identified Client Firms	0.72%	1.79%	-1.07%	0.84%	1.94%	-1.10%	-57%
Identified Unlicensed Leasing Firms and Identified Client Firms	1.49%	1.38%	0.11%	1.44%	1.61%	-0.17%	-11%

both unweighted and, where appropriate, weighted, for the combinations of licensed and unlicensed leasing and client firms for Florida.

4.4.3 Indications of Possible Tax Rate Manipulation

In addition to the reasons given above why leasing firms could be expected to have lower payroll tax rates than the average of their client firms, there are several ways in which leasing firms can manipulate their payroll tax rate over time to lower their UI contributions. These include the following:

1. Establishing a low rate for an employer account by maintaining an account with minimal (1 or 2 employees) employment and then moving their leasing employment into that account
2. Letting an account whose experience-rated tax rate has increased become inactive and transferring the leasing employment to another account (with a lower payroll tax rate)

Because Florida provided the most complete data of the three States, we attempted to identify instances of these methods of tax rate manipulation. To do this, we first determined how many of the identified leasing firms had tax rates lower than the beginning tax rate (2.7 percent in Florida) at the time of their first changeovers. Then, we identified firms that experienced a substantial increase in their employment level subsequent to becoming experience-rated. Finally, we examined the tax rate patterns of the leasing firms that became inactive in 1994 or 1995 and the universe of firms that became inactive in those same years.

Because Florida maintains only a 5-year archive of its firms' tax rates in electronic format, and we received the firm's data after the assignation of the 1995 tax rates, we were unable to determine the tax rate of all 101 identified leasing firms at the time of their first leasing occurrence. Of the identified leasing firms that did have a tax rate the year of their initial leasing occurrence, only 27 percent had a tax rate of 2.7 percent. This suggests that most firms have previously established tax rates before experiencing any leasing occurrences.

Using the tax rate and employment data, we also identified 33 firms that had a starting tax rate of 2.7 percent with a very low employment level (less than 5 employees) and experienced a decline in their tax rate with a subsequent substantial increase in their employment. Six of these firms were licensed leasing firms (three of which we also identified). All these firms' employment levels increased by more than 400 employees the year of or the year after the decrease in their tax rates.

Examining the tax rate patterns of firms that became inactive in 1994 or 1995 reveals that most of the 10 identified leasing firms that became inactive experienced increases in their tax rates in their previous years. On average, these firms experienced an annual increase of 0.26 percent in their tax rates. On the other hand, the universe of firms that became inactive in 1994 or 1995 experienced no increase in their tax rates in earlier years.

4.5 Tax-Benefit Ratio Analysis

In addition to the analysis of payroll tax rates of leasing and client firms discussed earlier, we examined the chargeable benefits and taxes paid by the leasing firms and client firms. For this we obtained additional data from Florida and Oklahoma. The employee leasing industry's effect on the State UI systems can also be measured by comparing the UI taxes paid and the benefits charged to the leasing firms to the UI taxes paid and the benefits charged to the client firms. Leasing firms argue that, because they have the ability to move employees from one client firm to another, they should have lower benefit charges than their client firms had previously. If this is the case, the ratio of taxes paid to benefits charged should be higher for the leasing firms than the client firms. To examine this issue, we requested total taxes paid and benefits charged for the firms we identified as leasing companies and for their client firms over the period used for the study. If the leasing firms' tax-benefit ratios were lower than the client firms' tax-benefit ratios, then the leasing arrangements would be having a negative impact on the State UI trust funds.

Exhibit 4-9 shows the totals of taxes paid and benefits charged to leasing companies and their client firms in Oklahoma and Florida for the period 1990 to 1994. Initially, these results would seem to contradict the argument that the leasing companies negatively affect the trust funds relative to the experience of their client firms. In both States the ratio of taxes to benefits is higher for the leasing firms than for the client firms. However, there are reasons why this conclusion may not be warranted.

In the previous analysis, we were able to compare the tax rates paid on the wages of the leased employees for the leasing firms and client firms. In this case we had to accept total taxes and benefits for the firms as a whole, not just for the leased employees. This is because the leased employees, of necessity, had to remain employed over the entire period. Therefore, no benefits would be charged for those employees. Consequently, the data cover all employees of the firms over the period.

Many leasing companies also provide temporary employees. Taxes are paid on temporary employees, but they are less likely than regular employees to qualify for unemployment benefits. Therefore, we might expect benefits charged to leasing (and temporary help) companies to be lower relative to taxes than for client firms.

Note that in Exhibit 4-9 the ratios of taxes to benefits for both leasing and client firms in both States are less than one in all but one case substantially. Because nonchargeable benefits are not included, the expectation was that these ratios would be greater than one. The fact that these ratios are less than one is perhaps a result of the recessionary period of the early 1990's. During this time, the trust fund in Florida fell from \$2.4 billion to \$1.6 billion and annual taxes were about two-thirds of annual benefits paid. In Oklahoma, total State taxes and benefits paid were approximately equal in these years. However, the ratio of taxes to benefits for both leasing firms and client firms declined by more than half over the period. Thus, some of the difference could result from the inability of the experience rating system to completely adjust the tax structure to cyclically higher benefit payout. Oklahoma is one of two benefit-wage ratio States.

All of this leads us to conclude from this analysis that the aggregate tax-to-benefit ratio is inadequate to measure leasing company effects on UI trust funds relative to their client firms.

Exhibit 4-9

**Unemployment Insurance Service
Department of Labor**

**Dollar Tax/Benefit Ratios
Leasing Companies and Client Firms
1990 to 1994**

State	Taxes	Benefits	Ratio
Oklahoma			
Leasing Co.	\$2,021,495	\$3,466,756	0.58
Client Firms	\$2,134,200	\$10,415,962	0.2
Florida			
Leasing Co.	\$54,713,627	\$59,445,823	0.92
Client Firms	\$69,722,183	\$121,000,295	0.58

* * * *

Appendix A

Employee Leasing Study

Appendix A

EMPLOYEE LEASING STUDY

Survey of State Unemployment Insurance Tax Administrators

This survey seeks information on the growth of the employee leasing industry in your State, how State Unemployment Insurance (UI) staff have dealt with employee leasing firms, and how the growth of this industry has affected the UI system.

Most questions ask you to check the most appropriate answer, although some questions allow you to check all answers that apply. Other questions ask for data on industry size and employment; estimates are encouraged if detailed data are not available.

We estimate that it will take an average of 1 hour to complete this survey. If you have any comments regarding these estimates or any other aspect of this survey, including suggestions for reducing this burden, send them to the Office of IRM Policy, Department of Labor, Room N-1301, 200 Constitution Avenue, N.W., Washington, D.C. 20210 and to the Office of Management and Budget, Paperwork Reduction Project (1205-0345), Washington, D.C. 20503. (Do not send the completed survey to either of these offices.)

Please mail the survey and all accompanying documents by November 1, 1994, to

Employee Leasing Survey
KRA Corporation
1010 Wayne Avenue, Suite 850
Silver Spring, Maryland 20910

Or fax to

KRA Corporation
ATTN: Robert Cook
(301) 495-2919

Your participation in this survey is entirely voluntary, but we hope you will be able to provide systematic information on your State's experience with the employee leasing industry to assist UIS in evaluating the impact of this industry on State UI Trust Funds. If you have questions about the survey, please call Robert Cook, Senior Economist, KRA Corporation, at (301) 495-1591.

