

Professional Employer Organizations And Uncharted Immigration Risks

*By Ted J. Chiappari and Angelo A. Paparelli**

The pitch to businesses is compelling:

- Improve compliance with burdensome state and federal regulation, in particular, tax, Workers' Compensation and unemployment insurance laws.
- Reduce overhead costs through a smaller in-house human resources team.
- Gain access to better benefits packages at lower cost through greater bargaining power and economies of scale.

Professional employer organizations (PEOs)—also known as employee leasing companies or payrolling companies—assume responsibility for payroll services, tax withholding and related HR compliance issues for their clients, becoming the "employer of record" for payroll purposes. While PEOs may deliver valuable benefits, U.S. businesses should also consider the immigration difficulties a contractual engagement with a PEO may create when sponsoring foreign employees for temporary work visas or employment-based permanent residence.

The lack of definitive guidance from U.S. government agencies on the immigration consequences of PEO arrangements, however, places businesses that engage PEOs at risk. These legal risks may involve opportunities lost (the loss of key foreign workers) or penalties imposed (the failure to maintain required immigration-related business records or the knowing employment of unauthorized workers).

The National Association of Professional Employer Organizations (NAPEO) identifies the key characteristic of a PEO as co-employment: "a contractual allocation and sharing of employer responsibilities between the PEO and the client."¹ NAPEO's accreditation arm, Employer Services Assurances Corporation (ESAC), defines PEO somewhat circularly as any enterprise "engaged in the business of providing services under a PEO Service Arrangement," and states that the term should be construed liberally. ESAC then defines PEO Service Arrangement in the negative to exclude: (a) service arrangements where the vendor does not co-employ all or part of a client's workforce, (b) where the vendor's services are as a contractor and the vendor assumes primary direction and control over the work performed; (c) service arrangements between affiliated companies within the same corporate group; and (d) temporary help services.²

¹ See NAPEO's website at <http://www.napeo.org/peoindustry/coemployers.cfm> (last accessed on December 15, 2010). In this article, the term "client" refers to the corporate customer of the PEO

² See ESAC's Standards and Procedures for ESAC accreditation and Client Assurance Program Participation (Effective October 2010), available online at <http://www.esacorp.org/StandardsProcedures.asp> (last accessed on December 15, 2010).

In a co-employment arrangement, the right to direct and control the employees' day-to-day duties generally remains with the client. While the PEO reserves the right to exercise at least some control over the client's employees in order to qualify as a co-employer, the client's direction and control of the employees' day-to-day activities generally make the client the common-law employer. The PEO, and not the client, appears as the employer of record on payroll records, IRS documents such as W-2s and on state unemployment insurance records.

U.S. Citizenship and Immigration Services (USCIS), an agency within the Department of Homeland Security (DHS), and its predecessor, the Immigration and Naturalization Service (INS), have issued only limited guidance explicitly on PEOs. Not surprisingly, USCIS holds both the client and the PEO liable for any violations involving (a) incorrect or nonexistent immigration documentation or (b) the employment of individuals whom the employer knows lack permission to work in the United States.

In USCIS's "Handbook for Employers, Instructions for Completing Form I-9 (Employment Eligibility Verification Form)," the agency makes clear that both the client and the PEO are each considered an employer for I-9 purposes. According to USCIS, both co-employers "are responsible for complying with Form I-9 requirements, and DHS may impose penalties on either party for [compliance] failure[s]."³ The agency has issued similar guidance in connection with its E-Verify program, DHS's online employment-verification database, operated in cooperation with the Social Security Administration (SSA). E-Verify allows employers to confirm electronically the employment eligibility of newly hired employees (and some or all current employees of certain Federal contractors required to use E-Verify). Either the PEO or the client may enroll in E-Verify, but – in the view of USCIS – both are accountable for immigration violations.⁴

As a general rule, USCIS expects that, in the temporary (nonimmigrant) work-visa context, a single employer will exercise direction and control over the foreign national's performance of job duties in order to serve as a qualifying petitioner authorized to sponsor a nonimmigrant to work in the United States temporarily. There are exceptions, however, for agents of persons who are traditionally self-employed or of workers who use agents to arrange short-term employment, or agents authorized by foreign employers to act for them. Agents who do not clearly identify the actual employers must ordinarily guarantee the wages and other terms and conditions of employment by contractual agreement with the beneficiary.⁵

None of these exceptions involving agents addresses the practice of contracting for the services of PEOs. Similarly, USCIS regulations governing specific work-visa and permanent-resident (green card) categories fail to address the specific legal consequences that flow from the use of PEOs.

