

Achieving Electronic Pay for All Employees

How to achieve 100 percent electronic pay while meeting
the needs of employees and remaining compliant
with state regulations

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Executive Summary

In today's competitive business environment, employers are continually looking for ways to save money, increase efficiency and improve productivity. However, many of the advances in technology that have automated business processes and optimized workflows have had minimal impact on the distribution challenges facing payroll managers at corporations across America.

Some of the most technologically adept businesses continue to struggle with age-old payroll distribution challenges that have a significant impact on their bottom line. From reducing the high costs associated with processing and distributing paper paychecks, to complying with state and federal regulations and working to avert fraudulent activities like counterfeit paychecks, organizations of all sizes are attempting to solve these challenges with solutions that don't fully meet their needs.

For many years the approach to payroll distribution has varied little: meet compliance regulations with a company-issued paper check and reduce payroll costs with an offer of voluntary direct deposit to employees with bank accounts. While this has been effective with a large portion of the employment base, it hasn't helped unbanked employees who represent almost 10 million U.S. households, according to the American Payroll Association.¹ By implementing a revolutionary new payroll distribution solution that meets state compliance requirements and the needs of unbanked employees, companies are on the verge of reaching the once unimaginable goal of 100 percent electronic pay.

Prepared for professionals tasked with managing corporate payroll systems, this paper examines the challenges of paper check solutions, electronic payroll distribution solutions, state compliance issues and inefficiencies created by unbanked employees. It also illustrates the benefits of choosing a payment distribution solution that meets state compliance requirements, the needs of the unbanked and the goals of the corporation.

¹ American Payroll Association. "Paycard Overview." July 30, 2008.
<http://www.payrollannex.org/paycard/paycardportal.cfm?pageid=2>.

Introduction

For many businesses, the cost of managing payroll is one of the single largest line items on the profit and loss statement.² Computerized payroll solutions, such as direct deposit, have brought a lot to the table in terms of improving efficiency and lowering costs. However, these solutions have offered little or no benefit toward containing the costs associated with actually processing and distributing paper-based payroll, which is still mandatory in many states. In fact, the expense for conventional paper paychecks only continues to increase. When considering that the cost of processing and distributing a single paper paycheck averages between one and two dollars per check,³ employers can hardly afford not to find an alternative. In addition to escalating payroll costs, traditional paper checks are increasingly subject to fraud.

While direct deposit programs designed to lower the costs associated with paper paychecks have gained traction in the past decade, employers struggle to convert all employees to electronic pay. An especially tough issue for employers is reducing the costs associated with processing paper checks for the “unbanked” employees who, by definition, are those people who lack any formalized transaction-based account, such as a savings, checking or money market account.

Challenges Facing Payroll Departments

One of the biggest problems facing employers is that payroll systems have not kept up with the pace of business. Here are just a few of the challenges payroll departments currently struggle with:

Unbanked employees

One of the most difficult payroll challenges for employers is the issue of unbanked employees. This part of the workforce is referred to as unbanked because they don’t have a formal relationship with a bank or other financial institution and they typically require a paper paycheck. Instead of depositing a paycheck into a savings or checking account, these workers usually cash paychecks at check-cashing services where they are required to pay a fee and carry their entire paycheck in cash with them.

In spite of the reasons unbanked employees have for resisting bank accounts, employers collectively spend millions of dollars each year on employee marketing campaigns that are designed to entice unbanked workers to join the ranks of electronic deposit programs (which require a bank account). The unfortunate and costly reality is that these efforts don’t convert unbanked employees simply because these workers don’t want bank accounts. Research shows that unbanked customers are often distrustful of banking institutions and that they harbor concerns about being charged fees for the banking relationship.⁴ Since a portion of the unbanked population can also be classified as underbanked (those that had relationships in the past) they are also painfully aware of service charges, minimum balances and non-sufficient funds (NSF) fees resulting from bounced checks for overdrawing accounts.

Payroll check fraud

With corporate crime on the rise in businesses all over the country, it’s no wonder criminals target payroll checks. After all, it’s where the easy money is. Employers are being hit particularly hard with the rising cost of check fraud, as the availability of advanced color printer products makes it easy for criminals to create and duplicate payroll checks.

² Robert E. Farina. “TI: Survey reveals top workforce-management priorities related to labor costs and customer satisfaction.” *Employment Relations Today* Vol. 33 No. 4; pg. 7-13. 2007.

