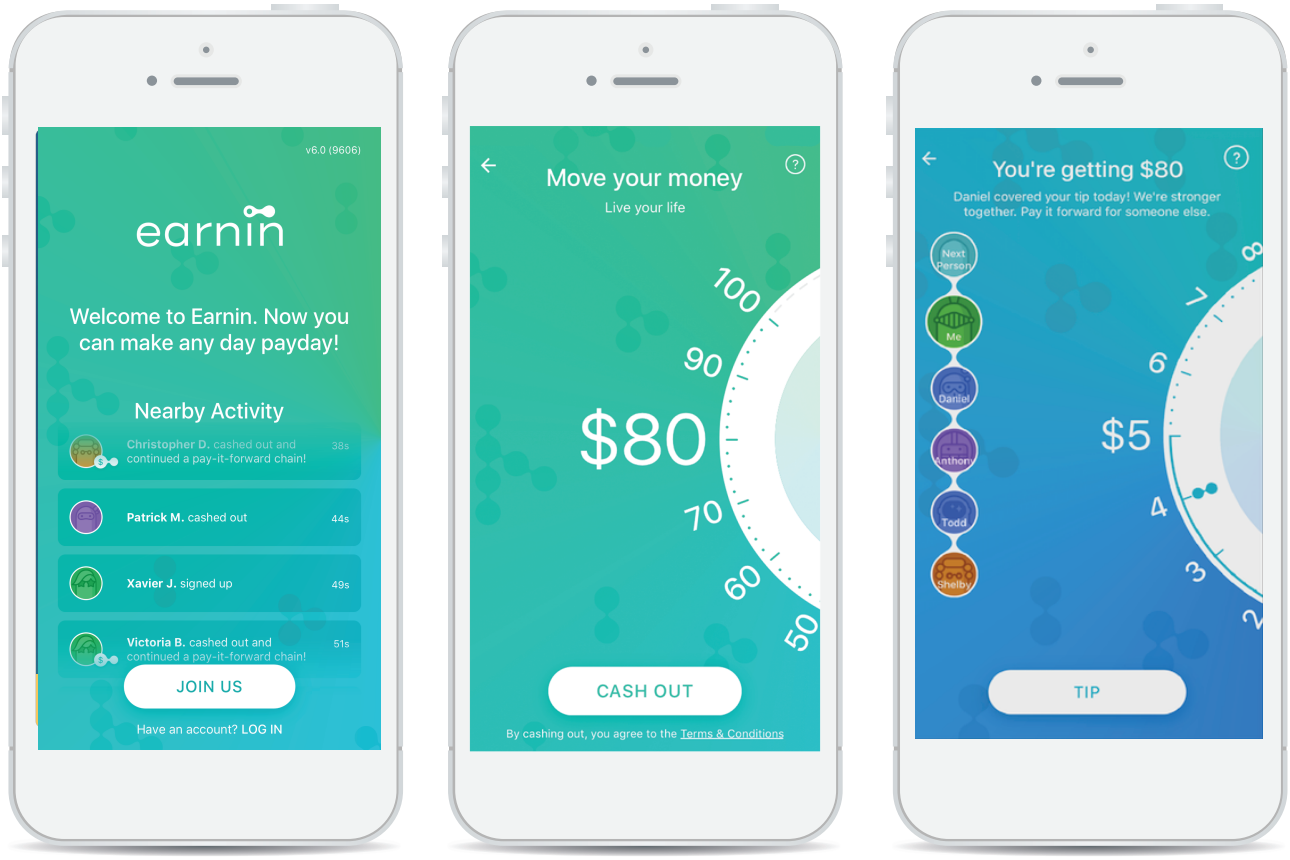
White Paper: On-Demand Payroll



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I. The Age Old Problem: Payroll

Payment is at the heart of the employment relationship. Although a host of variables influence how, when and where people work, people enter paid employment in order to turn their time and skills into money. Most people, however, do not give much thought to how the money they earn actually reaches their bank account. After all, the steps seem simple enough. The employer calculates how much the employee is owed, makes the necessary deductions to cover taxes and benefits, and the rest shows up in a bank account or as a check. However, things that seem simple in the abstract are often difficult in the concrete.

The challenge of calculating and delivering wages stems, in part, from the complex nature of the relationship between employees and employers. This relationship imperfectly aligns the interests of employers and employees, and timely delivery of wages that have already been earned is one of the many issues of contention. All else equal, many employers might prefer that employees work first and get paid later -- much later -- if possible. Employees, on the other hand, would prefer to get paid first and work later.

