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A Strategic Guide For New York State PEOs In Workers' Compensation Coverage Claims

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Commentary

A Strategic Guide For New York State PEOs In Workers' Compensation Coverage Claims

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[Editor's Note: Dustin W. Osborne is a partner at Goldberg Segalla LLP, where he co-chairs the firm's Professional Employer Organization (PEO) group. He focuses his practice on workers' compensation defense and subrogation strategy, with an emphasis on matters in New York and Georgia. He regularly advises national employers and PEOs on multistate compliance, risk management, and emerging trends in workers' compensation law. Any commentary or opinions do not reflect the opinions of Goldberg Segalla LLP or LexisNexis® Mealey Publications™. Copyright © 2025 by Dustin W. Osborne. Responses are welcome.]

I. Overview

A Professional Employer Organization (PEO) is a burgeoning way to provide comprehensive HR services to growing small and medium-sized businesses that are otherwise not suited to sustain a comprehensive HR department in-house. In simplest terms, PEOs are in the business of sharing employment responsibilities in exchange for an agreed upon fee or fees.

The PEO and its clients have different roles and responsibilities. Whereas the PEO is generally responsible for administrative functions such as securing insurance, payroll, taxes, and other traditional HR tasks, the client does not lose control of its employees. The PEO does not typically take over managing or directing the employees on a day-to-day basis; that remains the function

of the client, otherwise known as the “work site employer.” By this design, the covered employees have two employment relationships and are considered “co-employees of the PEO and the work site employer.” To illustrate this point a bit further, the co-employees may have identification and/or t-shirts bearing the work site employer's logo (e.g. “Senoia Construction Co.”), but their paychecks will be drawn on the PEO's account (e.g. “Stark HR”).

Once the client and PEO successfully execute a PEO contract, the client provides the PEO with the information for the workers it wants the PEO to “hire.” The workers will fill out new employment paperwork – including W9's and supply proof of eligibility to work in the United States as if they are starting a new job – and the “co-employment” relationship is consummated.

One of the primary responsibilities of the PEO is to secure an insurance policy that will cover the co-employees, or “covered/leased employees”, for work-related injuries. The named insured in the policy is “Stark HR l/c/f Senoia Construction Co.” The “l/c/f” designation stands for “labor contractor for.” The New York State Compensation Insurance Rating Board (CIRB) instructs insurers to include an endorsement, “The New York State Optional Labor Contractor Endorsement,” in the l/c/f policies that limits liability to covered employees. See Example 1.

Example 1.**WORKERS COMPENSATION AND EMPLOYERS LIABILITY INSURANCE POLICY**

WC 31 03 20

(Ed. 1-99)

NEW YORK OPTIONAL LABOR CONTRACTOR ENDORSEMENT

As used in this endorsement, employee leasing means an arrangement whereby an entity contracts with another entity to lease some or all of its workers. The entity providing the workers shall be referred to as the "labor contractor." The entity utilizing the workers shall be referred to as the "client."

This endorsement applies only with respect to bodily injury to the workers provided to the client identified in Item 1.A. of the Information Page and named in the Schedule below by the labor contractor identified in 1.A. of the Information Page under an employee leasing arrangement. This arrangement is for long-term leasing services, rather than for temporary help services to meet seasonal or short-term conditions.

This policy provides coverage for the workers leased to the client. Coverage for these leased employees may be provided by either the leasing firm or the client, which are both considered to be named insureds under this policy. This policy does not satisfy the client's duty for the complete payment of any obligations it may have under the workers' compensation law for nonleased employees or that the labor contractor may have for direct employees engaged by it.

Part One (Workers Compensation Insurance) and Part Two (Employers Liability Insurance) will apply as though the labor contractor is an insured.

Under Part One, we will reimburse the labor contractor named in Item 1.A. of the Information Page for the benefits required by the workers' compensation law if we are not permitted to pay the benefits directly to the persons entitled to them.

Part Four (Your Duties If Injury Occurs) applies to the labor contractor and client. The labor contractor and the client will recognize our right to defend under Parts One and Two and our right to inspect under Part Six (Conditions).

