EVALUATING THE TRUE COST OF ON-DEMAND PAY

EDITION I

DAILYPAY

NOTES AND DISCLAIMERS

I. INTRODUCTION

Several years ago, no one had ever heard the term "on-demand pay," also called earned wage access, instant pay, early wage access and myriad other names. But in the last few years, the idea of offering an on-demand pay benefit has taken the workplace by storm. Where there was once one or two main players in the on-demand pay provider game, there are now more than 30 and climbing.

So if your organization has decided to offer this benefit, how do you ensure that you are

offering the best program for your company and your employees? In this white paper, we provide the key decision-making criteria determined by companies who currently have a daily payment program in place.

For companies that currently offer a daily pay program, the four most important characteristics of a successful program are:

1. A program that presents zero incremental risk to the employer.
2. A program that creates zero disruption to the employer's and employees' existing payroll processes.
3. A program that results in maximum satisfaction for all employees.
4. A program that offers partner support that maximizes the employee experience

This white paper will help you assess vendor options by looking at these characteristics through a series of questions.

II. FIRST THE BASICS: WHAT IS ON-DEMAND PAY?

On-demand pay, also called earned wage access, is a voluntary benefit that allows employees to access their earned and unpaid wages prior to payday. By allowing employees to tap into their earned pay, they can pay their bills on time and meet emergency or unexpected expenses, without having to pay late fees, overdraft fees or resort to predatory payday loans that can charge a borrower up to 400% interest. The ability to transfer earnings before payday allows employees to feel more financially secure and to stress less while on the job, increasing their productivity and employee engagement.

When employers offer this benefit, it's easier to recruit employees. In fact, 1 in 6 employees actually applied to their current job because it offered a daily pay benefit. Employers also find that employees are more loyal and want to stay with them longer, reducing turnover and its associated costs by 45%, on average.

Because there are so many providers crowding the on-demand pay space, it might be helpful to evaluate them on the four characteristics of a successful program, mentioned above, based on the following questions.

III. A PROGRAM THAT PRESENTS ZERO INCREMENTAL RISK TO THE EMPLOYER

There are several legal, compliance and operational issues, which, if ignored, may present risk factors to your company. It is imperative that you completely address these key risk areas when evaluating an on-demand pay solution so that you do not expose your company to any compliance or regulatory risk:

1. **Does the on-demand pay provider require employers to fund employee early pay transfers, either in part or in full?**

   Employers need to understand the impact of funding early pay requests on their company, including increased tax-withholding requirements, the impact to corporate operating cash, deleveraging and paying down debt, and impact on operations.

   When an employer funds early pay transfers, this can trigger constructive receipt and the requirement to withhold and pay any required employee tax obligations. In this case, the employer needs to assess the increased burden of filing daily IRS tax withholdings. The IRS characterizes company-funded advances as payroll and, as such, requires daily payroll tax filings.

   When the vendor funds early transfers, there is no need to withhold taxes at that time; the only time the employer is responsible for tax withholding is when the company is legally making wage payments to the employee.

   In terms of operating cash, the employer must calculate the cost of capital for a full payroll, since the only responsible cash management approach is to assume a "worst-case scenario," which is that all employees use the program. Therefore, the company would be required to "pre-fund" an amount equal to an entire payroll at any given time.

   This calculation should also include the cost of short-term borrowing as well as any impact on bank credit revolver covenants (Note: the company may be required to obtain consent and approval from its commercial banking relationships to prefund payroll for this purpose).

2. **Does the provider's solution require the employer to make deductions directly from the employee's weekly paycheck?**

   Deducting earnings from an employee's wages (other than taxes, garnishments and certain types of insurance) is considered wage discounting. Most states have strict state labor laws that prohibit this practice, and a violation may result in a class-action lawsuit, Private Attorney General Action (PAGA), and/or criminal liability.

   When the employer deducts advance amounts from the employee's net pay, prior to remitting the final net wage amount, this is a direct violation of employer wage discounting prohibitions. As an employer, you are strongly encouraged to determine whether your company currently — or ever plans to — operate in the states that prohibit employer wage discounting. Please note that "employee consent" does not allow the employer to wage discount.

3. **Does the vendor have experience in providing on-demand pay?**

   By the day, new vendors, including Human Capital Management (HCM) companies, have entered the on-demand pay space. While these new entrants have seemingly extensive experience in "managing payroll," on-demand pay is a significant divergence from their core business and presents an entirely new set of risks (including credit risk). In addition, providing on-demand pay to an ever-more demanding workforce requires a very distinct set of operational capabilities and a specific company vision that is best found in firms specializing in this domain.

In order to make earned wages available 24/7 for employees, an ODP provider must have access to "instant funding" capacity. This instant funding capacity must be structured around the unpredictable and changing needs of employees and employers. In the case of HCM companies, employers and employees are being offered a limited menu of pre-established solutions, which employees and employers must fit into rather than the full flexibility offered by agile, standalone ODP providers. This approach doesn't meet the present needs of tech-savvy employees, in a world where instant payments are regarded as a virtual ATM, giving employees access to technology that used to be reserved for the most sophisticated companies.