For most of the history of the United States, employers had the upper hand in determining when their employees would get paid, and they employed a long list of practices to delay the payment of wages. Efforts to end those practices and to secure laws guaranteeing minimum wages and maximum hours helped to propel the modern labor movement in the U.S. and elsewhere.

The problem is not a new one. One of the oldest legal texts in the Western world, Deuteronomy, contains a provision that speaks directly to the issue, presumably because disputes about wages were a source of discord even among the ancient Israelites: "You shall pay them their wages daily before sunset, because they are poor and their livelihood depends on them … ."[1]

The challenge of paying wages goes beyond determining when they should be paid. The actual mechanics of calculating what an employer owes an employee, particularly an hourly employee, is quite complicated.[2] Take the issue of overtime for example; Employers pay their employees at a rate one-and-a-half times their usual hourly rate when those employees work more than forty hours in a given workweek.[3] This calculation is necessarily backward looking. An employer cannot know how much overtime pay an hourly worker is due until the workweek is completed.

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[1] Deuteronomy 24:15 (New Revised Standard Version) ("You shall pay them their wages daily before sunset, because they are poor and their livelihood depends on them….")

[2] *See, e.g., Compliance Instructions,* Department of Labor, Wage and Hour Division, http://www.dol.gov/whd/flsa/ (last visited Sept. 4, 2015).

[3] *See Overtime Pay,* Department of Labor, Wage and House Division, http://www.dol.gov/whd/overtime_pay.htm (last visited Sept. 4, 2015).

Calculating net wages adds a further level of complication. Federal, state and local tax codes require employers to withhold tax payments from their employees' paychecks. Employers also typically deduct the employees' contributions to health insurance or retirement benefits. These deductions often vary over the course of a given year if, for example, an employee hits the wage cap on Social Security taxes, adds (or loses) a dependent, or makes changes to his or her benefits. Termination and period-to-period variation in the number of hours worked further complicate the seemingly simple task.

The problem of accurately calculating payroll is complex enough that most companies outsource payroll processing. Firms like ADP[4] and Intuit[5] specialize in defining pay periods, calculating wages, withholding funds for taxes and benefits and actually delivering money to employees.

Those firms, however, work for the employers -- not the employees. They help ensure that employers correctly calculate what they owe their employees, withhold and pay the necessary taxes, and deliver wages within the time limits prescribed by law (but generally not a moment earlier).

II. How Big is the Problem?

The current system for wage delivery benefits employers at the expense of their workers. The problems associated with a delayed payroll schedule are striking. The sluggish nature of the payroll system costs workers over $50 billion per year in fees,[6] while they needlessly wait for their already earned pay. Each year, there is over $1 trillion held up for over two weeks in the payroll system.[7] This payroll delay affects the earnings of approximately 73.9 million hourly workers.[8] Their earnings

"The sluggish nature of the payroll system is costing workers over $50 billion per year in fees"

[4] *About ADP Payroll Services,* ADP.COM, http://www.adp.com/solutions/services/payroll-services.aspx (last visited Sept. 4, 2015).
[5] *About Intuit Payroll Services,* INTUIT.COM, http://payroll.intuit.com/?cid=seq_intuit_proll_click_nav (last visited Sept. 4, 2015).
[6] *Table B-8,* Economic News Release, http://www.bls.gov/news.release/empsit.t24.htm
[7] *Average annual hours actually worked per worker,* OEDC.Stat, https://stats.oecd.org/Index.aspx?DataSetCode=ANHRS; *Table B-8,* Economic News Release, http://www.bls.gov/news.release/empsit.t24.htm
[8] *Labor Force Statistics from the Current Population Survey: Characteristics of Minimum Wage Workers: 2011,* Bureau of Labor Statistics, Mar. 2, 2012, http://www.bls.gov/cps/minwage2011.htm

are spent on late fees, overdraft fees ($31.8B),[9] pawn shops ($15.5B),[10] and short-term loan fees ($7.4B).[11] Last year, 13.9% of customer accounts made 5 or more NSF fees.[12]

