PAYDAY

FORTHCOMING: 98 WASH. U. L. REV. 1 (2020)
Draft: Comments, Suggestions, and Critique Welcome!

Yonathan A. Arbel[*]

Legislation lags behind technology all too often. While trillions of dollars are exchanged in online transactions—safely, cheaply, and instantaneously—workers still must wait two weeks to a month to receive payments from their employers. In the modern economy, workers are effectively lending money to their employers, as they wait for earned wages to be paid.

The same worker who taps a credit card to pay for groceries in semi-automated checkout lines depends on dated payroll systems that only transfer payments on a "payday." Workers, especially those living paycheck-to-paycheck, are hard-pressed to meet their daily needs and turn to expensive, short-term credit—notably, payday lenders. These credit solutions may address a real need, but they also exact a heavy price, often culminating in endless debt spirals. So, why does the payday still exist?

This Article studies various explanations—economic, historical, behavioral, and legal. It concludes that the payday is a software problem, not a hardware problem. The hardware—i.e., money and payroll technology—is here; indeed, gig economy workers in developing countries will often be paid more quickly than an American employee for the same work. What holds us back is our legal software: Dated Eisenhower-era legislation that failed to anticipate technological change. Surprisingly, even pro-worker legislation, such as minimum wage laws, inadvertently encourage the practice.

By revealing the overlooked and dated legal infrastructure that sustains the payday, the Article suggests a path for legal reform. Daily streams of payment to workers are feasible, practical, and far more efficient than most people realize. A focused reform could effectively bring an end to the puzzling and pernicious practice of having workers lend money to their employers while they wait for their payday.

[*] Assistant Professor of Law, University of Alabma, School of Law. [many thanks] A companion playlist can be found here: http://bit.ly/payday_comp

INTRODUCTION

Legislation often lags behind technology. As Guido Calabresi observed, "laws are governing us that would not and could not be enacted today."[1] Nowhere is this failure more evident, nor more damaging, than in the context of employment contracts. Payment technology has made incredible advances, and today trillions of dollars are traded in the online economy, moving between parties almost instantaneously.[2] At the same time, workers still wait for weeks until a formal "payday" to receive their hard-earned wages. While workers sell their labor today, employers only pay them in the future, leveraging wages as another line of credit.

We seem to take the payday's existence for granted,[3] but it exacts a heavy price. Workers who wait for payment need to support themselves; the vicissitudes of everyday life—a sudden toothache, a flat tire, a stain on their only clean work shirt—demand money, now.[4] With many workers living paycheck-to-paycheck,[5] the current payday system pushes them to payday lenders and other short-term credit

[1] GUIDO CALABRESI, COMMON LAW FOR THE AGE OF STATUTES 2 (1982).

[2] *16.9%+ Growth for Online Payment Gateway Market Size Raising to USD 4020 Million by 2024*, MARKETWATCH (May 21, 2019), https://www.marketwatch.com/press-release/169-growth-for-online-payment-gateway-market-size-raising-to-usd-4020-million-by-2024-2019-05-21.

[3] The modern literature has mostly neglected this question. This omission is perhaps most glaring in law and economics analyses of employment contracts, but it is by no means confined to these works. *See, e.g.*, RICHARD POSNER, THE ECONOMIC ANALYSIS OF LAW (9th ed. 2014) (reviewing major topics but neglecting pay frequency); MARK ROTHSTEIN & LANCE LIEBMAN, EMPLOYMENT LAW, 420-21 (2011) (adumbrating pay frequency). *But cf.* JOHN R. COMMONS & JOHN B. ANDREWS, PRINCIPLES OF LABOR LEGISLATION 50–52 (1916) (noting the credit nature of the payday).

[4] The three leading reasons why individuals borrow from alternative lenders (such as payday lenders, pawn shops, and rent-to-own stores) are basic living expenses, making up for lost income, and house and car repairs. Neil Bhutta et al., *Consumer Borrowing After Payday Loan Bans*, 59 J.L. ECON. 225, 240 (2016). *See also* Rob Levy & Joshua Sledge, *A Complex Portrait: An Examination of Small-Dollar Credit Consumers*, CTR. FOR FIN. SERVS. INNOVATION 12 (Aug. 2012), https://www.fdic.gov/news/conferences/consumersymposium/2012/A%20Complex%20Portrait.pdf (reporting that approximately 37% of borrowers borrowed because "[they] had a bill or payment due before my paycheck arrived." In addition, 30% of respondents borrowed to meet some unexpected expense, another likely result of the payday). *See also* Nicholas Bianchi & Rob Levy, *Know Your Borrower: The Four Need Cases of Small-Dollar Credit Consumers*, CTR. FOR FIN. SERVS. INFO. 12 (2013), https://s3.amazonaws.com/cfsi-innovation-files/wp-content/uploads/2017/01/26054909/Know-Your-Borrower-The-Four-Need-Cases-of-Small-Dollar-Credit-Consumers.pdf (finding that 32% of consumers borrow because of misaligned cash flow and 32% to meet an unexcepted expense. Again, both reasons can be mitigated by regularized pay.).

[5] 15% of households reported having spent more than they earned over the last year. FED. RES. SYS., *Changes in U.S. Family Finances from 2013 to 2016*, 103 FED. RES. BULL. 1, 8 (2017). In addition, 40% of respondents said that "if faced with an unexpected expense of $400 [they] would either not be able to cover it or would cover it by selling something or borrowing money." *See also Report on the Economic Well-Being of U.S. Househoulds in 2017*, BD. OF GOVERNORS OF THE FED. RES. SYS. 56 (2018), https://www.federalreserve.gov/publications/files/2017-report-economic-well-being-us-households-201805.pdf.

providers that dot the modern urban landscape.[6] A payday loan is meant to help the worker bridge the gap until payday, but it involves interest rates which can be *twenty times* higher than those of credit cards. A $300 loan can quickly balloon into thousands of dollars of outstanding debt, leading to a debt spiral that can culminate in deep financial distress and even bankruptcy.[7]

This Article argues that payday is not a hardware problem; rather, it is a software problem. The hardware of the economy, both money and payroll technologies, have greatly advanced over the last century, allowing us to quickly and cheaply pay for both goods and services. To wit, a freelancer doing work in India for an American employer as part of the gig economy, who performs the same work as an American employee, will often be paid faster.[8] What hinders progress is our legal software:[9] Eisenhower-era legislation that failed to keep pace with modern technology. In fact, as this Article reveals, the culprit is often pro-worker legislation, which stands in the way of progress, sometimes actively encouraging longer pay periods. This Article suggests ways to reform legislation and to move workers to daily streams of payment, which will increase liquidity, enhance worker autonomy, reduce the size of the payday lending industry, and improve the American economy as a whole.[10]

The analysis of the payday covers a variety of potential explanations for its dogged persistence: economic, sociological, historical, legislative, and even psychological. On close analysis, none of these explanations justifies the payday. The employment relationship is, at its core, an exchange of money for labor.[11] The payday also injects into this relationship a credit transaction, one

[6] Paige Marta Skiba, *Regulation of Payday Loans: Misguided?*, 69 WASH. & LEE L. REV. 1023, 1031 (2012) (Noting that "payday lenders outnumber both Starbucks and McDonalds"). Roughly 64% of all adult Americans have at least one credit card and carry an average balance of $4,800. In addition, roughly 50% of all credit card holders carry a revolving balance on which they pay interest. *The Consumer Card Credit Market*, CONSUMER FIN. PROTECTION BUREAU 46–55 (2017), https://files.consumerfinance.gov/f/documents/cfpb_consumer-credit-card-market-report_2017.pdf.

[7] To experience firsthand the process of obtaining a payday loan, I borrowed $200 from a payday lender in Tuscaloosa, Alabama. I signed a postdated check to the benefit of the lender for $235, representing a 638.75% APR. *See* @ProfArbel, TWITTER (Nov. 22, 2019, 5:05 PM), https://twitter.com/ProfArbel/status/1198014702762283008. Sociologist Lisa Sevron worked for a payday lender and reported her experiences in LISA SEVRON, THE UNBANKING OF AMERICA (2018).

[8] The online platform upwork.com transfers payments within two days. *How Long to Get Paid?*, UPWORK COMMUNITY (June 21, 2017), https://community.upwork.com/t5/Freelancers/How-long-to-get-paid/td-p/361423.

[9] Conceptualizing legislation as software is productive in other regards and suggests a different paradigm to that envisioned in CALABRESI, *supra* note 1, with updates, revisions, branches, and commits—issues that would require a separate detailed treatment. *See generally Git Theory*, GITHUB, https://github.com/SCOREC/core/wiki/Git-Theory (last visited Feb. 13, 2020).

[10] For conceptual clarity, daily streams of payments are no longer payday in the conventional sense of a special day which aggregates pay for multiple days of work.

[11] *See, e.g.*, COMMONS & ANDREWS, *supra* note 3, at 2 (describing the employment contract as a "relation between a propertyless [sic] seller of himself, on the one hand, and a propertied buyer on the other").

where the employee is lending money to the employer. But this is a credit transaction that is completely artificial from the viewpoint of financial analysis. Put simply, workers should not be in the business of lending money to their employers.[12] Not only do workers lack capital or comparative specialization in lending, but they are also badly positioned to deal with counterparty risk.[13] The other explanations investigated likewise fail to pass muster.

This Article highlights the importance of bringing the economy's software up to date by showing how the very meaning and effect of legislation can be completely upended due to social and technological changes. Payday legislation started as a mode of progressive reform towards the end of the nineteenth century. Overcoming initial resistance from legislators and courts, payday laws were passed to discourage predatory behavior of companies, which were lending to their employees at usurious rates. Remarkably, despite the poor money and payroll technologies that existed at the time, the legislation was effective and for a short period of time, workers were paid weekly. By an ironic twist of fate, it is possibly the rise of the welfare state that led to the move from weekly to the much slower biweekly pay.[14] The birth of the welfare state was spurred by the introduction of social security and social security taxes. The administrative burden occasioned by various related laws, such as the Federal Insurance Contributions Act (FICA), the Federal Unemployment Tax Act (FUTA), the Fair Labor Standards Act (FLSA), and tax withholdings made frequent pay more difficult. Thus, the same laws that were meant to protect employees ended up harming them in an unanticipated way: by depressing the frequency of pay, they increased the need for expensive short-term credit solutions.

Today, however, many of the technological barriers to frequent pay are all but resolved. The computation of pay, once a real problem, is quickly and effectively done by payroll software. The costs of transferring payments are negligible for most employees, and for the remaining minority of unbanked and underbanked workers,[15] Fintech (companies specializing in financial technologies) alternatives abound, most promisingly through payroll cards that do not require a deposit account. Digital money is the reality for most Americans today, and neither the computation of pay nor its transfer are significant barriers to regular payments to employees. Thus, the Article concludes that moving to daily streams of payment is both feasible and desirable, although it contemplates a transition period.

[12] *See infra* Part I.B for a discussion of this point.

[13] Counterparty risk is defined as the "the likelihood or probability that one of those involved in a transaction might default on its contractual obligation." Chris B. Murphy, *Counterparty Risk,* INVESTOPEDIA (May 14, 2019), https://www.investopedia.com/terms/c/counterpartyrisk.asp

[14] There are various terms of art used to describe pay frequency. For expositional simplicity, this Article refers to payment modes that are more frequent than once a month and less frequent than once a week as 'biweekly.' *See infra* Part II.A.

[15] I discuss the phenomenon and problems of the unbanked and underbanked *infra* notes 184–197 and accompanying text.

This Article unfolds in four Parts. Part I offers a basic framework for analysis and the historical background for the payday. Part II explores a variety of potential explanations and justifications for this practice. Part III explains why the payday should be abolished and Part IV explains how this could be achieved in practice.

To understand why the payday exists, Part I covers the basic theory of employment contracts. It explains why the payday is not a natural part of employment contracts and why, from a finance perspective, it is an artificial and inefficient credit transaction.

If financial logic doesn't explain the existence of payday, what does? Part II explores a variety of potential explanations—historical, legal, economic, psychological, and sociological. Special attention is given to a psychological attempt to justify the payday: the idea that the payday helps employees overcome some of the behavioral challenges of saving and budgeting their own money.[16] Refuting this idea is important because some might worry that moving to daily streams of payment would lead to profligacy among employees. To this end, I present empirical evidence that frequent pay does not increase spending. In fact, there is some reason to worry that infrequent pay may result in excessive spending, because of the higher availability of cash on hand. Most important, however, is the argument that employer-side savings are extremely risky, as they expose employees to opportunistic behavior, counterparty risk, and employer bankruptcy.[17] To the extent that workers need help managing money, an insured, trusted financial institution provides a much more robust solution than the postponing wages.

What appears to be the reason why the payday still lingers is ineffective legislation. For public sector employees, legislation often mandates by fiat long pay periods. The President of the United States is paid, by law, on a monthly basis.[18] In the private sector, badly drafted legislation also encourages late payments; in particular, and not without irony, wage and hour legislation unwittingly encourages long pay schedules. These defects, overlooked by employment law scholars and policymakers, have substantial consequences for the welfare of employees.[19]

Understanding the sources of the payday allows the development of solutions. Part III first explains the large stakes involved in abolishing the payday. It then explains why abolishing the payday is imperative and why seemingly more moderate alternatives, such as advance payments, are insufficient and risky. It

[16] Christopher A. Parsons & Edward D. Van Wesep, *The Timing of Pay*, 109 J. FINANC. ECON. 373 (2013).

[17] *See also* Shlomo Benartzi et. al., *The Law and Economics of Company Stock in 401(k) Plans*, 50 J.L. & ECON. 45, 46 (2007) (arguing that employees over-invest in their employers' stock and that "investing a dollar in company stock . . . is often worth only 50 cents.")

[18] 3 U.S. Code § 102. U.s. Const. art. II § 1(7) ("The President shall, at stated Times, receive for his Services, a Compensation").

[19] The Restatement of Employment Law defers to the employer's choice regarding the payday. RESTATEMENT OF EMP'T LAW § 3.01 (AM. LAW INST. 2015) ("Employees also have a right to be paid the compensation they have earned on a timely basis, usually in conformity with the employer's normal payroll practices.")

then examines the legislative changes that would be needed to abolish the payday.

The key proposal here, developed in Part IV, is to move from biweekly pay to daily streams of payment of the good faith estimate of the employee's daily pay. Every two weeks, the employer will have an "accounting day," and will add to the day's pay any shortfall in payments. For the part of the workforce that is either unbanked or underbanked, payments can be made using pay cards and similar Fintech solutions. While there are some nuances and practical considerations in implementing this proposal, it is important to recognize at the outset that it does not derogate from the rights of either employees or employers. By contrast, adopting this proposal will greatly advance the welfare of all American employees and would also take a bite out of the large payday lending industry, increase worker autonomy, and correct some historical defects in legislation. In fact, implementing this proposal only requires modest changes to the legislative framework.[20]

While lawyers and economists debate the merits of the payday loan industry,[21] it is widely agreed that it responds to a real need for liquidity and that it charges a very high price for this service.[22] Solving this need has proved, so far, almost intractable. Abolishing the payday would greatly increase the liquidity of households, thus considerably reducing the demand for payday loans. Even by itself, this outcome makes the abolishing of the payday a compelling social policy.

Even if one disagrees with any of the specific policy prescriptions, the key message of this Article is that the payday should not be taken as a neutral or natural fact of the modern economy. The existence of the payday has substantial consequences in terms of efficiency, distribution, and autonomy. While we live in an exceptional period with historically low-interest rates; the harms of the payday will only be amplified as interest rates rise.[23] It is time to revisit this practice.

[20] Pay frequency interacts in complex ways with a variety of workers' rights and issues, such as wage theft, wage discrimination, and minimum wage. For example, frequent pay would expand workers' ability to sue for equal-pay violations, as the Lilly Ledbetter Fair Pay Act of 2009, Pub. L. No. 111-2, 123 Stat. 5 (codified at 42 U.S.C. § 2000e-5 (2009)) holds that every payment resets the 180-day statute of limitations. In general, frequent pay will either not derogate from worker rights or expand them.

[21] *See* Bhutta et al., *supra* note 4, at 226 (noting the debates). *See also* John P. Caskey, *Payday Lending: New Research and the Big Question*, *in* OXFORD HANDBOOK OF THE ECONOMICS OF POVERTY, 250 (2012) (concluding that "despite research efforts of a talented group of economists, we still don't know" whether payday lending helps their customers").

[22] MEHRSA BARADARAN, HOW THE OTHER HALF BANKS 108 (2015) ("Regulating the industry . . . is, in part, difficult because of the incredible market demand for what they offer.").

[23] *Federal Funds Rate—62 Year Historical Chart*, MACROTRENDS, https://www.macrotrends.net/2015/fed-funds-rate-historical-chart (last visited Feb. 13, 2020).