EMPLOYEE LEASING STUDY
Survey of State UI Tax Administrators

Definition of Leasing Firms

1. Do State UI staff use the following to distinguish employee leasing firms from temporary help firms?
- | | <u>Yes</u> | <u>No</u> |
|---|------------|-----------|
| (a) Special licensing of leasing companies | []1 | []2 |
| (b) Legislation requiring registration of leasing companies | []1 | []2 |
| (c) Discussions with employee leasing firm managers | []1 | []2 |
| (d) Whether the word "leasing" appears in the firm's name | []1 | []2 |
| (e) The length of staff placements | []1 | []2 |
| (f) Other (Please describe) | []1 | []2 |

1A. What is the State's definition of an employee leasing firm? (Please cite source.)

1B. What is the State's definition of a temporary help firm? (Please cite source.)

1C. What is the distinction between the two?

2. Who is considered the employer of leased employees in your State?
- (a) Employee leasing firm []1
 - (b) Client firm []2
 - (c) Other (Please describe) _____ []3
- _____
- _____

3. How does the State handle the leasing of:

- | | Partners and
Sole Proprietors? | Corporate
Officers |
|--|-----------------------------------|-----------------------|
| (a) They are considered employees of the employee leasing company | []1. | []1. |
| (b) They are considered employees of the client firm | []2 | []2 |
| (b) They are considered owners and, therefore, not eligible for UI | []3 | []3 |
| (d) Other (Please describe) _____ | []4 | []4 |
- _____
- _____

Applicable State Laws

4. Do any laws specifically govern the operation of employee leasing firms in your State?
- Yes []1
- No []2 (Skip to Question 7)

4A. If yes, when were these laws passed? 19_____

4B. Please list the citations and attach copies of the appropriate section of the laws.

5. Why was this legislation enacted?

6. What effects has this legislation had on the employee leasing industry? (Check all boxes that apply.)

- (a) Reduced industry size []1
- (b) Slowed industry growth []2
- (c) Increased financial liability of firms in the industry []3
- (d) Increased regulation of the industry []4
- (e) Increased financial entry requirements (bonding, reserves, insurance) []5
- (f) Increased reporting requirements []6
- (g) Other (Please describe) _____ []7

Effects on the UI Trust Fund

7. Is the employee leasing industry monitored by UI staff?

Yes []1

No []2

7A. If yes, please describe how and the level of effort involved:

8. Who is held liable when an employee leasing firm defaults on UI payroll taxes?
- (a) The employee leasing company []1
 - (b) The client firm []2
 - (c) Neither; losses are experienced by the State UI trust fund []3
 - (d) Other (Please describe) _____ []4

9. Has your State experienced any of the following problems with employee leasing firms?

- | | <u>Yes</u> | <u>No</u> |
|---|------------|-----------|
| (a) Firm with unpaid UI trust fund contributions filed bankruptcy | []1 | []2 |
| (b) Payroll tax rate manipulation | []1 | []2 |
| (c) Delinquent UI payroll taxes | []1 | []2 |
| (d) Other problems (Please describe) _____ | []1 | []2 |

10. How has the operation of employee leasing firms affected your State's UI trust fund? (Check all boxes that apply.)

- (a) It has reduced contributions because the employee leasing firm now reports as a professional services firm. []1
- (b) It has increased contributions because leasing firms now report employment of client firms that was previously not reported..... []2
- (c) It has reduced taxable wages because employees who previously worked for more than one client company now report wages from one employer only..... []3
- (d) It has reduced the number of covered employers by aggregate reporting..... []4
- (e) It has had no significant effect..... []5
- (f) Other (Please describe) _____ []6

11. How has the operation of employee leasing firms affected UI tax rates in your State? (Check all boxes that apply.)
- (a) It has raised tax rates statewide due to ineffective charges. []1
 - (b) It has raised tax rates for firms in SIC 7363 (Help Supply Services) []2
 - (c) It has had no significant effect. []3
 - (d) Other (Please describe) _____ []4

Industry Size and Employment

12. How many employee leasing firms operated within your State in the following years? (Please provide estimates if actual data are unavailable.)

- 12A. 1993? _____
- 12B. 1992? _____
- 12C. 1991? _____
- 12D. 1990? _____
- 12E. 1989? _____

Please check if the above data are estimates. []

13. How many workers did the employee leasing industry employ in the following years? (Please provide estimates if actual data are unavailable.)

- 13A. In 1993? _____
- 13B. In 1992? _____
- 13C. In 1991? _____
- 13D. In 1990? _____
- 13E. In 1989? _____

Please check if the above data are estimates. []

Reported Industry Classifications

14. Have increases in the employee leasing workforce been accompanied by shifts in the reporting of the workforce from one industry category to another (e.g., from manufacturing to services)?

Yes []1

No []2

Don't Know []3

- 14A. If yes, does your State have any evidence that this phenomenon is a result of aggregated reporting of employment by employee leasing firms?

- 14B. Does your State record the SIC codes of leasing company client firms or their employment in the appropriate SIC code?

Yes []1

No []2 (Skip to Question 18)

Other (Please Describe) _____

15. What are the major industries of client firms? (List SIC codes, if available.)

16. Have there been noticeable changes in the SIC codes of client firms of employee leasing firms during the past 5 years (i.e., a change in the industry mix)?

Yes []1

No []2

- 16A. If yes, please describe.

17. Have there been instances of improper reporting of SIC codes by employee leasing firms?
- (a) Yes, many (more than 10% of leasing firms misclassify) 1
 - (b) Yes, although infrequently (5-10% of leasing firms misclassify) []2
 - (c) No []3

17A. If yes, how has your State identified the misclassifications?

Registration Requirements

18. Are employee leasing firms required to fulfill additional business registration requirements in your State?

Yes []1

No []2 (Skip to Question 19)

18A. What year did mandatory registration begin? 19_____

18B. Why was registration made mandatory? (Check all boxes that apply.)

(a) To track the growth of the employee leasing industry []1

(b) To ensure that all UI taxes are paid properly []2

(c) To distinguish leasing firms from temporary help firms []3

(d) To ensure that proper SIC codes of client firms are reported []4

(e) Other (Please describe)_____ []5

18C. Has registration been successful in accomplishing each of the following goals? (Answer for all categories; not just for those reasons circled in 18B.)

- (a) To track the growth of the employee leasing industry []1 []2 []3
- (b) To ensure that all UI taxes are paid properly []1 []2 []3
- (c) To distinguish leasing firms from temporary help firms []1 []2 []3
- (d) To ensure that proper SIC codes of client firms are reported []1 []2 []3
- (e) Other (Please describe) _____ []1 []2 []3

Bonding Requirements

19. Does your State require each employee leasing firm to post a bond in order to operate within the State?

Yes []1

No []2 (Skip to Question 20)

19A. When was the bonding of employee leasing firms made mandatory? 19_____

19B. How is the size of the bond determined?

- (a) By the number of employees of the firm []1
- (b) As a percent of payroll []2
- (c) The bond is set at a flat dollar amount []3
- (d) Other (Please describe) _____ []4

- 19C. What liabilities does the bond cover? (Check all boxes that apply.)
- (a) UI payroll taxes []1
 - (b) Workers' Compensation premiums []2
 - (c) Health insurance premiums []3
 - (d) Pension contributions []4
 - (e) Other (Please describe) _____ []5
- _____
- _____

Client Firm Reporting Requirements

20. Does your State require employee leasing firms to submit a list of client firms?
- Yes []1
- No []2 (Skip to Question 21)
- 20A. When were employee leasing firms first required to submit client lists? 19_____
- 20B. Why was the reporting of client lists made mandatory? (Check all boxes that apply.)
- (a) Because the client firm is liable for unpaid UI payroll taxes []1
 - (b) To ensure that the proper SIC codes of client firms are reported []2
 - (c) To identify client firms for compliance audit purposes []3
 - (d) (Please describe) _____ []4
- _____
- _____

20C. What types of client information are employee leasing firms required to submit? (Check all boxes that apply.)

