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Paycards: The Next Step in Efficient Payroll

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How paycards lower employer payroll costs and improve employee satisfaction

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Executive Summary

The cost of labor is one of the largest expenses faced by most businesses. A part of that expense is the cost of actually producing the payroll itself including calculating pay, producing checks, delivering checks, replacing lost checks and paystubs, escheatment costs and reconciling the cashing of checks. Payroll distribution has proven to be an area where significant cost savings and higher employee satisfaction can easily be achieved. In recent years, companies' utilization of direct deposit has substantially lowered the cost of processing payroll, while increasing efficiency.

While direct deposit has been popular with many employees, some workers, typically those without a bank account, have been unable or unwilling to adopt this method of payment. This has resulted in many employers being unable to take full advantage of the substantial savings and efficiencies of applying best practices to their payroll production. Additionally, their unbanked employees are financially and administratively disadvantaged over their coworkers through having to manually receive their wages and then paying fees to cash their paycheck.

With the recent arrival of paycards, which are pre-paid debit cards loaded with an employee's pay, companies have been able to benefit from the same cost savings and administrative efficiencies they have typically been experiencing with their direct deposit employees. Furthermore, with paycards, employers are able to extend the financial

savings and conveniences that their direct deposit employees enjoy, to their entire employee population, substantially increasing employee satisfaction.

From a payroll perspective, the paycard is, in fact, just like a bank account - having the same characteristics for receiving funds electronically, withdrawing cash, utilization of online bill paying, allowing purchases of products and services with a debit card, viewing activity online, and benefiting from both \$250,000 of FDIC insurance and fraud protection services offered through the major card associations such as Visa. In many ways, the paycard helps bring unbanked employees into the modern electronic economy by giving them access to an account with nearly all the features of a standard bank account.

The Direct Deposit Revolution

According to the American Payroll Association (APA), the direct cost of issuing a paper paycheck is between \$1 and \$2 per check, while electronic transfer of pay through direct deposit averages just twenty cents.¹ The cost of issuing paper checks also continues to grow, for example, last year the median cost per paycheck rose 3.5% compared with 2007, according to a survey by the American Payroll Association.

When you add additional costs associated such as delivering paychecks, replacing lost or stolen checks, and mitigating check fraud, the costs associated with paper paychecks can increase substantially. The National Automated Clearing House Association (NACHA) recorded five billion direct deposits for payroll, benefits, and expense reimbursements in 2007, an increase of 6.2% from the previous year.² If we assume an average savings of \$0.80 per direct deposit (over traditional paper checks), this represents \$4 billion in savings for U.S. employers in one year.

Direct deposit offers benefits beyond savings for employers. It's easy to initiate direct deposits and the process is extremely accurate. Employees can usually access their funds on payday – much faster than depositing a paper paycheck. As a result, employee satisfaction with direct deposit is an extremely high at 97%.³ Additionally, many direct deposit initiators easily can accommodate over and under payments by, in the case of the former, enabling a reverse ACH transaction.

Where direct deposit fails

Clearly, direct deposit is well received by employees and has delivered tremendous savings for U.S. businesses. But what about the 25% of employees who do not opt for direct deposit? Why don't they participate in this benefit? Often, the answer is that these employees are unbanked.

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 More than 18 Billion ACH Payments in 2007," *press release*, May 19, 2008. www.nacha.org

³ "Fast Facts About Direct Deposit," NACHA and Electronic Payments Network. www.electronicpayments.org

“Unbanked” employees, also known as “self-banked,” are workers who do not have a relationship with any bank, and therefore lack both checking and savings accounts. There are also “Under banked” employees, who typically have a minimal banking relationship. Approximately 28 million people are unbanked, with another 44.7 million under banked.⁴ Taken together, these two groups represent nearly 25% of U.S. households.

