Bloomberg BNA

Daily Labor Report®

Compensation

Employers Paying Wages With Debit Cards Save Money But May Face Legal Hurdles

In recent years, many employers have started paying hourly workers with debit cards, a practice that is cost-effective but has prompted lawsuits from employees who claim they aren't receiving their proper wages.

Employers that use the debit card payment system generally do so because direct deposit isn't an option for all of their employees. Those that employ low-wage workers tend to have employees that don't have bank accounts, according to Matthew Hank, a shareholder and employer-side practitioner with the nationwide firm Littler Mendelson P.C.

''To pay those employees, employers find payroll debit cards, or 'paycards,' attractive because they are more flexible and convenient than paper paychecks,'' he told Bloomberg BNA in an Oct. 14 e-mail.

But workers have claimed this method can send their pay below the minimum wage, in violation of the Fair Labor Standards Act and state minimum wage laws. For example, a federal district court conditionally certified collective claims in August brought by hourly employees at a tire retailer in Florida. They claimed, among other things, that excessive transaction fees associated with the cards resulted in an FLSA violation (*Czopek v. TBC Retail Grp., Inc.*, M.D. Fla., No. 8:14-cv-00675-CEH-TBM, 8/7/15).

Hank, who is based in Littler's Philadelphia office, pointed out several factors that make the debit card payment system more attractive to employers than the traditional paper paycheck:

- When an employee paid by paper paycheck isn't scheduled to work on payday, that employee either has to wait to be paid or make a special trip to pick up a paycheck. Payroll debit cards solve that problem by making wages available immediately.

- Workers without bank accounts often incur fees when cashing paper paychecks. Debit cards solve that problem by allowing the employee to make at least one free withdrawal of wages per pay period. Employees may also use payroll debit cards to make free point-of-sale withdrawals of wages.

- When employees get cash for their paychecks, there is a risk their wages will be lost or stolen. Debit cards reduce that risk.

- By using payroll debit cards, employers avoid the administrative expenses of paper paychecks, such as the costs of check stock, toner, postage and stop-payment fees for lost or stolen paychecks.

Are Employers Getting Windfall? Jonathan Bernstein, who is a partner and represents employees for Levy Davis & Maher LLP in New York City, acknowledges that the cost savings associated with paying employees with debit cards make this system attractive to employers.

However, he also suspects that employers get an even bigger windfall than people realize. ''Just as people sometimes forget to spend the money on gift cards, which results in a windfall to the merchant, I would imagine that on occasion people forget that there are a few dollars left on the card, which would result in a windfall to the employer,'' he said.

Bernstein also acknowledged that many employees who are paid through this method can theoretically eliminate many of the fees and inconveniences they have to endure when they're paid with a paper check.

''These people are 'unbanked,' meaning they cannot afford bank fees or to keep minimum balances. This means they often have to pay high fees at check-cashing stores, money order fees, or go to the employer's bank,'' Bernstein told Bloomberg BNA in an Oct. 6 e-mail.

However, the reality of being paid with debit cards can be just as bad for these employees because many of them shop at neighborhood cash-only stores that don't accept the cards or charge fees. ''The biggest problem with the cards, of course, is the access fees (similar to ATM fees) that many users must pay. Theoretically, regulations like the ones proposed in New York would outlaw such fees,'' Bernstein said.

For employees, the biggest risks associated with this system of payment aren't only the potential fees, but ''not having access to their money,'' according to Bernstein.

To avoid any undesired fees, employees need to read and understand the instructions, and the fee schedule, before using the paycard, Hank said. ''Any reputable card will give employees the ability to access all of their wages without paying fees, but they have to know how to use it properly,'' he said.

FLSA Compliance Problems May Arise. While the FLSA doesn't regulate the method by which employers pay their workers, using payroll debit cards creates the risk that the company will end up running afoul of the law's minimum wage provisions. Using payroll debit cards to pay employees violates the FLSA ''to the extent that any fees associated with the cards would bring the employee's wage below the applicable minimum wage,'' Bernstein explained.

Hank acknowledged that the use of payroll debit cards carries risks for the employer, as FLSA regulations forbid any payment method that doesn't provide wages to the employee ''free and clear.''

''The use of payroll debit cards requiring the employee to pay fees in the course of withdrawing wages could, theoretically, violate that provision of the FLSA,'' Hank said. However, he also stated that this aspect of the FLSA is rarely implicated by the use of payroll debit cards because all reputable payroll debit cards allow employees to access all of their wages without paying fees.

According to Hank, the biggest risk to employers is legal, as employers must navigate a patchwork of federal and state laws regarding payroll debit cards. ''The laws in question are rarely intuitive, were usually written well before payroll debit cards even existed, and are often unknown to employers. That's why it is easy for even well-meaning employers to violate the laws governing payroll debit cards,'' explained Hank.

Although payroll debit cards are beneficial for employers and employees, Hank said employers should obtain independent legal advice tailored to each state in which they operate before using the cards to pay employees. ''When wage and hour violations do occur, they attract regulatory audits, class-action litigation, and penalties that can be ruinous for small companies,'' Hank said.

Legal and Regulatory Actions Afloat. The New York State Department of Labor has taken one of the most significant recent government attempts to address the problems of payroll debit cards. It published and implemented new regulations on the subject this summer. In New York State alone, an estimated 13,000 businesses pay approximately 200,000 workers through debit cards.

Under the new regulations, payment through a debit card requires the advance consent of the employee, which businesses must document and keep on record for six years. They also require employers to notify employees about nearby locations where they can access their wages for free and to provide unlimited free ATM withdrawals within a local network as well as a method to withdraw the full amount of wages each pay period. Fees for customer service, account maintenance, overdraft and inactivity are expressly prohibited.

While these rules are meant to protect employees' wages, the additional burden on employers to issue them and the lowered profitability for banks could make the cards a less attractive payment option, Hank said.

Bernstein said the new regulations add an administrative burden on employers, but he said such a burden would be minimal. ''However, to the extent that the regulatory prohibition on fees causes financial service providers to shift costs to the employer, the regulations might undermine the cost saving to the employer,'' Bernstein stated.

As for other states, Bernstein pointed out that New Jersey has also promulgated regulations that are similar to those in New York. The federal Consumer Financial Protection Bureau has also promulgated a rule that requires short- and long-form explanations of associated fees to be provided to payroll debit card users as well as language indicating that receiving wages via debit cards is voluntary.

Both litigators agree that in general, regulatory oversight of the use of paycards and private lawsuits involving alleged violations of the law surrounding paycards have increased. ''Although some of the regulatory oversight has ranged from skeptical to hostile, and some of the lawsuits have highlighted the risks of using paycards improperly, more recently employers' interest in paycards has increased, not decreased,'' Hank said.

Hank also noted that employers are approaching the use of debit cards with more sophistication. Specifically, they're taking steps to ensure that their paycard programs are legally compliant before they begin using the cards, and they are also attempting to reduce their exposure to class actions surrounding payroll debit cards, such as implementing arbitration programs with class-action waivers.

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   ISSN 0418-2693