Paycards: Flexible Electronic Payroll for All Employees

An overview of payroll card benefits and considerations for employers

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Who Are the Unbanked?

Surveys of consumer banking show that some employees have limited or no access to a checking or savings account. According to recent studies, unbanked or under-banked householders were more likely to be:

- ***Younger*** *– Over 56% were younger than 45.*[5]
- ***Lower income*** *– The average amount of a paycheck cashed by check cashing services is $500-$600.*[6]
- ***Minority*** *– 46% of U.S. born black householders and 34% of U.S. born Hispanic householders were unbanked.*[7]
- ***Immigrants*** *– 53% of immigrants from Mexico, 37% from Latin America, and 20% of Asian immigrants were unbanked.*

Introduction

U.S. businesses have recently enjoyed tremendous savings in payroll production costs by encouraging employees to accept direct deposit over paper paychecks. According to the American Payroll Association, businesses pay between one and two dollars to issue each paper paycheck. Conversely, an electronic transfer of payroll costs about twenty cents per employee.[1] Based on these statistics, a company with 300 employees paying $2 per bi-weekly paper paycheck could enjoy an annual savings of over $14,000 if all employees received paperless electronic payroll!

The employee adoption rate for direct deposit has been very high. Of the nearly 30,000 employees who responded to the 2005 American Payroll Association survey, "Getting Paid in America", 71% were paid by direct deposit. According to the National Automated Clearing House Association (NACHA), direct deposits for payroll, benefits, and expense reimbursements increased 5.5% in 2006 with approximately 4.7 billion direct deposits recorded.[2] That results in considerable savings for U.S. businesses. However, one key challenge remains—extending the savings of paperless payroll to employees who have no bank account to accept a direct deposit, despite the trend toward electronic payments.

The Challenge: Electronic Deposit for Employees without Banks

"Unbanked" employees have neither a checking nor a savings account. Because they lack a relationship with any financial institution, these employees generally rely on check-cashing businesses to convert their paychecks to cash. Check-cashing services typically charge one to six percent of the value of every paycheck to cash it. Unbanked employees must then pay monthly bills in cash or by purchasing money orders, payment services, or wire transfers.

How big is the unbanked population in the United States?

According to the most recent Survey of Consumer Finances completed by the Federal Reserve, 10.6 percent of US families do not have a checking account.[3] According to research firm BearingPoint, more than 28 million people in the US are unbanked, with another 44.7 million classified as "underbanked," meaning they have little access to financial services.[4]

Some types of businesses tend to have larger numbers of unbanked employees than others. These industries include retail, hospitality, delivery services, temporary staffing, landscaping, construction, and some parts of the manufacturing sector.

Paycards: The Electronic Payroll Solution

Many employers are using paycards to offer employees an alternative to paper paychecks and direct deposit. Paycards, also known as payroll cards, are plastic, stored-value cards that work like debit cards. Over $6 billion was placed on payroll cards in 2005. The use of payroll cards is expected to grow to $17 billion by 2009.[8]

For employees, the payroll card is a familiar concept that is easy to adopt. Conceptually, they are similar to prepaid phone cards or gift cards—products that most employees, banked or unbanked, have used. But unlike a gift card, the payroll card can be used anywhere that accepts debit cards, including ATM machines, retail point of sale checkouts, and online.

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[1] Sherrie L. W. Rhine and Sabrina Su, "*Stored Value Cards as a Method of Electronic Payment for Unbanked Consumers*," Office of Regional and Community Affairs, Federal Reserve Bank of New York, 2005, pp. 10-11.

[2] "NACHA Reports Nearly 16 Billion ACH Payments in 2006," *press release*, April 16, 2007.

[3] Brian K. Bucks, Arthur B. Kennickell, and Kevin B. Moore, "*Recent Changes in U.S. Family Finances: Evidence from the 2001 and 2004 Survey of Consumer Finances*," United States Federal Reserve Board, 2006, pp. A12-A15.

