

THE TRUTH ABOUT PEOs:

The Complete Guide to Professional Employer Organizations



Human resource management is a hefty task: It covers everything from recruiting talent to handling the complexities of compensation and compliance. HR is such a big responsibility that many companies outsource it to professional employer organizations, or PEOs.

PEOs are a growing industry—[the National Association of Professional Employer Organizations \(NAPEO\)](#) reports that over 200,000 small and mid-sized businesses use PEOs, and 17% of all US employers with 1–99 employees use one.

For many decision makers, the possibility of contracting a PEO brings up a lot of questions. For example, what exactly does a PEO do? Does your company need one? And how will a PEO impact your HR strategy?

In this guide, you'll find the answers to all your questions, including the services PEOs can provide, the pros and cons of using one, and the best ways to leverage HR solutions.

What Is a Professional Employer Organization (PEO)?

A PEO is a third-party company that provides HR services to other businesses. In other words, a PEO is a way to outsource some or all of your organization's HR functions.

According to the NAPEO, there are 523 PEOs in the United States. PEO is a fairly broad category, and different PEOs offer a varying range of services to clients. Some offer a full package of HR functions, while other PEOs specialize in specific HR needs.

For example, a company with a large international employee base might outsource their payroll management to a PEO like [Papaya Global](#), which provides international payroll solutions.

The Pros and Cons of Using a PEO

PROS

A PEO can help you manage important HR needs like payroll, employee benefits, and compliance. Companies may choose to hire a PEO if they're feeling overwhelmed by HR responsibilities, particularly issues related to risk and liability.



The typical PEO client is a small or mid-sized business that doesn't have the bandwidth or expertise for complex HR needs, but large companies may also opt to outsource some HR functions to a PEO.

Potential benefits of using a PEO include:

- **Time and Cost Savings:** By outsourcing certain HR functions, your company can redirect time and resources into growing your business. The **NAPEO** claims that small businesses who use a PEO grow 7–9% faster and reduce turnover by 10–14%.
- **Compliance:** PEOs can stay on top of your **HR compliance needs**, easing the burden on your internal HR team and helping you avoid costly legal problems down the road.
- **Better Benefits:** A PEO may give your employees access to better benefits packages than you'd be able to offer as a smaller business.
- **Recruiting and Retention:** Some PEOs help with recruiting processes and employee engagement efforts, providing expert guidance as well as direct services like professional development opportunities.
- **Administrative Support:** PEOs can improve administrative and reporting processes, making

CONS

Using a PEO is a big decision, and it isn't the best fit for every organization. If you prefer to have control over all the details, have a specific vision for your company culture, or anticipate rapid growth for your business, a PEO may not be right for you.

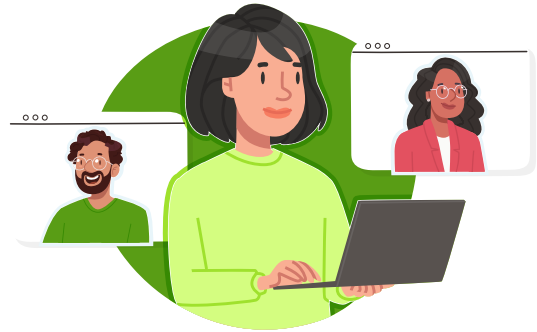


Before signing on with a PEO, consider the following risks:

- **Lack of Control:** In exchange for the convenience of outsourcing HR functions, you may be giving up control over decisions that impact your employees. This can become an issue if you and the PEO have conflicting values, priorities, or management styles.
- **Poor Service:** You aren't the PEO's only customer. Unless a PEO has amazing client services, your company's HR needs won't be receiving the same quality of attention and care as they'd get from a full-time internal team.
- **Data Access:** Most PEOs own the data they handle, particularly payroll data. This gives a third party control over data privacy and management and can make it more complicated for you to perform your own internal reports and analysis. You could also lose access to your data when you part ways with the PEO.
- **Liability:** A PEO is supposed to handle compliance, but what happens if they make a mistake? Your company could still be held responsible for legal issues, such as certain tax discrepancies. Plus, depending on your state's laws and how your PEO handles insurance, you could also be left exposed to worker's compensation lawsuits.

- **Company Culture:** Outsourcing HR functions can have a ripple effect on your company culture. Not only can the optics of outsourcing make employees feel unprioritized, but the impersonal nature of a PEO can create a disconnect between your company values and the employee experience, especially if the PEO isn't providing quality service.
- **High Costs:** PEOs typically charge based on a fee per employee or a percentage of your payroll. So while a PEO might initially help you save on HR costs, the expense of a PEO will rise as your company grows. And as your employee headcount increases, your HR needs may become more complex, requiring you to sign on for a more comprehensive (and more expensive) service package. Eventually, moving all of your HR functions in-house may become the most cost-effective option.

