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Eric J. Kodesch

kodesche@lanepowell.com

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A recurring question about Paycheck Protection Program (PPP) loans is whether compensation paid to temporary employees qualify as forgivable payroll costs. The answer is a resounding *maybe*.

As a threshold matter, there is no doubt that temporary employees count toward the 500 employee limit for general PPP eligibility.

For purposes of the 500-employee threshold, all employees must be counted, whether full-time, part-time, or employed on some other basis (including employees obtained from a temporary employee agency, professional employer organization, or leasing concern).¹

Similarly, compensation paid to temporary employees who are on a borrower's payroll constitutes payroll costs for purposes of PPP forgiveness.

However, the treatment of temporary employees employed by a staffing agency (aka "temp agency" or employee leasing company) depends on whether the staffing agency constitutes a Professional Employer Organization (PEO) or similar payroll provider.

PEO status is important because the SBA says it is – in an FAQ that is generally favorable to many borrowers. Specifically, in [FAQ 10](#), the SBA says a borrower is entitled to forgiveness for payroll costs paid for employees whose state law employer of record is a PEO.²

10. Question: What if an eligible borrower contracts with a third-party payer such as a payroll provider or a Professional Employer Organization (PEO) to process payroll and report payroll taxes?

Answer: SBA recognizes that eligible borrowers that use PEOs or similar payroll providers are required under some state registration laws to report wage and other data on the Employer Identification Number (EIN) of the PEO or other payroll provider. In these cases, payroll documentation provided by the payroll provider that indicates the amount of wages and payroll taxes reported to the IRS by the payroll provider for the borrower's employees will be considered acceptable PPP loan payroll documentation. Relevant information from a Schedule R (Form 941),

Allocation Schedule for Aggregate Form 941 Filers, attached to the PEO's or other payroll provider's Form 941, Employer's Quarterly Federal Tax Return, should be used if it is available; **otherwise, the eligible borrower should obtain a statement from the payroll provider documenting the amount of wages and payroll taxes.** In addition, employees of the eligible borrower will not be considered employees of the eligible borrower's payroll provider or PEO.

Emphasis supplied.

What is a PEO and How Does It Differ From Staffing/Temp Agencies and Employee Leasing Companies?

There are many types of PEOs, including administrative services organizations (ASOs)³ that should clearly be covered by FAQ 10 above because the party for whom the services are actually performed remains the employer of record. But not all temp/staffing/employee leasing agencies are necessarily PEOs. Because these distinctions are outside the scope of our usual legal work, we did some quick research (i.e., we Googled it)⁴ and [learned](#):

PEOs do not supply labor to worksites. PEOs supply services and benefits to a business client and its existing workforce. PEOs enter into a co-employment arrangement typically involving all of the client's existing worksite employees and sponsor benefit plans for the workers and provide human resources services to the client. In most cases, the PEO provides access to health insurance, retirement savings plans, and other critical employee benefits for the worksite employees of the business client. If a PEO relationship is terminated, the worksite employees' co-employment arrangement with the PEO ceases, but they will continue as employees of the client.

By comparison, a leasing or staffing service supplies new workers, usually on a temporary or project-specific basis. These leased employees return to the staffing service for reassignment after completion of their work with the client company. Some define employee leasing as a temporary employment arrangement where one or more workers selected by the leasing or staffing entity is assigned to a customer frequently for a fixed period of time or for a specific project. Upon termination of the staffing or leasing company arrangement, the worker has no continuing employment relationship with the client.

Historically, leasing terminology was used to describe what has evolved into PEO relationships. Some older state statutes governing PEOs still use the leasing terminology, contributing to the confusion about PEOs.

Like a leasing situation, a temporary staffing service recruits and hires 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 or seasonal workloads. These workers are traditionally only a small portion of the client's workforce.

PEOs do not supply labor to worksites. They co-employ existing permanent workforces and provide services and benefits to both the worksite employer and the employees.

When is a Staffing/Temp Agency or Employee Leasing Company "Similar" to a PEO?

Now that we know the difference between PEOs and staffing/temp and employee leasing companies, we have to address the question of whether the latter category constitutes a "PEO or similar payroll provider." If so, compensation paid for workers obtained from staffing/temp and employee leasing companies fall within the rule governing workers from PEOs (whose compensation clearly constitutes a PPP payroll cost eligible for forgiveness). Unfortunately, although the SBA provided a common-sense and borrower-favorable rule for *PEOs and similar payroll providers*, the SBA did not provide any standards for determining or testing such similarities.

As explained below, it is unclear when and whether the SBA considers staffing/temp and employee leasing companies as functionally equivalent to a PEO and there are good arguments on both sides. We also recognize that there are many different types of staffing/temp and employee leasing companies, some of which provide services similar to a typical PEO and some with services that far exceed a typical PEO. Accordingly, businesses may need to consider their individualized relationship with their staffing/temp or employee leasing company before claiming temporary employees as payroll costs.

We reach this conclusion for several reasons. First, the SBA defines an employee for SBA 7(a) eligibility and that definition "includes employees obtained from a temporary employee agency, professional employee [sic] organization or leasing concern." [13 CFR Section 121.106](#). At first blush, this rule would seem to suggest that temporary employees are a covered cost for on-site employers. But this rule is ambiguous and the SBA arguably may only apply it for purposes of eligibility testing, and not for purposes of computing payroll costs for forgiveness. We also know from some recent litigation that not all SBA lending rules graft well to the PPP program.⁵

Second, PEOs can be fundamentally different than many staffing/temp agencies. On the one hand, PEOs are administrators who typically handle HR and payroll functions. On the other, staffing/temp agencies usually find, train and supply the labor. As such, there is a reasonable argument that some staffing/temp agencies are not “similar payroll providers” to many PEOs because they engage in many more services than an employer of record for tax purposes.