³ Handbook for Employers, Instructions for Completing Form I-9 (Employment Eligibility Verification Form), Q&A 43 on page 37, available online at <http://www.uscis.gov/files/form/m-274.pdf> (last accessed on December 15, 2010).

⁴ Frequently Asked Questions: Federal Contractors and E-Verify (Revised April 2010), <http://tinyurl.com/ycx2v9f> (last accessed on December 15, 2010). The only other written guidance explicitly addressing PEOs is a December 2000 letter from the INS responding to questions about PEOs in the context of H-1B (specialty occupation) petitions (discussed later in the text).

⁵ See 8 C.F.R. §§ 214.2(h)(2)(F) (H petitions), 214.2(o)(2)(iv)(E) (O petitions for persons of extraordinary ability/achievement and essential support staff), 214.2(p)(2)(iv)(E) (P petitions for artists, athletes and entertainers)

H-1B (specialty occupation) visa petitions. Before USCIS will adjudicate an H-1B petition, the agency requires the submission of a “labor condition application” certified by the Department of Labor (DOL). The DOL’s regulations provide that the employment relationship is “determined under the common law, under which the key determinant is the putative employer’s right to control the means and manner in which the work is performed.”⁶ DOL regulations also provide, however, that despite the reference to the common law, the entity that files the petition with USCIS or the labor condition application with the DOL “is deemed to be the employer of that nonimmigrant.”⁷ This second provision was presumably included in the regulations to enable enforcement proceedings against either the actual employer (as determined by a facts-and-circumstances test under the common law) or the nominal entity identified as the “petitioner.” USCIS regulations governing H-1B petitions also require that the petition be filed by a “U.S. employer,” defined as a person or entity in the United States that: “(1) Engages a person to work within the United States; (2) Has an employer-employee relationship with respect to employees under this part, as indicated by the fact that it may hire, pay, fire, supervise, or otherwise control the work of any such employee; and (3) Has an Internal Revenue Service Tax Identification number.”⁸

Several years ago, in interpreting the H-1B definition of “employer” with reference to PEOs or “employee leasing companies,” legacy INS stated that “an entity can file an H-1B petition ... even though the ... salary is paid from another source, provided ... the entity has control over the H-1B nonimmigrant even though the ... salary is paid from another source.”⁹ Further, “there is nothing in the [INS] regulations that precludes a PEO from filing an H-1B petition for [a foreign national] as long as the PEO meets the definition of a United States employer.” In light of the facts presented to the INS (the PEO only acted as paymaster while the client exercised direction and control over the employee), the INS concluded that the PEO could not act as an H-1B petitioner on behalf of its clients.

More recently, the USCIS issued a 19-page memorandum addressing how it determines the employer-employee relationship when adjudicating H-1B petitions.¹⁰ The memorandum reaffirmed that “USCIS has interpreted [the employer-employee relationship] to be the ‘conventional master-servant relationship as understood by common-law agency doctrine.’” This memorandum addressed various scenarios, including independent contractors, self-employed beneficiaries and beneficiaries placed at third-party

⁶ 20 C.F.R. § 655.715, citing a 1968 Supreme Court decision in its explanation of common law: “Under the common law, ‘no shorthand formula or magic phrase ... can be applied to find the answer.... [A]ll of the incidents of the relationship must be assessed and weighed with no one factor being decisive.’ *NLRB v. United Ins. Co. of America*, 390 U.S. 254, 258 (1968).”

⁷ 20 C.F.R. § 655.715.

⁸ 8 C.F.R. §214.2(h)(4)(ii).

⁹ Letter from Efren Hernandez III, Director, Business and Trade Services, Office of Adjudications, U.S. Department of Justice, Immigration and Naturalization Service, to attorney Kari Ann Woodward, HQ 70/6.2.8, Dec. 20, 2000, copy on file with author and also available to members of the American Immigration Lawyers Association on www.aila.org (AILA Doc. No. 01062632).