Unbanked employees rely on check-cashing services to cash paychecks. Then, in order to pay their monthly bills, they purchase money wires or money orders. According to TIME magazine, check cashing services charge fees of up to 10% (the average is 1% to 3%) of the value of the check, at an annual cost to U.S. families of more than \$10 billion per year.⁵ Sadly, these exorbitant fees are paid by the workers who least can afford them; unbanked employees are disproportionately young with lower income⁶. Even under banked employees are often compelled to pay check cashing fees to their own banks if they lack the required minimum balance in their accounts.

Paycards: The Next Step in Payroll Efficiency

Today, employers are using paycards to offer employees the convenience and savings of direct deposit without the need for a bank account. A paycard is a stored-value card that holds an employee’s pay and allows him or her to pay bills or make purchases with any merchant or vendor who accepts debit cards (e.g. everywhere Visa is accepted). Employees can also use their paycards to withdraw cash at ATM machines or over-the-counter at any bank.



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

⁵ Anita Hamilton-Norcross, “Profiting from the Unbanked,” *TIME*, August 16, 2007.

⁶ 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.

The substantial conveniences and savings provided by paycards have led to their rapid adoption by both employers and employees. Independent research firm Pelorus Group estimates that 7 million paycards were distributed in 2006.⁷ More than \$17 billion in employee wages and expense reimbursements are expected to be distributed annually on paycards by 2009.⁸

Unbanked employees save hundreds each year

To conduct their daily business, most unbanked employees rely on companies that provide alternative financial services. Many employees could be paying hundreds of dollars per year for services that would cost a small fraction when using paycards. Here's a look at the costs and other factors related to using these financial services companies.

Let's consider the case of an hourly truck driver, Sam, who earns \$300 a week and does not have a bank account. Each week, Sam cashes his paycheck and buys money orders to pay his rent, telephone, water and electric bills. For other purchases, Sam has to carry lots of cash, and therefore cannot participate in the card-based economy that provides easy access to online purchases, travel bookings, phone order purchases, and protection in the event of loss or theft.

Check Cashing: According to the annual Consumer Federation of America survey of check cashing outlets,⁹ Sam will pay an average of 2.44% of his pay in fees to check cashing outlets, or \$31.72 a month (\$380 a year) just to turn his company-issued check into spending money,

At the lower end of the check cashing scale, if he has access to a Wal-Mart, Sam can take advantage of their lower \$3 flat rate per paycheck cashed. Wal-Mart check cashing is a popular service with unbanked workers; Wal-Mart cashes over 45 million paychecks per year, earning the company over \$135 million annually. However, even at Wal-Mart it costs Sam \$13 monthly or \$156 per year, much more than a paycard.

Using a paycard, Sam could make purchases at any store or website that accepts signature debit cards. Or, he could remove all funds free of charge over-the-counter at any bank.

Total monthly check cashing savings with paycard –\$13 to \$32

Money orders: In order to pay his monthly bills without a checking account, Sam must either personally deliver cash to each supplier during business hours, or purchase money orders. Each U.S. Postal Service money order costs \$1 to \$2 and an additional

⁷ American Payroll Association, *Paycard Guide*, February 2008, pp. 1.

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

⁹ Jean Ann Fox and Patrick Woodall, "Cashed Out: Consumers Pay Steep Premium to 'Bank' at Check Cashing Outlets," Consumer Federation of America, November 2006. (The Consumer Federation of America (CFA) is a nonprofit association of some 300 national, state, and local consumer-focused organizations created in 1968.)

\$.42 to mail. With a paycard, Sam could pay his electric, water, and telephone bills online or by phone.

Total monthly savings on money orders with paycard – \$6

Altogether, each month Sam pays somewhere between \$19 and \$37 for financial services on approximately \$1,200 worth of paychecks. Over the course of the year, Sam loses between \$228 and \$444, or up to approximately 3.7% of his take home pay. The same transactions via a paycard could cost less than \$30 per year if the paycard is used correctly.

Paycards make life easier and safer for employees

By adding paycards to existing direct deposit payroll processing, businesses are able to deliver immediate benefits to employees who adopt them. In addition to the savings explained above, paycards offer employees numerous conveniences, as well as improving their financial and personal safety.