Third, staffing/temp and employee leasing companies – compared to PEOs – may have differing impacts on the demand for paying workers. As to PEOs, they do not often drive employee compensation and demand, which is a key purpose of the PPP. But the same may or may not be true for a particular employee of a staffing/temp agency. For instance, some staffing/temp and employee leasing companies merely serve as a broker (matching employers with workers) and an administrator (handling HR and payroll functions). Under this model, the staffing/temp or employee leasing agencies fill, but not create, the demand for workers. Yet other staffing/temp and employee leasing agencies may actually fill the demand by finding talent, training employees, and then selling unique services to on-site businesses. Further, some staffing/temp agencies pay employees even when they are not placed at an on-site business. This would seem to be a critical factor in light of the oft reiterated purpose of the PPP to protect employee compensation.

Fourth, since the SBA doesn't define what type of business constitutes a PEO, much less what might qualify as a “similar payroll provider,” it seems appropriate to consider the scope and intent of FAQ 10 from a policy perspective. Because all temporary employees are treated as employees of the borrower for purposes of testing PPP eligibility, it arguably makes sense to treat a worker as an employee for purposes of testing eligibility as an expense of the same borrower for purposes of determining the amount of the loan and the payroll costs eligible for forgiveness.

Nevertheless, we acknowledge that some reputable practitioners have suggested that compensation paid to employees “on payroll” of the staffing/temp or leasing agency is only a PPP payroll cost of the agency.⁶ We think the answer is arguably more nuanced and depends on the relationship between the entities, at least until the SBA tells us otherwise.

Unless and until the SBA provides a more helpful test, we suggest on-site co-employers and staffing/temp agencies consider three questions: 1) who exerts more control over the terms and conditions of employment; 2) who takes on the greater risk and liability; and 3) whose business has the greater impact on employee demand and compensation? Relevant

factors may include the type of labor provided as well as who is responsible for recruiting, hiring, training, onboarding, preparing and enforcing policies, accommodations, investigations, leaves, discipline, termination, benefits, payroll, taxes and insurance.

We also acknowledge the complexity in determining the extent to which health insurance, retirement and state/local taxes paid by a staffing/temp agency or employee leasing company (or a PEO for that matter) should be computed and proven to a lender when requesting forgiveness. This can become particularly challenging if this non-cash compensation needs to be shared between multiple borrowers for whom a temporary employee may have worked. Maybe the easiest answer is that the borrower should be able to claim as payroll costs the (marked up?) amounts the borrower pays to any staffing/temp agency or employee leasing company?

Maybe the real answer depends on whether a particular staffing/temp agency or employee leasing company is willing to provide the documentary support required by FAQ 10. Asking your staffing/temp agency or employee leasing company now might avoid a surprise later.

¹ 13 CFR § 121.106(a).

² [Wikipedia](#) explains: A professional employer organization (PEO) is an outsourcing firm that provides services to small and medium sized businesses (SMBs). Typically, the PEO offering may include human resource consulting, safety and risk mitigation services, payroll processing, employer payroll tax filing, workers' compensation insurance, health benefits, employers' practice and liability insurance (EPLI), retirement vehicles (401(k)), regulatory compliance assistance, workforce management technology and training and development. The PEO enters into a contractual co-employment agreement with its clientele. Through co-employment, the PEO becomes the employer of record for tax purposes through filing payroll taxes under its own tax identification numbers. The PEO enters into a contractual co-employment agreement with its clientele. Through co-employment, the PEO becomes the employer of record for tax purposes through filing payroll taxes under its own tax identification numbers.

³ [Wikipedia](#) explains: An **administrative services organization** (ASO) is an organization that provides outsourced solutions to meet the administrative and HR needs of the client, with the client retaining all employment-related risks and liabilities.^[1] The term ASO was established by the [PEO industry](#) in the late 1990s in order to distinguish between selective administrative support and full-scale PEO services.^[2] The principal difference between the two types of service is that, in an ASO arrangement, the employer remains the *employer of record* for tax purposes.^[3] Ultimately, with this structure, tax and insurance filings are done through the administrative firm, but under the

client company's [employer identification number](#). All [W-2](#) and [workers' compensation](#) policies remain the responsibility of the employer and not the administrative firm.

⁴ Not that you can't trust everything you read on the internet, we still confirmed the accuracy of this information with our excellent employment law colleagues.

⁵ *DV Diamond Club of Flint, LLC, et al. v. U.S. Small Business Administration, et al.*, decided on May 11, (D.Mich) *appeal docketed*, and *Camelot Banquet Rooms, Inc. v. U.S. Small Business Administration*, decided on May 1, (D. WI). In both cases, so called "gentlemen's clubs" successfully argued that the CARES Act broadened eligibility for PPP loans by providing that "any business concern... shall be eligible...if the business employs less than 500 employees...." The Michigan court further found that SBA rules and guidance promulgated under its general small business lending rules was not applicable or controlling with respect to the clear intent of Congress to broaden eligibility requirements for PPP loans.

⁶ E.g., [Here](#) (at Q.25), [here](#) and [here](#).