- (a) Leased employment at their client firms []1
- (b) SIC codes of their client firms []2
- (c) Multiple Worksite Reports (MWRs) []3
- (d) Employer IDs of their client firms []4
- (e) Other (Please describe) _____ []5

Failure Rates of Leasing Firms

21. Can you identify the number of employee leasing firms inactivated with delinquent account balances?

- Yes []1
- No []2
- Don't Know []3

21A. If yes, in the last calendar year,

How many such occurrences were there? _____

What was the dollar amount of the associated delinquencies? _____

21B. How do the number of occurrences and the dollar amount of the associated delinquencies compare with those of the following:

		Higher	Lower	No Difference	Don't Kow
(a)	All other industries in the State?	[]1	[]2	[]3	[]4
(b)	Small firms (fewer than 25 employees) in the State?	[]1	[]2	[]3	[]4
(c)	Temporary help firms in the State?	[]1	[]2	[]3	[]4

Experience-Rating Procedures

22. How is the experience-rated tax rate for an employee leasing firm determined?
- (a) Different tax rates for each client firm based on the previous experience of each client firm []1
 - (b) Identical tax rates for all client firms based on the overall experience of the leasing company []2
 - (c) Other (Please describe) _____ []3

23. Does this method differ from the experience-rating procedures used for temporary help firms?
- Yes []1
- No []2
- 23A. If yes, please explain how the methods differ.
- _____

Associated Changes in Successor Rules

24. What special considerations concerning business successorship does your State make for employee leasing firms?
- (a) They may not transfer the experience record of client firms. []1
 - (b) They must maintain the experience record and tax rates of client firms. []2
 - (c) They are treated like any other firm. []3
 - (d) Other (Please describe) _____ []4

25. Were business successorship laws altered as a result of the growth of the employee leasing industry?

Yes []1

No []2

25A. If yes, please explain how the laws were altered.

Additional Comments

Name of Person Completing Questionnaire_____

Telephone Number _____

[] Please check if you would like a copy of the report on the survey results.

Thank you for taking the time to respond to this survey.

Appendix B

**State Employee Leasing Statutes
and Regulations**

Appendix B

STATE EMPLOYEE LEASING STATUTES AND REGULATIONS

- AL None; Master-Servant provisions determine employment.
- AK None
- AZ Arizona Revised Statutes, Employment Security, Section 23-614(a)-(g) definition and determination of employing unit status for temporary services employers and leasing employers; establishes employee leasing firms and temporary services firms (not clients) as employers.
- AR Arkansas Code Annotated 23-92-301 through 23-92-315, "Arkansas Employee Leasing Act;" Emergency Rule & Regulation 58 (licensing of Employing Leasing Firms); Employment Security Law Section 11-10-717(e) & Regulation 20 refers to who is liable for contributions and the posting of surety bonds by the employee leasing firm to relieve clients lessees from joint and several liability; Unemployment Insurance statutes begin at 23-601.
- CA Assembly Bill No. 2733, Chapter 793 amended California Unemployment Insurance Code added section 606.5 determining factors in classifying temporary services employers and leasing employers as the employing units.
- CO Colorado Employment Security Law 8-70-114 defines employee leasing company.
- CT Definition of Employee Leasing Company from Agency Policy based on Massachusetts Regulations Section 5656-5659C; Connecticut Agency Policy deals with registration and establishes the employee leasing firm as the agent of the client firm.
- DC None.
- DE None.
- FL Florida Statutes Annotated, Chapter 468, Business & Professional Regulations, Part XI-468.520 through 535, "Employee Leasing Companies" legislation has definition and deals with employer licensing; Florida Statutes (Unemployment Compensation) Section 443.036(16) defines employee leasing company and the client; Florida Statutes Annotated, Section 440.01 "Workers Compensation."
- GA Georgia Employment Security Law 1991, Section 34-8-32 definition of an employee leasing company; Section 34-8-172 requires surety bond to be posted by employee leasing firms; Rules of Georgia DOL Employment Security Law, Section 300-2-7-.07 detailed explanation of surety bond requirements.

- HI No specific mention of employee leasing; Hawaii Revised Statutes 383-1 through 10 defines employing unit, defines employment, master-servant relationship; Administration Rules 12-5-17a filing of a report by employing units to determine liability for contributions.
- IA None
- ID Idaho Code Chapter 24, 44-2401 through 2407 "Idaho Professional Employer Recognition Act" and Chapter 13, 72-1349D define employee leasing firms as "professional employers" and details the financing of benefit payments by professional employers and their clients respectively; Unemployment Insurance statutes at 72-1301.
- IL Illinois Administrative Code Chapter 4, Section 2732.305.c (rules) definition and criteria, employer criteria; proposed amendment.
- IN None currently; trying to pass legislation.
- KS Kansas Statutes Annotated, Employment Security Law, Section 44-703(ff) & (gg) defines "lessor employing unit" & "client lessee"; Section 44.758 client lessee jointly and severally liable for contributions.
- KY None
- LA None
- MA Code of Massachusetts Regulations 430-5.07 through 5.13 establishes procedures regarding reporting requirements for employee leasing companies and their clients, discusses benefit charges and experience rates; Massachusetts General Laws Annotated (MGLA), Title XXI, Chapter 152 (Workers Compensation) Section 14A definitions; Unemployment Insurance at Chapter 151A.
- MD None
- ME 26 Maine Revised Statutes Annotated (MRSA), "Unemployment Compensation Act," Section 1043.6A,8A definitions; 26 MRSA 1221.A1 through 8 liability & posting of surety bonds; 32 MRSA 14051 through 14058 additional definitions, employee leasing company criteria, registration, workers' compensation, and unemployment insurance contributions.
- MI None
- MN Minnesota Statute 268.163 Subd 2 definition, liability, bonding; Minnesota Statute 79-255, Sub 1 employee leasing registration for workers' compensation insurance; additional legislation proposed.

- MO Missouri Employment Security Law 288.032.2 definition & criteria, joint and several liability, bonding; Missouri Employment Security Regulation 8 CSR 10-4.160 details on posting of surety bonds; Vernon's Annotated Missouri Statutes 287.282 (Workers' Compensation Law) definition, liability, registration.
- MS None
- MT None; proposed legislation.
- NC Employment Security Law Sec. 96.8(5)r definition and criteria.
- ND None
- NE Nebraska Revised Statutes of 1943 Section 48.602 definition; Section 48.648 contributions; payment; rules and regulations.
- NH New Hampshire Revised Statutes Annotated 277-B.1-18 definitions, criteria, licensing, unemployment contribution liability and bonding; Proposed Interim Rules Emp 306.01-05 definitions, reporting and payment requirements
- NJ None
- NM New Mexico Statutes Annotated (NMSA) 51.1-52.1 definition & criteria; NMSA 59A-2-9.1 defining, classifying temporary and leased employees, and employer experience ratings; NMSA 60-13A-1, "Employee Leasing Act" definitions, registration, licensing, compliance with workers' compensation laws, bonding, employment contributions; Unemployment Insurance statutes at Section 51-1-1.
- NV Nevada Revised Statutes 616.254 through 616.255 definitions, registration, joint and several liability if employee leasing firm fails to make proper insurance contributions; LCB file No. R084-94 regulations detailing the preceding statute; 616 Nevada Administrative Code; Unemployment Insurance statutes at Section 612.010-612.720.
- NY None
- OH Ohio Administrative Code (rule) Section 4141-3-07 definition.
- OK Oklahoma Statutes Annotated Title 40, Chapter 1, Article 1, Part 2, Sec. 1-209A definition, joint and several liability, bonding.
- OR Oregon Revised Statutes 656.850 through 990 (Workers Compensation) definition, licensing, workers' compensation requirements; Workers Compensation Division Administrative Order 94-052, Oregon Administrative Rules, Workers' Compensation Division, 436-50-001 through 436-50-470 definitions, responsibility for compensation coverage, licensing, recordkeeping, reporting requirements
- PA None