I. THE PAYDAY PUZZLE

A. The Two Employment Contracts

What is the purpose of an employment contract? Roughly 128 million Americans are considered employees and are thus parties to an employment contract.[24] These contracts feature a great deal of variability, as they each stipulate different norms the employee must abide by—the employee's various rights, benefits, and perquisites, as well as the employee's duties, obligations, and loyalties. Still, at its core, the contract is premised on a very basic economic transaction: "a bargained-for exchange of labor for consideration."[25] The employment contract is an exchange relationship, which the parties seek to optimize according to their own circumstances.[26]

This exchange transaction stands at the heart of the employment contract, and I denote it here as K_1. In this K_1, the employee is selling labor, broadly defined as time, skill, effort, and any other aspect of his or her human or social capital. In consideration, the employer gives the employee "money," which could include wages, tips, perquisites, in-kind transfers, and any other value that redounds to the employee from the employer. When the employment contract describes the employee's duties, it outlines the scope of labor that is exchanged. When the employment contract stipulates the employee's pay and benefits, it states the payment that is exchanged for this labor. The concept of K_1 is sufficiently capacious and abstract to capture all employment contracts, despite the fact that they differ in almost any other respect. In this high level of abstraction, we can say that K_1 is responsible for the annual exchange of at least 55 trillion dollars.[27]

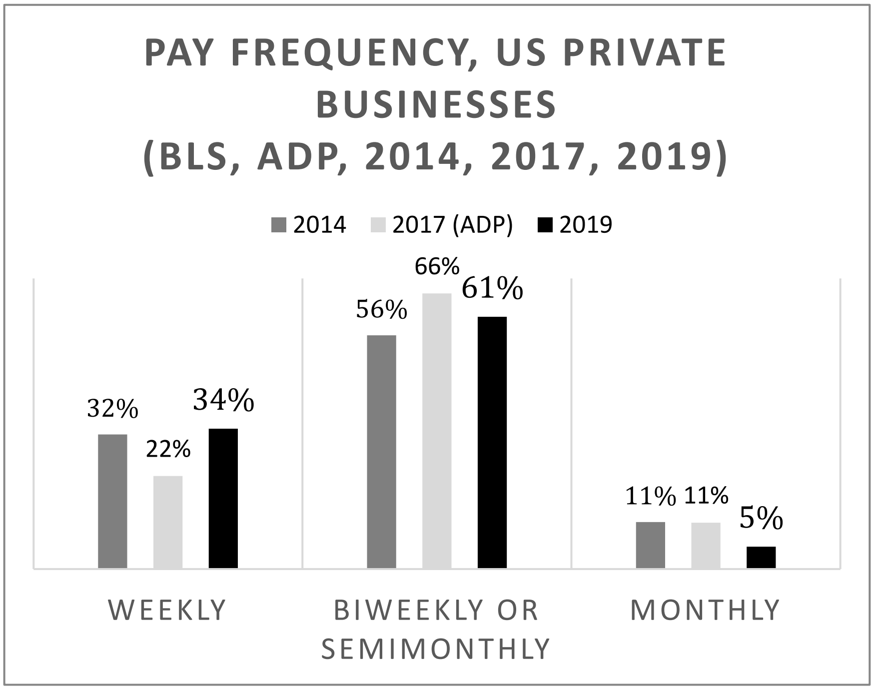
What both economists and lawyers will often miss is another striking regularity in modern employment contracts. Besides the K_1 aspect of the transaction, most contracts also include a *payday*—a gap in time between the moment work is rendered and payment is transferred. Almost all payments by the employer are paid in *arrears*—that is, *after* the employee "gave" their labor to the employer. The following figure summarizes the frequency of the payday and the typical lag involved in payments, based on data made available by the Bureau of Labor Statistics for the years 2014 and 2019:

[24] *Labor Force Statistics From the Current Population Survey*, BUREAU OF LAB. STAT. (2019), https://www.bls.gov/cps/cpsaat08.htm.

[25] Vanskike v. Peters, 974 F.2d 806, 809 (7th Cir. 1992).

[26] PATRICK BOLTON, CONTRACT THEORY 4 (2005) (studying the optimal design of the exchange relationship).

[27] This estimation is based on Bureau of Labor Statistics data. *Usual Weekly Earnings of Wage and Salary Workers, Third Quarter 2019*, BUREAU OF LAB. STAT. (2019), https://www.bls.gov/news.release/pdf/wkyeng.pdf.



This figure summarizes pay frequency data for almost all employees in the economy.[28] As can be seen, most American employees are paid twice a month, on either a biweekly or a semimonthly basis.[29] The difference between biweekly and semimonthly is fairly subtle; a biweekly payday takes place every fourteen days, while a semimonthly payday takes place twice a month, on two separate days (e.g., the 1st and the 20th). Given the existence of fifty-two workweeks in a year, this means that a biweekly payday translates to either twenty-six or twenty-seven paydays per year, whereas a semimonthly payday entails a fixed number of twenty-four paydays. Beyond the twice-monthly pay, a sizable minority of employees are paid weekly and a small minority on a monthly basis.[30]

The existence of a payday may seem obvious—indeed, many take it for granted—but it hides significant complexity. The worker is providing work today: stacking the shelves, cleaning the floor, building a wall, attending to customers, etc. But for services rendered today, the employee is only paid in the future, on payday. In other words, payments in the economy are, by and large, in arrears. To be

[28] *Length of Pay Periods in the Current Employment Statistics Survey*, BUREAU OF LAB. STAT. (2019), https://www.bls.gov/ces/publications/length-pay-period.htm#fn5 (farm workers were excluded from the study). The ADP data comes from a private payroll company, ADP, as reported in Cajner, Tomaz et al., *Using Payroll Processor Microdata to Measure Aggregate Labor Market Activity, Finance and Economics Discussion Series 2018-005*, BD. OF GOVERNORS OF THE FED. RES. SYS. 44 (2018), https://doi.org/10.17016/FEDS.2018.005.

[29] Biweekly also denotes twice a week; however, in the wage payment context, it is used to denote payment frequency of once every 14 days.

[30] The data collection methodology is not sufficiently clear to discern what share of American employees are paid on shorter time spans than weekly.

sure, one could define work in two-weeks increments, such that the employee only earned pay once she has completed two weeks worth of pay. In fact, employers tried to make this argument by defining the work as only coming in a one-year installment.[31] This way, employers hoped, they did not have to pay until the end of the year and if the employee quits—or is encouraged to quit—before the end of the year, they could avoid the obligation to pay. For sound policy reasons, courts and legislators rejected this view. More theortically, if the employee is understood to be selling time, then time does not come at two weeks increments.[32]

Thus, the very idea of the payday implies a temporal distance between the moment the employee is providing services, the quid in K_1, and the moment she is paid, the quo of K_1. As noted by Commons and Andrews in their 1908 treatise on labor law:[33]

> When the laborer starts to work for [the employer], he also becomes, for a time, a creditor. He contributes his services in advance of compensation. He is a temporary investor in the business. While he works he passes over to the employer the title to his product, and retains a claim for wages. When his wages are paid his investment is liquidated.

The economic classification of this aspect of the transaction is straightforward. When a person buys a car from the dealership, he or she can pay on the spot for the exchange. But he or she can also agree with the dealer to pay in the future, perhaps in monthly installments. This is the financing part of the exchange. By the same logic, when an employer receives services today but pays for them in the future, on payday, this is a credit transaction. In addition to the exchange relationship, what we called K_1, the employment contract thus embodies a second credit transaction, what we might call K_2. This K_2 contains the agreement between the parties to defer payment for money *earned* until payday. The parties will not always explicitly set the payday in the contract, but of course, they agree to some kind of payday—and this part of the agreement, explicit or implicit, makes K_2. As in any credit agreement, we can identify three parts: an employee-lender, and employer-borrower, and wages-principal.

A natural question is whether this is a true credit transaction, as K_2 does not seem to indicate any interest rates. This, however, should not be too distracting: Credit transactions do not require

[31] Britton v. Turner - 6 N.H. 481 (1834) (holding that, despite the employee quitting before the end of the stipulated year of work, the employer still had an obligation to pay under restitution); di Matthew T. Bodie, *Employment As Fiduciary Relationship*, 105 GEO. L.J. 819, 840, note 133 (2017) ("Modern wage payment schemes require that employees be paid . . . for all time worked, regardless of the length of the term").

[32] With independent contractors, it is sometimes the case that payment is made on an project-completion basis (even though, even there, advances are common). Employment contracts, however, normally separate work tasks and payment, and pay on the basis of time worked.

[33] COMMONS & ANDREWS, *supra* note 3, at 50.

explicit quotes of interest or even any interest at all to count as credit transactions. Consider how auto traders will sometimes offer 'zero-interest financing.' The auto trader will not really offer a free loan, but rather, will build the cost of the loan into the price of the car. Some part of the price, then, can be seen as interest—the premium the dealer charges for offering 'free' finance. And even if the trader charges no interest at all, it would still be a loan that would have to be repaid on pain of default and collection. That is to say, a loan is a loan even if it does not involve interest payments.[34]

The labor economist would emphasize the possibility of a *wage premium*. It may be possible, at least in theory, that the employer is paying implicit interest through higher pay, what economists call a "compensating wage differential."[35] In the standard economic model of wages, what determines wages is productivity—how much value the employee is producing for the employer. When an employee offers credit in addition to labor, the employee is more "productive" in a sense. Hence, the wage should reflect this.[36] Consider an employee earning $1,923 biweekly.[37] This salary can be broken down to $1,800 for K_1 and $123 for K_2. Of course, this breakdown is arbitrary; moreover, whether the wage premium actually exists is an empirical question that depends on market organization and regulation. This empirical question has not been investigated to date and so I will not make any specific assumptions on the size of this wage premium—indeed, in some cases it may well be zero.[38] What I wish to show is

[34] Loans also have a maturity date; here, the it is the payday. In a biweekly K_2, the worker lends 1/14 of the salary daily to the employer. The period until maturity shortens every day; at first, the loan is for 13 days, but on the last day of work, the loan is only for that same day. On average, the maturity date is 6.5 days in the future and the loan is remade every two weeks. In a daily pay system, the loan mature on the same day it is paid, so it involves minimal interest, and so I do not explore here the possibility of hourly pay.

[35] The existence of wage premiums was consistently confirmed. *See e.g.,* Don Fullerton & Gilbert E. Metcalf, *Tax Incidence*, NAT'L BUREAU OF ECON. RES. 28 (Mar. 2002), https://www.nber.org/papers/w8829.pdf (Noting that the shared incidence of payroll taxes "has been tested and confirmed repeatedly."); Johnathan Deslauriers et al., *Estimating the Impacts of Payroll Taxes: Evidence from Canadian Employer-Employee Tax Data*, INST. OF LAB. ECON. (2018), http://ftp.iza.org/dp11598.pdf ("The consensus is that [payroll] taxes are partially to completely shifted to workers, at least in the long run."). *But see* Saez, E, B. Schoefer, and D. Seim, *Payroll Taxes, Firm Behavior, and Rent Sharing: Evidence from a Young Workers' Tax Cut in Sweden*, CEPR Discussion Paper No. 12391 (2017) (finding firm-level differences in incidence and employment effects of payroll tax cuts). In other contexts, see e.g., John M. Abwod & Orley Ashenfelter, *Anticipated Unemployment, Temproary Layoffs, and Compensating Wage Differentials*, *in* STUDIES IN LABOR MARKETS (1981) (premium for risk of layoffs); John R. Graham et al., *Employee Costs of Corporate Bankruptcy*, NAT'L BUREAU OF ECON. RES. 25922 (Jun. 2019) (Bakruptcy risk).

[36] PIERRE CAHUC, STEPHANE CARCILLO & ANDRE ZYLBERBERG, LABOR ECONOMICS 82–83 (2d ed. 2014) (exploring, in the simple model of labor demand, optimal wages).

[37] Analysis based on data from the Social Security Administration. *Measures of Central Tendency for Wage Data*, SOC. SECURITY ADMIN., https://www.ssa.gov/oact/cola/central.html (last visited Feb. 13, 2020).

[38] Interestingly, minimum wage legislation may be a reason why employers would not offer a wage premium. Minimum wage legislation only mandates nominal payments and does not require any wage frequency. If the employee would have been willing to work for less money but for the law, the employer may be able to offset some of the cost of the minimum wage by paying less frequently, offering no wage premiums, and still retaining the employee.

that even if one assumes that a wage premium exists, it will normally not be enough to compensate the employee for the cost of providing credit.

*

To quickly recap, so far, we have considered the existence of two "contracts" implicit in the employment relationship: K_1 and K_2. K_1 is the standard exchange of labor for money; K_2 is the credit transaction whereby payments for K_1 will only be made on payday. The K_2 loan includes some "interest" payment in the form of higher than otherwise wages. With this in mind, we can turn our attention to how odd K_2 appears from a finance perspective.

B.The Puzzle of K2

Finance theory teaches that, at the most fundamental level, loans create value by moving money from those who have it to those who need it.[39] Banks lend money to cash-strapped businesses, venture capitalists to promising entrepreneurs, and bondholders to growing companies. If the borrower is successful, she pays back the principal and compensates the lender with interest. Naturally, the lender will not lend if the interest payment is too low to reflect the risk inherent in the investment and the cost of giving away one's money. The borrower, on the other hand, will not borrow if the interest payments will completely erode the profits of the investment. We would thus expect interest payments to be in between these two ends—the cost of lending and the value of borrowing. In other words, the extension of credit creates value that benefits both parties to the transaction.

K_2 is also a credit transaction, so it might seem like it would obey a similar logic. Observe that, in practice, K_2 covers almost all employment contracts in the economy. It covers the Walmart employee stocking the shelves, the grocery store teller working the register, and the cook at McDonald's flipping the burger; it covers employees from store clerks to university professors to executives. In all of these cases, K_2 facilitates a loan from employees to employers—it is a loan from those with little money to those with more money. Why, then, is the Walmart employee lending money to Walmart? Why are service technicians lending money to Comcast? And why are police officers lending money to the government? Despite K_2 being a credit contract, it defies the logic of finance.[40]

The puzzle of K_2 is perhaps clearest when it is practiced by firms that do not even need money. Consider how the publicly listed firm

There is empirical evidence that employers sometimes cut fringe benefits in response to higher minimum wages. Jeffery Clemens et al., *The Minimum Wage, Fringe Benefits, and Worker Welfare*, NBER Working Paper-24635 (2018), https://www.nber.org/papers/w24635.pdf.

[39] *See generally* Dan Bernhardt, *Money and Loans*, 56 REV. ECON. STUD. 89 (1989).

[40] An early court decision, discussing wage statutes, recognized this issue: "[the] statute was intended to protect that class of laborers only who, as a rule, are dependent upon their daily wages for subsistence, and who enter upon their employment with no view of giving credit to the corporation for their wages, and, expecting prompt payment, had no occasion to rely on its credit or solvency. Palmer v. Van Santvoord, 47 N.E. 915, 917 (1897).

Alphabet, despite holding $117 billion in cash, still uses K_2 with its janitors, programmers, and marketers.[41] Apple holds $100 billion in cash, and Microsoft lags with only $50 billion, yet both use the payday.[42] The Federal Government is also not particularly cash hungry, and yet it mandates the use of a biweekly payday in all of its employment contracts.[43] (Even employees of the Federal Reserve—which quite literally prints money—are paid on a biweekly basis).[44]

But even for businesses that need cash, borrowing from their employees makes little sense. When a business has a profitable business opportunity but lacks liquidity, it can fund it using banks, financial markets, and sophisticated investors or lenders. The business will also often have assets to secure the loan. As a result of this and the specialization of lenders, even small businesses can borrow at a rate of 4%–8% per year.[45] If we use this rate to measure the gain the business receives from paying employees in arrears, it becomes clear that the gain is fairly small. For an employee earning $50,000 who is paid on a monthly basis, the *annual* payday credit benefit to the employer is only $105.[46]

By contrast, workers are often subject to severe liquidity constraints which makes it very costly for them to offer loans to their employers. Many Americans simply lack the funds to lend in the first place: 40% of Americans carry a credit card balance,[47] and roughly one-third of households in the lowest and second-lowest income quintile reported difficulty paying their daily expenses.[48] Securing funding is a real issue to many households: In a survey, roughly 21% reported that they were either turned down from credit or feared credit denial.[49]

[41] Richard Waters, *Alphabet Overtakes Apple to Stake Claim as King of Corporate Cash Pile*, FIN. TIMES (Aug. 1, 2019), https://www.ft.com/content/332dd974-b349-11e9-8cb2-799a3a8cf37b.

[42] *Id.*

[43] 5 U.S.C. § 5504 (2018).

[44] Phone Conversation with Payroll Department, 2.5.2020.

[45] *See* FED. RES. BANK OF KAN. CITY (Sep. 2019), https://www.kansascityfed.org/~/media/files/publicat/research/indicatorsdata/smallbusiness/2019/sbls_aggregatedatapdf_sept2019.pdf?la=en; Alina Comoreanu, *Credit Card Landscape Report – Terms, Trends & More*, WALLETHUB (Oct. 17, 2019), https://wallethub.com/edu/cc/credit-card-landscape-report/24927/#interest-ratesl-business-loan-interest-rates.

[46] Analysis assumes 5% APR, a monthly pay cycle, and the average salary in 2019 of $50,000. The benefit is much smaller for biweekly and weekly pay.

[47] *The Consumer Credit Card Market*, *supra* note 6, at 55. The bottom 20% of Americans have a median $2,000 in financial assets. *Survey of Consumer Finances*, BD. OF GOVERNORS OF THE FED. RES. SYS., https://www.federalreserve.gov/econres/scfindex.htm (last visited Feb. 13, 2020) (Table 6.89); *cf.* Kathleen Elkins, *Here's How Much Money Americans Have in Savings at Every Income Level*, CNBC (Oct. 11, 2018), https://www.cnbc.com/2018/09/27/heres-how-much-money-americans-have-in-savings-at-every-income-level.html ("29% of households have less than $1,000 in savings.)

[48] Julie Siebens, *Extended Measures of Well-Being: Living Conditions in the United States: 2011*, Figure 4, U.S. CENSUS BUREAU (2013), https://www.census.gov/prod/2013pubs/p70-136.pdf.