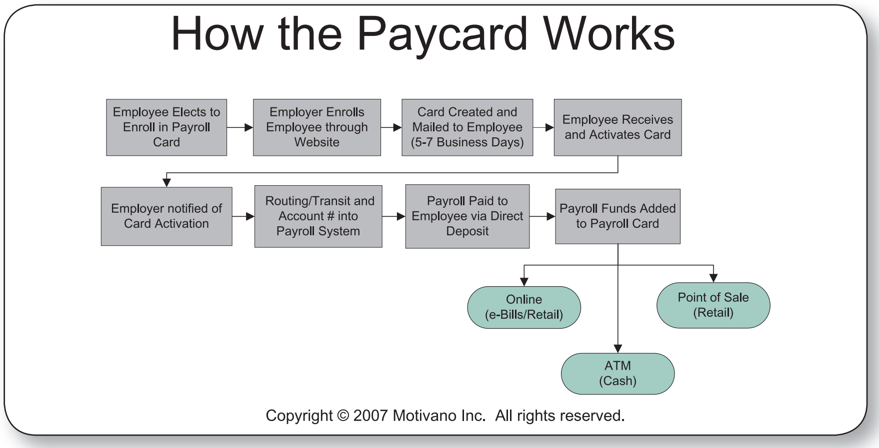
[4] Maria Bruno-Britz, "Targeting the Banked and Underbanked with the Right Solutions," *Bank Systems & Technology*, July 28, 2006.

[5] Brian K. Bucks, Arthur B. Kennickell, and Kevin B. Moore, "*Recent Changes in U.S. Family Finances: Evidence from the 2001 and 2004 Survey of Consumer Finances*," United States Federal Reserve Board, 2006, p. A15.

[6] Mark S. Gottlieb, CPA "*Check Cashing: An Industry Study*," 2006. Accessed online 8/8/2007 at http://msgcpa.com/files/check%20cashing.pdf

[7] Sherrie L. Rhine and William H. Greene, "The Determinants of Being Unbanked for U.S. Immigrants," *Journal of Consumer Affairs*, summer 2006, Vol. 40 Issue 1, p. 21-40.

[8] W. Gregory Kerwick, "Payroll Card Best Practices Cut Costs and Time," *Benefits & Compensation Solutions*, January/February 2007, pp. 42-43.



Advantages of Paycards to Businesses

For employers, paycards work exactly the same way that direct deposit does. A paycard program blends into your existing payroll process and requires no additional systems, software, or hardware. Companies simply enroll in the paycard service. Employees then have a choice to enroll in the paycard program and receive all or a portion of their paycheck using the paycard. The paycard is assigned a routing/transit and account number that is entered into the employer's payroll system. The paycard provider issues the card, delivers it to the employee, and notifies the employer of paycard activation.

For businesses, the primary advantage of paycards is the immediate elimination of costs associated with producing paper paychecks. This savings can equate to more than $1 per employee, per pay period. By reducing or eliminating the need to issue paper paychecks, companies save the cost of:

- Paper check forms
- Paycheck window envelopes
- Ink or toner used in the check printing process
- Postage or overnight shipping fees to send checks to multiple business locations

Additionally, as many as four million paychecks are lost and stolen each year, costing U.S. businesses approximately $48 million annually.[9] The average cost to replace a paycheck is $8 to $10, according to the American Payroll Association.[10] Moving to paycards can reduce or eliminate stop payment fees to banks. When a lost or stolen paycard is reported by an employee, it can be immediately deactivated and a replacement issued. Furthermore, most card associations protect the cardholder from unauthorized use of their card or account information. In most instances, cardholder liability for unauthorized transactions is zero.

