

Paycards: Flexible Electronic Payroll for All Employees

An overview of payroll card benefits and considerations for employers.



The Sage Payroll PayCard white paper will address the following areas:

- Introduction..... 1

- The Challenge: Electronic Deposit for Employees without Banks 1
 - How big is the unbanked population in the United States?

- Paycards: The Electronic Payroll Solution 2
 - Who are the unbanked?

- Advantages of Paycards to Businesses 2

- Advantages of Paycards for Employees 3-4
 - Paycards are popular with banked employees
 - Other advantages to employees

- Successful Implementation of a Paycard Solution 5
 - Choosing a paycard provider
 - Structure of employer payroll bank accounts
 - Branded vs. unbranded paycards
 - Typical Fees
 - Paycard adoption for non-English speakers
 - Employee education and adoption

- Federal and State Compliance Considerations for Employers..... 6

- Summary 7



Introduction

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.

According to the National Automated Clearing House Association (NACHA), direct deposits for payroll, benefits and expense reimbursements increased by more than 475 million transactions in 2009, with approximately 18.76 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, 10.3 percent of U.S. families do not have a checking account.³ According to the Center for Financial Services Innovation, that equates to more than 9 million people in the U.S. being classified as unbanked, with another 21 million classified as “underbanked,” meaning they have little access to financial services.⁴ In total, the number of people without a traditional banking relationship is over 30 million.⁵

Some types of businesses tend to have larger numbers of unbanked employees than others. These industries include retail, hospitality, restaurant and transportation.⁶

- 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 18.76 Billion ACH Payments in 2009,” press release (<http://www.nacha.org/news/newsDetail.cfm?RecentBusinessNewsID/140>)
- 3 Brian K. Bucks, Arthur B. Kennickell, and Kevin B. Moore, “Changes in U.S. Family Finances from 2004 to 2007: Evidence from the Survey of Consumer Finances,” United States Federal Reserve Board, 2009, p. A21
- 4 Center for Financial Services Innovation, “Mobile Opportunities: New Customers and the Underbanked,” Feb. 23, 2010. (<http://www.federalreserve.gov/communityaffairs/national/2010mobile/presentations/Panel%203%20Jennifer%20Teschler.pdf>)
- 5 U.S. Census Bureau (<http://www.census.gov/main/www/popclock.html>)
- 6 Visa Payroll Card Info Sheet (http://usa.visa.com/download/corporate/corporate_solutions/payroll_product_large.pdf)

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.

Who are the unbanked?

According to recent studies, unbanked or under-banked householders were more likely to be:

- Younger: Over 56.3% were younger than 45.⁷
- Lower income: The average amount of a paycheck cashed by check cashing services is \$500-\$600.⁸
- Minority: 58.3% were nonwhite or Hispanic.⁹
- Immigrants: 53% of immigrants from Mexico, 37% from Latin America, and 20% of Asian immigrants were unbanked.

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.

Advantages of Paycards to Businesses

For employers, paycards work exactly the same way that direct deposit does. A paycard program works with any 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 have all or a portion of their paycheck deposited onto a paycard.

The paycard is assigned a routing/transit number, identical to the kind used for checking accounts, 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 \$2 per paycheck, per pay period, according to the Comptroller of the Currency.¹⁰ 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

7 Brian K. Bucks, Arthur B. Kennickell, and Kevin B. Moore, "Changes in U.S. Family Finances from 2004 to 2007: Evidence from the Survey of Consumer Finances," United States Federal Reserve Board, 2009, p. A21.

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

9 Brian K. Bucks, Arthur B. Kennickell, and Kevin B. Moore, "Changes in U.S. Family Finances from 2004 to 2007: Evidence from the Survey of Consumer Finances," United States Federal Reserve Board, 2009, p. A21.

10 Cathy S. Beyda, "A Greener Wage," HR Magazine, Vol. 55 No. 3, March 1, 2010

Additionally, as many as four million paychecks are lost and stolen each year, costing U.S. businesses approximately \$48 million annually.¹¹ The average cost to replace a lost or stolen paycheck is \$8 to \$10, according to the American Payroll Association.¹² 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, such as Visa® and MasterCard®, protect the cardholder from unauthorized use of their card or account information.