- Workers' compensation insurance
- Recruiting
- Onboarding
- HR administration (employee policy development, employee training, **conflict resolution**, etc.)



Free Download: 10 Red Flags of Bad Company Culture

It's never too late to turn a struggling workplace culture around! We identified 10 red flags to look out for—plus strategies for fixing what's broken.

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How PEOs Work

Essentially, a PEO is a B2B service provider: It provides your business with HR services. When your company enters a service contract with the PEO, your company pays the PEO to handle whatever HR functions are included in your service package, such as managing payroll and benefits or handling certain administrative tasks.

Here are some services that a PEO might provide:

- Payroll
- Benefits administration
- **Compliance and risk management**

A COMMON MISCONCEPTION

A PEO is not a staffing agency. Although a PEO can help with recruitment, they don't provide your company with workers. Instead, they take on a shared responsibility for your workforce—the PEO industry often refers to this as being a “co-employer.”



PEO CO-EMPLOYMENT, EXPLAINED

A PEO is not a staffing agency. Although a PEO can help with recruitment, they don't provide your company with workers. Instead, they take on a shared responsibility for your workforce—the PEO industry often refers to this as being a “co-employer.”

To be clear, a PEO does not have any ownership over your company and has no say in business decisions about marketing, sales, or product. You also retain sole control over hiring, firing, and performance management.

Co-employment with a PEO can be a helpful option if you're a smaller business and want to ensure you're staying in compliance with tax and labor laws, as well as offer your employees more expansive benefits that a PEO can provide.

IS CO-EMPLOYMENT LEGAL?

Co-employment is legal as long as you and the PEO are in compliance with all local and federal regulations. You should always consult your legal counsel before entering into a co-employer relationship. Here are a few legal factors to keep in mind as you explore PEOs:

- Each state varies on PEO licensing and registration requirements, as well as restrictions on how PEOs function. Some states do require that a company uses their own EIN—in those cases, a PEO will likely assist you in properly filing taxes in each state using third-party access to your EIN.
- On the federal level, the **Internal Revenue Code** doesn't officially recognize a "co-employer." When it comes to federal payroll taxes, the "common-law employer" is usually responsible. The IRS defines a common-law employer as the entity for whom the employee performs tasks, so even if the PEO is filing the payroll taxes under its own EIN, the IRS could still potentially view your company as a responsible party when a tax issue arises.
- The IRS has policies in place regarding **third-party wage payers**. Any reputable PEO you're considering should be able to outline how they navigate those policies and the impact they might have on your liability.



RUNNING PAYROLL WITH A PEO

Payroll is the service that most people associate with PEOs. By having a PEO run your payroll, you can reduce some of your employer liability while saving on the cost and time burden of **running payroll in-house**.

When you outsource payroll to a PEO, the PEO becomes a co-employer and takes over all payroll responsibilities, such as issuing paychecks, filing payroll taxes, and **distributing W-2s**. PEOs usually take responsibility for workers' compensation insurance, as well. The PEO will likely use its EIN when processing payroll, acting as the employer of record, unless you're operating in a state that requires PEO clients to use their own EINs.



Your company is still financially responsible for paying employees. The process varies depending on your agreement with the PEO, but typically you'll have a set schedule for transferring funds to the PEO's account so they can run payroll on your behalf.

Ultimately, as the business owner and the common-law employer, you'll be legally accountable for ensuring that the PEO is properly paying your employment taxes and staying in compliance with all relevant laws—so do your research and choose a PEO you trust!

HOW IS A PAYROLL SERVICE DIFFERENT FROM A PEO?

A payroll service processes your payroll and gives you access to valuable tools, like **automated tax filing**. However, you remain the employer of record and have sole responsibility for taxes and compliance. This is a great option if you want to retain full access and control over your data and payroll operations, while still enjoying the time and cost savings you can get from a powerful platform.



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Managing Employee Benefits Administration with a PEO

Alongside payroll, **benefits administration** is one of the major selling points of a PEO. Smaller business owners often struggle with finding affordable, quality benefits for their employees. As a co-employer, a PEO will sponsor the benefit plans and offer your employees options they otherwise wouldn't have had access to.

A PEO can negotiate with carriers, handle enrollment, and communicate benefits information to employees. As an industry expert, a PEO will also help with any benefits-related compliance needs.



Your PEO will most likely give you a menu of benefits packages (medical and dental insurance, retirement accounts, disability insurance, etc.) they've already put together. You can then choose which of those packages you'd like to offer your employees.

pays the PEO to handle whatever HR functions are included in your service package, such as managing payroll and benefits or handling certain administrative tasks.