We will not ask any other insurer of the client to share losses with us covered by this policy.

We will charge premium for the workers leased to the client company by the labor contractor.

If we cancel the policy, we will send notice to the labor contractor and to the client at the address shown in the Schedule below.

The labor contractor will separately maintain payroll records needed to compute the premium for the workers leased to the client, to satisfy the obligations under Part Five (Premium). We will charge the labor contractor premium for workers leased to the client.

Schedule**Name of Client**

[REDACTED]

Address

[REDACTED]

PEOs are primarily regulated at the state level. Most states have some form of PEO licensing, registration, or regulation.

In the context of a work-related accident involving a covered employee co-employed by both entities, the case can be handled like any other generic workers' compensation claim subject to the conventional defenses of accident, notice, and causal relationship (or lack thereof). However, there are two scenarios in which a question of coverage and liability arise: (1) when the client/work-site employer hires and pays a worker without the PEO's knowledge or involvement; (2) when the client/work site employer subcontracts work to an uninsured employer and that entities' employee is injured at work.

II. New York Statutory Law

In New York, Article 31 of the New York Labor Law – commonly referred to as the "Professional Employer Act" – is the relevant statute. Article 31 section 922 of the New York Labor Law defines the relationship between the PEO and the client employer.¹ The employer generally recruits and hires its employees and contracts with the PEO to handle the payroll, taxes, and benefit packages for its employees. PEOs must be licensed by the New York State Department of Labor.

Currently, clients of PEOs may be covered by either of the following methods:

1. Each client of a leasing firm may procure its own workers' compensation insurance

policy to cover its leased employees (as well as any non-leased employees); or

2. The leasing firm can procure a separate workers' compensation insurance policy to cover the leased employees of each of its client firms. Such a policy would identify the insured as: ABC Leasing Company Inc. L/C/F XYX Machine Shop Inc. This policy only covers the leased employees of the client firm. If the client firm hires any non-leased employees (and/or wishes to protect itself from the claims of uninsured subcontractors working for it), the client firm must purchase a separate workers' compensation policy to provide coverage to individuals not specifically listed on their contract with the PEO.

As long as a professional employer agreement remains in force between a PEO and its client, the PEO shall pay wages and collect, report, and remit employment taxes of its worksite employees from its own accounts and secure and provide required workers' compensation coverage for its worksite employees either in its own name or its client's name. Labor Law § 922(3)(a)(c).

The New York Workers' Compensation Board has a dedicated web page addressing leased employees as well.² As indicated therein, the Board notes clients of PEOs may be covered either: (1) by each client of a leasing firm purchasing its own workers' compensation insurance policy to cover its leased employees, or (2) the PEO obtaining a workers' compensation insurance policy in the name of the client which would cover the leased employees only.

III. Application: Work-Related Injuries Sustained by Non-Leased Employees

While this scenario is uncommon, there are instances wherein a non-leased employee sustains a work-related injury; this most frequently occurs in the construction space. Typically, but not always, the worker is paid in cash and off the books. These claims are protested primarily on the grounds of no employer-employee relationship and no coverage.

When these claims arise, a few specific documents are necessary to establish the issue in controversy; these include: (1) a copy of the contract between the PEO and the worksite employer; (2) an exhaustive list/roster of the covered employees on the payroll on the date of accident (which needs to be redacted); (3) a copy of the l/c/f policy. These materials are submitted as attachments to our PH-16.2, along with preserving the right to produce a witness from the PEO to testify with respect to the coverage defense. To the extent that the PEO's interests are in alignment with the work site employer's (independent contractor, failure to provide timely notice, etc.) those defenses are preserved as well.