¹⁰ Memorandum from Donald Neufeld, Associate Director, Service Center Operations, “Determining Employer-Employee Relationship for Adjudication of H-1B Petitions, Including Third-Party Site Placements,” HQ 70/6.2.8, AD 10-24, Jan. 8, 2010, citing *Nationwide Mutual Ins. Co. v. Darden*, 503 U.S. 318, 322-322 (1992), available at <http://www.uscis.gov/USCIS/Laws/Memoranda/2010/H1B%20Employer-Employee%20Memo010810.pdf> (last accessed on December 15, 2010).

worksites, but unfortunately was silent on PEOs. The memo may even make it more difficult for a PEO to file H-1B petitions as agent for its clients, since the government focused solely on agents for persons who are traditionally self-employed or who use agents to arrange short-term employment with numerous employers.¹¹

These H-1B sources of authority would appear, at least conceptually, to address the most typical PEO arrangement, where the client exercises primary control over the worker while the PEO possesses residual authority to control (which may never be and never have been exercised): the client must act as petitioner because it is the common-law employer. Regrettably, these sources do not, however, address the practical obstacles, discussed below, facing a petitioner who relies on a PEO. Moreover, there remains a regulatory gap that leaves unanswered two questions for those arrangements where the PEO provides a more comprehensive outsourced HR or business process management service:

- May or must both the client and the PEO formally petition for the foreign worker for H-1B or other work-related immigration benefits?
- Will the non-petitioning entity be treated by the government as employing the foreign worker with knowledge that the individual lacks permission to work for that entity, and therefore become subject to civil or criminal immigration penalties?

As will be seen, agency guidance involving PEOs in the context of other work-visa and green-card categories is likewise unclear or nonexistent.

L-1 (intra-company transferee) petitions. The L-1 regulations say nothing explicitly about PEOs. The regulations merely provide that the petitioner must be “doing business ... as an employer in the United States....”¹² Administrative precedent also makes clear that the transferring employee must be placed under the control of a U.S.-based entity.¹³ In situations where the client retains the right to direct and control most if not all of the employees’ day-to-day activities (which is the case in the vast majority of PEO service arrangements), the client would of course be expected to act as petitioner for L-1 workers. What remains unanswered, however, is whether a PEO providing services more comprehensive than payroll administration must petition for concurrent employment authorization on behalf of the L-1 worker.

O and P petitions (involving extraordinary athletes and artists, as well as their support staff, and culturally unique performers). USCIS recently issued guidance that makes it more difficult for agents to act as O

¹¹ Memorandum from Donald Neufeld, Associate Director, Service Center Operations, “Determining Employer-Employee Relationship for Adjudication of H-1B Petitions, Including Third-Party Site Placements,” HQ 70/6.2.8, AD 10-24, Jan. 8, 2010, available at <http://www.uscis.gov/USCIS/Laws/Memoranda/2010/H1B%20Employer-Employee%20Memo010810.pdf> (last accessed on December 15, 2010).

¹² 8 C.F.R. § 214.2(l)(1)(ii)(G)(2). “Doing business means the regular, systematic, and continuous provision of goods and/or services ... and does not include the mere presence of an agent or office....” 8 C.F.R. § 214.2(l)(1)(ii)(H).

¹³ *Matter of Penner*, 18 I. & N. Dec. 49, 54 (Comm’r 1982); see also *Matter of Pozzoli*, 14 I. & N. Dec. 569, 572-573 (Reg’l Comm’r 1974).

and P petitioners.¹⁴ A PEO under limited circumstances may file an O or P visa petition but only if it qualifies as the USCIS-recognized “agent” of the client.

Practical obstacles. An employer/client filing any of the foregoing work visa petitions or sponsoring other categories of nonimmigrant workers may face practical problems in getting its petitions approved if it is relying on a PEO as employer of record for tax and payroll purposes. The client/petitioner may find it difficult to establish that its foreign employees are eligible for work-related immigration benefits based on its employer-employee relationship with the foreign beneficiary. For example, USCIS generally expects that copies of pay statements be submitted with work-visa extensions in order to prove that the individual has been working in valid nonimmigrant status. If the pay statements show the PEO's employer information with no indication that this is for payroll purposes only, USCIS may well doubt that the employee is indeed working for the client/employer. The client should therefore anticipate the need to explain the arrangement and fully document that it remains in control of the employee despite the payroll arrangement.