[49] *See* FED. RES. SYS., *supra* note 5, at 27–28 (2017). *See also* Matt Tatham, *The Decline of the Unbanked and Underbanked*, EXPERIAN (Mar. 25, 2019),

The lack of access to funds is not only a financial issue; concerns with liquidity create financial stress, which is associated with higher mortality and worse health outcomes.[50]

Employees are not in a position, nor do they have the skills, to lend money to their employers;[51] rather, many households find themselves borrowing money to bridge the gap until payday.[52] To meet this demand, there are a plethora of short-term credit solutions—such as payday lenders, credit card companies, advance tax refunds, and pawnshops—and the size of these industries illustrates the demand for credit among households.[53] The cost of such borrowing is considerable. Congress estimated (quite crudely) that every late-paid dollar costs the employee an additional dollar—i.e., 100% cost of borrowing.[54] However, the real costs tend to be even higher. When households borrow, they use a variety of sources, which include bank loans (with a ~10% cost of borrowing on average),[55] credit cards (a 19% cost of borrowing),[56] and payday lenders (a 400%-600% cost of borrowing).[57] For those households that use payday lending regularly, the cost of finance can amount to a large percentage of their annual earnings.

Critically, K_2 is not a one-off transaction. It is not just that households need to bridge the first two weeks of employment; instead, K_2 involves a continuous cycle of borrowing and repayment. Consider a hypothetical low-pay employee starting work on January 1, 2020,

https://www.experian.com/blogs/ask-experian/research/the-decline-of-the-unbanked-and-underbanked/ (In 2017, nearly 20% did not have access to mainstream credit. In 2017, 14 million with no bank account)

[50] Todd H. Baker, *FinTech Alternatives to Short-Term Small- Dollar Credit: Helping Low-Income Working Families Escape the High-Cost Lending Trap FinTech Alternatives to Short-Term Small-Dollar Credit—Helping Low-Income Working Families Escape the High-Cost Lending Trap*, HARV. KENNEDY SCH. 8 (2017), https://www.hks.harvard.edu/sites/default/files/centers/mrcbg/files/75_final.pdf.

[51] Most lenders will not lend absent a credit check and, where a large part of their portfolio is staked with a specific borrower, would require contractual controls. None of these characterize household lending decisions to employers.

[52] Levy & Sledge, *supra* note 4, at 12 (reporting that approximately 37% of borrowers borrowed because "I had a bill or payment due before my paycheck arrived. In addition, 30% of respondents borrowed to meet some unexpected expense; this issue can also be considered as resulting from payday); *See also* Bianchi & Levy, *supra* note 4 (finding that 32% of consumers borrow because of misaligned cash flow and 32% to meet an excepted expense. Again, both reasons can be mitigated by regularized pay).

[53] In 2016, the revenue of short-term lenders (i.e., fee and interest payments) was $57.9 billion dollar. *See* Eric Wilson & Eva Wolkowitz, *Financial Underserved Market Size Study*, CTR. FOR FIN. SERVS. INNOVATION (2017), https://s3.amazonaws.com/cfsi-innovation-files-2018/wp-content/uploads/2017/04/27001546/2017-Market-Size-Report_FINAL_4.pdf.

[54] 29 U.S.C. § 216(b) (2018) ("Any employer [in violation] . . . shall be liable to the employee . . . in the amount of their unpaid minimum wages . . . and in an additional equal amount as liquidated damages").

[55] *See* Federal Reserve System, *Consumer Credit* (Feb., 7, 2020), https://www.federalreserve.gov/releases/g19/current/default.htm.

[56] In practice, however, 50% of Americans carry a balance on their credit cards and so they pay interest on credit-card purchases. *The Consumer Credit Card Market*, *supra* note 6, at 55–56. Banked/unbanked data: 20% data on access to credit is taken from Experian.

[57] CFPB, *What is a Payday Loan?*, (Jun 2, 2017) https://www.consumerfinance.gov/ask-cfpb/what-is-a-payday-loan-en-1567/

with only a small amount of cash on hand. The employee is paid biweekly and so has to borrow on January 1 against future earnings to support daily expenses. Come payday on January 15, the employee is paid and finally has cash on hand. But the employee also owes money. Now the employee has to repay the loan, plus interest, and make do with whatever is left. If the remainder is insufficient, the employee will have to borrow again. And again. And again. Unless something happens—a lucky windfall or a large raise—the employee would need as many as twenty-six loans throughout the year. And even with a windfall, adverse events can quickly bring one into the debt cycle.

Even if the business will not particularly care about the household's cost of borrowing, the market would force the employer to bear some of this cost. Recall our discussion of the wage premium used to compensate employees for their cost of extending credit. If the employer fails to offer an appropriate wage premium, some employees might quit, move to a competitor, or work fewer hours.[58] Perhaps these pressures are not very strong in a particular industry; still, if the employer has to pay a part of these costs, the wage premium can easily exceed the cost of borrowing from a specialized lender.

The lack of financial logic presents the payday puzzle. Households are in no position to lend money to their employers, at least in the general case. Businesses have better access to liquidity, pay lower interest rates, and do not face the same pressures as individuals do when funds are running out. We shall now explore alternative explanations, the topic of the next Part.

II. PAYDAY: LEGAL, SOCIAL, AND ECONOMIC EXPLANATIONS

A. Path-Dependence

As Justice Holmes once noted, the path of the law is not logic; it is experience.[59] From keyboard layouts to tax legislation, path-dependence explains a variety of social arrangements.[60] In these cases, past choices, justified by historical contingencies, continue to affect decisions far into the future. Once adopted, too many social arrangements are designed to reflect this choice, making the transition to an alternative system (even if superior) too costly. Path-dependence occasionally results in lock-ins, social equilibria bounded by constraints that are now obsolete, like the use of area codes in phone numbers.[61] For participants within the system, the inefficient

[58] *But see* discussion of the effects of the minimum wage, which may limit the wage premium paid by employers, *supra* note 107 and accompanying text.

[59] Oliver Wendell Holmes, *The Path of the Law*, 10 HARV. L. REV. 457, 457 (1897).

[60] *See generally* Paul A David, *Path Dependence, Its Critics, and the Quest for "Historical Economics*,*"* in THE EVOLUTION OF ECONOMIC INSTITUTIONS (2007); Mirit Eyal-Cohen, *Path-Dependence in Temporary Legislation* (unpublished manuscript) (on file with author) (discussing the role of path dependence in tax legislation).

[61] David, *supra* note 60, at 10–12.

equilibrium may seem logical, if not inevitable, but there can be large gains to transitioning to an alternative equilibrium. Thus, the payday may be yet another instance of inefficient social equilibria. To understand the payday, it is worth studying its past and understanding how it emerged in an environment with inferior money and payroll technologies.

The first moral exhortation on the payday is in the Bible, where it is admonished that one should not "take advantage of a hired worker who is poor and needy. . . Pay them their wages each day before sunset, because they are poor and are counting on it."[62] Whether daily pay was indeed broadly practiced with any regularity, though, is historically unclear.

Under common law, employers were only required to pay within the pre-agreed pay period; in the absence of a specific agreement, the default was payment at the end of the contract.[63] In England, there are some indications that in both the seventeenth and eighteenth centuries, weekly and even daily pay was prevalent.[64] By contrast, if one counts certain agricultural workers, such as sharecroppers, as wage laborers, their pay was only seasonal.[65] In the U.S., however, factory laborers and most other employees were paid, usually, on a monthly basis.[66]

The primary obstacle to frequent pay was payroll and money technology, which were radically different in the past—and far less efficient—than they are today.[67] To appreciate how difficult it was to disburse payments in the past, consider the following complaint of a nineteenth-century business owner:[68]

> If the larger mills should pay once a week it would entail considerable more expense. The Pacific Company employs between five and six thousand hands, and it

[62] *Deuteronomy* 24:14–15; *Leviticus* 19:13 ("Do not hold back the wages of a hired worker overnight.")

[63] ROBERT GILDERSLEEVE PATERSON, WAGE PAYMENT LEGISLATION IN THE UNITED STATES 68–70 (1918).

[64] JAMES E. THOROLD ROGERS, WAGE PAYMENT LEGISLATION IN THE UNITED STATES 430 (1884), https://socialsciences.mcmaster.ca/econ/ugcm/3ll3/rogers/sixcenturies.pdf; Peter H. Lindert & Jeffrey G. Williamson, *English Workers' Living Standards During the Industrial Revolution: A New Look*, ECON. HIST. REV. 3, 13 n.38 (Feb. 1983); Jeremy Boulton, *Wage Labour in Seventeenth-Century London*, 49 ECON. HIST. REV. 268 (1996) (noting daily pay).

[65] *See generally* Joseph D. Reid Jr., *Sharecropping as an Understandable Market Response: The Post-Bellum South*, J. ECON. HIST. 103 (Mar. 1973).

[66] PATERSON, *supra* note 63 at 77 (noting the "custom of monthly wage payments which prevailed in most lines of industry prior to 1885"). *See also* FRANCES PERKINS & ISADOR LUBIN, HISTORY OF WAGES IN THE UNITED STATES FROM COLONIAL TIMES TO 1928, at 93. BUREAU OF LABOR STATISTICS (1934) (Noting that in 1777 pay-per-product was abolished in the glass industry in favor of monthly pay). However, this source does not find any regular pay period across industries. *See, e.g.*, *id*. at 90, 92. *See also* CHRISTOPHER L. TOMLINS, LAW, LABOR, AND IDEOLOGY IN THE EARLY AMERICAN REPUBLIC 275 (citing M'Millan and M'Millan v. Vanderlip, 12 Johnson 165 (N.Y. 1815)).

[67] I turn to this issue *infra* Part II.F.

[68] Redmount et al., *The Effect of Wage Payment Reform on Workers' Labor Supply, Wages, and Welfare*, 72 J. ECON. HISTORY 1064, 1069 (Dec. 14, 2012).

> would be extremely difficult for the paymaster to visit all these people once a week, carrying his trunk up and down stairs, and taking receipts from each one. He has to go to the help so as not to stop the work.

Beyond the cost of paying workers, one has to also account for the difficulty of monitoring the hours worked and computing the proper withholdings, garnishments, benefits, and deductions.[69] Even cash was not always freely available, and the Supreme Court had to take action to encourage the use of the Federal Dollar.[70] These difficulties with cash and computation seem dated today, but they were of utter importance in the past.

For a brief historical moment, there was a boom in payday legislation. Towards the end of the nineteenth century, workers started organizing and lobbying for legislation that would mandate more frequent pay.[71] Their efforts met much resistance. Many legislators were unresponsive, and even when the legislature was responsive, courts were reluctant to approve pay frequency legislation.[72] Such regulation was seen as an unwarranted imposition on the parties' freedom of contract and a due process violation.[73]

The first large win for workers was in Massachusetts.[74] The charismatic governor of Massachusetts, George D. Robinson, was a champion of regular pay. In the legislative hearing, he urged that a weekly payday be implemented for several reasons. The proposed law would increase worker autonomy, limit the scope of debt collection lawsuits, increase the use of cash (a major concern at the time),[75] and instill a better sense of money management among employees.[76] He also noted that the experience from voluntary weekly pay was favorable and thus refuted many of the chief concerns. Workers still saved and did not "waste their earnings in frequent debaucherie [sic]."[77] Indeed, even large employers found that the system was practicable and added few costs.[78]

[69] *See infra* Part II.G.

[70] SHARON ANN MURPHY, OTHER PEOPLE'S MONEY: HOW BANKING WORKED IN THE EARLY AMERICAN REPUBLIC (2017).

[71] PATERSON, *supra* note 63, at 70.

[72] Lindley D. Clark & Stanley J. Tracy, *Laws Relating to Payments of Wages*, BUREAU OF LAB. STATS. 16–19 (1926), https://fraser.stlouisfed.org/files/docs/publications/bls/bls_0408_1926.pdf.

[73] *See* PATERSON, *supra* note 63, at 92–93 (documenting twelve cases where wage regulation was deemed unconstitutional and fourteen where it was also constitutional).

[74] Massachusetts Acts of 1879 Ch 128 p. 483; cited in PATERSON, *supra* note 63, at 70; Redmount et al., *supra* note 68, at 1024; *see also* PATERSON, *supra* note 63, at 68 (noting that wage period laws are "comparatively recent origin"). For the legislative history, see Am. Mut. Liab. Ins. Co. v. Comm'r of Labor & Indus., 163 N.E.2d 19, 21 (1959).

[75] *See* MURPHY, *supra* note 70, at 17–20.

[76] *See* George D. Robinson, Address of His Excellency George D. Robinson to the Two Branches of the Legislature of Massachusetts 33 (Jan. 3, 1884) ("the lesson of economy be practically taught every day."). *See also id.* at 36–38.

[77] *Id.* at 33.

[78] *Id.* at 34 ("It is, I submit, always wise and salutary to devise legislation of such a character as will reach the humblest and the poorest citizen, who has no voice but his own to present his needs, — no power in combination with others to emphasize his opinions.")

The weekly payday in Massachusetts signaled a national change. Reports on the enforcement of this law seem positive.[79] [80] Other states followed suit and adopted weekly or biweekly pay periods.[81] Courts, too, changed their attitude and grew increasingly accepting of such provisions.[82] One reason for this growing acceptance was the concern that employers use their bargaining power to offer unfair loans (advances) to employees.[83] Another was the concern that regular payment is "much more a matter of life and death to a workingman . . . than to the employing corporation."[84] Even the Supreme Court weighed in and held that states are well within their powers to regulate pay frequency legislation.[85] This ruling came only nine years after *Lochner*,[86] but it withstood *Lochner* era standards, as it was seen more as a form of preventing fraud and abuse than substantive regulation of the terms of the deal.[87]

The boom in payday regulation was followed by a quick bust. As soon as 1908, most states had already moved to the modern system of biweekly pay.[88] Massachusetts was the last bastion of weekly pay,[89] but even there the practice has changed drastically. In 1959, the weekly pay law was still on the books, but many companies were paying biweekly.[90] In a high-profile case, the Supreme Judicial Court of Massachusetts ruled that weekly pay was still the norm,[91] but the decision recognized that it was perhaps time for a change.[92] Others

[79] *Third Annual Report of the Bureau of Labor and Industrial Statistics*, KAN. DEP'T OF LAB. AND INDUS. 324–25 (1888), . *See also* Robinson, *supra* note 76, at 36–38.

[80] *See Seventh Annual Report of the Factory Inspectors of the State of New York*, ST. OF N.Y. 63, 45–46 (1893).

[81] PATERSON, *supra* note 63, at 70–88. A few states adopted a monthly pay obligation. *Id*. at 88–92. One example of weekly pay is Rhode Island Pub. Laws R. I. c. 918, of March 4, 1891.

[82] Claudio J. Katz, *Protective Labor Legislation in the Courts: Substantive Due Process and Fairness in the Progressive Era*, 31 L. HIST. REV. 275, 288 (2013).

[83] Steven L. Willborn, *Indirect Threats to the Wages of Low-Income Workers: Garnishment and Payday Loans*, STETSON. L. REV. 35, 40 (2015); State v. Brown & Sharpe Mfg. Co., A. 246, 252 (1892) (grounding payday legislation in a concern with "the greed of corporate capital.")

[84] COMMONS & ANDREWS, *supra* note 3, at 51.

[85] Erie R. Co. v. Williams, 233 U.S. 685 (1914).

[86] Lochner v. New York, 198 U.S. 45 (1905).

[87] *See* Adkins v. Children's Hosp. of D.C., 261 U.S. 525 (1923), *overruled in part by* W. Coast Hotel Co. v. Parrish, 300 U.S. 379 (noting that "in none of the statutes thus sustained was the liberty of [the parties] interfered with. Their tendency and purpose was to prevent unfair, and perhaps fraudulent, methods in the payment of wages"). *See also* David E. Bernstein, *Lochner Era Revisionism, Revised: Lochner and the Origins of Fundamental Rights Constitutionalism*, 92 GEO. L.J. 1, 9 (2003); David N. Mayer, *Substantive Due Process Rediscovered: The Rise and Fall of Liberty of Contract*, 60 MERCER L. REV. 563, 650 (2009).

[88] COMMONS & ANDREWS, *supra* note 3, at 51.

[89] Emilie Tavel, *Companies Request Talk With State On Weekly Pay Ruling: 'Ample Time' Indicated*, CHRISTIAN SCI. MONITOR (1908).

[90] *Id*.

[91] Am. Mut. Liab. Ins. Co. v. Comm'r of Labor & Indus., 163 N.E.2d 19 (1959).

[92] *Id.* at 22. ("[m]any good reasons may today exist for the payment of wages less often than weekly, including the greater financial responsibility of most employers, the payment of family obligations on a monthly basis or better family financial security than existed in years

criticized the decision for creating "unnecessary paper work . . . and add[ing] administrative burdens."[93] Soon thereafter, the legislature changed the law to allow for biweekly pay.[94]

Labor historian Nelson Lichtenstein proposed a more provocative explanation for the decline of weekly pay. In the 30s, as part of the New Deal, President Franklin D. Roosevelt introduced the Federal Insurance Contributions Act (FICA) tax as part of the social security reform. In 1938, Congress introduced the minimum wage and the Fair Labor Standards Act (FLSA).[95] Then, in 1943, Congress also introduced the payroll tax, which required employers to withhold federal income tax from employees' pay.[96] The result was an increased administrative load on employers who had to compute pay without computers.[97] According to Lichtenstein, the effect of this legislation was to make weekly pay too expensive, leading to a push to move to biweekly pay.[98] There is a bitter irony here, as legislation that is ostensibly pro-worker might have had this unanticipated adverse consequence on pay frequency. The same legislation that guarantees minimum wage, unemployment insurance, and Medicare may be inadvertently pushing employees into the hands of payday lenders and other short-term credit providers.

*

Path-dependence may explain why we still have the payday today: we are relying on a century-old body of legislation that was optimized to deal with inferior money and payroll technology.

B. The Synchronization of Bills and the Payday

Another potential explanation for the continued existence of the payday is the seeming alignment of the timing of bill payments and the payday. Today, households pay most of their bills—utilities, rent, mortgage, internet, phone, insurance payments, and so on—on a monthly basis. Monthly outlays place the payday into a larger social equilibrium, with both ingoing and outgoing money streams being closely tied together. Monthly bill payments, it is worth noting, are a somewhat recent historical development—a fact that played a role in the debates over longer pay periods.[99]

gone by.")