Employees, who receive paper paychecks, usually do so either by getting them in the mail or in person at the worksite. This is a problem for Sam as he is a truck driver, and is often on the road. This in turn may cause Sam to be late in paying his bills, as he has no way to pay them online or by phone. With a paycard, pay is always on time and funds are available around the clock, 365 days per year. There is no reason for payroll delays, even if the corporate office is closed. Employees, who work from home or in remote locations, as well as shift workers, enjoy the convenience of receiving their pay without needing to travel to the office during business hours. With a paycard in his wallet, no matter where he is located, Sam has access to his full pay at the same time as his fellow employees who are on direct deposit.

If Sam is picking up his paycheck from a work site, this means he has to be present to receive his pay. For some employees this is a huge inconvenience as they may have to return to the work site or wait around after their work is finished (if, for example, they are a shift worker). Obviously, if they are sick or away they will need to arrange for someone else to pick up their pay.

Paycards offer employees all of the conveniences of bank debit cards when shopping or paying bills. Whether banked or unbanked, employees easily understand the concept behind payroll cards. They work in the same way as other prepaid cards, such as phone or gift cards, and according to Visa, 83% of Americans used gift cards in 2007, with sales totaling \$97B. Paycards can be used at any store, ATM, or website that accepts debit cards.

Even employees with bank accounts benefit from the convenience of paycards, with many requesting additional cards for family members, such as teenagers or college students.

Carrying a paycard is much safer than carrying cash. Criminals know that persons visiting check cashing and money wire establishments are likely to have large amounts

of cash in hand, making them ideal targets. It's also easy to stop payment on a lost or stolen paycard, and request a replacement. And Visa's Zero Liability policy¹⁰ protects card holders from losing any money if their cards are lost or stolen.

Paycards significantly lower employer payroll costs and administrative burden

For employers, the direct costs associated with generating paper paychecks, including paper check stock, printing, envelopes, postage and delivery, and replacing lost checks and paystubs, are easy to quantify. An example showing annual savings of \$39 for each employee receiving a paper check is provided below. Additionally, there are the stop payment fees for lost or stolen paychecks. As many as four million paychecks are lost or stolen each year, with an average replacement cost of \$8 to \$10 each, according to the American Payroll Association.¹¹

Employer Savings

Let's examine the potential savings at a company with 1,000 employees that issues paychecks twice per month.

Employees receiving paper checks: 300
Total annual paper paychecks: 7,200
Processing costs per check: \$1.25
Annual processing costs: \$9,000
Checks lost/stolen: 1%
Locations: 3
Overnight delivery fee: \$25
Annual delivery fees: \$1,800
Stop payment and replacement costs: \$15.00
Annual cost to replace lost/stolen checks: \$1,080

Potential Annual Savings with Paycards: \$11,880

There are also the indirect costs of issuing paper paychecks. With paycards, companies can enjoy greater worker productivity. Employees will no longer need to leave work early on Fridays to cash paychecks and pay bills. If employees leave just one-half hour early every payday (weekly), it costs as much as 3.25 days of lost productivity, per worker, each year.

¹⁰ Visa's Zero Liability policy means 100 percent protection for Visa Card Holders which guarantees maximum Protection against fraud. Should a Visa Card be used fraudulently the Card holder will have zero liability subject to the terms and condition of their Visa Card holder agreement. For more information please visit www.visa.com/security.

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

Because direct deposit and paycards are so affordable for employers, companies can pay employees as frequently as they would like, without raising payroll costs. Nearly 65% of employees surveyed by the American Payroll Association said it would be very difficult or somewhat difficult to meet financial obligations if their next paycheck was delayed by just one week¹². More than ever before, with family budgets stretched that tight, moving to a weekly payroll could be an easy way to improve employee satisfaction.

With paycards, companies find it much easier to get accurate, timely payroll to their employees. Workers in the field do not need to come to a company office to pick up paychecks or expense reimbursements. Recently terminated employees also do not need to return to the office, and the company does not have to pay to deliver their last check. And for businesses with multiple locations that process payroll centrally, there is no need to ship checks to the company's other offices, often using expensive overnight couriers.