In summary, the advantages paycards offer employers include:

- **Reduce payroll processing costs** – Employers can reduce costs associated with paper-based payroll by more than 85%.[11]
- **Eliminate stop payment fees for lost/stolen checks** – The process of replacing a paper paycheck costs an employer $8-10 per check, on average.
- **Easy delivery of final pay to terminated employees** – Employers no longer have to have terminated employees come to the office to pick up their last paycheck and they avoid overnight delivery fees if shipping the final paycheck.
- **Eliminate employer escheatment liability** – In many cases, escheatment liability is passed on to the financial institution holding the employees' funds.
- **Minimize check fraud**
- **Improve employee satisfaction and retention**

Paycards are popular with many employees.

Although unbanked employees primarily use payroll cards, more than ten percent of paycard users also have bank accounts. Paycards first became popular with long-haul truckers who were often far from their home-town banks when payday rolled around. And paycards are popular with temporary employees, who work at different locations and times, and find it inconvenient to travel to the staffing agency to collect their paycheck.

A growing number of employees using direct deposit are also adopting paycards. Some employees use paycards to distribute money to relatives on a budget, such as college-aged children. Others use their paycards to carry their spendable 'fun money' safely. Keeping a separate paycard for disposable income can help them stay within their monthly budgets.

[9] Dee Nelson, "Payroll Cards: Fixture or Fad?" *Direct Deposit Directions*, October 2005, pp. 62-63.

[10] Jane J. Kim, "Employers Offer Prepaid Cards for Workers to Tap," *Wall Street Journal*, February 11, 2004.

[11] Kerwick.

Advantages of Paycards for Employees

Employees enjoy an immediate savings when they use paycards. Unbanked employees can eliminate substantial fees they currently incur for check-cashing, money order, and bill payment services. A 2005 study by the Federal Reserve Bank of New York compared the annual costs of employees using paycards, checking accounts and check-cashing services. The study modeled expenses based on employees with low, moderate, and high transaction volume. In every case, paycards yielded significant savings over check-cashing services charging 5% fees.[12]

Annual Costs by Transaction Pattern			
Type of Financial Services	***Low***	***Medium***	***High***
Paycard with no monthly fee, some transaction fees	$101.64	$168.60	$249.96
Checking Account with average fees	$115.54	$159.22	$193.07
Check-cashing with 5% fees	$789.00	$789.00	$789.00
Savings of Paycard over Check-Cashing	***$687.36***	***$620.40***	***$539.04***

Other advantages to employees

In addition to affordable access to their pay, employees enjoy a number of conveniences with paycards. Some of the employee advantages of using paycards are:

- **24x7 Access to Funds** – Employees do not have to worry about getting to a bank or check-cashing service during business hours.
- **No waiting in line** – Employees save time and expenses that would otherwise have been spent making trips to financial institutions, or to pay bills.
- **Safety & Security** – A paycard allows employees to have access to their pay without carrying large amounts of cash on their person.
- **Easy to make purchases** – Paycards work like debit cards, which are accepted nearly everywhere. In fact, an employee will find that they can use their paycard at many retail locations that would not accept a personal check.
- **On-time pay no matter what** – In a natural disaster or other unforeseen event, employees still receive pay. Paycards eliminate the need to visit the employer's location.
- **Can be combined with direct deposit** – Employees can opt to receive only a portion of their pay on a paycard, while the rest is directly deposited into their bank account. Employees can give the paycards to relatives on a budget, or use them to spend and track disposable income, while paying regular monthly bills from their bank account.

Successful Implementation of a Paycard Solution

There are several things employers must consider when implementing paycard programs. Decisions need to be made about the structure of the paycard solution, and a plan developed for encouraging employee adoption.

Choosing a paycard provider

Companies should choose paycard providers that they trust and who are known to be financially sound. Research the history and financial stability of providers. Other factors that affect the selection of a paycard provider include:

- ease of implementing the program
- employee educational support
- flexible paycard program configuration
- fee structures for both employers and employees

[12] Rhine and Su, pp. 20-21.