- RI General Laws of Rhode Island Annotated 44-30-71.4 (Division of Taxation laws) definition, certification, joint and several liability; (Unemployment Insurance statutes at 42-19-1 through 42-10-9).
- SC Code of Laws of South Carolina 40-68-10 through 40-68-180 "Staff Leasing Services Act" (Workers Compensation) definitions, licensing, contract requirements, client responsibility for contributions; No statutory provision or regulation for employee leasing as pertains to unemployment insurance; common law rules apply.
- SD None
- TN Tennessee Code Annotated 62-31-102 (current legislation) definitions; "Tennessee Employee Leasing Act" amending Tennessee Code Annotated, Title 62, Chapter 31 (adding sections 2-20) effective January 1, 1996 definitions, licensing, client and staff leasing contract, staff leasing responsibilities as employer (wages, taxes, unemployment and workers' compensation); Unemployment Insurance statutes at 50-7-101.
- TX "Staff Leasing Services Act," Section 13, Texas Civil Statutes Article 9104 definitions, licensing, contract and contract requirements, workers' compensation, unemployment taxes, health insurance; Staff Leasing Services Rules and Regulations Chapter 72.1 through 91 provides further details to Staff Leasing Services Act; Unemployment Insurance statutes at Title 83 Chapter 14.
- UT Utah Code Annotated 58-59-101, "Employee Leasing Company Licensing Act" definitions, licensing; General Rules of the Division of Occupational and Professional Licensing R156-1-101 through 404d additional details regarding Employee Leasing Company Act; Unemployment Insurance statutes at 35-4-1.
- VA None
- VT Vermont Code 21 V.S.A. defines "employee leasing company" as a person engaged in the business of providing individuals to perform ongoing services for an indefinite time period for client companies; Additional rules and regulations regarding employee leasing company provided in Vermont statute.
- WA Employment Security Department Tax Policy Manual has definition (not a "legal" definition); proposed legislation; Unemployment Insurance statutes at 50.01.005.
- WI Wisconsin State Statutes 108.02-12m defines "employee service company" as a leasing company or temporary help service and lists criteria; Additional rules regarding employee service company provided in compensation manual.
- WV None
- WY Criteria for service supplier at 27.3.502(g) of state statutes- also joint and several liability; definition of service supplier.

Appendix C

**Employee Leasing and Temporary Help
Definitions by State**

Appendix C

Employee Leasing and Temporary Help Definitions by State

State	Employee Leasing Definition	Temporary Help Definition
Alabama	None.	None.
Alaska	None.	None.
Arizona	<p>For purposes of this section, "leasing employer" or "temporary services employer" means an employing unit that contracts with clients or customers to supply workers to perform services for the client or customer and that performs all of the following:</p> <p>(1) Negotiates with clients or customers for such matters as the time of work, the place of work, the type of work, the working conditions, the quality of services and the price of services.</p> <p>(2) Determines assignments or reassignments of workers, even though workers retain the right to refuse specific assignments.</p> <p>(3) Retains the authority to assign or reassign a worker to other clients or customers if a worker is determined unacceptable by a specific client or customer.</p> <p>(4) Assigns or reassigns the worker to perform services for a client or customer.</p> <p>(5) Sets the rate of pay of the worker, whether or not through negotiation.</p> <p>(6) Pays the worker from his own account or accounts.</p> <p>(7) Retains the right to hire and terminate workers. (Arizona Revised Statutes Chapter 4, Section 23-614(G).</p>	
Arkansas	<p>"Employee leasing firm" shall mean any person engaged in providing service of employees pursuant to one or more employee leasing arrangements. (Arkansas Regulation 58 Section 4D)</p> <p>"Employee Leasing Arrangement" shall mean an arrangement or agreement, under written contract or otherwise, whereby:</p> <p>1. an employee leasing firm assigns or purports to assign human beings, or the labor or services of human beings, to clients, for whom the human beings either do perform or are expected to perform such labor or services;</p> <p>2. the arrangement is entered to be, or is, on-going rather than temporary in nature; and</p> <p>3. common law employment rights and responsibilities relative to the "assigned" human beings, including the employer's right of direction and control of the "employee" as to the method and manner of doing the work, are shared by the employee leasing firm and the client. (Arkansas Regulation. 58, Section 4G)</p>	<p>"Temporary Employee" shall mean a person employed either through another person or directly by an employer to support or supplement the existing work force in special situations such as employee absences, and temporary skill shortages, seasonal workloads, and special assignments and projects with the expectation that the person's position will be terminated upon completion of the task or function. Contracting for services to be performed by temporary employee shall not be considered the making of employee leasing arrangements. (Arkansas Regulation 58 Section 4H)</p>

California	<p>A "temporary services employer" and a "leasing employer" is an employing unit that contracts with clients or customers to supply workers to perform services for the client or customer and performs all of the following functions:</p> <ol style="list-style-type: none"> (1) Negotiates with clients or customers for such matters as time, place, type of work, working conditions, quality, and price of services. (2) Determines assignments or reassignments of workers, even though workers retain the right to refuse specific assignments. (3) Retains the authority to assign or reassign a worker to other clients or customers when a worker is determined unacceptable by a specific client or customer. (4) Assigns or reassigns the worker to perform services for a client or customer. (5) Sets the rate of pay of the worker, whether or not through negotiation. (6) Pays the worker from its own account or accounts. (7) Retains the right to hire and terminate workers. (California Unemployment Insurance Code Section 606.5(b)) 	
Colorado	<p>For the purposes of this section, an "employee leasing company" shall be defined as any employing unit which, for a fee, places a client company's workers onto its payroll and assigns them to the client company for at least six consecutive months. (Colorado Revised Statutes 8-70-114(2)(c))</p>	<p>For the purposes of this section, "temporary help contracting firm" means any person who is in the business of employing individuals and, for compensation from a third party, providing those individuals to perform work for the third party, under supervision of the third party. (Colorado Revised Statutes 8-73-105.5(1))</p>
Connecticut	<p>An employing unit that contracts with a client company to supply workers to perform services for the client company, excluding part-time or temporary workers. (Agency policy based on Massachusetts Regulations Section 5656-5659c.)</p>	<p>Any person conducting a business which consists of employing individuals directly for the purpose of furnishing part-time or temporary help to others. (Connecticut Statutes Section 31-129(e))</p>
Delaware	<p>A firm that supplies another organization with its entire staff and manages all personnel affairs for that other firm. (NSLA Literature)</p>	<p>A firm that supplements the staffing needs of another organization. (Working Definition)</p>
District of Columbia	<p>A firm that provides temporary and permanent employees for a fee to employers. (Working Definition)</p>	<p>A firm that provides temporary help, for a fee, to employers who have a vacancy that must be filled at once. (Working Definition)</p>
Florida	<p>The term "employee leasing company" means an employing unit which maintains a valid and active license under chapter 468 and which maintains the records required by s. 443.171(7) and, in addition, maintains a listing of clients of the employee leasing company and of the employees, including social security numbers, who have been assigned to work at each client company job site. Further, each client company job site must be identified by industry, products or services, and address. The client list shall be provided to the division by June 30 and by December 21 of each year. For purposes of this subsection, "client" means a party who has contracted with an employee leasing company to provide a worker, or workers, to perform services for the client. Leased employees shall include employees subsequently placed on the payroll of the employee leasing company shall notify the division within 30 days of the initiation of termination of the company's relationship with any client company pursuant to chapter 468. (Section 443.036(16) Florida Statutes - Unemployment Compensation)</p> <p>"Employee leasing" means an arrangement whereby a leasing company assigns its employees to a client and allocates the direction and control over the leased employees between the leasing company and the client. (Section 468.520(4) Florida Statutes - Employee Leasing Companies)</p>	<p>A temporary help arrangement, whereby an organization hires its own employees and assigns them to clients to support or supplement the client's workforce in work situations such as employee absences, temporary skill shortages, seasonal work load and special assignments and projects. (Section 468.520(4)(a) Florida Statutes - Employee Leasing Companies)</p>