In summary, the advantages paycards offer employers include:

- **Reduce payroll processing costs** – Employers can reduce or eliminate costs associated with paper-based payroll.
- **Eliminate stop payment fees for lost/stolen checks** – The process of replacing a paper paycheck costs an employer \$8-10 per check, on average.
- **Free to employers**
- **Achieve 100% direct deposit**
- **Eliminate the costs and risks associated with paper checks**
- **Reduce the administrative burden of payroll processing**
- **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**

Advantages of Paycards for Employees

Employees enjoy an immediate savings when they use paycards. Unbanked employees can eliminate the substantial fees they incur for check-cashing, money order, and bill payment services. A study by the Federal Reserve Bank of New York compared the annual costs of employees using paycards 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.¹³

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
Check-cashing with 5% fees	\$789.00	\$789.00	\$789.00
Savings of Paycard over Check-Cashing	\$687.36	\$620.40	\$539.04

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

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

Paycards are popular with banked employees.

Although unbanked employees primarily use payroll cards, more than 10% of paycard users also have bank accounts. Paycards first became popular with long haul truckers who were often far from their hometown banks when payday rolled around. Paycards are also 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 family members they support financially, 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.

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 and 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.
- **Online payments** – Employees can book hotels, flights and rental cars.

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
- 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 \$250,000. 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 \$250,000, 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 may incur some fees in setting up and using paycards. Some fees that might be charged to employees include: monthly fee, transaction fees, ATM surcharges, point of sale 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 over-the-counter fee-free transaction per pay period.

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.¹⁴ 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.

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.

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 regulators. 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 January 2011, 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 January 2011, 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.¹⁵

State Regulations – Only one state, Vermont, prohibits the use of paycards. The other states view paycards as follows:

- States that expressly permit, or can be interpreted as permitting payroll cards: Alabama, Colorado, Delaware, Indiana, Kansas, Kentucky, Louisiana, Massachusetts, Maine, Missouri, Mississippi, Nebraska, North Carolina, Ohio, Oklahoma, South Carolina, South Dakota, Tennessee, Texas, Utah, Washington, Wisconsin.¹⁶

¹⁴ Kathryn Tyler, "Financial Fluency," HR Magazine, July 2006

¹⁵ Ed Maldonado, "Regulatory Rundown: Telecom, Money Services, and Payroll Cards," The Prepaid Press, July 18, 2007. Accessed online 8/8/2007

¹⁶ American Payroll Association (http://www.americanpayroll.org/pdfs/paycard/10d14-green_states_april_2010.pdf)

- States that expressly permit, or can be interpreted as permitting, employers to eliminate paper checks for some, but not all employees: ¹⁷
 - Florida – For new hires on or after 7/1/09
 - Iowa – For new hires on or after 7/1/05
 - Virginia – For new hires on or after 1/1/10
- States with bills pending concerning payroll cards: Arkansas, Iowa, New Jersey, Vermont, Montana, and New York.
- In the remaining states, direct deposit is permitted or the states do not regulate the method of wage payment.¹⁸

Summary

With potential savings of \$20-50 annually per employee, businesses have ample motivation to encourage their workers to accept electronic paperless 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.

¹⁷ American Payroll Association (http://www.americanpayroll.org/pdfs/paycard/10d14-green_states_april_2010.pdf)

¹⁸ American Payroll Association, "State Recognition of Payroll Debit Cards," June 2008, p. 5 (<http://legacy.americanpayroll.org/pdfs/paycard/APAPaycardGuide.pdf>)

About Sage Payroll PayCard

Sage Payroll PayCards are prepaid Visa cards designed to save your company money by reducing costs and making it easier for you to pay employees. They are easy to set up, providing your employees with 24/7 access to funds through ATMs or by making purchases wherever Visa debit cards are accepted. With the Sage Payroll PayCard, you can save money while offering your employees additional benefits and convenience.

About Sage North America

Sage North America is part of The Sage Group plc, a leading global supplier of business management software and services. At Sage, we live and breathe business every day. We are passionate about helping our customers achieve their ambitions. Our range of business software and services is continually evolving as we innovate to answer our customers' needs. Our solutions 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 North America employs more than 5,000 people and supports nearly 2.9 million small and medium size business customers. The Sage Group plc, formed in 1981, was floated on the London Stock Exchange in 1989 and now employs 14,800 people and supports 5.7 million customers worldwide.

The Sage Payroll PayCard is issued by CenterState Bank of Florida NA.

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