HOW DO PEOS GET BETTER BENEFITS PLANS?

The answer is simple: They're bigger than a small business and have more buying power. While you might be looking for medical coverage for your 50 employees, a PEO is buying coverage for all their clients' employees, which could be thousands of people.

HOW IS A BENEFITS ADMINISTRATION SERVICE DIFFERENT FROM A PEO?

A benefits administration service or platform can help you streamline and automate your enrollment process, while letting you stay in control of what carriers you work with and what benefits you offer.

Without a PEO, you'll have to negotiate independently and choose your own benefits providers. This can be a challenge, but it allows you to advocate on behalf of your people and seek out the unique benefits that your workforce needs, rather than use the one-size-fits-all packages offered by a PEO.

Alternatively, by using a benefits admin platform on your own, you have access to all your employee elections data, so you can strategically maximize your benefits offerings.



Free Resource: Open Enrollment Survival Kit

Gearing up for open enrollment? Don't miss a thing with our resource kit, featuring all the tools you need for a smooth enrollment season.

[DOWNLOAD THE FREE KIT →](#)

Exploring Solutions: How Does a PEO Compare to Other Options?

A PEO can be an attractive HR solution, especially if you're a small or mid-sized company that would benefit from the resources and expertise of a third-party organization. But while PEOs have their advantages, they're not ideal as an indefinite solution for all of your HR needs.

PEOs are useful for managing complex HR needs, such as **international payroll**. They can also serve a valuable role for small businesses who need help with payroll management or want to offer employees more affordable benefits.

That said, PEOs become expensive as your company grows, and their control over data and decision-making can limit you in the long run.

For this reason, it's a good idea to invest in an internal HR team as soon as possible, as well as your own HR information system (HRIS), while using PEOs or HR consulting firms as third-party resources to support specific HR functions as needed. Read on to explore how these resources compare, and how they can best work together to maximize the impact of your HR team.

	Purpose	Perks
PEO	<ul style="list-style-type: none"> Manages complex HR tasks, such as payroll. Can serve as your full HR apparatus. 	<ul style="list-style-type: none"> Acts as the employer of record, taking on compliance responsibilities. Provides your employees with more comprehensive HR services.
In-House HR	<ul style="list-style-type: none"> Internally manages HR functions. Helps develop strategic HR initiatives. 	<ul style="list-style-type: none"> Has an intimate understanding of your business and your workforce. Builds the foundation to scale your HR team with your business.
HR Consulting	<ul style="list-style-type: none"> Advises on how to make HR processes more efficient and effective. Provides select services, such as internal audits and HR policy development. 	<ul style="list-style-type: none"> Gives you access to experts in the field. Allows you to remain the employer of record and have full decision-making power.
In-House HR	<ul style="list-style-type: none"> Brings all your essential HR tools into one centralized database. Automates and streamlines HR functions. 	<ul style="list-style-type: none"> Guarantees you full control over your HR data while empowering your internal team with advanced analytics tools. Offers pre-built integrations to connect your data with all your favorite HR resources and tools, including PEO payroll platforms.

IN-HOUSE HR VS. A PEO



Having an **in-house HR team**, even if it's just a team of one, is incredibly beneficial for your organization. An internal HR professional understands your business and your workforce on an intimate level and can lay the groundwork to scale your HR functions as your company grows.

When you're building your in-house HR team, you might start with hiring for HR management (HRM) experience. HRM focuses on all your employee needs, such as hiring, payroll, and performance management. If you need an HR team with a bigger scope, you can look for HR pros with experience in human capital management (HCM). HCM covers all the same employee needs as HRM but also helps develop strategic initiatives for your business.

Meanwhile, outsourcing some HR functions to a PEO can help expand your HR team's capacity, especially when

it comes to important—but time-consuming—tasks like payroll and benefits enrollment.

For example, you can use a PEO to ensure international employees are paid properly, while your internal HR pros focus on matters like company culture, employee policies, and performance management.

Keep in mind that for many companies, the cost-effective nature of a PEO has an expiration date. Once your employee headcount hits a certain threshold, it might make more sense to bring all of your HR in-house. This transition will be a lot simpler if you already have an internal HR team.

EXPANDING HR CAPACITY WITH AN HRIS

An HRIS is an invaluable resource for expanding your HR team's capacity. It provides a centralized database, automates and streamlines HR functions, and can generate insightful data reports and analysis.

We recommend investing in an **all-in-one HRIS**. Bringing all your essential HR tools into one place simplifies processes, eliminates double data entry, and improves the employee experience.