IV. A Program That Creates Zero Disruption To Existing Payroll Processes

It is recommended that an on-demand pay program result in zero changes to your existing payroll, IT and HR processes. Time-consuming and costly integrations can make what should otherwise be a big win for your organization, a painful experience for both you and your employees. A vendor should be able to work within your existing processes to create the optimal solution for your organization.

4. **Is there any change(s) required in your current payroll processes?**

   If the employer needs to deduct on-demand pay transfer amounts from the employee's net pay prior to remitting the final net wage amount (as described in Question 2), this will require additional responsibility for your payroll department, which will now need to process the essential functions of processing payroll on a more regular basis (or even daily) throughout a pay period. You should assess and budget for any additional resource requirements needed to complete tasks associated with, in essence, processing payroll daily.

5. **Will the solution require employers to issue a pay card to our employees?**

   Another thing to be wary of is a requirement that your employees must sign up for a new, special vendor-issued pay card to receive any of their earned income in advance of payday. Employees should be able to use the same account to receive pay daily as they did before enrolling in a daily payment program, including bank accounts, pay card(s) issued by the employer, or cash cards that they use to receive their pay.

   If a daily pay provider requires a specific pay card, employers should evaluate the internal cost and effort of replacing any existing pay card they may already be using. They should also consider the impact on employees who would need to change the way they receive pay. If your company does not have an existing pay card program, you should look to partner with an on-demand pay vendor that has a pay card option as part of its program, but that isn't a requirement.

6. **Are there any other fees the employee pays, including any card fees?**

   In terms of fees that the on-demand pay provider may change to offer the program, look for fees that are transparent and that are charged only when an employee requests an early transfer of their earned pay. Generally, these fees can be paid by the employer or the employee, or by a combination of the two.

   In general, if an on-demand pay provider offers "free transfers" or "zero fees for transfers," that could be a warning sign that there are other hidden fees that are charged to the employer or the employee. Typically, payroll card programs carry usage fees, above and beyond the typical payroll card. In addition, when an employee has to sign up for a new vendor-issued pay card to receive on-demand pay transfers, the employee typically pays an average of $300/year in cardholder fees. Employers are encouraged to examine carefully the impact of a payroll card that offers "zero transfer fees." This is often a stalking horse for collecting "out-of-network ATM fees" and "cardholder inactivity fees."

V. A Program That Results In Maximum Satisfaction For All Employees

Employee satisfaction is all about meeting employee expectations. Employees have the expectations regarding a daily pay benefit program, so carefully evaluate the following questions.

7. **When an employee requests funds, can they use the funds instantly?**

   True instant payments are a market requirement. The employee must be able to receive and use funds instantly 24/7/365.

   There are many solutions in the marketplace that purport to be "instant," but this may simply mean that the vendor sends the funds instantly and not that the employee receives them instantly. This occurs when funds are sent via the ACH network.

   Some solutions force employees to choose restrictive banking/card networks in order to use the service. For example, funds are sent instantly, but only received instantly if an employee establishes a specific pay card relationship that ultimately results in significant fees to then transfer the funds to an employee's preferred account or to withdraw these funds at an ATM.

8. **Is the on-demand pay product only available on an app and/or smartphone?**

The on-demand pay program should not be limited to iOS or Android smartphone app format. The benefit should be available to the highest number of employees to ensure successful enrollment and program success. A significant proportion of your employees may not have access to expensive smartphones, so ensuring that your program is available across mobile and web platforms will allow for maximum coverage of your employee base.

VI. A Program That Offers Partner Support That Maximizes the Employee Experience

9. Is customer support readily available to field employee questions?

Any offering should provide vendor-supported, high-quality customer support selections (phone, email, chat) across all local time zones. Additionally, a significant portion of the employee base may require non-English speaking support, so a bilingual solution may be needed. If the vendor does not offer customer support, you will need to factor in the cost of additional resources to handle employee questions or any issues they may encounter.

10. Does the on-demand pay program provide a 360 launch strategy?

It's important that the on-demand pay program provides the support needed to ensure the best employee experience possible. This may include the creation of custom program marketing materials and resources that educate employee users about the on-demand pay offering to encourage participation and increase adoption rates. It may also include user surveys to gauge the value of the program, onsite activities and other forms of user engagement and manager/leadership training.

These are some of the key considerations to keep in mind when evaluating the true cost of implementing an on-demand pay benefit. To succeed in your endeavor to offer a benefit that truly increases your employees' financial security and your company's bottom line, it is imperative that you perform thorough due diligence, to ensure that the program meets the expectations of your employees and your company, and that you don't end up with any surprises that catch you off guard.