Paycards integrate easily into an employer's existing payroll process, working exactly like direct deposits. Paycards also help minimize check fraud, and employees can report lost or stolen paycards directly to the paycard provider, easily obtaining a replacement card as quickly as within 24 hours and with the comfort of knowing their funds will be protected.

By offering employees a choice between direct deposit and paycards, many companies have been able to eliminate paper paychecks.

How to Choose a Paycard Provider

Look for a provider that specializes in employer solutions

Several types of companies offer paycards, including banks, credit card companies, and employer solution providers. But paying your employees is more than a financial service – it's the most important benefit your company provides them. It is therefore important to choose a paycard provider who understands employee benefits and specializes in employer solutions. Be sure to investigate the track record of any provider you consider and ask for references to other customers who also use their service.

Compare employee costs to minimize fees

Different paycard providers charge different fees to employees. To ensure employee satisfaction and a high adoption rate, you'll want to shop several providers and compare their fee structures to get the best deal for your employees. Employee fees might include monthly maintenance fees, transaction fees, ATM charges, POS fees when making purchases at stores, inactivity fees, replacement fees for lost/stolen cards, overdraft fees, and fees for optional services such as paper statements or additional cards.

¹² American Payroll Association, *Getting Paid in America*, 2006. Accessed online at http://www.nationalpayrollweek.com/documents/FinalResults_FORMATTED.pdf

Some providers may also charge for telephone customer service. Evaluate each fee structure using models of how you believe employees will normally use the cards. It's not enough to simply compare each fee – examine the effective rates of using each card.

Ensure no-cost, responsive customer service

Customer service is key to a positive cardholder experience. If your employees have difficulty accessing help, they will complain and reject your paycard program. As an employer, you should not have to pay extra for employees to receive fast, responsive telephone support for their questions. This service should be included in the monthly maintenance fee for the paycard.

Choose a paycard provider that offers live telephone support, in addition to any automated voice-response system. Consider whether some of your employees would benefit from bi-lingual customer support. Finally, make sure that the educational materials provided to your employees fully explain the benefits of paycards, as well as all associated costs, and make sure the chosen payroll provider will educate your employees on how to best use the cards. In any paycard program it is important to ensure price transparency to employees.

Online Pay Stubs

Companies who wish to go totally paperless should look at paycard providers who can also incorporate online pay stub production, access and distribution into their paycard program. Online pay stub providers may also include an additional document service that offers quick, easy, and secure access to W-2s and 1099 forms.

Find greater value for your employees with added services

If you can find a paycard provider that offers other benefits for employees, at no additional cost to your company, the employees will perceive greater value in the paycard. Ask providers whether they offer additional programs, such as an employee discount program for products and services, especially where these are combined with the paycard. Some providers can also offer access to voluntary employee-purchased benefits, such as home insurance, auto insurance, or pet insurance, at competitive prices.

Rolling Out Your Paycard Program

Once you have decided to implement a paycard program, it pays to create a comprehensive strategy surrounding your payroll process. Remember, you are not solely introducing a paycard program; rather your company is “changing the way we pay”. In other words, by providing an alternative direct deposit solution, your company is moving towards 100% direct deposit for all employees, either through a traditional bank account or by utilizing paycards. It is also recommended that you review all new hire material and ensure that your new strategy is clearly articulated. Here are a few tips:

Ensure Support from all levels of management

Depending upon the size and the complexity of your organization and your hiring process, you will need to ensure that the changes to your payroll processes are clearly communicated to all levels of management.

- Senior management should be aware of the changes and fully supportive of your initiatives. You must be able to show them the savings associated with changing your payroll process. You should establish clear goals and set targets on what percentage of employees you want on direct deposit.
- Human Resources and the Payroll Department must be the driving force behind this initiative. All parties need to fully understand the payroll card program, including both the product functionality and the policies.
- Frontline Managers, Department Managers and all Hiring Managers will need to understand the changes in the policies and be able to answer questions and/or provide appropriate information surrounding your payroll process.