[93] Tavel, *supra* note 89.

[94] M.G.L.A. 149 § 148. For the reforming act, see St.1992, c. 133, § 502, approved July 20, 1992, and by § 599 made effective as of July 1, 1992.

[95] Fair Labor Standards Act, 29 U.S.C. § 201 (2018).

[96] Current Tax Payment Act of 1943, Pub. L. 68, Ch. 120, 57 Stat. 126 (June 9, 1943).

[97] For proportion, today, roughly 30% of the pay is made through "fringe benefits" which are often paid to third parties. *Employer Costs for Employee Compensation Historical Tables*, BUREAU OF LAB. STATS. 2 (Sept. 2019), https://www.bls.gov/web/ecec/ececqrtn.pdf.

[98] Chris Hayes, *The Breakdown: Why Are We Paid Every Two Weeks?*, THE NATION (Jan. 21, 2011), https://www.thenation.com/article/breakdown-why-are-we-paid-every-two-weeks/.

[99] Am. Mut. Liab. Ins. Co. v. Comm'r of Labor & Indus., 163 N.E.2d 19 (1959).

The synchronization of bills and the payday appears, at first glance, harmonious; like clockwork, money comes in and goes out. But this is deceptive. Households pay bills for goods and services that they consume or use throughout the month. Whereas households consume daily, they only pay monthly.[100] This means that the service provider is not only providing the service, but it is also providing credit: selling electricity today but receiving payment only at the end of the month. We see here K_2 attaching again to a primary transaction, the sale of electricity, only that this time around it is the household that borrows rather than lends.

Utility providers charge for this service and for the risk of default. Households, however, are not the most reliable borrowers. Some households default on their utility payments, and the cost borne by all other households is greater for this reason.[101] After all, the provider bears both the cost of not having access to their earned payments and the risk of default by the household. Hypothetically, out of every $150 in the electric bill, perhaps $10 can be seen as interest. Exactly how much households today pay for this loan is not clear, but the overall economic effect is likely to be noticeable.[102]

Consider, then, the situation from the individual's perspective. Jane is working all month as a store clerk, but she is paid at the end of the month. Throughout the month, she needs to consume groceries, utilities, and other everyday expenses, but her employer will not pay her until the end of the month. For groceries, she uses her credit card—paying a few dozen dollars on her revolving balance. For utilities, she doesn't need to borrow per se, but she is paying a higher price, perhaps a dozen more dollars. And while most of her daily expenses are financed by someone else, she is lending money to her employer. Somehow, on each transaction, she is on the losing end. Being a risky borrower, Jane is paying a large amount to the utility company in implicit interest; having worse access to capital than her employer, Jane is receiving less in wage premia than her cost of borrowing.[103]

Overall, households both borrow and lend, always on worse terms. Borrowing and lending do not offset each other; instead, they amplify each other, being two unnecessary and costly credit transactions. Rather than clockwork, bills and the payday are more like oarsmen—rowing in opposite directions, only to stay in place.[104]

[100] Technically, mortgage payments are in arrears, but rent is most often paid in advance.

[101] *See Residential Energy Consumption Survey (RECS)*, U.S. ENERGY INFO. ADMIN. (2015), https://www.eia.gov/consumption/residential/data/2015/hc/php/hc11.1.php (roughly 10% of all households received disconnect notices.) The cost of default by some households is then spread to the bills of all other paying households.

[102] The savings from abolishing K_2 will be split between the utility providers and the end-consumer—but the exact split requires a more nuanced analysis of the market and tariff regulation.

[103] The loan from the utility company relives some of the liquidity pressure of the household, but it comes at a cost, and is a forced loan.

[104] The reasons for K_2 in this context are likely to be distinctive from the ones in the employment context. It is possible that houesholds prefer lump sums outlays because they allow for easier detection of overcharges or gives them power in disputes vis-à-vis the

C. Employer Power and Lack of Sophistication

One possible explanation for the persistence of K_2 is rooted in the unequal distribution of power and sophistication between employers and employees. As employers wield an asymmetrically-strong bargaining position vis-à-vis their employees, they use it to exert the benefit of K_2: cheap credit. Alternatively, workers may be unsophisticated and fail to recognize that K_2 is essentially a credit transaction. If they fail to think of K_2 as a credit transaction, workers will not know to demand an appropriate wage premium that would compensate them for the cost of providing credit. Under either possibility, employers do not feel the cost of infrequent pay, and they have no reason to opt for a more regular pay schedule.

One issue with this explanation is its lack of generality. It is clear that many employers wield considerable bargaining power (think of a single employer in a small town), but surely this does not describe the entire economy. Even middle-class employees often find themselves in a position to negotiate portions of their salary and benefits, and firms invest considerably in the retention efforts of these employees. Yet, we do not find daily pay common even among these employees. The same issue arises with respect to sophistication. While most workers would not describe their employment contract as a credit transaction, they viscerally feel the consequences of insufficient liquidity. It is, therefore, quite unlikely that workers are indifferent to pay frequency.

More importantly, even when employers wield such immense power, there are better and worse ways to exercise it. Supposing the employer can dictate both the wages paid and the terms of the contract, it would still face *some* limits on the exercise of this power. The employer cannot offer to pay a few cents per hour with payment once a quarter and still expect employees to come to work.[105] If an employer only pays $9 per hour for manual labor, the employees may prefer working in retail for $8.50 per hour. This suggests an additional trade-off. The manual labor employer can either increase pay from $9 to, say, $9.50, or it may make working conditions better, by adding breaks, investing in workplace safety, and offering workers flexibility. Stated differently, with better contract terms, the employer can afford to pay less. Thus, even when the employer has a superior bargaining position, it will often find it advantageous to offer the optimal mix—from its perspective—of wages and work conditions.

The employer wants to design the mix of a pay period and wages that is most beneficial to itself. It would compare the benefit of prolonging the pay period,[106] against the cost of doing so—having to

company. This is a fertile area for future research.

[105] For the sake of exposition I avoid the various exceptions, but it is worth remembering that prisoners earn as little as 33 cents per hour. Wendy Sawyer, *How Much Do Incarcerated People Earn in Each State?,* PRISON POL'Y. INITIATIVE (Apr. 10, 2017), https://www.prisonpolicy.org/blog/2017/04/10/wages/.

[106] The value of infrequent pay also includes savings on check-cutting costs and stronger leverage against the employee, issues that are described below.

pay more. Now, as discussed earlier, infrequent pay is more costly to the employee than it is beneficial to the employer. Thus, it is optimal for the selfish, dominant employer to pay lower wages frequently rather than pay higher wages infrequently. Of course, there are administrative costs to paying more frequently, so this will also figure into the employer's calculus—but in the basic trade-off between wages and frequency, the employer would prefer the frequent, lower payment.

That the employer would find it in its own self-interest to pay frequently is subject to one potential exception: minimum wage.[107] As noted earlier, minimum wage legislation imposes on employers the duty to pay more than they would have paid otherwise. To return to the earlier example, if before minimum wage the employer was able to hire employees for $7 per hour, the minimum wage would force them to pay $7.25. This means that the employer is paying to the employee more than would be the market-clearing equilibirum.[108] The consequence of this higher pay is that there might be some 'slack'—some room for employers to offer inferior terms to employees without reducing the employee's willingness to work for them—at least so long as the cost of these inferior terms does not exceed the $0.25 pay raise. Hence, there is a theoretical possibility that, in the presence of minimum wages, employers would seek longer payment periods. This possibility has not been investigated in the voluminous literature on the effects of minimum wages and should be analyzed in future research.

Overall, employers' market power is useful in explaining many facets of the employment contract. However, it seems unlikely as a general explanation, as we find prolonged payment periods even among higher-paid employees.[109]

D. Collateral

Another type of explanation grounds the existence of the payday in the need of employers to control their employees. Employers worry that employees may decide to quit midstream, leaving the employer without the necessary personnel or skill necessary to produce their

[107] I emphasize that this is only a possible effect, as the literature on the effects of minimum wages is complex, nuanced, and hotly-debated. Here I consider the classic wage model, noting that its applicability in different markets may be limited. *See generally* David Neumark, *The Employment Effects of Minimum Wages: Some Questions We Need to Answer*, NBER Working Paper 23584, at 1 (2017), https://www.nber.org/papers/w23584 ("the debate among researchers about the employment effects of minimum wages remains intense and unsettled.")

[108] The market-clearing price of labor may be unjust or unfair, a thick normative position on which I take no stance. In particular, I do not argue that the employer is overpaying or underpaying the employee, as such a stance requires a clear normative baseline. I do highlight the generally acceptable position that relative to the market-clearing equilibirum (the point where supply meets demand), minimum wage laws would raise wages.

[109] As of 2013, the average hourly pay per period was $18.6/weekly; $24.8 biweekly; $29.7 semimonthly; and $28.4 monthly. Matt Burgess, *How Frequently Do Private Businesses Pay Workers?*, 3 PAY & BENEFITS 3 (2014).

products or serve their clientele. Contract law can protect employers against this possibility—they can require the employee to give notice. But such protection is quite weak, as employees can be judgment-proof and the cost of litigation can be prohibitive.[110] Postponing pay thus creates collateral; if the employee disappears, the employer may threaten to expropriate this collateral.[111]

Collateral explains, quite persuasively, why the payday is always in arrears. The reason that employers do not *prepay* employees is clearly rooted in the difficulty of recovering unearned wages from an employee who absconds. Anticipating this difficulty in recovery, some workers may want to assume positions just for the sake of prepayments, making the hiring process difficult and costly. Hence, a "reverse" K_2, where the employer lends money to the employee, is not a general solution—a point worth remembering as we move the normative discussion.

However, when it comes to the payday itself, i.e., K_2, collateral fails to provide a justification. The biggest problem is that employers are legally prohibited from sequestering collateral.[112] A large number of jurisdictions have enacted "final pay statutes" which compel the payment of all unpaid wages upon termination, or soon thereafter.[113] Final pay, statutes are often accompanied by penalties and fee-shifting provisions to further compel employers to make timely payments. State courts have likewise recognized the public policy imperative in favor of prompt payment.[114] The policy of such statutes is strongly endorsed. The Supreme Court held that legislation requiring prompt payment upon discharge—i.e., payment without "abatement or deduction"—is constitutional.[115] The Department of Labor denounced any pay practices that have the effect of payment deferral.[116] In some jurisdictions, courts adhere to the "faithless servant" doctrine, which denies employees any pay (even in quantum meruit) if they are disloyal to their employers.[117] However, disloyalty

[110] *See e.g*, 80 Fed. Reg. 62,957 (Oct. 16, 2015) (Private employers asking, in the context of new rules on commissions, "that DOL permit employers to withhold a portion of wages as an incentive for the employee to complete the contract period and to discourage workers from leaving to work in other industries").

[111] Redmount et al., *supra* note 68, at 1065.

[112] *See, e.g.*, Britton v. Turner - 6 N.H. 481 (1834) (establishing the duty to pay an employee for part performance); Pineda v. Bank of Am., N.A. 241 P.3d 870, 877 (Cal. 2010) ("[t]he public policy in favor of full and prompt payment of an employee's earned wages is fundamental and well established") (citing Smith v. Superior Court, 137 P.3d 218 (Cal. 2010)).

[113] William C. Martucci & Jennifer K. Oldvader, *Avoiding Another Wage-and-Hour Pitfall:State Late-Paycheck Laws*, EMP. REL. TODAY 71 (2011).

[114] *See Pineda*, 241 P.3d at 877 ("[T]he public policy in favor of full and prompt payment of an employee's earned wages is fundamental and well established.").

[115] St. Louis, I.M. & S. Ry. Co. v. Paul, 173 U.S. 404 (1899). It is worth noting that in this case, the legislation required payment without "abatement or deduction." However, if the K_2 theory is accepted, the early payment results in a (small) windfall to the employee in the form of a credit wage premium.

[116] *See, e.g.*, 80 Fed. Reg. 62,957 (Oct. 16, 2015).

[117] Charles A. Sullivan, *Mastering the Faithless Servant?: Reconciling Employment Law, Contract Law, and Fiduciary Duty*, 2011 WIS. L. REV. 777, 779 (2011).

is generally understood to mean unlawful competition with the employer or perhaps dissemination of trade secrets.[118] This doctrine is of little relevance, then, to employees who quit midstream.[119]

The collateral explanation also fails to explain infrequent payment to employees who are not flight-risks or are not judgment-proof. Indeed, the average worker stays with his or her employer for at least four years.[120] It may still be true that employers are reluctant to sue employees for reputational reasons, rendering the employment contract unprotective of the employer's interests. But the same logic would also lead employers to avoid sequestering the collateral—that is, to avoid paying earned wages.[121] Overall, collateral may explain the absence of "reverse K_2," but it fails to justify K_2.

E. Behavioral Biases

In the finance literature, the most developed explanation for the payday is rooted in behavioral economics. In a recent contribution to one of the leading journals in finance, economists Christopher Parsons and Edward Van Wesep study the basic puzzle of timing employee payments.[122] They argue that a rational employee should not care about pay frequency, for a simple reason. If the employer were to pay only once in the employment relationship, say at the beginning, the employee could simply save the excess amount and budget to make regular payments as they come due. Even if the employer were to pay this amount at the end of the contract, the employee could still borrow from a bank, using the employer's promise to pay as collateral. Parsons and Van Wesep observe that in practice, employees do care and that pay is more frequent than only once in the employment relationship. Why is that so?

To explain pay frequency, they advance a theory rooted in human psychology (or one account thereof). In their view, individuals manage their money imprudently because they are impulsive, myopic, or suffer from a "present-bias," which causes them to spend now at the expense of their long-term goals.[123] Under this view, employees *benefit* from their employers withholding pay, as it prevents them from wasting their own money and allows them to meet their expenses as they come due. When employers pay in installments, they facilitate their workers' savings and prevent them from wasting their own money.

[118] Alan Hyde, *What Should the Proposed Restatement of Employment Law Say About Remedies?*, 16 EMP. RTS. & EMP. POL'Y J. 497, 508 (2012).

[119] *See also S*TEVEN L. WILLBORN ET AL., EMPLOYMENT LAW: CASES AND MATERIALS 609–12 (4th ed. 2007).

[120] *Employee Tenure 2018,* BUREAU OF LAB. STATS. (2018), https://www.bls.gov/news.release/pdf/tenure.pdf (based on the median).

[121] Reputational concerns may indeed push the employer to sue and sequester the collateral to develop a reputation for "toughness."

[122] Parsons & Van Wesep, *supra* note 16.

[123] *Id*.

The idea that households need help budgeting money is consistent with some evidence showing that the timing of payments influences household money management. One study shows that pension recipients consume the fewest calories the week before the benefits are paid, perhaps suggesting a difficulty in saving evenly across the entire pay period.[124] Similarly, another study showed that individuals make most of their food and necessity purchases right after receiving benefit payments.[125] Parsons and Van Wesep further argue that their findings are consistent with the fact that low-paid employees are paid more frequently than higher-paid employees. To them, this is simply the result of low-paid employees being more presently-biased than their wealthier counterparts and lacking in a financial buffer, making their need for money exceed their desire to save.[126]

There is no doubt that saving money can be difficult, but this theory suffers from some deep flaws, both theoretical and empirical.

First, there is a behavioral force that is arguably stronger than present-bias that works in the opposite direction. By waiting until payday, employees receive a large paycheck. This large payment may create a sense of windfall—an illusion of plenty.[127] This illusion may exacerbate the problem of self-control, which was precisely the reason why wage period legislation started. Legislatures and courts thought that large payments would lead to the "dissipation on payday of a large part of the accumulated sums by irresponsible employees with consequent adverse effect on family and community."[128] Indeed, some research shows that individuals consider the lump-sum tax refund to be "extra" money, leading them to spend it more easily than their "regular" money.[129] Another effect of large payments is evidenced by the link between dates of benefit payments and drug abuse,

[124] Mastrobuoni & Weinberg (2009) [need more info on this source]. *See also* Jani-Petri Laamanen et al., *Once or Twice a Month? Impact of Payment Frequency on Consumption Patterns*, (Feb. 2019), https://pdfs.semanticscholar.org/794a/c54611eeff7bd40efa93729cada5e0e03fa5.pdf.

[125] Melvin Stephens, *"3rd of tha Month": Do Social Security Recipients Smooth Consumption Between Checks*?, 93 AMERICAN ECON. REV. 406 (2003)

[126] Parsons & Van Wesep, *supra* note 16, at 390 ("Insofar as education and wealth correlate negatively with time-inconsistency, more educated and more wealthy workers should be, and are empirically, paid less frequently.").

[127] Such debates are not new; in nineteenth-century Massachusetts, mill owners thought that moving to weekly pay would lead to more employee intoxication, but "our treasurer determined to give it a fair trial and the result exceeded our anticipations, for we found that instead of increasing drunkenness, it has had a contrary effect, so far as we could ascertain by the working days of our operatives". Redmount et al., *supra* note 68, at 1083.

[128] Am. Mut. Liab. Ins. Co. v. Comm'r of Labor & Indus., 163 N.E.2d 19, 21 (1959). *See also* Rebekah D. Provost, *Punishing and Deterring the Unknowing: Mandatory Treble Damages Under the Massachusetts Wage Act*, 18 SUFFOLK J. TRIAL & APP. ADVOC. 305, 311 (2013).