Immigrant visa petitions. In situations involving employment-based green card sponsorship, problems in the use of a PEO may arise when attempting to satisfy the required labor-market test (known as PERM labor certification and administered by the DOL) – a necessary preliminary step in many employment-based green card petitions – as well as in submitting the I-140 immigrant petition to the USCIS.

DOL regulations governing the PERM labor certification process require that the employer engage in various recruitment steps to prove to the DOL that there are no qualified and willing U.S. workers available for the position. For PERM purposes, an eligible “employer” is defined as “[a] person, association, firm, or a corporation that currently has a location within the United States to which U.S. workers may be referred for employment and that proposes to employ a full-time employee at a place within the United States....”¹⁵ Moreover, the term, “employment,” means ... [p]ermanent, full-time work by an employee for an employer other than oneself. ... [and in] the event of an audit, the employer must be prepared to document the permanent and full-time nature of the position by furnishing position descriptions and payroll records for the job opportunity involved in the [PERM] Application for Permanent Employment Certification.”

The USCIS regulations require that the petition be filed by a “United States employer.”¹⁶ (Although this term is not further defined in the regulations, it presumably has the same meaning as in the nonimmigrant

¹⁴ See Memorandum from Donald Neufeld, Acting Associate Director, Domestic Operations, “Requirements for Agents and Sponsors Filing as Petitioners for the O and P Visa Classifications,” HQ 70/6.2.18, HQ 70/6.2.19, Nov. 20, 2009, available at <http://www.uscis.gov/USCIS/New%20Structure/Laws%20and%20Regulations/Memoranda/2009/o-p-visa-agents-11-20-2009.pdf> (last accessed Dec. 15, 2010).

¹⁵ 20 C.F.R. § 656.3.

¹⁶ 8 C.F.R. § 204.5(c).

context discussed above.) The employer must also provide evidence in the form of annual reports, federal tax returns or audited financial statements establishing the ability to pay the proposed salary.¹⁷

In light of these provisions, it seems highly unlikely that a PEO would agree to act to sponsor a foreign national for one of its clients and, if it did, the PEO would have a difficult time showing an offer of full-time employment in a permanent position. For the client of a PEO, difficulties would also arise in trying to document its role as employer, given that both USCIS and DOL look to payroll records as evidence of the employment relationship.

Moreover, the PERM process requires employer registration based on a federal employer identification number, and one step of the recruitment process, a job order with the state department of labor, also typically requires employer registration based either on a federal employer identification number (FEIN) or a state unemployment insurance (SUI) number. Anecdotally, there have been reports of employers unable to register with the state department of labor, presumably because of a discrepancy in FEIN or SUI or because the client seemingly lacks an SUI or its SUI shows no payroll. Likewise, immigration lawyers report that USCIS has denied green card petitions because of the failure to document the petitioning employer's ability to pay because the payroll documentation shows the PEO information rather than that of the client/petitioner.

* * *

Employers considering a PEO service arrangement must weigh carefully the advantages of the arrangement against the unresolved legal issues and difficulties likely to arise with its immigration petitions on behalf of foreign employees. Until USCIS and DOL provide definitive guidance on the immigration consequences of engaging with PEOs, employers heavily reliant on foreign nationals should proceed with caution when entering into a PEO arrangement. Some things, regrettably, may be too good to be true.

* Ted J. Chiappari is a partner at Satterlee Stephens Burke & Burke LLP in New York City. Angelo A. Paparelli is a partner in Seyfarth Shaw in New York and Los Angeles.

Reprinted with permission from the December 22, 2010, edition of the New York Law Journal. © 2010 ALM Properties Inc. All rights reserved. Further duplication without permission is prohibited. The authors thank the Journal for permission to reprint this article.

¹⁷ 8 C.F.R. § 204.5(g)(2). As a practical matter, USCIS also asks for W-2s, payroll records and pay statements as evidence of ability to pay.