- 24/7 account access via online, IVR and live agent support
- employer and employee customer service
- multi-language capabilities
- size of the participating network of ATM and point of sale locations

Structure of employer payroll bank accounts

The bank accounts associated with the paycards can be structured in one of two ways. In the first structure, all payroll for a company is transmitted to one pooled account, with sub accounts contained for each employee. The pooled account method allows businesses to create just one transaction to transmit the entire payroll. But placing money in a single, pooled account also limits the FDIC insurance on your entire payroll to $100,000.

Alternatively, separate accounts may be set up for each employee, with separate deposit transactions for each. This set-up provides FDIC insurance for each account, up to $100,000, protecting each employee.

Branded vs. unbranded paycards

Paycards can be branded by Visa®, MasterCard®, Discover®, or a similar card association logo. These cards are usually personalized and can be signature based, allowing employees to sign for purchases, as well as use a PIN code. Transactions are debited and posted to the account in real time. Paycards are not credit cards—they are not attached to a line of credit. Paycards, along with credit cards, are accepted at any location that has a merchant account with the cardholder's association. Unbranded paycards are not personalized to the employee and function only by the use of a PIN code at ATM machines or stores that accept PIN-based cards. Non-personalized cards, which can be issued instantly, historically have a higher incidence of internal fraud associated with them. A branded card takes longer to produce, but offers the benefit of being more secure while also providing access to point of sale and online transactions.

Typical Fees

Both employers and employees will incur some fees in setting up and using paycards. Some fees that might be charged to employees include: monthly fee, transaction fees, ATM surcharges, POS fees at stores, inactivity fees, replacement fee for lost/stolen card, or load fees when funds are placed on the card. Employers typically incur a set-up fee and a monthly fee. Many states have laws that require employers pay employees "without discount", meaning that employees do not have to pay to receive their paychecks. In reaction to these laws, many paycard providers allow card holders to withdraw their entire paycheck in one fee-free transaction.

Employee Education and Adoption

Employers need to develop a program for employee education that will ensure successful adoption of paycards. This education should include the benefits of both paycards and direct deposit to checking accounts as well as an explanation of the cost savings associated with each. To make the program work, offer training on-the-clock during business hours. Make the training mandatory, even if your paycard program is not. Use paper enrollment forms if employees find online or telephone enrollment prohibitive.

Finally, businesses must consider federal and state regulations pertaining to paycards in each of their business locations, as well as current paycard compliance issues.

Paycard Adoption for Non-English Speakers

Keep in mind that some employees may have cultural resistance to banks. Non-U.S. born employees have often come from countries in which banks were unreliable, frequently bankrupt, or even where assets were easily confiscated by the government.[13] *They may not fully understand the American banking system, or the protection that FDIC insurance offers to checking and savings account holders. Employers should obtain or create educational materials in Spanish, with illustrations, if they have non-English speaking employees. Companies might wish to select a paycard issuer that employs Spanish speaking customer service representatives.*

[13] Kathryn Tyler, "Financial Fluency," *HR Magazine*, July 2006.

Federal and State Compliance Considerations for Employers

The use of paycards and types of statements issued to employees about financial payroll transactions are topics for both federal and state labor and wage regulations. This is a rapidly changing area of compliance, as state labor departments and legislatures try to update existing payroll laws to address paycard technology. It is important for businesses implementing a paycard program to look up the most current federal regulations as well as those in each state where workers are employed. **As of the writing of this guide, in August 2007, the following federal and state regulations apply to paycards:**

Regulation E (Electronic Funds Transfer Act) – This Federal Reserve Board regulation governs electronic fund transactions. As of July 1, 2007, Regulation E (REG-E) was amended to cover payroll cards, whether issued directly or indirectly by employers. It also grants financial institutions flexibility for periodic statements. Institutions are not required to provide paper periodic statements to consumers if the institution makes account transaction information available via phone and electronically. Upon customer request, they must make the information available in writing.[14]

State Regulations – Some states expressly prohibit the use of paycards, others allow it, and still other states have made no rulings or legislation whatsoever. Most states with pending bills involve a debate over whether paycard vendors must notify paycard users if the terms of the paycard agreement is changed, and/or obtain their consent. States also have varying requirements about whether employers must provide printed statements for payroll, or simply access to this information electronically.