[129] *See* C. Yiwei Zhang & Abigail B. Sussman, *The Role of Mental Accounting in Household Spending and Investing Decisions*, (forthcoming) (last revised Feb. 10, 2019) (noting the evidence of a higher propensity to spend tax refund relative to other funds); William Adams, Liran Einav, & Jonathan Levin, *Liquidity Constraints and Imperfect Information in Subprime Lending*, 99 AM. EC. REV. 49 (2009) (finding a sharp increase in auto purchases in the subprime market during tax refund season).

hospitalization, and mortality; individuals potentially use the lump sum payment to purchase excess drugs and alcohol.[130] Another study compared the expenditure profile of benefits recipients who receive payment twice a month with those who receive a larger payment once a month. It found that the single payment leads to high within-month variability, with most of the money spent early, thus concluding that "two temporally separate payments might lead to smoother spending than just one payment."[131] It is also possible that it is easier to save pennies than dollars, which is the business model of a few recent start-ups.[132]

Second, the authors believe that income strongly correlates with present bias, but there is a reason to suspect this account.[133] Are middle-income employees less likely to overspend than paycheck-to-paycheck counterparts?[134] And even if that were the case, low-paid employees are hardly homogenous, but their pay period is. Among the low-paid employees are many who are on the path to higher earnings in the future—think interns, students working a side job, or a manager-track employee working the ranks.

Third, there is a fine legal point that belies the theory. Employees can ask their employers for an advance, and the employer might be willing to provide one. The authors recognize that such renegotiation will cause our results thus far to unravel, implying a need for regulation."[135] They claim that such regulation does exist, noting that "regulators in 45 U.S. states require wages to be paid at a minimum frequency."[136] But the concept of these minimums is quite different than what they highlight. An employer can presumably pay nothing each period, so long as the employee was advanced her entire period pay. Because the authors see their model as explaining the regulatory landscape, this inconsistency suggests a problem with regulation rather than a justification for its existence.

Lastly and perhaps most importantly, the empirical evidence suggests that employer-based savings are neither necessary nor helpful. A recent study concludes that "pay frequency does not affect household's savings" and that the amount of money that households spend over the month has no relation to the frequency of pay.[137] The

[130] *Laamanen* et al., *supra* note 124.

[131] *Id*.

[132] *See, e.g.*, *Invest Your Spare Change*, ACORNS, https://www.acorns.com/ (last visited Dec. 25, 2019) (a micro-investing platform with corresponding app that allows customers to invest spare change as part of other users into an aggregated portfolio managed by industry professionals). To be clear, I am not endorsing this alternative explanation, but I see it as an equally-compelling assumption to make but which the authors fail to acknowledge.

[133] At least in the aggregate data presented by the Bureau of Labor Statistics, the correlation between pay and pay frequency breaks if one excludes weekly paid employees—in fact, semi-monthly paid employees are paid somewhat more than monthly-paid employees. *See supra* note 27.

[134] Economists are divided on these questions. *See* Leandro Carvalho, *Poverty and Time Preference*, RAND LAB. AND POPULATION (forthcoming May 2010), https://www.rand.org/content/dam/rand/pubs/working_papers/2010/RAND_WR759.pdf.

[135] Parsons & Van Wesep, *supra* note 16, at 382.

[136] *Id.*

[137] Ines Berniell, Pay Cycles, Individual and Aggregate Effects of Paycheck Frequency,

evidence also suggests that households do not change their spending categories based on pay frequency. It would seem, then, that withholding pay does not plausibly change either saving or consumption patterns. Moreover, while almost all households are paid infrequently, only a minority needs help saving money. Over 55% of households have liquid assets at their disposal, thus demonstrating their ability to save and manage money without a third-party.[138] As these households are demonstrably capable of not wasting the money sitting in their checking and savings accounts, they do not suffer from such a degree of present-bias that would make them dependent on the employer's paternalistic withholding of cash.

Overall, then, while the inability to save may explain a portion of the payday phenomenon, more work is necessary to explain the actual practices we encounter today.[139] As the authors themselves note, their model is limited in many ways and is mostly meant as "a first attempt to tackle issues related to pay timing."[140]

F. Legislation

Employment law is highly regulated at both the federal and state level, and the payday is no exception. While federal law does not mandate pay frequency, both federal and state legislation affect the payday in ways both visible and invisible.

Most states regulate pay frequency by setting frequency floors rather than mandatory pay periods. Almost all states require payments to be made within, at most, biweekly intervals, with some states requiring at least weekly or monthly payments. This legislation, however, is also riddled with occupation-specific exceptions, often for farm workers and sometimes for executive or administrative employees.[141] These exceptions appear quite unprincipled, as some states require that farmhands be paid on shorter intervals and others on longer intervals.[142]

Payday legislation also fails to explain why employers do not choose to pay more frequently than biweekly. As many biweekly-paid employees find themselves borrowing at high rates, they are likely to benefit from more frequent pay, even if it comes with a lower wage premium.[143] This suggests that employers can increase profits by

manuscript (2019) https://inesberniell.weebly.com/uploads/9/1/2/2/91228902/pay_cycles_berniell_ines.pdf

[138] *See* FED. RES. SYS., *supra* note 5, at 17. Conditional on having financial assets, the median family held $23,500 in assets. *Id.* at 18.

[139] I return to some additional issues with this theory *infra* Part III.B.

[140] *Id.* at 389.

[141] *See, e.g.*, *Summary of New York State Labor Laws Relating to Farm and Food Processing Employment*, N.Y. DEP'T OF LAB. (2019), https://www.labor.ny.gov/formsdocs/wp/ls118.pdf.

[142] MASS. GEN. LAWS ANN. ch. 149, § 148 (West 2019) ("[E]mployees engaged in agricultural work may be paid their wages monthly.").

[143] *Id.*

paying their employees less, but more frequently. To the extent that debt spirals also affect worker productivity, stability, and reliability, we would expect the private sector to be somewhat responsive to such pressures.[144]

In the public sector, the choice of pay frequency is made by fiat. As a result of pay regulation, most public employees are paid on a biweekly or a semimonthly basis. Federal legislation sets a biweekly pay period,[145] one with a venerable history—a report from 1879 already notes that "most Federal employees are paid on a biweekly basis."[146] State laws, similarly, will often set a biweekly or a semimonthly pay schedule for state employees.[147] Local governments also pay twice a month. Of the 200 largest cities in the United States, 189 (94.5%) pay on a biweekly or semimonthly basis.[148]

Public sector legislation explains the prevalence of K_2 among 22 million Americans who are considered government employees.[149] It may also help explain private sector practices by way of imitation or coordination with the public sector. However, it fails to *justify* the practice. If, by force of fiat, public employees are paid biweekly, why not pay them more often? The low return on treasury bonds shows that the government can easily borrow at low rates.[150]

While payday legislation does not explain private sector pay practices, other legislation creates strong incentives for private employers to pay infrequently. Ironically, the legislation that promotes infrequent pay is exactly the same legislation that is meant to protect workers—minimum wage laws and overtime legislation.

Minimum wage laws inadvertently favor longer pay periods. The problem emerges in the context of tipped and commission-based employees—an important part of the workforce, with approximately 4.3 million tipped workers in the United States.[151] For these

[144] A set of economic arguments involve nominal rigidity of wages or "sticky wages"—the failure of payments to adjust, mostly downward, to changing market conditions. This may further explain the pattern of biweekly pay, although even sticky wages are thought to adjust in the long run. *See generally* Barattieri et al., *Some Evidence on the Importance of Sticky Wages*, 6 AMERICAN ECON. J. 70 (2014).

[145] 5 U.S.C. § 5504(a) (2018) ("The pay period for an employee covers two administrative workweeks.").

[146] *Statistical Abstract of the United States*, U.S. GOV'T PRINTING OFF. 302 (1879), https://www.google.com/books/edition/Statistical_Abstract_of_the_United_State/R7M_0HXXZ48C?hl=en&gbpv=1&dq=biweekly+payroll&pg=PA302&printsec=frontcover.

[147] ALA. CODE § 36-6-1 (2018) (semi-monthly); N.Y. STATE FIN. LAW § 200(1) (McKinney 2018) (biweekly); WASH. ADMIN. CODE § 82-50-021 (2018) (semi-monthly).

[148] *Chesapeake, Virginia Payroll Cycles Special Audit,* CITY OF CHESAPEAKE AUDIT SERVS. DEP'T. Appendix B (2018), http://www.cityofchesapeake.net/Assets/documents/departments/audit/department-audits/Payroll+Cycle+Full+Report.pdf.

[149] *Employment, Hours, and Earnings from the Current Employment Statistics survey (National),* BUREAU OF LAB. STATS., https://data.bls.gov/timeseries/CES9000000001 (last visited Feb. 13, 2020).

[150] *Daily Treasury Yield Curve Rates*, DEP'T OF TREASURY https://www.treasury.gov/resource-center/data-chart-center/interest-rates/Pages/TextView.aspx?data=yield (last visited Feb. 13, 2020)

[151] Sylvia A. Allegretto & David Cooper, *Twenty-Three Years and Still Waiting for Change: Why It's Time to Give Tipped Workers the Regular Minimum Wage*, ECON. POL'Y

employees, the Fair Labor Standards Act (FLSA) permits employers to pay below minimum wage, so long as the lower wage plus tips averages to the minimum wage *over the pay period*.[152]

Consider the following example. Suppose that an employee makes $1,300 in tips in one week and $100 in the next. The average is $700—well beyond the biweekly federal minimum of $580—so the employer need not pay the employee any extra amount.[153] But what happens if the pay period is shorter? Suppose an employer instead paid on a weekly basis. The employee makes $1,300 the first week, well beyond the minimum wage, so the employer would again not need to compensate the employee. But in the second week, the employee only makes $100, well below the weekly minimum wage of $290. By making the payday shorter, the employer now has to pay the employee an extra $190.

As the above example illustrates, minimum wage laws currently incentivize employers to favor *longer* pay periods. Arguably, the only thing keeping employers from further prolonging pay periods is the pay frequency legislation. Thus, the interaction of minimum wage laws and pay frequency ceilings may partly explain the existence of the current payday.

Overtime legislation presents a more nuanced issue. In general, employers must pay employees one-and-a-half the rate of their so-called straight pay for overtime work.[154] The key is that, *independent of the pay period*, the assessment of overtime is done with respect to a workweek, defined as forty hours. Thus, even if the employee is paid biweekly, the employee should receive payment for overtime in week one, even if they worked fewer than forty hours in week two.[155] Even employees paid on a daily basis are eligible for weekly adjustments for overtime.[156] While a fixed weekly assessment is the approach taken by the Department of Labor and several courts, some

INST. 23 (2014), https://www.epi.org/files/2014/EPI-CWED-BP379.pdf. This estimate does not cover commission-based employees.

[152] AM. JUR. 2D, LABOR AND LABOR RELATIONS § 3108. *See also Chapter 30, Records, Minimum Wage, and Payment of Wages*, DEP'T. OF LAB. 30b01(b) (Nov. 17, 2016), https://www.dol.gov/whd/FOH/FOH_Ch30.pdf "the salary is sufficient to meet the minimum wage requirements for all hours worked during the pay period;" *id.* at 30b05(1) ("There is no requirement that wages be paid weekly, as long as some regular pay period (such as biweekly or monthly) is established . . . The only requirement is that employees receive prompt payment of the minimum wage covering all hours worked during the pay period."). In California, see 8 CCR § 110104(B) (2018) ("minimum wage for all hours worked in the payroll period")

[153] The employer still owes the employee the federal minimum wage per hour for a tipped employee of $2.13/hr, which is not included in the example for the sake of clarity.

[154] 29 C.F.R. § 778.104 (2018). *See also* Freixa v. Prestige Cruise Servs., 853 F.3d 1344, 1346 (11th Cir. 2017) ("A district court ordinarily may not allocate compensation or hours across multiple weeks.").

[155] *Overtime Frequently Asked Questions*, N.Y. DEP'T. OF LAB., https://www.labor.ny.gov/legal/counsel/pdf/overtime-frequently-asked-questions.pdf (last visited Dec. 25, 2019). *See also* Fernandez v. Centerplate/NBSE, 441 F.3d 1006, 1007 (D.C. Cir. 2006) ("FLSA requires employers to pay overtime compensation for time worked in excess of forty hours per *week*, but not for time worked in excess of eight hours per *day*.").

[156] 29 C.F.R. § 778.112 (2018).

disagree.[157] Judge Easterbrook took the position that, "it is unlikely that Congress meant to require employers to pay overtime in the lean weeks when the fat weeks more than make up."[158] Thus, he approved of employers averaging pay over multiple weeks.[159] From a payday perspective, such an approach may incentivize longer paydays to allow the employer the opportunity to average over future "lean" months.

A deeper problem with overtime legislation concerns the definition of salaried employees, which constitute a large minority of the working population.[160] The idea of a salary is a fixed payment that does not depend on actual hours worked.[161] As such, salaried employees are not covered by standard overtime requirements. The FLSA distinguishes between two types of salaried employees: exempt and non-exempt.[162] The former are not eligible for any overtime pay, while the latter can be paid—in some circumstances—a rate significantly lower than overtime pay.[163] The legislation allows employers to avoid overtime obligations by opting to pay certain employees a salary rather than hourly payments.[164]

The law is concerned that employers would abuse the concept of salaried employees.[165] The employer could effectively circumvent overtime pay by designating any employee as a salaried employee and avoiding overtime pay. To avoid this possibility, the law defines certain criteria for what counts as a salaried employee. These criteria are meant to capture real differences between salaried and non-salaried employees. For example, if a worker is docked pay for working fewer hours, then the employer can no longer claim that the worker is salaried.[166]

The problem is that the FLSA also imposes a formal test: an employee cannot be considered salaried "if the employee regularly

[157] *Id*. at § 778.104 ("The Act takes a single workweek as its standard and does not permit averaging of hours over 2 or more weeks."). *See also Freixa*, 853 F.3d at 1348.

[158] Walton v. United Consumers Club, 786 F.2d 303, 307 (7th Cir. 1986).

[159] *See also* Triple "AAA" Co. v. Wirtz, 378 F.2d 884, 887 (10th Cir. 1967) (allowing for averaging over a year).

[160] BUREAU OF LAB. STATS., *Characteristics of Minimum Wage Workers, 2018*, BUREAU OF LABOR STATISTICS REPORTS (2018), https://www.bls.gov/opub/reports/minimum-wage/2018/home.htm.

[161] Garrett Reid Krueger, *Straight-Time Overtime and Salary Basis: Reform of the Fair Labor Standards Act*, 70 WASH. L. REV. 1097, 1103 (1995) ("Typically, salaried employees do not 'punch a clock,' are not paid by the hour, and are not docked pay if they do not work forty hours in a given week.").

[162] 29 U.S.C. §§ 213(a)(1), 213(a)(17).

[163] When employers pay employees who work in a "fluctuating workweek" arrangement, they need to pay only one half of the regular hourly rate, rather than 1.5 of that rate. The hourly rate, oddly, is lower the more overtime hours the employee clocks, a practice approved by the courts. *See generally* C.W. Von Bergen, *Using the Fluctuating Workweek Compensation Method to Reduce Overtime Expenses in Public Organizations*, 40 PUB. PERS. MGMT. 165 (2011).

[164] Fair Labor Standards Act, 29 U.S.C. § 213 (2018).

[165] Robert L. Levin, *Salaried or Hourly? Do Your Exempt Employees Meet the "Salary Test" Under FLSA?*, 11 LAB. LAW. 25, (2011).

[166] Brock v. The Claridge Hotel & Casino, 846 F.2d 180, 185 (3d Cir. 1988).

receives each pay period on a weekly, or less frequent basis."[167] That is, the law links pay frequency and pay status. As a result, if the employer chooses to pay an employee more regularly, the employer might not be able to claim that the employee is salaried for overtime exemption purposes.[168] This result appears absurd given legislative intent. The connection between pay frequency and overtime protection was made to describe some practical reality, not to influence it. However, by tying pay frequency to legal protections, the law deters employers from paying employees daily, lest they be considered unsalaried.

In sum, legislation explains some of the pay frequency patterns. Public sector employees are paid biweekly by fiat. Private employers may conform to public sector standards and are, in any case, incentivized to delay payments because of well-intentioned but poorly-drafted legislation. And while fiat may explain these practices, it does not justify them.

G. Check Cutting Costs

Paying workers is expensive. Schematically, paying involves four different stages: (1) determining pay due; (2) calculating withholding for compliance purposes; (3) transferring payments; and (4) receiving payments. The first two stages can be grouped as issues relating to payroll technology; the latter two can be grouped as issues relating to money technology.

The first cost is that of the determination of payment due. This is mostly a technological problem, and it has largely been resolved. Determining due pay for salaried employees is almost trivial in modern times.[169] For other types of employees, the determination may be somewhat more complex—but not by a large margin. The employee time clock was invented in 1888,[170] and with the broad integration of computers and mobile devices in the modern workplace, most time-tracking today is automated.[171] True, employers want to verify every reported work hour—a task that does not scale up well.[172] However, this difficulty is inherent to the employment relationship for reasons other than pay frequency, and, as we shall see, this

[167] 29 C.F.R. § 541.602 (2018).

[168] This topic was never litigated, so it is open to argument how the courts would rule. Conversations with practitioners suggest a general belief that courts would be willing to divorce pay frequency from the actual definition of salaried employees, although given the plain language of the text, it is unclear how they would reach this outcome.

[169] Even salaried employees may face certain deductions, so the determination is not always automatic.

[170] U.S. Patent No. 452,894 (issued May 26, 1891).

[171] Roughly 2.9% of US employees are reportedly working remotely, requiring alternative arrangements (such as salary or software tracking). Brie Weiler Reynolds, *The State of the Remote Job Marketplace*, FLEXJOBS (Mar. 27, 2018), https://www.flexjobs.com/blog/post/state-of-the-remote-job-marketplace/.

[172] The proposed solution depends on biweekly accounting, so employers can limit close verification to accounting day, rather than conduct it daily.

concern can be effectively resolved with careful design of pay obligations.