Georgia	<p>As used in this chapter, the term "employee leasing company" means an independently established business or entity which engages in the business of providing leased employees to any other employing unit under the following conditions:</p> <p>(1) Negotiates with clients or customers for such matters as time, place, type of work, working conditions, quality and price of service;</p> <p>(2) Determines assignments of individuals to its clients or customers, even if the individuals retain the right to refuse specific assignments;</p> <p>(3) Sets the rate of pay of the individuals, whether or not through negotiation;</p> <p>(4) Pays the individuals from its accounts; and</p> <p>(5) Hires and terminates individuals who perform services for the clients or customers. (Georgia Employment Security Law 34-8-32(a))</p>	<p>As used in this chapter, the term "temporary help contracting firm" means any person who is in the business of employing individuals and, for compensation from a third party, providing those individuals to perform work for the third party under the general or direct supervision of the third party. Employment with a temporary help contracting firm is characterized by a series of limited-term assignments of an employee to a thirdparty, based on a contract between the temporary help contracting firm and the third party. A separate employment contract exists between the temporary help contracting firm and each individual it hires as an employee. Completion of an assignment for a third party by an employee employed by a temporary help contracting firm does not, in itself, terminate the employment contact between the temporary help contracting firm and the employee. (Georgia Employment Security Law 34-8-46)</p>
Hawaii	<p>A contractual arrangement under which the leasing firm is the employer of all or part of the client's workforce. (Hawaii Revised Statutes 383-6)</p>	<p>A contractual arrangement under which the temporary help firm is the employer who provides workers to a client company on a temporary basis. (Hawaii Revised Statutes 383-6)</p>
Idaho	<p>"Professional employer arrangement" means an arrangement, under contract or otherwise, whereby:</p> <p>(a) A professional employer assigns workers to perform services for a client;</p> <p>(b) The arrangement is intended to be, or is, on-going rather than temporary in nature; and</p> <p>(c) Employer responsibilities are in fact shared by the professional employer and the client for assigned workers. (Chapter 24, Title 44, Idaho Code 44-2403(5))</p>	<p>"Temporary employee" means a worker employed by an organization which hires its own employees and assigns them to a third party to support or supplement the third party's work force in work situations such as employee absences, temporary skill shortages, seasonal workload conditions, and special assignments and projects. (Chapter 24, Title 44 Idaho Code 44-2403(7))</p>
Illinois	<p>"Employee leasing company" means an individual or entity which contracts with a client to supply one or more workers to perform services for the client on an on-going rather than temporary basis. (56 Illinois Administrative Code 2765.5)</p>	<p>"Temporary help firm" means an employing unit that hires its own employees and assigns them to clients to support or supplement the client's workforce in work situations such as employee absences, temporary skill shortages, seasonal workloads, and special assignments and projects. (56 Illinois Administrative Code 2865.1)</p>
Indiana	None.	None.
Iowa	None.	None.
Kansas	<p>"Lessor employing unit" means any independently established business entity which engages in the business of providing leased employees to a client lessee. (Kansas Statutes Annotated 44-703(ff))</p>	<p>Private employment agencies which provide temporary workers to clients on a temporary help basis provided the private employment agencies are liable, as employer, for the payment of contributions on wages paid to the temporary workers. (Agency Policy Manual)</p>
Kentucky	<p>"A practice whereby the payroll of our business is assumed by a second business." (Kentucky Field Audit Manual Operational Definition)</p>	<p>"Temporary employment agencies provide workers to client businesses to meet needs which are of limited duration." (Kentucky Field Audit Manual operational Definition)</p>
Louisiana	None.	None.

Maine	<p>"Employee leasing company" means a business entity that engages in the business of leasing employees to client companies without the client company severing an employer-employee relationship with the employees for services performed for the client company. (Statute: 1043, 8-A Employee leasing company)</p> <p>"Employee leasing company means a sole proprietorship, partnership, corporation or other form of business entity, a substantial portion of the business of which consists of leasing employees to one or more client companies under contractual arrangements that are characterized by the following.</p> <p>A. Employment responsibilities are carried out by the employee leasing company or are shared by the employee leasing company and client company.</p> <p>B. Direction and control of employees provided by the employee leasing company are handled by the employee leasing company and the client company. "Direction and control" includes the right of the employee leasing company to hire and fire employees.</p> <p>C. The leasing arrangement is long term and does not including arrangements to provide temporary help services.</p> <p>D. The leasing arrangement does not include providing labor dispute workers. "Labor dispute worker" means a worker who is furnished to an entity to replace workers involved in strikes, lockouts or other labor activities. (Maine Revised Statutes Annotated Section 14051-3)</p>	<p>"Temporary help services" means a service whereby an organization hires its own employees and assigns them to a third party to support or supplement the third party's work force in work situations such as employee absences, temporary skill shortages, seasonal work load conditions and special assignments and projects. (Maine Revised Statues Annotated Section 14051- 3c)</p>
Maryland	None.	None.
Massachusetts	<p>Employee Leasing Company: an employing unit that contracts with a client company to supply workers to perform services for the client company; provided that, the term employee leasing company does not include private employment agencies that provide workers to employers on a temporary help basis or entities such as driver-leasing companies which lease employees to an employing unit to perform a specific service. (430 Code of Massachusetts Regulations 5.09)</p> <p>"Employee leasing company," a sole proprietorship, partnership, corporation or other form of business entity whose client companies under contractual arrangements that retain for personnel management functions, such as payroll, direction and control of workers, and the right to hire and fire workers provided by the employee leasing company; provided, however, that the leasing arrangement is long term and not an arrangement to provide the client company temporary help services during seasonal or unusual condition. (Massachusetts General Laws Annotated Chapter 152 Section 14A)</p>	None.
Michigan	None.	None.

Minnesota	"Employee leasing firm" means an employing unit that provides its employees to other firms, persons, and employing units without severing its employer-employee relationship with the worker for the services performed for the leasee. (Minnesota Statutes 268.163 Subsection 2)	None.
Mississippi	None.	None.
Missouri	"Lessor employing unit" means an independently established business entity which engages in the business of providing leased employees to any other employer, individual, organization, partnership, corporation, or other legal entity, referred to in this section as a client lessee. (Missouri Employment Security Law Section 288.032.2(4))	For the purposes of this section, the term "employee leasing arrangement" shall not include temporary help services arrangements which assign their employees to clients for a finite period of time to support or supplement the client work force in special work situations, such as employee absences, temporary skill shortages and seasonal workloads, and which are not knowingly utilized as a mechanism of depriving one or more insurers of premiums which otherwise is properly payable. (Missouri Statutes 287.282(3))
Montana	A company which provides employees to a client company on a long-term basis, under a contract. Leasing firm performs employer functions of hiring, firing and supervision. (Working Definition)	None.
Nebraska	An independently established business entity which engages in the business of supplying leased employees to a client-leasee. (Nebraska Revised Statutes 48-602(8))	None.
Nevada	"Employee Leasing Company" means a company which, pursuant to a written agreement, places all or substantially all of the regular, full-time employees of a client company on its payroll and, for a fee, leases them to the client company on a regular basis without any limitation on the duration of their employment (Nevada Revised Statutes 616.254(3))	"Agreement for temporary employment" means an agreement pursuant to which a business hires employees and assigns them to another employer for a definite period, usually not exceeding 12 months, to support or supplement the employer's work force in special circumstances, such as when employees are absent from work, when there is a temporary shortage of skilled labor or during seasonal times when the workload increases. (Adopted Regulation of the Manager of the State Industrial Insurance System LCB File No. R084-94, Section 3)
New Hampshire	"Employee leasing company" means any person engaged in providing the services of employees pursuant to one or more employee leasing arrangements and who satisfies the standards of RSA 277-B:9 (Rules Emp 306.01(c))	"Temporary help service" means a service whereby an organization hires its own employees and assigns them to clients to support or supplement the client work force in special work situations such as employee absences, temporary skill shortages, seasonal workloads, and special assignments and projects. (New Hampshire Revised Statutes Annotated Chapter 277-B:2)