Use of Payroll Cards	
States prohibiting payroll cards	Vermont, West Virginia
States with specific legislation allowing payroll cards.	Delaware, Maine, Maryland, Michigan, Kansas, Minnesota, New Hampshire, Nevada, North Dakota, Oklahoma, Oregon, and Virginia
States with bills pending concerning payroll cards.	Arkansas, Iowa, New Jersey, Vermont, Montana, and New York

Employers Issuing Paper Payroll Statements	
States requiring employers to issue a printed statement. (E-statements may be acceptable if employees agree to receive them.)	California, Colorado, Connecticut, Hawaii, Minnesota, New Mexico, North Carolina, Texas, and Vermont.
States allowing businesses to issue electronic statements.	Arkansas, Florida, Iowa, Louisiana, Mississippi, Nebraska, South Dakota, Tennessee, and Virginia.

The information above is current as of July 1, 2007.

[14]Ed Maldonado, "Regulatory Rundown: Telecom, Money Services, and Payroll Cards," *The Prepaid Press*, July 18, 2007. Accessed online 8/8/2007 at www.prepaid-press.com

Summary

With potential savings of $20-50 annually per employee, businesses have ample motivation to encourage their workers to accept electronic paper-less payroll, in the form of direct deposit or payroll cards. However, in some industries, more than one-third of a business' employees may lack bank accounts, creating an obstacle to direct deposit. By offering paycards, employers can help unbanked employees enjoy the flexibility and security of a debit card containing payroll.

In addition to the savings this arrangement affords the employer, the employees also benefit from an immediate reduction in costs associated with financial services received outside of a banking arrangement, such as check-cashing. Many employees will save more than $500 annually by avoiding such services with the use of a paycard.

When implementing a new paycard system, businesses must plan carefully in order to select the appropriate card features and structure, choose a reliable card issuer, and educate employees to encourage adoption of the paycards. Additionally, attention must be paid to federal and state regulations concerning the use of paycards and the issuance of electronic payroll statements. Rules can vary from state to state, as labor legislation is updated to include payroll cards.

About the Sage Payroll PayCard

With the Sage Payroll PayCard, you can offer your employees 24/7 access to funds, safety and security, on-time payment no matter what (e.g., employees on vacation or sick leave, remote employees, etc.), elimination of time-consuming trips to the bank and more. For your company, the Sage Payroll PayCard is an alternative to paper paychecks and direct deposit, and can be offered as an additional benefit to employees. The Sage Payroll PayCard is easy to implement since it works the same way as a direct deposit transaction. The program blends into your existing payroll process and requires that no additional systems, hardware or software be installed. With the Sage Payroll PayCard, you can save money while offering your employees additional benefits and convenience.

About Sage Software

Sage Software supports the needs, challenges and dreams of nearly 2.8 million small and mid-sized organizations in North America through easy-to-use, scalable and customizable software and services. Our products support accounting, operations, customer relationship management, human resources, time tracking, merchant services and the specialized needs of the construction, distribution, healthcare, manufacturing, nonprofit and real estate industries. Sage Software is a subsidiary of The Sage Group plc, a leading international supplier of accounting and business management software solutions and related products and services for small and mid-sized organizations. Formed in 1981, Sage was floated on the London Stock Exchange in 1989 and the Group now has 5.4 million customers and employs over 13,000 people worldwide. For information on the Sage Payroll PayCard, visit our web site at **www.sagepayrollpaycard.com** or call **888-835-6244**.

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