A seemingly more serious cost is compliance. Even after assessing the employees' wages, the employer must still verify that it is properly assessing compulsory and voluntary deductions, that levies are effectively put aside, that child support and alimony payments are correctly computed, and that any wage garnishments are deducted. Then, the employer must verify compliance with all minimum wage and overtime legislation. Finally, the employer must keep a record of hours worked and communicate this information to the employee. These challenges may have been enormous in the past, as properly computing withholding manually is a long, arduous, and error-prone process. But today, none of these challenges are especially onerous with the advent of the modern computer and payroll software. The per payroll cost of paying an employee in medium-sized companies appears to be between $1 to $5, although companies differ significantly in their pricing methodologies.[173] Completing a payroll "run" may involve a real cost, but this cost is no longer prohibitive.[174]

Despite the availability of software, employers still want to verify the accuracy of all payments, because failure to comply can result in criminal, civil, and ethical sanctions. The FLSA, for example, imposes criminal fines and even imprisonment for failures to comply.[175] This liability also extends to corporate officers.[176] The consequences can also be disciplinary for some professionals. One lawyer was put on probation for eighteen months for failure to file and pay various federal, state, and local payroll tax obligations on a timely basis.[177] The FLSA also includes a civil sanction: failure to pay wages can result in liquidated damages equal to all unpaid wages[178] and attorney fees.[179] Given the costs of mistakes, the employer will want to include safeguards—such as manual revision of at least some of the paystubs. Under the current system, these safeguards should be

[173] *See Real-World Payroll Services Prices From BuyerZone Buyers*, BUYERZONE, https://www.buyerzone.com/hr-personnel/payroll-services/ar-prices-payroll-large/ (last visited Dec. 25, 2019). *See also* GUSTO, https://gusto.com/product/pricing (last visited Dec. 25, 2019); *cf. Online Payroll Service Prices*, PRICE IT THERE, https://priceithere.com/online-payroll-cost/ (last visited Dec. 25, 2019); CORPORATE PAYROLL SERVICES, https://www.corpay.com/pricing/ (last visited Dec. 25, 2019).

[174] As I discuss later, the compliance cost would remain largely the same under my proposal, because the verification process will only take place once every two weeks. *See infra* Part IV.A.

[175] 29 U.S.C. § 216(a) (2018) (setting a fine of up to $10,000 and imprisonment of up to six months for intentional violations).

[176] Erwin v. United States, 591 F.3d 313, 316 (4th Cir. 2010); Hina Shah, *Broadening Low-Wage Workers' Access to Justice: Guaranteeing Unpaid Wages in Targeted Industries*, 28 HOFSTRA LAB. & EMPL. L. J. 9, 30 (2010).

[177] In re Finestrauss, 32 A.3d 978, 979 (Del. 2011).

[178] *See* 29 U.S.C. § 211 (2018). These damages are meant to be compensatory, so if the employer can prove that the employee suffered less damages, the damages can be reduced. But in practice, this is rarely the case. *See* Kinney v. D.C., 994 F.2d 6, 12 (D.C. Cir. 1993) (citing Walton v. United Consumers Club, Inc., 786 F.2d 303, 310 (7th Cir. 1986)).

[179] 29 U.S.C. § 216(b) (2018) ("The court in such action shall, in addition to any judgment awarded to the plaintiff or plaintiffs, allow a reasonable attorney's fee to be paid by the defendant, and costs of the action.").

employed at every pay cycle, and because they do not scale well, increasing the pay frequency can drastically increase costs. Illustrative was the momentary expression of horror when, in an interview with a payroll director for a large organization, I mentioned the possibility of moving to a daily payday.[180]

Overall, in terms of technology, payroll is sufficiently mature today to make its costs relatively small. There is a concern with verification, which does not scale as well. Still, these costs are small relative to the costs associated with money technology.

For most employers and employees, transferring money is a largely invisible process. Roughly 87% of households are paid using direct deposit,[181] a money transfer technology that involves the Automated Clearing House (ACH) system. Normally, there are no charges on the employee side; but employers are charged roughly $0.26–$0.50 per transfer. Employers also incur an additional administrative cost (in terms of personnel and IT) of $0.11–$0.25, suggesting a total cost of $0.37–$0.75 per single employee payment for one pay period.[182] These costs are not substantial by themselves, although moving from biweekly to daily payments can increase costs by $4.81–$9.75 per two weeks.[183] Even for a minimum wage employee, this is roughly the cost of another hour of work—a real, but not prohibitive, cost.

The problem is the "Other America."[184] In 2017, 14.1 million adults were unbanked, meaning they did not have either a checking or a savings account.[185] In addition, 48.9 million were "underbanked," i.e., they were using non-banks for financial products (such as check cashing, payday lending, or money orders) despite having a bank account.[186] As a consequence, 27.6% of households receive some of their payments in a paper check or a money order, and 7.9% receive payments in cash.[187] The under- and unbanked are also poorer on average.[188]

[180] Interview with anonymous payroll director, (Nov. 19, 2019) (details on file with author).

[181] *FDIC National Survey of Unbanked and Underbanked Households*, FED. DEPOSIT INS. CORP. 12 (2017), https://www.fdic.gov/householdsurvey/2017/2017report.pdf.

[182] *Payment Cost Benchmarking Survey*, ASS'N FOR FIN. PROFS. 7 (2015), https://www.bottomline.com/application/files/faster-cost-effective-afp-payments-cost-benchmark-survey-gen-us-srr-1510.pdf.

[183] In addition, ACH only recently (in 2016) started moving to a same-day process, a transition that is still on going.

[184] MICHAEL HARRINGTON, THE OTHER AMERICA (1962) (documenting the spread of poverty in the U.S.).

[185] *FDIC National Survey of Unbanked and Underbanked Households, supra* note 181, at 1.

[186] *Id.*

[187] *Id.* at 12. Note that the percentages do not add up to 100% as households may be paid in more than one method.

[188] For example, roughly half of Walmart's 1.4 million employees do not use direct deposit. LaRita Heet, *More Employees Say "Hello" to Payroll Cards*, CREDITCARDS.COM (Sep. 29, 2019), https://www.creditcards.com/credit-card-news/payroll-cards-pay-cards-walmart-1271.php.

Employees not paid via direct deposit are mostly paid by check or money orders—two dated, lengthy, unreliable, and expensive money technologies. For the employer, the simple cost of writing a check is estimated at $2.87–$3.15.[189] Checks are also physical objects, which add friction and costs related to security and delivery. Even the delivery of checks is unreliable; one employee described her experience: "[the] checks . . . were delivered by oft-delayed trucks that, living paycheck-to-paycheck, sometimes left her family in dire financial straits."[190]

Checks must be cashed somehow, and cash checking services flourish around the nation.[191] These services offer immediate money for checks, but because checks are such a slow and unreliable technology, these businesses assume a considerable risk for their services.[192] A check can be easily forged and, even if authentic, can still bounce. Cash checking services provide a real service, but they charge high rates. One study reports a range of 1.5%–3.3% of the check's face value.[193] This means that, on average, there is a cost of $40 *per paycheck* for typical households with full-time workers to even access their earned money.[194] If used regularly over one's career, the household will spend $41,600 in fees—money that could otherwise be used to build wealth for retirement.[195] Indeed, some of these fees are avoidable, by cashing the check at the bank of issue (i.e., the employer's bank), but this involves the time and cost of travel to the bank.[196] Getting to the location, safely carrying the check, and waiting in line are non-trivial costs; especially since paydays tend to be synchronized, leading to congestion.[197]

[189] NACHA, The Electronic Payments Association, http://www.electronicpayments.org/small-business/direct-deposit/learn/calculator.

[190] Michael M. Oswalt & César F. Rosado Marzán, *Organizing the State: The "New Labor Law" Seen from the Bottom-Up*, 39 BERKELEY J. EMP. & LAB. L. 415, 453 (2018). In 1908, a similar report emerged: the "pay car" containing payments was delayed, suspending all of the employees monthly pay. *Missouri Pacific Postpones Payday, Gives no Reason*, ST. LOUIS. POST (Febm 17, 1908).

[191] Check cashing is not unique to the unbanked. *See* Michael S. Barr, *Banking the Poor*, 21 YALE J. REG. 121, 144 (2004).

[192] *Beware of Fake Checks*, FED. DEPOSIT INS. CORP. (Aug., 26, 2019), https://www.fdic.gov/consumers/consumer/news/august2019.pdf.

Anecdotally, online users report their experience running a check cashing service as "Check Cashing Business is a Big NO. . . . it will ruin you." V. Sheth, *Answer to "Does Check Cashing Business Bring Good Profit?*, QUORA (Jun. 20, 2019), https://www.quora.com/Does-check-cashing-business-bring-good-profit.

[193] Barr, *supra* note 191, at 146–47. *See also* Robin A. Prager, *Determinants of the Locations of Alternative Financial Service Providers*, 45 REV. INDUS. ORG. 21, Section 2.2 (2014).

[194] Matt Fellowes & Mia Mabanta, *Banking on Wealth: America's New Retail Banking Infrastructure and its Wealth-Building Potential*, BROOKINGS (2008), http://community-wealth.org/_pdfs/articles-publications/cdfis/paper-fellowes-miabanta.pdf.

[195] *Id.* at 14.

[196] Barr, *supra* note 191, at 145 ("[A] large portion of the unbanked manage to avoid paying high costs for at least some of their financial services.").

[197] The concern with congestion is a longstanding one. *See e.g.*, *Congested Payday*, WASHINGTON POST (May 13, 1941) ("Residents of Washington . . . always know when payday

Finally, the use of cash presents its own difficulties. Roughly 8% of households are paid in cash.[198] Paying with cash requires carrying large amounts, which involves administrative overhead. More importantly, the perfect liquidity of cash invites theft risk, both for the employer and for the employee. Carrying large amounts of cash exposes one to risks, and there is little wonder why most people prefer to carry small amounts of cash on their person.

In conclusion, while money technology has improved dramatically over the last century, many employees are still being paid using dated technologies—checks and cash. These dated payment methods impose significant costs, making daily payment prohibitively expensive. While digital money exists and offers important efficiencies, it still has to overcome the under-banking gap and other issues of implementation.

III. ABOLISHING THE PAYDAY

The payday is a common feature of employment contracts. The payday implicates a credit transaction (K_2), but this credit transaction is not motivated by the logic of credit. Instead, the investigation of this practice suggests that it owes a large part of its vitality to outdated legislation and money technology. Even the most sympathetic justifications of the payday—those which are rooted in employee psychology—still leave the current arrangements in a poor light.

The goal of this Part is to explain why abolishing the payday and moving to daily streams of payment is critical, valuable, and more effective than some intermediate solutions that are currently being proposed. If abolition initially strikes one as radical, recall that in 1879 weekly payment systems were already in place—during a time in which one had to do all calculations by hand and transport a chest with coins between work locations.[199] Daily payments are well within reach today.

A. The Stakes of Abolishing the Payday

Suspending for a moment the *how*, let us consider the implications of abolishing the payday and moving to daily streams of payment.

In the first instance, the current biweekly payday harms workers. True, paying employees more frequently will not make households wealthier; but it will make them more capable of meeting life challenges as they come. Over the last few years, interest rates

arrives. For twice each month they are subjected to major and minor inconveniences"). At one point, President Roosevelt ordered the spreading of payday to 20 days, for this reason: Federal Paydays To Be Increased: U.S. Employees' Paydays to Be Increased The Washington Post (1923-1954); Washington, D.C. [Washington, D.C]17 Oct 1942: 1 (On file)

[198] FED. DEPOSIT INS. CORP., *supra* note 181.

[199] *See supra* note 146. *See also* Reid, *supra* note 65 (noting the practice of daily payments).

were at a historic low; but the stakes of abolishing payday will only increase if interest rates revert to their historical rates.[200] Lack of liquidity is associated with a variety of negative outcomes such as anxiety, divorce, and adverse health outcomes.[201] Abolishing the payday would help ease some of this pressure. The stress of thinking about how to pay for groceries the next day, whether one should skip the next dentist appointment, or the arguments with one's partner can be alleviated with greater control over one's finances. Indeed, the records from the nineteenth-century move to weekly payments suggest a marked increase in reported employee well-being.[202]

Greater liquidity also allows one to seize opportunities as they present themselves. Some of these opportunities are humdrum, although consequential for one's financial health, like buying discounted items in bulk. Other opportunities can have even larger effects, like buying a ticket to fly out to an interview with another employer. It is perhaps natural for a well-off reader to discount the difficulty insufficient liquidity imposes on life choices, but even the cost of dry cleaning or a haircut can prevent some from attending a job interview.[203]

One potential negative aspect of abolishing payday is that it will restrict credit access to businesses. Firms today borrow at cheap rates through the withholding of pay, and abolishing the payday might limit their access to credit, especially if the firm is a small business. This issue should not be overstated. Witholding pay from workers to finance firm operations is a risky and costly proposition. While Walmart enjoys the float from withholding pay, the costs endured by its employees far exceed this benefit. And if a small business can only afford to stay in business by withholding salaries, then there is a good reason to worry that the business overextends itself and is too risky. More generally, credit markets are there for a reason; households should not be in the business of lending money.

Another related negative consequence of abolishing the payday is the elimination of the wage premium associated with it. As discussed, one might expect a wage premium for longer paydays for two reasons. First, the employer receives the benefit of holding (and using) the money until the payday, and, second, the employer saves the costs of making more regular payments. Now, for those who think that employees do not receive a meaningful wage premium today for K_2 loans, this consequence is largely irrelevant. Even for those who believe that there may be a wage effect, there is some reason to doubt its magnitude, if not its existence. The single study that evaluated the effect of moving from the monthly payday to the weekly payday—

[200] MACROTRENDS, *supra* note 23.

[201] Joan R. Kahn & Leonard I. Pearlin, *Financial Strain over the Life Course and Health among Older Adults* 47 J. HEALTH SOCIAL BEHAVIOR 17 (2006).

[202] Redmount et al., *supra* note 68, at 1083.

[203] *A Good Impression Begins with the Way You Dress*, JAILS TO JOBS https://jailstojobs.org/free-interview-clothes/ (last visited Dec. 24, 2019);_Amelia Ward, *Barber Gives Homeless Free Haircuts and Trains Them to Work in His Shop*, LAD BIBLE (Dec. 21, 2019), https://www.ladbible.com/news/daily-ladness-barber-gives-homeless-people-free-haircuts-and-trains-them-up-20191220.

while admittedly dated and incomplete—found that this move actually led to an *increase* in the effective pay and well-being of employees.[204] This is, in part, because workers chose to work more when pay was more frequent (what economists call a 'wealth effect'). This finding should not be overstated because of various methodological and data issues, but it at least suggests that the effects of abolishing the payday may be more nuanced than what appears at first sight.

Whatever the case might be about the wage premium, daily pay would also have strong positive effects. Most directly, more frequent pay would remove workers from the unnatural position of lending money to their employers. The employer's benefit from retaining this money is more than offset by the worker's need for the money. In a very early decision, the Supreme Court clearly recognized this point: "[t]here [is] certainly . . . advantage to those who work for a living of a ready purchasing power for their needs over the use of credit."[205] The lack of purchasing power manifests itself in many ways—most painfully, in the cost of short-credit solutions. The average American has $5,600 in revolving credit card debt,[206] on which they pay 16% APR ($580 per year, roughly).[207] Credit cards appear cheap relative to the burgeoning installment loans industry, which charges an effective APR of 40%–90%.[208] The installment loans industry serves 10 million Americans annually and earns over $10 billion in finance charges.[209] And this industry is still cheaper than the payday lending industry, which charges a typical 300%–400% APR.[210]

I do not mean to argue that abolishing the payday would abolish either the payday industry or the short-term credit industry.[211] People borrow for many reasons—smoothing consumption, pursuing opportunities, bracing shocks, etc.[212] The demand for short-term credit solutions is based on real need, and the lack of liquidity due to the payday is but one of them. Still, there is little doubt that short-term credit solutions are very expensive and can often lead to inescapable debt spirals. Thus, achieving even a meaningful reduction in the *demand* for these services is a worthy social goal. To get a sense of the potential impact, consider the results of a study that

[204] Redmount et al., *supra* note 68, at 1083.

[205] Erie R.R. Co. v. John Williams, 233 U.S. 685, 704 (1914).

[206] Jeff Herman, *Average Credit Card Debt Statistics*, CREDITCARDS.COM (Jul. 16, 2019), https://www.creditcards.com/credit-card-news/credit-card-debt-statistics-1276.php.

[207] This is not an exact calculation, as the households do not carry the same balance throughout the year, and it does not account for monthly compounding.

[208] *State Laws Put Installment Loan Borrowers at Risk*, PEW (Oct. 17, 2018), https://www.pewtrusts.org/en/research-and-analysis/reports/2018/10/17/state-laws-put-installment-loan-borrowers-at-risk.

[209] *Id.*

[210] Michael A. Stegman, *Payday Lending*, 21 J. ECON. PERSP. 169, 170 (2013).

[211] *Cf.* Jim Hawkins, *The End of Payday Lending*, MANUSCRIPT 1, 7 (2019) ("[E]arned wage advances have the potential to end payday lending.").