Individuals report having to delay everything from grocery shopping to medical care while they await their delayed income.[13] Bill Simon, CEO of Walmart US, said, "The paycheck cycle we've talked about before remains extreme…And you need not go further than one of our stores on midnight at the end of the month. And it's real interesting to watch, about 11 p.m., customers start to come in and shop, fill their grocery basket with basic items, baby formula, milk, bread, eggs, and continue to shop and mill about the store until midnight, when electronic — government electronic benefits cards get activated and then the check-out starts and occurs. And our sales for those first few hours on the first of the month are substantially and significantly higher."[14]

A study by the Center for Economic Demography found that there is an adverse health effect caused by our current paycycle. The authors of the study said, "We find a dramatic increase in mortality on the day salaries arrive. The increase is especially pronounced for younger workers and for deaths due to activity-related causes such as heart conditions and strokes. Additionally, the effect is entirely driven by an increase in mortality among low income individuals, who are more likely to experience liquidity constraints."[15]

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[9] Annamaria Andriotis, "Overdraft Fees Continue to Weigh on Bank Customers, Wall Street Journal Blog, May 12, 2015, *available at* http://blogs.wsj.com/totalreturn/2015/05/12/overdraft-fees-continue-to-weigh-on-bank-customers/

[10] *Pawnbrokers pitch loans to kings and queens,* MarketWatch, http://www.marketwatch.com/story/pawnbrokers-pitch-loans-to-kings-and-queens-2013-01-08

[11] *Payday Lending in America: Who Borrows, Where They Borrow and Why*, 1, Pew Charitable Trusts, July 2012, *available at* http://www.pewtrusts.org/~/media/legacy/uploadedfiles/pcs_assets/2012/PewPaydayLendingReportpdf.pdf

[12] *FDIC - NSF (Bounced Checking Fees) Study,* Ohio Consumer Lenders Association, http://ohiocla.org/industry-studies/fdic-nsf-bounced-checking-fees-study/

[13] Earnin. "Waiting Game" Survey. 24 April 2014.

[14] Watching Walmart at Midnight, Wallstreet Journal, http://blos.wsj.com/economics/2010/09/20/watching-walmart-at-midnight/

[15] Income Receipt and Mortality: Evidence from Swedish Public Sector Employees, Iza, http:/ftp.iza.org/dp8389.pdf

III. On-Demand Pay vs Legacy

On-demand payroll systems and legacy payroll systems both move money to employees' bank accounts. The transfers are initiated from the payroll system's bank accounts. While on-demand systems move money as the employee requests it, legacy payroll systems move money for every employee at the company on the same day. Both on-demand and legacy payroll systems are reimbursed for the employee payments they make. Both types of systems take on some risk, as the reimbursement is not confirmed until after payment to the employee has been made.

In an age when you can order anything from a hot meal to a comfortable ride in minutes with the touch of a button, on-demand pay just makes sense. Unlike legacy payroll systems which get a batch data update from the time & attendance system only once per pay cycle, in an on-demand world, payroll can be run several times a day at the user's request. With legacy payroll systems, the employee's pay is held back until calculations such as overtime pay and deductions can be completed. With on-demand pay, workers can access the wages they've earned that are not dependant on the future.

Legacy payroll systems also require a payroll administrator. The timeliness and frequency with which employees get their pay is determined by the company and the payroll administrator. On-demand payroll systems are used directly by employees. This frees wages from being held captive to the schedule of the payroll administrator.

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IV. Earnin Gives Workers Access to On-Demand Pay

Earnin is an app that gives people easy access to the pay they've earned — when they want it, without waiting for payday. It seeks to solve the problem that has vexed employees for thousands of years:getting paid for completed work. It lets employees, rather than employers, control when employees get paid. It provides its service without mandatory fees, generating income entirely through a "pay-what's-fair" model.

Earnin believes that employees should have access to their pay immediately upon completion of their work. Through the mobile application that Earnin freely distributes, workers receive a portion of their wages when they want it. The technology platform that Earnin has built gives individual workers continuous access to the wages they have earned. It enables each user to decide when and how often he or she gets paid. This flexibility allows workers to manage their cash flow and to spend their wages according to their own needs and schedule, not the arbitrary schedules that employers adopt to meet the minimum requirements of state labor laws.

The Earnin service is simple to use. When an account is created, Earnin automatically pulls a user's direct deposit and employment history. Earnin has integrated with several time and attendance systems to further expedite payment. Partners include uAttend, Deputy, NimbleSchedule, TSheets, WebPunchClock, Brink Software and When I Work. Earnin is being used by employees from more than 4,000 companies.