An all-in-one HRIS also **saves your company significant time and money**: BambooHR customers save hundreds of hours and reduce costs by 40% on average. For comparison, the NAPEO reports that the average **ROI for PEOs** is 27%.

What It Costs: BambooHR vs. PEO*

Solutions	PEO	BambooHR**	Difference per Month	Annual Difference
HRIS + Payroll + Benefits Admin	\$25,000/mo	\$1,569.93/mo	\$23,430.07/mo	\$281,160.84

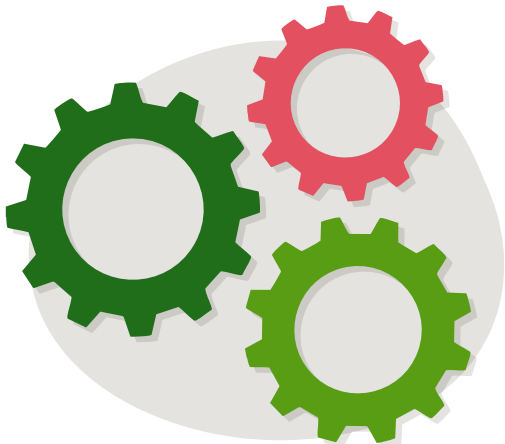
*Amounts based on a business with 100 employees and a \$5 million annual payroll cost. PEO expense estimated with a typical fee of 6% payroll costs.

**BambooHR Core Plan with Payroll + Benefits Administration Bundle

A high-quality, all-in-one HRIS will include the following features:

- [Centralized records and data storage](#)
- [Reporting and analytics](#)
- [Payroll](#)
- [Benefits administration](#)
- [Time tracking](#)
- [PTO management](#)
- [Applicant tracking system](#)
- [Onboarding](#)
- [Performance management](#)

And unlike PEOs, an HRIS ensures you stay in full control of your company's data and HR decision-making, empowering your internal HR team with efficient, automated processes and powerful analytics tools.



An HRIS and a PEO aren't mutually exclusive. You can leverage the power of an all-in-one HRIS while still contracting a PEO to support certain HR functions. However, PEOs usually have their own software they use for their services. If you currently work with a PEO for a function such as payroll, or are considering working with one, make sure you choose an all-in-one HRIS that offers an integration with your PEO's software.

With a pre-built integration, you can effortlessly sync your data between your PEO and your HRIS, empowering your internal HR team to continue using their preferred tools and take the lead on [data-driven strategy](#).

Free Resource: The HRIS Buyer's Guide

Choosing an HRIS is a big decision. To help, BambooHR created an in-depth guide that provides a comprehensive overview of what makes an HRIS all-in-one—plus tips on how to choose the right HRIS for your organization.

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HR CONSULTING VS. A PEO

If you need the advice and support of HR experts but are a little nervous about the level of control you'd be giving to a PEO, an HR consulting firm is an excellent resource.

Like other types of consultants, an HR consultant can advise you on how to make your HR process more efficient and effective, and provide select HR services to your company.

Sometimes this is called HR outsourcing, so pay close attention to whether an HR outsourcing group is offering its services as a PEO or a regular consulting firm.

The biggest difference between HR consulting and a PEO is that a PEO becomes an employer of record, while an HR consultant is a regular service provider and doesn't take responsibility for your workforce. Additionally, an HR consulting firm will probably only focus on specific HR support services, whereas a PEO could serve as your entire HR apparatus.



Here are some examples of services an HR consulting firm might offer:

- Audit your HR department
- Assist with compliance issues
- Create or review internal policies
- Manage or review payroll processes
- Analyze benefits packages
- Assess and advise on employee engagement

How to Switch From a PEO

Thinking about transitioning away from a PEO? Making the switch can feel intimidating, but with the right tools and support, you can smoothly implement your own internal HR processes.

Once you decide to switch from a PEO, you'll need to make sure you have an in-house HR pro to help with the transition. If you don't already have an internal HR team, aim to hire an HR pro at least six months before you make the switch.

You'll also need to assess your HR tech stack. After you part ways with the PEO, you'll have to choose tools for things like payroll and benefits administration. If you don't already have an all-in-one HRIS, now's the time to **start shopping.**

As you research all-in-one HRIS options, look for a vendor that offers in-depth implementation services and has experience supporting clients who've also switched from a PEO. A vendor that understands the transition process can give you an easy implementation roadmap and provide thorough assistance **along the way.**



An Award-Winning, Complete HR Platform

In BambooHR, everything works together to help you manage data and benefits, hire talent, run payroll, and help employees thrive. Best of all, it's easy and intuitive for busy HR teams!

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