[212] *See* Robert B. Nielsen et al., *Consumer Finances of Low-Income Families*, *in* HANDBOOK OF CONSUMER FINANCE RESEARCH 167, 169 (2016) ("Credit can help low-income consumers smooth consumption, invest in human capital, and build assets, but the high cost of credit can crowd out current consumption and saving").

examined the effects of an unexpected $600 tax rebate on payday borrowing. Using a variation in the timing of the rebate, the researchers found a large and marked effect on the demand for payday loans. In their analysis, payday borrowers were roughly 16% less likely to borrow from payday lenders within two pay cycles of receipt of the rebate.[213] This effect, unfortunately, disappeared after two pay cycles.[214]

Another important potential effect of abolishing the payday is that it may also lead to the abolition of the wasteful monthly utility payment practice. As noted, households consume daily but pay monthly. In consuming now and paying later, households are essentially borrowing from utility providers. And of course, this credit transaction comes at a cost; utility providers charge for offering credit services. This credit transaction is artificial; it may be an artifact of the payday itself. With greater liquidity, perhaps service providers can be made to charge households on a daily basis as well. By moving to daily payments, the cost of utilities can decline by what is now the cost of the interest payments that are implicit in the monthly bill. If the technology is ripe—and to a large extent it already is—then the costs of these additional transactions would be trivial. This means that removing this unnecessary credit transaction *may* result in dramatic savings—think about a household that borrows a few hundred dollars every month and its annual cost of doing so, multiplied by almost all households.[215] How much of the savings will actually be passed on to households is an important question, and while there is no reason to assume that all of the savings will be passed to households, there is also no general reason to assume that none of the savings will pass. It is enough for now to note that even if some of the savings will pass, the effect of abolishing the payday on households can be significant.

Overall, paying workers more frequently would have an important positive effect on their well-being and reduce the demand for short-term credit solutions.

B. Would Abolishing Payday Lead to Excessive Spending?

At this point, I should return to, and dispense with, the paternalistic objection to the idea of abolishing the payday. Regular payments strike some, at least on first blush, as unwieldy—wouldn't they lead to more spending? Would individuals be able to meet their monthly expenses if they are paid daily? Wouldn't regular pay exacerbate the need for payday lending, as individuals overspend their money?

[213] Marianne Bertrand & Adair Morse, *What Do High-Interest Borrowers Do with Their Tax Rebate?*, 99 AMERICAN ECON. REV. 418, 422 (2009).
[214] *Id.*
[215] As noted, millions of households default on utility payments and the costs of default are spread, at least in part, among all other consumers. *See supra* note 101.

We already encountered this argument as an explanation for the practice of the payday.[216] I noted there the evidence that rebuts the idea that frequent pay leads to more spending, and noted some of the theoretical problems with this account.[217] Here I would like to take a step back from the question of whether employees need help saving and focus on the question of whether employers should be the ones who help them save.

One way of thinking about this question is trying to magnify its logic. Suppose that employers moved from biweekly to an annual payday.[218] Each year on December 31st, the employer would send its employees a single check with all of the annual wages. For the full-time employee making minimum wage, that would mean moving from a $580 biweekly check to an annual check for $15,080.[219] I think it is fairly evident that such a system would put workers at a significant detriment; few would willingly opt-in to such a system. Indeed, we rarely see employees asking employers to delay payments.

Another way is to think about forced savings as a form of paternalism. In the past, some expressed concerns that frequent pay would result in "frequent debaucherie."[220] Thus, perhaps a way to save workers from themselves is to create a forced-savings system. The response here is that even if one subscribes to a paternalistic worldview, this form is particularly strong: it calls to withhold property from individuals because one thinks they are insufficiently responsible to handle it. Such a claim, if true, would require strong evidence. But as noted, the evidence suggests otherwise.[221] In fact, there are some deeply disturbing stories of how the larger lump sum payments, due to infrequent pay, result in substance abuse.[222]

[216] *See supra* Part II.E.

[217] *Id.*

[218] As unusual as an annual payday may seem, in 1902 an Illinois court seems to have accepted, begrudgingly, such a possibility. *See* Chicago Soap & Polish Co. v. Stansbury, 99 Ill. App. 488, 489 (Ill. App. Ct. 1902) ("An engagement to work for one year for $2 per day, payment to be made at the expiration of the term, is so unusual that it is not to be presumed." Note that the court only requires positive proof of such an agreement).

[219] For a minimum wage worker, that would be the difference between a biweekly check for $580 and an annual check for $15,080.

Nothing in this analogy would be diminished—and in fact, it would be stronger—if the employer was willing to offer higher pay to its employees, passing 100% of the value the employer gets from writing fewer paychecks and from the credit value of keeping the money. This is because the employer's value (their cost of borrowing) would be minimal compared with the household's cost of borrowing for the year.

[220] Robinson, *supra* note 76, at 33. Payday was a special occasion, in turn of the century America, when mostly men engaged in communal binge drinking, spending a large portion of their payday wages. *See also* MADELON POWERS, FACES ALONG THE BAR: LORE AND ORDER IN THE WORKINGMAN'S SALOON, 1870-1920, at 52–53 (1998); COMMONS & ANDREWS, *supra* note 3, at 52 (noting that some states had special legislation mandating payment during pay hours, to avoid the payment bar-rooms).

[221] *See supra* Part II.E.

[222] Martin Selsoe Sorensen, Greenland Calls On Denmark to Help Fight Child Sexual Abuse, N.Y. Times (Sept. 27, 2019) ("Pay days are the worst time for the children of Tasiilaq, . . . With their salaries or social benefits in hand, many adults tend to drink and parents become too inebriated to look after their children . . . So on the last Friday of every month, officials open a sports hall in the district as a shelter to keep children away from sexual abuse.")

But the core of the problem lies elsewhere: employers are simply unreliable agents for the management of employee savings.[223] There is a reason why pension funds, such as 401(k)s, are mostly handled by third-parties. Employers are not some neutral bank; in practice, wage theft—the withholding of pay due—is "rampant in the low-wage workforce."[224] Employers (and the government is no exception) sometimes unilaterally suspend pay.[225] Moreover, keeping money with one's employer also gives the employer leverage, and the employer may abuse it.[226] Worse, unlike banks, employers are not insured against bankruptcy. Thus, using employers as vaults not only exposes employees to abuse but also to the risk of bankruptcy, a risk over which the employee has little control.[227] Bankruptcy risk also exposes another problem with employer-side saving. Employers, after all, are also humans and are inherently not immune to the same present bias that would lead employees to squander money. The manager may be tempted to spend the money on a new machine, a shiny business opportunity, or a private car, not leaving enough slack to pay wages.[228] Given these problems, employees are likely better off facing their own temptations than dealing with those of their employers. At the very least, employees would benefit from having reliable, insured third parties manage their savings (such as their 401(k) retirement accounts), rather than having their bankruptcy-prone employer manage them.[229]

C. Alternatives to Abolition

At this point, I hope, the question is no longer whether the payday is worth preserving, but rather what the viable alternatives are. As I propose the abolition of the payday in favor of daily streams of payment, I should explain why other more "moderate" solutions are ill-advised.

[223] A key component of prudent financial planning is diversification. Tying one's money with one's place of employment is the opposite of diversification.

[224] Llezlie L. Green, *Wage Theft in Lawless Courts*, 107 CAL. L. REV. 1303, 1309 (2019). *See also* Immigrants' Rights/International Human Rights Clinic at Seton Hall University, *All Work and No Pay: Day Laborers, Wage Theft, and Workplace Justice in New Jersey* (2011), available at: https://www.immigrationresearch.org/report/seton-hall-university-school-law/all-work-and-no-pay-day-laborers-wage-theft-and-workplace-ju.

[225] The concern with suspended government pay is longstanding. *See, e.g.*, *Payless Payday*, WASHINGTON POST (Aug. 17, 1949) (noting that "year after year, Federal employees [sic] face suspensions of income").

[226] *See supra* Part II.D.

[227] Aside from bankruptcy, letting the employer control more money provides it with leverage which it can use against the employee in various ways, making quitting, for example, more difficult. Employers are also less efficient than financial institutions at making periodical payments.

[228] Even without present-bias, it is well known that large debts (such as to unpaid employees) exacerbate risk taking by managers, which may lead to bankruptcy.

[229] The authors foresee this objection but dismiss it: "it is not particularly important *who* conducts the timing-welfare calculation, as long as *someone* does." Parsons & Van Wesep, *supra* note 16, at 383 (2013). The fact that, despite the considerable risks, employers are the ones who supposedly save for employees is too important to be casually dismissed.

What is perhaps the leading alternative to dealing with the problem of the payday is the use of wage-advances. Today, there is a flurry of activity in this space by Fintech companies that compete over a variety of wage advance solutions.[230] These products go by different names—wages on demand, earned income access, advance wage payment—but they all share a basic structure: the employee is paid ahead of the payday as part of the anticipated pay.[231] The advance is paid by either the employer or a third party, which specializes in making advances against the employee's wages. In a strict sense, these are not really advances, as they mostly apply to *earned* wages. Hence, the employee is not paid *early* but is instead lending *less*. But whatever the terminology, the effect is the same—bridging the gap between earning one's pay and the payday. Thus, the concentration of activity in this sector is a good indication of the size of the problem of K_2 and vividly demonstrates K_2's inefficiency.

Such advances can offer a response to short-term liquidity shocks, such as a car that suddenly needs a costly repair or an emergency hospital visit. Nonetheless, advances are a flawed, incomplete, and potentially harmful solution to the underlying problem—justified only if deeper solutions are unavailable but otherwise a band-aid for a lost limb.

The central objection is cost. Paying employees in advance involves cost on the side of either the employer or the third-party company. Someone has to hold sufficient capital, handle requests, and create mechanisms to ensure proper deductions come payday. Few would be willing to bear this cost for free.

While Fintech and terms such as "wage on-demand" sound novel, the history of employer advances is longstanding, and it is not wholesome. In the nineteenth century, American employers would regularly issue advances to their employees.[232] Against these advances, employers charged fees and made deductions.[233] In fact, "states were worried about employers that took improper deductions from worker wages or forced them to borrow from employers."[234] The effect of these issues is reflected in the memorable "Sixteen Tons," written by Merle Travis in 1946 and modeled after his father's experiences working in the coal mines:[235]

> You load sixteen tons, what do you get?
> Another day older and deeper in debt
> Saint Peter don't you call me 'cause I can't go
> I owe my soul to the company store

[230] Hawkins, *supra* note 211, at 5–6.

[231] Stephen T. Middlebrook, *What Business Lawyers Need to Know About Wage Advance Products*, AM. B. ASS'N (Sep. 5, 2019), https://businesslawtoday.org/2019/09/business-lawyers-need-know-wage-advance-products/.

[232] *See* Donald J. Harris, *On the Timing of Wage Payments*, 5 CAMBRIDGE J. ECON. 369, 378 (1981).

[233] *Id.*

[234] Willborn, *supra* note 83, at 40.

[235] Sixteen Tons: *The Story Behind the Legend*, TENNESSEE ERNIE FORD, https://www.ernieford.com/sixteen-tons (last visited Feb. 13, 2020). The song resonates other problems of the time – payment in script and company credit and wage theft.

To combat abuse, "states passed legislation that regularized paydays and limited employer's ability to deduct fees and interest from employees' wages."236 It is not without irony, notes Professor Willborn, that "the payday loan industry had arisen to do almost exactly what employers were doing prior to the state wage- payment laws."[237]

Today, there is still great regulatory uncertainty regarding advances. While some view these as services that provide the consumer with much-needed credit, others see them as opportunities to profit at employees' expense.[238] The relevant framework, even at the Federal level, is complex—involving the interpretation of the Truth in Lending Act (TILA), the Equal Credit Opportunity Act (ECOA), the Fair Credit Reporting Act (FCRA), the Fair Debt Collection Practices Act (FDCPA), and the Consumer Financial Protection Act (CFPA).[239] Article 9 of the Uniform Commercial Code (UCC) also adds complexity, as it views the sale of accounts (i.e., future payments), as a secured transaction, thus subjecting it to its burdensome framework.[240] Some state laws also require licenses to lend, limit wage assignments, and impose usury limits.[241] This results in a very complex regulatory landscape, and employers explain their reluctance to offer advances in this complexity.[242]

Third-party advance companies are for-profit companies, and they turn a profit by charging fees, commissions, and, oddly, tips. One such product is called Earnin', where users are encouraged to leave a tip of $0-14 per $100 advanced; failure to leave a tip is believed to restrict the user's access to cash.[243] A $14 charge per $100 is very close to the costs of payday lending ($15). Another study of Fintech companies finds that the average APR ranges from 20% to 145%.[244] It is damning with faint praise to say that these products, "although [expensive] in absolute terms, appear[] clearly superior to [short-term loans] alternatives."[245]

[236] Willborn, *supra* note 83, at 40.

[237] *Id.*

[238] For the debate, see Hawkins, *supra* note 211, at 36–40.

[239] Adam Levitin, *What Is "Credit"? AfterPay, Earnin', and ISAs*, CREDIT SLIP (Jul. 16, 2019, 1:31 PM), https://www.creditslips.org/creditslips/2019/07/what-is-credit-afterpay-earnin-and-isas.html (arguing that, inasmuch as no finance charges are levied, some advance products are exempt from TILA but subject to other forms of credit legislation).

[240] U.C.C. § 9-109(a)(3) (AM. LAW INST. & UNIF. LAW COMM'N 1977).

[241] Hawkins, *supra* note 211, at 33–34.

[242] *Id.* at 8.

[243] Kevin Dugan, *Cash-advance App Earnin Gets Subpoenaed by NY Regulator*, N.Y. POST (Mar. 28, 3019), https://nypost.com/2019/03/28/cash-advance-app-earnin-gets-subpoenaed-by-ny-regulator-source/ ("Earnin encouraged users to leave a tip of anywhere between zero and $14 on a $100 weekly loan. Users who don't leave a tip appear to have their credit restricted. Meanwhile, a $14 tip would equate to a 730- percent APR—nearly thirty times higher than New York's 25 percent cap."). In evaluating the costs, one should consider the regulatory uncertainty; if it would ever be resolved, one might expect greater competition in this space.

[244] Todd H. Baker, *FinTech Alternatives to Short-Term Small-Dollar Credit: Helping Low-Income Working Families Escape the High-Cost Lending Trap*, HARV. KENNEDY SCH. 46 (2017), https://www.hks.harvard.edu/sites/default/files/centers/mrcbg/files/75_final.pdf.

[245] *Id.*

Some of the costs are less visible. Professor Jim Hawkins recently reviewed the contracts used by market players. He finds that despite Fintech companies' self-attestation to being "concerned with their social impact" and notwithstanding the intense regulatory scrutiny, their contracts are "surprisingly unfriendly" to the consumer.[246] Arbitration, disclaimers of warranties, unilateral contract amendments, and high fees are some of the more common issues.[247] It is highly likely that, even if permitted to operate, purveyors of advances will be held under strict regulation.[248]

Reforming laws to facilitate advances would result in a complicated and costly patchwork of legislation. It is inevitable that some advance companies will go the way of many lenders in the past: resorting to abusive terms, one-sided "mistakes," and excessive rates. The issue is not so much that companies seek to profit; it is that the problem they seek to solve is artificial. The problem is the payday itself. The payday is an artifact of badly-designed legislation and dated money technology. Treating this problem directly can resolve the liquidity problem directly without requiring the development of a newly-regulated industry. Although the focus should be on eradicating the payday entirely, advance payments are a step in the right direction. They highlight, quite clearly, the unreasonable burden K_2 imposes on workers. They also develop technologies and solutions for regularizing payments. And, to the extent the solutions provided here would take time and political will to implement, wage advances can serve an interim solution.

IV. A WORLD WITHOUT THE PAYDAY

The abolition of the payday requires steps that are far more conservative than the goal might seem to imply. Indeed, while the problems caused by the payday are severe, the solutions are fairly mild. This suggests a low-hanging policy fruit: large effects with small changes—ones that do not risk complex, unanticipated systemic effects. With sufficient goodwill, this policy can be implemented in a very short time span, dramatically improving the welfare of millions of Americans.

Let us first reflect on the two most important barriers to regular pay: compliance costs and money technology for the underbanked. Both of these issues create a scale problem: while payroll software can fairly accurately estimate pay, the costs of inadvertent compliance errors are high, thus requiring human supervision and authorization for each payment. Whereas ACH money transfers provide a fairly cheap solution, even with daily payments, it is inapplicable with respect to the unbanked and the underbanked, who must rely on inefficient alternative money instruments, such as checks.

[246] Hawkins, *supra* note 211, at 23–24.
[247] *Id*.
[248] *Id*, at 43–48 (proposing regulation).

In considerations of these issues, here is the proposal.[249] At the end of each day, employers will be required to pay employees at least 93% of a good-faith estimate of their earned income.[250] The payday will be replaced by an "accounting day," once every two weeks, when the employer must complete a final calculation of the employee's full earned income for the period. After making this calculation, including all adjustments for unclaimed deductions, bonuses, commissions, etc. , the employer will adjust the daily pay to reflect outstanding amounts. If no adjustments are necessary, the employer will pay the employee the daily 7% shortfall, which would come to an extra day's worth of pay—once every two weeks. As long as the employer makes a good faith estimate of the daily pay, the employer will not be held liable for regulatory compliance issues for daily pay—such liability will only follow if, as is today, the employer fails to pay in full on accounting day.

Under this proposal, employers will not pay their workers their full daily pay but only an estimate of part of it. The reason why employers will not be required to pay in full is grounded in a few considerations. It is very difficult to know the total amounts due to employees, given all the possible deductions, taxes, and levies. Hence, some estimation may be unavoidable, and this means that there will often be errors, either of over- or under-payment. If employers are not afforded some margin of error, that would require them to carefully review each payment—and the costs of doing so daily may be prohibitive.[251] Another important consideration is that it is arguably harder for the employer to collect money owed from the employee than vice versa, given the greater mobility of the employee and lack of collateral. Leaving 7% of the income to the last day of the fourteen-day period is calculated to create a buffer that, on the one hand, allows the employee to keep most of the daily pay and, on the other hand, accounts for potential errors in daily estimates. Subject to further experimentation, this margin should be sufficient to allow employers to make offsets against mistakes in overpaying employees.[252] It also means that the employee is receiving on the last day of the biweekly period an extra day's pay (which is deducted from their on-going payments). This feature may appeal to those who think employer-based budgeting is helpful.