New Hampshire (Continued)	<p>"Employee leasing arrangement" means an arrangement, under written contract or otherwise, whereby: (a) An employee leasing company assigns an individual to perform services for the client company;</p> <p>(b) The arrangement is intended to be, or is, on-going rather than temporary in nature; and</p> <p>(c) Employer responsibilities are carried out by an employee leasing company which meets the standards of RSA 277-B:9, or are shared by the employee leasing company and the client company. (New Hampshire Revised Statutes Annotated Chapter 277-B: 2-IV)</p>	
New Jersey	<p>None.</p> <p>Proprietorship, partnership, corporation or any other entity that contracts with clients to supply workers to perform services for the client and that performs all of the following functions:</p> <ol style="list-style-type: none"> 1. Negotiates with clients for such matters as time, place, type of work, working conditions, quality and price of the services; 2. Determines assignments or reassignments of workers, even though workers retain the right to refuse specific assignments; 3. Retains authority to assign or reassign a worker to other clients when a worker is determined unacceptable by a specific client; 4. Assigns or reassigns the worker to perform services for a client; 5. Sets the rate of pay of the worker, whether or not through negotiation; 6. Pays the worker from its own account or accounts; 7. Retains the right to hire and terminate workers; and 8. Provides copies of all state and Federal forms, as well as copies of all payroll records to the client.(Proposed regulation, currently no definition.) 	None.
New Mexico	<p>"Employee leasing arrangement" means any arrangement in which a client contracts with an employee leasing contractor for the contractor to provide leased workers to the client' provided, "employee leasing arrangements" does not include temporary workers; (New Mexico Statutes 60-13A-2D)</p> <p>"leasing employer" means an employing unit that contracts with clients or customers to supply workers to perform services for the client or customer and performs the following functions:</p> <ol style="list-style-type: none"> (a) retains the right to hire and terminate workers; and (b) pays the worker from its own account (New Mexico Unemployment Compensation Statutes 51-1-51.1) 	<p>"temporary services employer" means an employing unit that contracts with clients or customers to supply workers to perform services for the client or customer and performs all of the following functions:</p> <ol style="list-style-type: none"> (a) negotiates with clients or customers for such matters as time, place, type of work, working conditions, quality and price of the services; (b) determines assignments of workers, even through workers retain the right to refuse specific assignments; (c) retains the authority to reassign or refuse to reassign a worker to other clients or customers when a worker is determined unacceptable by a specific client or customer; (d) assigns the worker to perform services for a client or customer; (e) sets the rate of pay for the worker, whether or not through negotiation; and (f) pays the worker directly. (New Mexico Unemployment Compensation Statutes 51-1-52.1)
New York	None.	None.

North Carolina	For purposes of this chapter, "employee service company" means a leasing company or temporary help service which contracts with clients or customers to supply individuals to perform services for the client or customer and which, both under contract and in fact: 1. Negotiates with clients or customers for such matters as time, place, type of work, working conditions, quality and price of the services; 2. Determines assignments or reassignments of individuals to its clients or customers, even if the individuals retain the right to refuse specific assignments; 3. Sets the rate of pay of the individuals, whether or not through negotiation; 4. Pays the individuals from its account or accounts; and 5. Hires and terminates individuals who perform services for the clients or customers. (North Carolina Employment Security Law Section 96-8(r))	
North Dakota	None.	None.
Ohio	"Employee leasing company" means an entity which provides individuals to third party clients to perform services on a permanent basis and receives a fee for providing such individuals. (Ohio Administrative Code 4141-3-07)	"Temporary services agency" means any employer which employs staff to perform services on a temporary basis for a third party and receives a fee for providing such services. (Ohio Administrative Code 4141-3-06)
Oklahoma	"Lessor employing unit" means any independently established business entity which engages in the business of providing leased employees to any other employer, individual, organization, partnership, corporation or other legal entity, referred to herein as client lessee. (Oklahoma Statutes Annotated Title 40, Chapter 1, Article 1, Part 2, Section 1-209A)	None.
Oregon	"Worker-Leasing Company" means a person who provides workers, by contract and for a fee, as established in ORS 656.850. (Oregon Revised Statutes 436-50-005(25)) (1) "Worker leasing company" means person who provides workers, by contract and for a fee, to work for a client but does not include a person who provides workers to a client on a temporary basis to supplement the existing work force in special situations such as employee absences, professional skill shortages, seasonal workloads and special assignments and projects with the expectation that the position or positions will be terminated upon completion of the special situation. (Oregon Revised Statutes 656.850) (2) If a person provides workers, by contract and for a fee, to work for a client and any such workers are not provided on a "temporary basis," that person will be considered a worker-leasing company. (3) If a person provides both leased workers and workers on a temporary basis, that person shall maintain payroll records that show specifically which workers are provided on a temporary basis. If the payroll records do not specify which workers are provided on a temporary basis, all workers are deemed to be leased workers. (Oregon Revised Statutes 436-50-420)	(1) A person who provides a worker to work for a client will be considered to be providing the worker on a "temporary basis" only if there is a written contract which states the period to time the worker will be provided and the worker is provided under one or more of the following conditions: (a) to replace an absent worker who will return, such as during a maternity leave vacation, jury duty or illness; (b) to fill a professional skill shortage; (c) to staff a seasonal workload; (d) to staff a special assignment or project where the worker will be terminated or assigned to another temporary project upon completion; (e) where student trainees are provided through a work experience program which is operated by a school district or community college, and in which the trainee is paid by the school district or community college; or (f) the work contract is part of the client's overall employment selection program, such as where new workers must satisfactorily pass a probationary period before being granted permanent employee status. (Oregon Revised Statutes 436-50-420)
Pennsylvania	None.	None.