The statutory scheme of the Professional Employer Act provides the basis for defense:

- "Professional Employer Organization" means any person whose business is entering into professional employer agreements with clients. In determining whether the professional employer organization employs all or a majority of the employees of a client, any person employed pursuant to the terms of the professional employer agreement after the initial placement of client employees on the payroll of the professional employer organization shall be included..." N.Y. Lab. Law § 916 (4)³

- "Professional Employer Agreement" means a written contract whereby: (a) a professional employer organization expressly agrees to co-employ all or a majority of the employees providing services for the client; (b) the contract is intended to be ongoing rather than temporary in nature; (c) employer responsibilities for worksite employees, including those of hiring, firing, and disciplining, are expressly allocated by and between the professional employer organization and the client in the agreement; and (d) the professional employer organization expressly assumes the rights and responsibilities as required in section 922 of this article. N.Y. Lab. Law § 916 (3)⁴

- N.Y. Lab. Law § 922 (3)(c) requires that a professional employer organization provide workers' compensation coverage for its worksite employees either in its own name or its client's name.⁵

- “Worksite employee” means a person having an employment relationship with both the professional employer organization and the client. Such term may also include the client’s officers, directors, shareholders, or partners to the extent such persons act as operational managers or perform services for the client. N.Y. Lab. Law § 916 (6)⁶

Over the past several years and notwithstanding the aforementioned statutory provisions, the Board has resolved a number of claims in which a PEO has contested liability for injuries sustained by individuals that the work site employer hires without the PEO’s involvement. Ultimately, the Third Department of New York has established that by providing the insurance policy, the client leasing agreement, an exhaustive list of all covered employees, and testimony from the PEO, the PEO can meet its burden to have a non-leased employee excluded from its policy. However, it should be noted that the New York Workers’ Compensation Board continues to chip away at this law and, thereby, a PEO’s protections. The four seminal Third Department cases thus far are *Matter of Gaylord*, *Matter of Cardona*, *Matter of Brown*, while the Board Panel Decision Judges in New York keep relying upon – much to the chagrin of PEOs everywhere – is *Matter of Chateau GC LLC*.

A. *Matter of Gaylord v. Buffalo Transportation*⁷

Summary: The Third Department affirmed the Workers’ Compensation Board’s finding that the PEO’s carrier was liable for the claimant’s injuries, holding that the claimant was a statutory employee of the PEO under Labor Law §§ 916(6) and 922(4). Rejecting the carrier’s argument that the claimant was excluded as a non-leased employee, the Court found the policy covered leased employees broadly, and the PEO failed to provide sufficient evidence that the claimant was not one.

Key Takeaway: While the Court ruled against the PEO, it implicitly established a framework for successfully contesting coverage in future cases – suggesting that, with the right evidence, a PEO can overcome liability for non-leased employees.

B. *Matter of Cardona v. DRG Constr. LLC*⁸

Summary: The Court found that, while the employee list provided by the PEO did not include the claimant’s name, there was no accompanying affidavit or testimony establishing that the list was complete or that it limited the policy’s scope. Without that proof, the PEO failed to meet its burden of demonstrating the claimant was not covered.

Key Takeaway: When read in tandem with *Gaylord*, *Cardona* helps establish a clear evidentiary test: a PEO must submit its insurance policy, leasing agreement, exhaustive employee list, and credible testimony to prove a claimant is a non-leased worker excluded from coverage.

C. *Matter of Chateau GC LLC*⁹

Summary: While purporting to apply *Gaylord* and *Cardona*, the Board Panel in *Chateau* imposed a significantly stricter standard on PEOs. The Panel held that: (1) the client must obtain separate coverage for non-leased employees; (2) the PEO and its carrier must ensure the client obtained such coverage and document who is leased at all times; and (3) absent this, the injured worker will be deemed a leased employee unless the PEO and carrier provide: (i) proof they demanded coverage documentation from the client, (ii) a date-specific employee roster, and (iii) evidence that the list was incorporated into the policy.

Key Takeaway: Though non-binding, *Chateau* has become a recurring obstacle at the trial and Board Panel levels, effectively shifting the burden to PEOs to monitor client compliance with their own insurance obligations. This creates a near-impossible practical burden for most PEOs, and yet it remains a frequently cited decision in coverage disputes, pending appellate or legislative correction.