Once Earnin verifies hours worked, it allows the person to accelerate the distribution of her paycheck (based on the person's expected take-home pay and subject to certain limits). Earnin deposits the funds directly into the person's bank account either instantly or overnight (depending on the bank that the employee uses). On the persons's regularly scheduled payday, Earnin automatically withdraws the amount from their bank account. This process allows people to use Earnin without their employer needing to sign up for it. Earnin does not charge any interest for its service. Instead, people may choose to pay what they think is fair for the service. That amount is automatically withdrawn on the person's payday.[16]

[16] *See Terms of Service,* EARNIN.COM, Section 7, https://www.earnin.com/PrivacyAndTerms#termsFees (last visited July 20, 2015) ("There are no fees to use the Service. You may make voluntary additional payments in appreciation of the services rendered. These voluntary additional payments help fund Earnin."); *see also What is Earnin? Earnin FAQ,* EARNIN.COM, https://www.earnin.com/FAQ (last visited July 20, 2015) ("There are no fees or interest; we only ask you to pay us an optional tip based on what you think is fair.").

V. Benefits of On-Demand Pay

Putting the control of payday in the hands of the employee benefits the user greatly. Earnin user William uses on-demand pay when his usual paycycle doesn't suit his needs. He says, "[Earnin] has made things so much easier to deal with when I am between paychecks. I don't have to stress or worry about how I'm going to pay them when payday is still a week away."

In a survey, 96 percent of people who use an on-demand payment method reported feeling less stress when given this flexibility.[17] One user, Heather, is familiar with the stresses of waiting for payday. "So many times I'll have a bill due on a week that I don't get paid," she says. "I used to stress; now I just click on the app and I'm done. No stress." Another user says, "[It's] such a stress reliever! When you just need that x amount of money before your next payday, it's a lifesaver."

94% of users have used on-demand pay to avoid overdraft fees or payday loans,[18] and sometimes, the issue can become even more costly. One user, Andrew, reported, "[On-demand pay] helped keep me from being homeless."

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It is to the benefit of both employers and workers to move to on-demand wages. When a worker feels in control of their finances, it improves his work, as well as his health. In the survey, 89 percent of users reported feeling more motivated and productive at work when they had access to their wages before payday, and 74 percent reported having fewer unplanned absences.[19] One user wrote, "I can't begin to explain how much [on-demand pay] has helped me get out of bad situations when times get tough and I just need some money for gas or food. [It] has been there to help me keep my bills going and has eliminated the choice of do I pay my bill or do I get to eat or drive to work."

In a study, one in four participants expressed that on-demand pay would be the best financial support their employer could offer, outranking even an increase in salary.[19]

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94% on-demand pay users have used it to avoid overdraft fee or payday loans

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1 in 4 workers express that on-demand pay would be the best financial support their work could offer

[17-18] Earnin. "Your experience with Earnin." Survey. 17 August 2015.
[19] Earnin. "Earnin Millennial Study." YPulse Survey. 12-22 September 2014.

VI. Conclusions

On-demand pay is the ideal payment solution for both individuals and companies. When individuals have access to their earned wages, they are more productive and reliable workers. Employees who have access to their pay report better attendance, less stress, and more focus.[20] These individual improvements translate into higher bottom lines for businesses. On the other hand, having control of their earnings means workers are able to manage their money better and no longer have to use exploitative and abusive alternatives in order to pay their bills.

Michael Watson, adjunct professor at Northwestern University and author of Managerial Analytics and Supply Chain Network Design, drew a comparison between on-demand pay and just-in-time (JIT) manufacturing. The JIT system involves more frequent delivery of parts in smaller quantities to an assembly line. This has led to more disciplined management and big savings. Watson sees on-demand pay providing similar benefits to individuals through smaller, more frequent paychecks that can be accessed rapidly.[21]

Gone are the days of big batch payroll and overdraft frustration. With on-demand pay, workers can breathe easier, work harder, and finally take control of their payday.

"On-demand pay can provide individuals with benefits similar to JIT manufacturing; Through smaller, more frequent paychecks that can be accessed rapidly."

[20] Earnin. "Your experience with Earnin." Survey. 17 August 2015.

[21] Michael Watson, Just In Time and Lean Concepts in New Areas (Oct. 20, 2014), http://opexanalytics.com/-just-in-time-and-lean-concepts-in-new-areas/