³ Fitter, Fawn. “The End of the Paycheck.” *Fortune Small Business*. December 1, 2006.

⁴ Bernanke, Ben S. “Increasing Economic Opportunity: Challenges and Strategies.” Board of Governors of the Federal Reserve System. June 13, 2006. <http://www.federalreserve.gov/newsevents/speech/bernanke20060613a.htm>.

According to the Federal Trade Commission (FTC), check fraud will cost American businesses and banks an estimated \$50 billion in 2008 alone,⁵ and anybody with access to a personal computer, a scanner, and an off-the-shelf software program can create counterfeit corporate checks that the most seasoned CFO would have trouble spotting. Technology-savvy criminals can reproduce hundreds of realistic counterfeit or forged checks in a matter of hours if they have access to a single legitimate paycheck.

State payroll compliance laws

State and federal regulations pertaining to payroll solutions place additional financial and logistical strains on employers. For example, many state compliance laws mandate the necessity of a paper paycheck for employees. This can make it costly and difficult for employers operating in multiple states to have a single payroll solution yet remain compliant with the laws of the individual states in which they operate.

As of September 2008, 33 states require not only a paper check option but also free check cashing for payroll checks. This means that employers must establish a process to guarantee free check cashing for all their paychecks. For a geographically dispersed workforce this is a real challenge. Some states require a company to disburse "final pay" to employees by the next scheduled pay day, while other states mandate that final pay is paid on the day of termination. What this means for employers is that short of all 50 states standardizing payroll compliance regulations, payroll departments are currently limited in their ability to drive down payroll costs with a single pay distribution solution.

Transient workers

Another challenge facing payroll departments of U.S. corporations is the transient nature of our nation's workforce. On average, employees working at hourly-wage jobs change employers two to three times per year and frequently lack a permanent mailing address.⁶ For employers, this means higher payroll costs and increased complications due to state escheat laws, which cover unclaimed or abandoned paychecks. Escheat laws require that the funds from uncashed or unclaimed payroll checks be turned over to the state after a designated period. Even if an employee never claims the money or cashes the check, he or she is entitled to credit on Social Security and Medicare accounts for wages earned. For unemployment benefit and tax purposes, wages must also be reported as paid by the employer. Further problems exist for any employer in terms of tracking the uncashed checks, making and recording the state-required attempts to contact and redeliver the check, and then ultimately having to complete the state-required unclaimed property report and remit the money to the state.

Delivering paper paychecks to transient employees poses significant challenges. Even if payroll is handled out of a centralized location, checks delivered to transient employees are frequently sent to the wrong location. In these cases, employers must absorb the added cost of re-routing the same check, if they have an accurate forwarding address. If not, these funds must be reconciled until they are ultimately escheated to the state.

Same Old Payroll Solutions—Same Old Results

With challenges ranging from paycheck distribution and fraud to compliance issues and high employee turnover, it's no wonder many organizations continue to struggle with payroll distribution issues. Because paper paychecks continue to drive up costs, and direct deposit programs do little to serve unbanked employees, employers have been unable to find solutions that cover their needs.

⁵ Abagnale, Frank. "Identity Theft, Check Fraud Bigger than Ever." *Tulsa World*. July 31, 2008. http://www.tulsaworld.com/business/article.aspx?subjectID=46&articleID=20080731_46_E4_spancl870577.

⁶ Dominion Enterprises. "Hourly Employees are Optimistic, Satisfied and Loyal." January 25, 2007. http://www.dominionenterprises.com/main/newsID/13/do/news_detail.

In recent years, payroll departments have attempted to resolve these challenges by offering paycard solutions, which are, in effect, payroll debit accounts established by companies on behalf of their unbanked employees. However, because of the large number of states that still require employers to provide the option of a paper paycheck, paycard programs must be voluntary. The marketing and training required for voluntary paycard programs has prevented them from achieving the desired success.

Conducting annual voluntary direct deposit and paycard enrollment campaigns is time consuming, expensive and largely ineffectual because they don't address the root of the problem. What payroll departments need is a solution that meets compliance requirements in all 50 states, addresses the issues of unbanked employees and enables companies to reach 100 percent electronic pay.

A Payroll Solution for the 21st Century

For companies across the U.S. to effectively reduce payroll costs and meet both state compliance and unbanked employee needs, a payroll distribution solution must offer full electronic pay capabilities along with a paper paycheck option. A solution like this needs to include direct deposit capabilities for banked employees and for the unbanked, a PIN-protected paycard with a paper paycheck option.