Rhode Island	<p>A firm which has no financial interest, management rights, or control in the company to whom they supply workers. The term of employment is long term and the employees are under the control of the lessee. (Working Definition)</p> <p>Any individual, firm, partnership or corporation engaged in providing workers to employer/firms under a contract or leasing arrangement...(General Laws of Rhode Island 44-30-71.4(2))</p>	Workers remain under the control of the temporary firm. Employment is usually short term. (Working Definition)
South Carolina	<p>An entity that enters into a contractual relationship with a client to assume the position of the employer. (UI Office Working Definition)</p> <p>"Staff leasing services" means an arrangement by which employees of a licensee are assigned to work at a client company and in which employment responsibilities are shared by the licensee and the client company. The employee's assignment is intended to be of a long-term or continuing nature, rather than temporary or seasonal in nature, and a majority of the work force at a client company worksite or a specialized group within that work force consists of assigned employees of the licensee. This does not include family-related businesses or similar groups, that do not meet the requirements of item (8). Staff leasing does not include temporary employees. (South Carolina Statutes 40-68-10(8))</p>	An entity that provides temporary staffing needs. (Working Definition)
South Dakota	None.	None.
Tennessee	<p>"Employee leasing organization" means any firm which places employees of another business on its payroll and leases such employees back to the client on an ongoing basis. (TCA 62-31-102(7) - prior to January 1, 1996)</p> <p>"Staff leasing arrangement" means an arrangement, under contract or otherwise, whereby:</p> <ul style="list-style-type: none"> (i) A staff leasing company assigns employees to perform services for a client; (ii) The arrangement sets no restriction or limitation on the duration of employment; and (iii) Employer responsibilities are in fact shared by the staff leasing company and the client. <p>(B) For purposes of this chapter, a staff leasing arrangement does not include:</p> <ul style="list-style-type: none"> (i) Personnel services defined under chapter 31 of this title; (ii) Arrangements where in a person, whose principal business activity is not entering into staff leasing arrangements, shares employees with a commonly owned company within the meaning of section 414(b) and (c) of the Internal Revenue Code of 1986, as amended and which does not hold itself out as a staff leasing company; or 	"Temporary help services firm" means an organization that assigns its employees to perform services to others with the understanding that the temporary employee's services will be terminated at the completion of the assigned tasks or functions or time period. (TCA 62-31-102(15))

Tennessee (Continued)	<p>(iii) arrangements for which a person assumes full responsibility for the product or service performed by such person or his agents and retains and exercises, both legally and in fact, a complete right of direction and control over the individuals whose services are supplied under such contractual arrangements, and such person and his agents perform a specified function for the recipient which is separate (TCA 62-31-102(9)(A)) - effective January 1, 1996)</p> <p>"Staff leasing company" or "leasing company" means an individual or business that, under an agreement between client company and the leasing company, and for a fee, places all or substantially all of the regular, full-time employees of the client company on the leasing company's payroll and leases them to the client company on an ongoing basis with no restriction or limitation on the duration of employment. (TCA 62-43-103(a)10) - effective January 1, 1996)</p>	
Texas	<p>An individual business entity that offers staff leasing services. Staff leasing services means an arrangement by which employees of a licensee are assigned to work at a client company in which employment responsibilities are in fact shared by the licensee and the client company, the employee's assignment is intended to be of a long-term or continuing nature, rather than temporary or seasonal in nature, and a majority of the workforce at a client company worksite or a specialized group within the workforce consists of assigned employees of the licensee. The term does not include:</p> <p>(A) a temporary help service (B) an independent contractor (C) a public company or any other person in which that public company has a direct or indirect ownership interest in excess of 33-1/3 percent, including ownership through subsidiaries and affiliates; or (D) a temporary common worker agency or employer as defined in Volume 15, Article 5221a-10, Vernon's Texas Civil Statutes. (Staff Leasing Services Act, Section 12 of Texas Civil Statutes Article 9104 Section 1(11))</p>	<p>An arrangement by which an organization hires its own employees and assigns them to clients to support or supplement the client's workforce in special work situations such as employee absences, temporary skill shortages, seasonal workloads, or special assignments and projects. (The Staff Leasing Services Act, Section 12 of Texas Civil Statutes Article 9104 Section 1 (14))</p>
Utah	<p>"Employee leasing company" or "leasing company" means an individual or business that, under an agreement between the client company and the leasing company, and for a fee places all or substantially all of the regular, full-time employees of the client company on the leasing company's payroll and leases them to the client company on an ongoing basis with no restriction or limitation on the duration of employment. (Utah Code 58-59-102(3))</p>	<p>"Temporary help company," as may be further defined by rule, means a person or entity that provides temporary employees to fill assignments with a finite ending date to another independent entity in special, unusual, seasonal, or temporary skill shortage situations. (Utah Code 58-59-102(11))</p>
Vermont	<p>Employee leasing company@or leasing company@means a person engaged in the business of providing individuals to perform ongoing services for an indefinite time period for client companies pursuant to one or more employee leasing agreements executed between the leasing company and the client company. (Vermont Code 21 V.S.A.)</p>	<p>Temporary help company@means a person who hires its own employees and provides them to another business entity as temporary full or part-time personnel to provide services for a finite period of time in special or unusual situations such as employee absences, temporary skill shortages, seasonal workloads and special work assignments and projects (Vermont Code 21 V.S.A.)</p>
Virginia	None.	None.

Washington	Employee leasing companies exist for the purpose of supplying employees to other businesses. They are not usually considered a temporary employment agency since they normally provide permanent employees. They may provide employee searches, interviewing, hiring and, in some cases, pay the individuals their wage from payday to payday. The leasing company simply charges the business a periodic fee (usually monthly) for their services which includes the pay for the employees. The leasing company does not usually have any investment in the client business. On the other hand, most private employment agencies charge the ultimate employer a one time fee for placing an individual, then have nothing more to do with that employee or the employer. (Employment Security Department Tax Branch Policy Manual Status Section 219)	None.
West Virginia	An independently established business entity that engages in the business of providing leased employees to a client-lessee. (Working Definition)	An employing unit that contracts with client-lessee or customers to supply workers to perform services for the client-lessee or customer. (Working Definition)
Wisconsin	"Employee service company" means a leasing company or temporary help service which contracts with clients or customers to supply individuals to performs services for the client or customer and which, both under contract and in fact: (a) Negotiates with clients or customers for such matters as time, place, type of work, working conditions, quality, and price of the services; (b) Determines assignments or reassignments of individuals to its clients or customers, even if the individuals retain the right to refuse specific assignments; (c) Sets rates of pay of the individuals, whether or not through negotiation; (d) Pays the individuals from its account or accounts; and (e) Hires and terminates individuals who perform services for the clients or customers. (Wisconsin State Statutes, Section 108.02 (12m))	
Wyoming	None.	None.

Appendix D

**Using Wage Records to Identify Leasing and
Client Firms**

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Using Wage Records To Identify Leasing and Client Firms

State UI Wage Records

Employers are required to submit the quarterly wages of all of their covered employees to the State UI administrative offices. Since UI taxes are levied individually on each employee's wages up to a maximum, the State collects wage records for every covered employee in the State. Generally, each UI wage record contains an employer identification number (EIN), an employee Social Security number (SSN), and the wages received by the employee from the employer for a given year and quarter. Cases in which an individual receives wages from multiple employers for the same year and quarter would appear as multiple wage records collected by the State from each of the individual's employers.

Using all of the UI wage records collected from every employer, it is possible to examine an individual's employment and earnings history. It is a relatively straightforward matter to track an individual's SSN either forward or backward through time to discover from which employers that individual received wages for each year and quarter. It is the ability to track individuals from one employer to the next that makes it possible to use UI wage records to identify employee leasing firms and their client firms.

When employees are leased, the leasing firm becomes the employer of record and is responsible for the payment of payroll taxes. Thus, upon an employee being leased, the EIN associated with that employee's wage record will change from the client (old) firm to the leasing (new) firm. Changes of employees from one EIN to another can also occur as the result of employee turnover and firms going out of business as well as buyouts, partial purchases, and divestitures that may or may not be captured by successorship rules. As a result, identifying firms engaged in employee leasing requires the use of additional selection criteria.

Identifying Firms Engaged in Employee Leasing

Using wage records to identify firms engaged in employee leasing is, in essence, a two-step process. First, it is necessary to identify those occurrences in which it appears likely that one firm begins to lease its employees from another firm. Then, criteria must be established to determine exactly which firms are engaged in employee leasing.

