

Sommet raid put HR firms in spotlight

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For businesses that have entrusted their human resources functions to third party companies like Sommet Group, last week's raid and federal allegations of fraud set off alarm bells.

But for the growing number of businesses use professional employee organizations like Franklin-based Sommet, experts say there are steps companies can take to protect themselves and their employees. Meanwhile, other industry players are scrambling to reassure their own customers that their practices are above board and limit collateral damage.



Whitfield

Professional employee organizations were the fastest growing business service in the U.S. during the 1990s, according to a *Harvard Business Journal* article in early 2002, and the industry continued to grow at a rate of 30 percent a year. Small businesses hire them to become the "employer of record" for employees. The organizations then handle functions like payroll, benefits and other human resources functions — while taking advantage of scale to be able to deliver less expensive services.

Milan Yager, president and CEO of **Human resources | 39**

the National Association of Professional Employee Organizations, said the industry is now valued at \$69 billion a year, includes about 700 companies and provides benefits to about 3 million American workers. The average customer is a small business with 17 employees.

"This is a huge industry that generally operates well," Yager said. "But in

any new industry, there are potential for bad players."

According to the Internal Revenue Service, Sommet Group was allegedly one of those players.

Federal agents raided Sommet's Cool Springs offices last week, alleging in a search warrant that the company, principally through managing partner Brian Whitfield, lied about where client money was going. Since last year, businesses that contracted with Sommet to handle services such as payroll, insurance benefits and retirement plan contributions began to discover that their obligations were not being met, according to the federal affidavit. In 2009 and 2010, Sommet Group had 778 unpaid health insurance claims totaling \$776,000, according to the affidavit, and as of June 23, "the amount of Sommet's unpaid medical and pharmacy claims had increased to \$2.1 million." The company had more than 100 clients.

The troubles arose from Sommet Group's underlying business plan, according to the affidavit, which was to charge below-market health premiums to undercut competitors, and make up the shortfall with the payroll fees it charged.

According to the affidavit, which was based in part on statements a former Sommet executive provided to an IRS investigator, the model only worked if Sommet kept signing new clients.

Bill Hutter, CEO of Columbus, Ohio-based professional employer organization Sequent Inc., which has an office in Cool Springs, said Sommet's prices should have been considered a warning sign. "Product is product. Insurance carriers are going to determine what happens (with price)," Hutter said.

Hutter said he expects to lose clients as a result of the Sommet controversy. Leslie Garrett-Stephens, senior director of business development at XM Human Resource Solutions in Nashville, said the company was in contact with customers in an attempt to quell concerns.

"They had a name on the arena and all of a sudden they blew up and disappeared," Hutter said of Sommet.

Yager said up-front work can minimize the danger for clients. He noted that Sommet Group was not a member of the National Association of Profes-



sional Employer Organizations, which represents 350 companies representing 90 percent of the industry.

Yager said businesses should also check to see if outsourcers have staff members who are members of the Society of Human Resource Professionals. Art Smith, president of the Middle Tennessee chapter, said Whitfield was not, but that he couldn't say for certain whether other Sommet Group employees were.

Both Yager and Hutter said the gold standard in the industry is accreditation by the Employer Services Assurance Corporation, which requires stringent quarterly reporting requirements and provides an \$11 million surety bond. It's the industry's equivalent of the FDIC for banks, Yager said.

"If you want a rock solid guarantee, that is one," Yager said.

Charles Grant, a Nashville employment attorney at Baker Donelson Bearman Caldwell & Berkowitz, said he also would advise clients to run a background check on the people who run a professional employer organization. In 2003, Whitfield sued DigiScript for wrongful termination, and the company countered by accusing Whitfield of fraudulent and inappropriate activities, according to *Nashville Business Journal* archives. The suit was settled out of court.

"I would think some of those customers would have had second thoughts if they knew that the managing principal was involved in some litigation," Grant said.

The ins-and-outs of outsourcing your HR functions

Businesses should follow these guidelines when considering whether to hire a professional employer organization, or PEO, a firm that allows clients to outsource functions such as human resources, employee benefits, payroll and workers' compensation:

- **Assess your workplace** to determine your human resource and risk management needs.
- **Make sure the company is capable of meeting your company's goals.** Meet the people who will be serving you.
- **Ask for references.**
- **Investigate if the company has a history of adherence to the industry's professional performance practices.** Check to determine if the PEO's financial statements are independently audited by a certified public accountant, whether their risk management practices have been certified by the Certification Institute, or if their operational, financial, and ethical practices have been independently accredited by Employer Services Assurance Corporation.
- **Check to see if the company is a member of the National Association of Professional Employer Organizations, the trade group for the industry.** A

searchable database is available at napeo.org.

- **Investigate the company's administrative and management expertise and competence.** What experience and depth does their internal staff have? Does the PEO corporate staffing allocation follow the priorities of the PEO's marketed services? Does their senior staff have professional training or designations?
- **Understand how the employee benefits are funded.** Is the PEO fully insured or partially self-funded? Who is the third-party administrator or carrier, and is it authorized to do business in your state?
- **Understand how the employee benefits are tailored.** Determine if they fit the needs of your employees.
- **Review the service agreement carefully.** Are the respective parties' responsibilities and liabilities clearly laid out? What guarantees are provided? What provisions permit you or the PEO to cancel the terms of the contract?
- **Make sure that the company meets all state requirements.**

Source: *National Association of Professional Employer Organizations*; for more information, visit www.napeo.org.