For this type of solution to work, it needs to offer a paycard with an optional paper check that is *cashable for full value in all 50 states*. This would meet compliance issues by providing a negotiable instrument under the Uniform Commercial Code that allows employees to access all of their pay to the exact penny without any fees. However, this paper check is different from a typical paycheck that is printed for an individual employee, incurring the expenses discussed earlier. Instead, this is a blank paper check that is filled out by the employee and is only valid up to the amount of net pay funds. This important quality removes the need for employers to print individual pay checks and distribute them to specific employees, and minimizes the issue of payroll check fraud.

The single biggest benefit of this solution for employers is that whether an employee chooses the paper paycheck option or the paycard option, all employees have their pay electronically distributed. This means an end to printing individualized paper pay checks for employees, while still meeting state laws. What's more, with this payroll distribution solution, all employees are automatically qualified for the program, and they don't need a traditional bank account to participate.

While many financial institutions and vendors offer paycard solutions, First Data's paycard and optional paycheck combination is the only electronic payroll solution that truly meets the needs of employers and unbanked employees.

Additional Benefits to Payroll Departments

A payroll solution combining a paycard and optional paper checks helps employers solve some of the toughest payroll issues facing them today by providing several important benefits:

Streamlines payroll operations to lower expenses

- **Reduces supply costs**—Dramatically reduces recurring costs associated with paper paychecks and paycheck printers
- **Decreases check delivery charges**—Significantly lowers postage and overnight delivery charges associated with sending paychecks to individual employees or multiple work sites
- **Reduces costs related to check handout**—Minimizes time spent spend time distributing checks, holding unclaimed checks and handling lost check requests

Deters fraud and optimizes payroll services

- **Mitigates fraudulent activities**—Offers employees the safety of PIN-protected debit cards
- **Accelerates replacement**—Transfers the balances of lost or stolen cards to new cards without the delays associated with replacement checks
- **Delivers superior service**—Enables payroll departments to deliver better, more dependable service to all employees because of reduced administrative responsibilities
- **Fast resolution**—Allows payroll departments and banks to quickly resolve payment and compliance obstacles

Creates risk-free opportunities with electronic payroll distribution solution

- **Employee benefit**—Offers opportunities for traditionally unbanked employees to receive the benefits of a typical banking relationship without having to initiate and maintain one
- **No qualification requirements**—Enables all employees to be eligible for an electronic payroll program
- **Minimal risk**—Virtually eliminates risks for businesses and banks by utilizing a debit card in combination with a check backed with 100% guaranteed funds
- **Social responsibility**—Provides a much needed service to lower and moderate income individuals who cannot readily afford high-cost check cashing charges and banking fees

Addressing Today's Payroll Challenges

Payroll challenges can be both predictable and unpredictable. For example, some of the most critical issues that employers have faced in recent years have been dealing with the aftermath of devastating events such as Hurricane Katrina and the 2008 floods in the Midwest. These events have forced employees who rely on paper checks to be without pay for weeks. With an electronic payroll distribution system in place, thousands of at-risk individuals and their families, despite being evacuated, would have no-fee access to their pay through in-network ATMs around the country.

Today, companies all over America are enjoying the benefits of lower payroll costs and increased efficiency by implementing this unique electronic payroll distribution solution that combines a paycard with optional blank paper checks.

Meeting the Payroll Needs of 21st Century Corporations

As the competitive landscape in America continues to shift, employers are challenged to find new ways to reduce costs, improve service levels and improve productivity. Advances in technology that have automated many daily business operations are finally available to streamline payroll distribution, which is a significant cost center for most businesses today. Now, more than ever, employers must use these advances to balance the ever changing needs of their workforces with increasing state compliance requirements while maintaining profitability.

Serving thousands of companies with employees located throughout the U.S., First Data understands the challenges payroll managers face every day, and provides the expertise and insight to help them overcome those obstacles while improving their bottom line. This deep knowledge helps customers deploy innovative payroll solutions—like the paycard and optional paper check combination discussed in this paper—that serve both the banked and unbanked population with safe, dependable, anytime, anywhere payment programs.



About The Authors

Mark Smith, Vice President of Client Services at First Data, is responsible for helping clients devise plans for implementing the use of paycards. Before joining First Data in 2002, Mark was Payroll Manager for Sears, Roebuck & Co. He has been involved in the payroll profession since 1989 and a member of the American Payroll Association since 1990.

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