Identifying Leasing Occurrences

A leasing occurrence is a situation in which one firm, the client firm, ceases to be responsible for paying the wages and UI payroll taxes on some or all of its employees and instead leases those employees from another firm, the leasing firm, which becomes

responsible for paying the employees' wages and UI payroll taxes. Leasing occurrences were identified using the following methodology:

Employee receiving wages from every firm in the first quarter of 1994 (the *base period*) were tracked by their SSNs from the first quarter of 1994 backwards in time to determine at that point (the *transition period*) they began working for that particular firm (their base period).¹ In order to simplify the process, only the first quarter of each year was used for comparative purposes.² For each SSN, the first incident of their receiving wages from a firm other than their base firm (their *transition firm*) was noted and its EIN was recorded. The SSN was then removed from searches in earlier time periods. In this manner, the SSNs were traced to their most recent previous employers and the EINs of the previous firms were recorded.

Every incident in which a worker's SSN switched firms was noted and considered a changeover. Most changeovers were individuals changing jobs or, less frequently, successor employers. Therefore, not all changeovers were considered leasing occurrences. First, all changeovers from a transition firm with a SIC code of 7363 (Help Supply Services) to any base firm with a SIC code of 7363 were removed from consideration. Then, depending upon the employment of the transition firm in the transition period, the changeover was required to meet one of the following criteria:

- For transition firms with at least 500 employees, at least 2 percent of the transition firm's employees had to be involved in the changeover.
- For transition firms with fewer than 500 employees, at least half of the transition firm's employees had to be involved in the changeover *or* the number of employees in the changeover had to be at least a certain minimum, depending upon the year of the changeover (see Exhibit 1).

As displayed in Exhibit 1, the minimum number of employees required in order for a changeover to be considered a leasing occurrence increases as the transition period approaches the base period. Given the natural turnover rate of the workforce, the likelihood of an employee (or group of employees) being continuously employed by their base firm from their transition period through the first quarter of 1994 decreases as the transition period becomes more distant. Thus, the size necessary for a changeover to be classified as a leasing occurrence diminishes as the transition period grows more distant from the base period. This assumes that a leasing

¹For Texas and Florida, the SSNs were tracked backward to the first quarter of 1990; for Oklahoma, the SSNs were tracked backward only to the first quarter of 1991.

²The first quarter was used because firms pay UI payroll taxes on all employees at the rate existing during that quarter. In other quarters, employees' wages may exceed the maximum taxable wage. In most cases, new experience rated schedules take effect in the first quarter.

Exhibit 1

**Unemployment Insurance Services
Department of Labor**

**Minimum Size Requirements of Changeovers
for Transition Firms with Fewer than 500
Employees, by Transition Period**

Transition Period	1990:1	1991:1	1992:1	1993:1
Min. No. of SSNs in Changeover for Leasing Occurrence	5	6	7	8

arrangement is more permanent in duration than other contingent work arrangements (the most notable being temporary help) but also takes into account the normal turnover within the workforce.

In cases in which the transition and base firms had identical SIC codes, the changeover had to constitute at least 25 percent of the transition firm's workforce to be considered a leasing occurrence. This screen was applied to all changeovers regardless of the employment level of the transition firms in order to reduce the number of successorships and takeovers mistakenly classified as leasing occurrences.

Using this methodology, the study identified leasing occurrences in all four States. A substantial portion of the identified leasing occurrences involved a relatively small percentage of the transition firm's workforce. Although a "traditional" leasing arrangement is one in which all of the employees from one firm (the client firm) are transferred to another firm (the leasing firm), many leasing arrangements include only part (a division or specific sector) of the client firm's workforce. An example of such an arrangement is one in which a hospital (or other large firm) decides to lease out its cafeteria workers or other service workers. Also, due to the natural turnover in the workforce, the likelihood of identifying a leasing occurrence in which all (100 percent) of the employees from the client firm were subsequently leased decreases as the time between the leasing occurrence and the base period increases. For example, a firm with 100 employees and ten percent turnover each year will appear to have 110 employees, of whom only 90 could have changed over during the year, 81 in the year prior, etc.

Identifying Leasing Firms

The second step in the use of UI State wage records to identify employee leasing firms involves setting criteria by which base firms can be classified as leasing firms and by which their client firms can be identified. Depending upon the purpose of identifying leasing firms, the criteria can be set to identify as broad a range of firms as desired; i.e., one could define the criteria stringently, thereby reducing the number of firms identified as leasing firms, or loosely, thereby increasing the possible number of firms identified as leasing firms. The more stringent the criteria, the more confident one could be that all of the base firms identified as leasing firms were, in fact, engaged in employee leasing. On the other hand, a State that wanted to administratively identify leasing firms might use a loose definition and then follow up to identify successors, partial divestitures, etc.

The criteria used to identify leasing firms in this study were based upon the following factors:

- The base firm's SIC code
- The number of clients identified for the base firm; i.e., the number of different transition firms from which employees moved in a leasing occurrence.

- The number of leasing occurrences for the base firm
- The percentage of the base firm's workforce made up of employees involved in a leasing occurrence (i.e., those employees who had changed from a transition firm to the base firm)

The final criteria used in this study were as follows:

- Base firms with a SIC code of 7363 and at least three leasing occurrences involving four or more employees and at least three client firms were classified as leasing firms.
- Base firms with all other SIC codes were required to have at least three client firms and, depending upon the number of leasing occurrences involving four or more employees, a specific percentage of their workforce made up of employees involved in al leasing occurrence (see Exhibit 2) to be classified as leasing firms.³

Many employee leasing firms are classified in the 7363 SIC code (Help Supply Services). As a result, it was necessary to apply different criteria to base firms in the 7363 SIC code to ensure their appropriate classification as employee leasing firms. Many 7363 firms do provide both temporary help and employee leasing services and, due to the size of their temporary help workforce, would have a relatively small percentage of their workforce made up of leased employees. Non-7363 employee leasing firms, however, are more likely specialized employee leasing firms, such as those providing truck drivers, surgical nurses, specialized professional services, security guards, or food service workers. As a result, a higher percentage of their workforce is composed of leased employees.

Potential Limitations of Using UI Wage-Record Data

This kind of analysis does have limitations. First, the criteria that are set for both identifying potential leasing occurrences and identifying leasing firms are extremely important in determining how many base firms are identified as leasing firms. As mentioned earlier, these criteria can be set to "capture" either more broad or more narrow ranges of firms, depending upon the use to which the list of identified firms will be put. The criteria chosen for this study, for example, automatically exclude the smallest leasing firms (i.e., fewer than about 25 employees). This was though appropriate since the economics of employee leasing requires a large number of leased employees.

³ With only 3 years of data from Oklahoma (compared to 4 from the other States), the minimum requirements for both the number of leasing occurrences of four or more employees and the number of client firms were reduced to two for firms in Oklahoma.

Exhibit 2

**Unemployment Insurance Services
Department of Labor**

**Percentage of Workforce of Leased Employees
Required for Non-7363 Base Firms**

Number of leasing occurrences involving four or more employees	Required percent of workforce made up of leased employees
3	50%
4	40%
5	30%
6	20%
7 or more	10%

including Oklahoma, keep firm successorship data in their UI files.⁴

Despite these limitations, using UI wage records remains a plausible method for States to identify leasing firms. States have the ability to track employees both forward and backward through time, thus allowing them more options with which to identify potential leasing occurrences. In addition, States have the ability to audit firms and to look much more closely at firms' operations and backgrounds, which can provide invaluable information about whether a particular employer is engaged in employee leasing. Finally, interstate cooperation allows States to identify those leasing firms operating across State borders.

⁴ In fact, the successorship information for Oklahoma was used in the analysis to eliminate successors from the identified leasing firms.