Establish whether paycards are voluntary or mandatory

When you introduced direct deposit, it was necessary to make it a voluntary program because some of your employees were unbanked. When you add paycards to your payroll program, you have the ability to mandate that employees choose either direct deposit or a paycard to receive their pay. The benefit of such a policy is that you could eliminate paper paychecks and their associated costs all together.¹³

Decide if your company will pay any of the fees

While it is possible to reduce the employer payroll costs to nearly zero with paycards, many employers choose to pay some fees rather than passing them on to the employees. You might decide to pay for any upfront costs of issuing the card. Additionally, you may choose to pay any monthly maintenance fee associated with the card program. If you choose to cover some of the cardholder fee's you can easily accommodate this through a post-tax deduction, for the amount which you want to pay, right through your payroll system. This simplifies the process dramatically as in most instances it is a monetize set up and this ensures that you are only paying for current employees. This will remove the paycard provider from having to bill you and eliminate the reconciliation headaches associated with terminated employees.

Plan to educate employees about paycards

You should require your paycard provider to provide you comprehensive educational materials to distribute to your employees. These materials explain how paycards work and illustrate the benefits of using paycards. It is important to plan how this information will be distributed throughout your organization. When you educate employees properly about the benefits of paycards, your adoption rate will be higher and you will ultimately save money.

¹³ Check with your state payroll agency.

Summary

Paycards offer significant advantages to employers and employees. By eliminating the need to issue paper paychecks to some employees, your company can enjoy more efficient payroll processing and significantly reduce transaction costs. Paycards also help minimize check fraud and eliminate the cost of replacing lost or stolen checks.

Your employees also have much to gain – especially employees without a banking relationship. These workers will save hundreds of dollars every year by avoiding check cashing, money order, and wire transfer fees. When they keep their pay on a prepaid card, rather than in cash on their person, they'll remain both physically and financially safer.

If your company decides to implement a paycard system, you'll want to shop carefully for the right provider. You will want to select a provider that can develop a long term successful strategy to reduce your payroll costs and provide superior technology and customer support. It is beneficial to find a provider that specializes in employer solutions, and offers responsive customer support at no additional cost to your company or your employees. You'll also want to compare the fees for employees to make sure your workers enjoy the best possible savings. A provider that offers additional voluntary benefits to employees, such as discount programs or insurance plans, may help you boost adoption rates and increase employee satisfaction with the program.

With proper planning, implementing paycards for employees can be fast and easy. First, decide whether paycards will be mandatory for employees who do not participate in direct deposit. Then determine what fees the employee should pay and what will be paid by the company. Plan your education strategy to ensure that all employees can participate on-the-clock, during business hours. Don't forget to educate front-line managers so they can answer questions from their employees.

About Motivano

Motivano is the market leader in employee benefits technologies. Products include Core and Voluntary Benefits Enrollment, Payroll Deduction and Provider Payments, Employee Discounts, and Payroll and Incentive Cards. In the last 5 years, over 5,000 companies and government organizations have signed on with Motivano. Clients include large, global organizations, such as, Citi, GSK, Time Warner, and Sage Software. We also provide services to thousands of small to mid-size companies. Government clients include the State of Delaware and other state and local governments.

Motivano's products include:

SmartCash

Visa Payroll Card

A reloadable Visa Payroll Card that is funded each pay period with the employee's payroll

SmartSavings

Member Discount Marketplace

The largest online employee discount marketplace in the US, providing millions of employees access to hundreds of thousands of merchant brands

SmartPay

Voluntary Benefits Administration

Online service for payroll deduction and provider payment management

SmartAwards

Visa Incentive Card

An online employee incentive and reward program using a reloadable Visa debit card

SmartPaystubs

Online Paperless Paystubs

A secure, easy-to-use, online tool that enables employees to view their current and past pay stubs and pay statements

SmartEnroll

Benefits Enrollment Platform

An online education and enrollment platform for core and voluntary benefits

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