D. *Matter of Brown v. Buffalo Transp., Inc.*¹⁰

Summary: Relying upon the backdrop of *Gaylord* and *Cardona*, the Third Department in *Brown* found that the PEO had satisfied the prongs of *Gaylord* by providing the policy, cli-

ent leasing agreement, list of leased employees, and testimony on behalf of the PEO. While some deficiencies were found pertaining to the comprehensiveness of the list, the testimony provided was sufficient to overcome said issues. Ultimately, given the standard was met, the Third Department affirmed the decision to find that the non-leased claimant was not covered by the PEO policy.

Key Takeaway: *Brown* is a seminal case for PEOs, demonstrating that, with strong documentation and a well-prepared witness, they can defeat coverage for non-leased employees. While the decision did not directly address *Chateau*, it offers a much-needed blueprint for defense and perhaps a soft counterbalance to *Chateau*'s overreach.

IV. Strategic Considerations Post-*Brown*

The Third Department's evolving case law – particularly *Gaylord*, *Cardona*, and *Brown*—has clarified the evidentiary framework governing PEO liability for injuries sustained by non-leased employees. At the same time, decisions like the Board Panel's *Matter of Chateau* ruling demonstrate that the Workers' Compensation Board continues to impose aggressive expectations on PEOs, often extending obligations beyond what is practicable or contemplated by the statute.

Together, these cases underscore the need for proactive compliance and defensive positioning by PEOs operating in New York. As a result, here are the key strategies to keep in mind:

1. Maintain Clear and Comprehensive Leased Employee Rosters

- a. Maintain an exhaustive, date-specific list of leased employees for each client.
- b. Ensure the list is readily available and regularly updated as employees are onboarded or terminated.
- c. Where possible, incorporate this list by reference into the PEO's workers' compensation insurance policy.

2. Review and Strengthen Client Leasing Agreements

- a. Clearly delineate in the client leasing agreement which employees are being leased.

- b. Include a provision requiring the client to obtain separate coverage for all non-leased employees.

3. Document Due Diligence on Client Compliance

- a. Retain records of all communications with the client regarding coverage obligations.
- b. If feasible, formally request proof from clients that they have secured coverage for any non-leased personnel.

4. Be Prepared to Litigate the Coverage Defense

- a. Ensure that the PEO can present a witness with direct knowledge of the leasing arrangement and employee onboarding process.
- b. Submit the following with any PH-16.2 where coverage is disputed:
 - i. The executed client leasing agreement.
 - ii. The PEO's workers' compensation policy.
 - iii. A redacted, date-specific list of leased employees.
 - iv. An affidavit regarding the claimant's employment status from the PEO's perspective.
 - v. The name of someone who can provide testimony on behalf of the PEO.

5. Anticipate Board-Level Resistance

- a. Even when the evidentiary standard outlined in *Brown* is met, the Board Panel may still rely on *Chateau* to stretch PEO liability.
- b. PEOs and their counsel should be prepared to appeal unfavorable decisions, particularly where Board interpretations exceed statutory obligations.

The recent case law provides PEOs with a viable path to avoid liability for injuries sustained by non-leased workers but only if the evidentiary foundation is strong. To protect against unwarranted exposure, PEOs must treat coverage compliance as a core operational priority, embedding documentation, client communication, and insurance coordination into their day-to-day risk management strategy.

Endnotes

1. <https://law.justia.com/codes/new-york/2015/lab/article-31/922>
2. <https://www.wcb.ny.gov/content/main/coverage-requirements-wc/leased-employees.jsp>
3. <https://dol.ny.gov/system/files/documents/2021/03/article-31-nys-professional-employer-act-ls667.pdf>
4. Id.
5. Id.
6. Id.
7. 195 A.D.3d 1200 (3d Dep't 2021)
8. 196 A.D.3d 388 (3d Dep't 2021)
9. 2022 NY Wrk Comp G2581160 (2022)
10. 219 A.D. 3d 1096 (3d Dep't 2023) ■

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