The design of the biweekly pay is meant to address two concerns: wage monitoring and compliance-cost control. Wage theft is

[249] The mode of reform can be legislative, but it is worth noting that the Restatement of Employment Law also recognizes the possibility of changes to employment law through the common law. *See* RESTATEMENT OF EMP'T LAW § 3.01 (AM. LAW INST. 2015) ("wage-payment laws . . . do not generally preclude common-law development because they are based on contract principles found in the common law.")

[250] To pay daily, the business itself must be liquid, and maintaining liquidity is often a challenge, especially for small business owners. Fortunately, business owners can borrow against

[251] *See supra* Part II.F (discussing costs of payroll).

[252] In most industries, a much smaller buffer would be needed—and perhaps no buffer is even needed for salaried employees with fix wages. Still, it is prudent to start with a moderate buffer in experimenting with the implementation of this proposal.

an important concern, and monitoring daily payments may be harder than monitoring the transfers of larger lump sums.[253] Of course, once the employee grows accustomed to daily pay, he or she could detect deviations by comparing actual payments to normal payments. Still, with possible daily fluctuations, deviations are harder to detect. To deal with this problem, on accounting day, the employer would produce a pay stub that accounts for all of the biweekly payments. The employee can then compare this amount to amounts paid, just as easily as can be done today.[254] The second function is controlling compliance costs. As noted, a large part of the cost of making payments is due to the need to verify compliance with a variety of different laws. Because the final accounting is only done once every two weeks, the employer would not need to engage in more compliance than they do today, besides the fairly trivial calculation of 93% of the expected daily pay. Note that the employer does not bear liability for small or unintentional deviations, making it unnecessary to verify daily payments with the same degree of attention as the biweekly pay.

One remaining issue is the control of money-transfer costs. As noted, this is not an issue for the majority of workers,who are banked and can benefit from ACH transfers, but it is still a pressing and painful issue for the under- and unbanked. The solution here is technological and I explore in greater length the use of pay cards as a viable solution to this problem.[255] In addition to pay cards, others have proposed non-technological alternatives, such as postal and public banking, which can also mitigate these issues.[256]

An optional addition to this proposal would be to allow employees to elect a biweekly pay. That is, the daily pay would be presented as an option alongside biweekly pay, and employees could elect which payment option they prefer. In terms of preserving employee choice, this would seem superior, as those employees who find biweekly pay superior would elect it. Such a choice may be preferred by some—if the worker has no need for liquidity or finds it difficult to budget otherwise. But for the reasons I laid out earlier, I believe employer-side savings is a bad idea due to the counterparty risk.[257] If employees need help budgeting, bank-side savings programs are a superior alternative. And if employees want to lend money, they can always do so in explicit capital markets, where there is more robust competition for their money. Hence, presenting this

[253] On wage theft, see *supra* note 224 and accompanying text.

[254] It may be necessary to add in the bank's user-interface support for easy comparisons of employer-pay per wage period. Such technology is already implemented in the apps and websites of most banks, which allow to filter deposits by recipient per period.

[255] *See infra* Part IV.D.

[256] The U.S. postal banking system was abolished in 1966. On its history and for a proposal to reinstate it, see BARADARAN, *supra* note 22, at 183–226. *See also Know the Facts*, CAMPAIGN FOR POSTAL BANKING, http://www.campaignforpostalbanking.org/know-the-facts/ (last visited Feb. 13, 2020).

[257] *See supra* Part III.A.

option may be a trap for the unwary and will serve little other function.[258]

The final part of this proposal is that it envisions a transition and experimentation period. Wages and payments are systemic issues; they affect every part of the economy. The urgent need for reform should be tempered with patience and understanding that immediate implementation may be harmful. Instead, an announcement of a target date for daily pays in a few years, perhaps coupled with a transition to weekly pay, is likely the most prudent course of action.

Implementing this reform would require some legislative changes. The key changes are focused on changing labor laws that impede more frequent pay; changing our money infrastructure; improving market education; and changing the market by leadership. Each of these interventions deserves separate consideration and the rest of this Part discusses them in order.

A.Changing by Information

One reason why the payday persists is related to the employer's power in employment negotiation. Perhaps employees are insufficiently aware of the credit nature of K_2. If that is the case, employees would also be unaware of the true cost of K_2 and will not demand an appropriate wage premium. This imbalance of information or sophistication tilts the balance in favor of the employer and leads to inefficiently infrequent pay periods.

This idea—that individuals misprice credit transactions—is a central impetus for the enactment of TILA. Congress diagnosed that consumers engage in "uninformed use of credit" and prescribed "meaningful disclosure of credit terms."[259] By conspicuously disclosing credit terms using a uniform standard, TILA hopes to improve consumer finance decisions.[260]

The logic of TILA can be brought to bear on payday. If employers want to borrow money from employees through the payday, they might be required to disclose the fact that payday is a credit transaction. This can be done in the written employment contract or in a separate disclosure. More importantly, the employer might be required to display the (implicit) cost of credit: specifically identify what portion of the pay serves as interest payment and, given the frequency of pay, what is the APR of this transaction. This will allow the employee to better understand the meaning of the credit element of the payday and to "shop" effectively—that is, to understand how pay frequency compares to the cost of borrowing from other sources and choose, if given the option, a shorter pay period.

[258] A more compelling reason to favor biweekly pay is if the check-cutting costs are high, so the employee could be paid more by being paid less frequently. However, this is a transitionary issue until the money and payroll technology are sufficiently advanced.

[259] Truth in Lending Act § 102(a), 15 U.S.C. § 1601(a) (2018).

[260] *See generally* Hosea H. Harvey, *Opening Schumer's Box: The Empirical Foundations of Modern Consumer Finance Disclosure Law*, 48 U. MICH. J.L. REFORM 59 (2014)

The use of disclosure also has one substantive implication in the context of the minimum wage. If an employer borrows money, it should identify the portion of the pay that is the wage premium. The remaining pay is the pay-for-work portion of the wage paid to the worker. A prolonged pay period undercuts the minimum wage obligations of the employer; paying $7.25 hourly with a daily payday is not the same as paying it monthly. In the latter case, the employer is arguably failing to meet the minimum wage obligations. That federal legislation does not account for this difference suggests a serious blind spot, even among legislators and judges. Once advertised, courts could start paying better attention to what the proper baseline the FLSA envisions is—is it daily pay, weekly pay, or something else?

B.Changing by Leading

One potential explanation for the persistence of the payday is that government employees are paid biweekly.[261] Social norms can have a significant effect on market outcomes, and if the government declares a certain pay period to be the standard, then this pronouncement might have downstream effects on private employers.

If this explanation carries any explanatory power, it opens the road to straightforward intervention. Under Title 5 of the United States Code, all federal employees are to be paid once every two administrative workweeks.[262] This period could be changed to a daily payment of 93% of the daily pay, subject to a biweekly accounting. Notably, the change will not infringe on any employee's rights. Nor will this reform require large substantive changes. Admittedly, changing federal legislation is not easy, and I do not mean to discount the political and procedural challenges, especially because state law is so diverse and will also have to be amended. However, the importance of the goal, and its non-partisan nature, promise some optimism.

C.Changing Employment Law

One impediment to abolishing the payday is, ironically, minimum wage legislation. As I have noted, the FLSA makes employers average the minimum wage payments over the entire pay period. This incentivizes employers to extend the pay period as much as possible so they can benefit from averaging. If a tipped employee is making above minimum wage in week one and below minimum wage in week two, the employer could avoid compensating the employee for week two by setting a biweekly payday. We also saw that overtime legislation, at least in theory, does not have this flaw.

[261] *See supra* Part II.E.
[262] 5 U.S.C. § 5504(a) (2018).

The faulty legislative design opens the door to a number of potential interventions. The key to all of these options is to divorce the averaging period from the pay period. Hence, the option with the least effect on the status quo would permit employers to choose their accounting periods. The accounting period will substitute today's payday and will be the day on which the employer will average the employee's pay and see if any amounts are still due to meet the minimum wage requirement for the accounting period. The length of the accounting period could be regulated by the same limitations set today by state legislation on pay periods. This way, the employer will pay the employee each day of the week and then, come accounting day, make sure that a minimum wage was paid. If there is any shortfall in payments, the employer will add it to that day's pay. Over a two-week period (or however long the accounting period is) the employee will be paid *the exact same amount* the employee would have been paid under the payday—but at more frequent intervals. This aspect of the proposal means that neither employee nor employer rights are harmed by this transition, yet the indignities of the payday are avoided.

Similarly, overtime legislation should divorce pay frequency from the definition of who is a salaried employee; there is no reason to tie the definition to the (in)frequency of pay.[263] A daily-paid employee can equally be salaried or unsalaried, and the frequency of pay need not reflect on this determination.

Finally, employers' compliance with wage and hour laws should be evaluated at the accounting period. Thus, if an employer makes a compliance error on a specific day, this should not be a cause for a lawsuit. The goal is to reduce on-going compliance costs, and allowing lawsuits to proceed based on random errors would undermine this goal. At the same time, employers are still under a duty to make a good-faith estimate of the 93% pay the employee deserves. This means that employers do not have a carte-blanche right to underpay employees daily. While one-off or even occasional mistakes should not be grounds for a lawsuit, the employee should be allowed to sue for systematic mistakes if they are done in the employer's favor. Hence, the proposal does not derogate in any way from minimum wage laws or overtime laws under the status-quo; it neither increases pay nor reduces it. The only effect is on pay frequency.

D.Reforming Money Technology

Transferring money is more difficult than would appear at first glance. I have already noted the various costs associated with bank transfers, the difficulty of storing and handling cash, and the many costs of writing and liquidating checks.

Digital money is clearly the future, and, to a growing extent, it is the present.[264] In particular, employers are now increasingly using

[263] If one believes that this definition tracks any meaningful practical distinction, it is possible to use the accounting period instead of the current pay period.

[264] An estimated 4% of Americans hold only a prepaid card. Analysis based on data

payroll cards.[265] A payroll card is akin to a debit card and is issued by a bank or another financial institution. The account is not attached to any depository account, and thus, the card owner is spared the cost and difficulty of opening a bank account. Instead, the owner charges the card against the available balance. In 2017, roughly 3.4% of households reported receiving income with a payroll card,[266] and the CFPB estimates a 6% growth, amounting to $44.6 billion loaded onto these cards.[267] In 2015, nineteen state governments were already using payroll cards,[268] and various large employers such as Walmart and ___ are also using them.

Payroll cards are convenient, safe, and allow the immediate use of the funds paid. Importantly, the employee does not have to have a bank account to use a payroll card. This means that one's creditworthiness and legal status are not hurdles. Moreover, the employee need not maintain a minimum balance in his or her bank account or pay fees. The cost of depositing funds is also reportedly low: $0.35 in deposit costs.[269] It is not surprising, then, that many low-paid employees view payroll cards positively.[270]

There are also various concerns with payroll cards, many of which will be familiar to users of bank accounts.[271] One concern is the insurance of amounts deposited on these cards—what prevents a "run on the card"? Then there is the issue of fees: ATM-use fees, point of sale fees (i.e., a transaction fee), overdraft fees, and even balance inquires fees.[272] By one estimate, the average per-employee fees were $20 per month.[273] The fees are badly disclosed.[274] Initial reports on this growing practice were accordingly alarmists.[275]

presented in FED. RES. SYS., *supra* note 5, at 18–19.

[265] On the other hand, a survey by the FDIC found that usage of prepaid cards by households ranged between 7.9% (2013), 9.8% (2015), and 9.2% (2017). FED. DEPOSIT INS. CORP., *supra* note 181, at 7. 9.2% of households using a prepaid card reported receiving it as a payroll card. *Id.*

[266] *Id.* at 12. One estimate by a consulting firm from 2015 estimated that payroll payments will exceed check payments by 2017, but FDIC data still shows that checks are far more common. *See* Madeline K. Aufseeser, *Checkmate: U.S. Payroll Card Programs Trump Paper Checks* AITE (2015), http://www.aitegroup.com/report/checkmate-us-payroll-card-programs-trump-paper-checks.

[267] *See* Prepaid Accounts Under the Electronic Fund Transfer Act (Regulation E), 12 C.F.R. § 1005 (2018); *see also* Truth in Lending Act (Regulation Z), 12 C.F.R. § 226 (2018).

[268] *Rating State Gov't Payroll Cards*, NAT'L CONSUMER L. CTR. 3 (2015).

[269] *Pinched by Plastic: The Impact of Payroll Cards on Low-Wage Workers*, NEW YORK STATE ATT'Y GEN., NY.GOV 3 (2014), http://www.ag.ny.gov/pdfs/Pinched%20by%20Plastic.pdf.

[270] Oswalt & Marzán, *supra* note 190, at 453.

[271] Payroll cards do not bear interest, but given the typical rates in checking accounts, this concern is of little practical consequence. *See* Haim & Mann, *supra* note 159, at 1008.

[272] *See supra* note 220, at 6.

[273] *Id.* at 9.

[274] *Id*. at 13.

[275] Jessica Silver-Greenberg & Stephanie Clifford, *Paid via Card, Workers Feel Sting of Fees*, N.Y. TIMES (June 30, 2013), http://goo.gl/VzyTz.

Federal legislation partially covers payroll cards. Under the Electronic Fund Transfer Act (EFTA) and Regulation E,[276] financial institutions that offer payroll card accounts must make account information available to consumers by specific means, but they are exempted from providing periodic statements.[277] In addition, the financial institution must allow consumers to report errors and limit customers' liability for unauthorized transfers.[278] In April 2019, a new CFPB rule came into effect, expanding the fraud, error, and unauthorized charges protections to these cards; requiring simplified disclosure; and providing for easy access to information.[279] State legislation in this area is developing. Roughly half of the states have some laws that regulate payroll cards.[280] The regulations usually permit the use of these cards but impose some limits on fees and set rules on proper fee disclosure.[281] Finally, a series of class actions were filed against employers who offered payroll card programs, for failing to obtain employee consent and for violating wage and hour laws.[282] In one of these cases, a court in Pennsylvania ruled that the mandatory use of pay cards that impose fees is illegal.[283]

Facilitating the use of payroll cards is an important step towards the abolition of the payday. The recent CFPB regulation offers an initial framework, safeguarding certain employee rights, although more experimentation is needed.[284] Still, the fragmented nature of state legislation impedes much innovation.[285] Admittedly, it is difficult to design a fee structure that would make payroll cards profitable to operate and yet not encumber poor households with additional expenses. Still, others have made the case that increasing

[276] Electronic Fund Transfer Act (EFTA), 15 U.S.C. § 1693 (2012).

[277] *Electronic Fund Transfer Act*, FED. RES. 18, https://www.federalreserve.gov/boarddocs/caletters/2008/0807/08-07_attachment.pdf (last visited Dec. 28, 2019).

[278] *Regulation E: Electronic Fund Transfer Act*, FED. RES. 6, https://www.federalreserve.gov/boarddocs/supmanual/cch/efta.pdf (last visited Dec. 28, 2019).

[279] *See generally* CFPB, https://files.consumerfinance.gov/f/documents/20161005_cfpb_Final_Rule_Prepaid_Accounts.pdf (last visited Dec. 28, 2019).

[280] Rachel Blakely-Gray, *Pay Card Laws By State and Regulations*, PATRIOT SOFTWARE (June 5, 2019), https://www.patriotsoftware.com/payroll/training/blog/pay-card-laws-by-state/.

[281] *See generally id.* (surveying state laws); *see also* Sarah Jane Hughes & Stephen T. Middlebrook, *Are These Game Changers? Developments in the Law Affecting Virtual Currencies, Prepaid Payroll Cards, Online Tribal Lending, and Payday Lenders*, 70 BUS. LAW. 261, 265 (2015).

[282] *See* Joint Stipulation of Class Action Settlement and Release ¶¶ 42, 47, Chavez v. PVH Corp., No. C 13-01797-LHK (N.D. Cal. Feb. 12, 2014); First Amended Compl. ¶¶ 1-4, Lapan v. PVH Corp., No. C 13-05006-YGR (N.D. Cal. Dec. 9, 2013); Plaintiffs' Original Petition ¶¶ 14, 16, 19, Branson v. Destiny Foods, Inc., No. D-1-GN-14-001131 (Travis Cty., Tex., May 13, 2014).

[283] *See* Siciliano v. Mueller, 149 A.3d 863 (Pa. Super. 2016).

[284] *See* Haim & Mann, *supra* note 271, at 1014–19.

[285] *See* Benjamin Lo, *Fatal Fragments: The Effect of Money Transmission Regulation on Payments Innovation*, 18 YALE J. L. & TECH. 111 (2016).

access to banking through public subsidies can be justified both as a matter of redistribution and efficiency.[286]

Against this regulatory backdrop, positive steps can be taken to promote payroll cards, at least for an initial period of adoption, such as by offering certain tax subsidies or requiring all employers to offer this option.

A less obvious hurdle in the way of payroll cards is pro-employee regulation that mandates that employers offer the choice of payment methods. The Electronic Fund Transfer Act and Regulation E prohibit employers from forcing employees to receive wages via pay card.[287] New York law requires employers to provide employees with at least one fee-free method of payment every payday.[288] This choice creates unanticipated problems: if, when setting a daily payday, employers must pay some employees in cash or cash, this cost could be significant. Employee choice, then, can undermine the viability of payment streams.

The solution, however, is quite moderate and uses the same distinction as before between payments and accounting day. Employers who offer daily pay using pay cards or direct deposit could still be required to offer employees a choice; but if the employee opts for a costly method, such as cash or check, the employer can make payments on accounting day. This option will not harm either employees or employers relative to the status quo but will offer better choices to both.

V. THE DAY AFTER PAYDAY: CONCLUDING THOUGHTS

A complicated dynamic of dated legislation, path-dependence, and inefficient money technology has contributed to the economy-wide practice of paying employees in arrears. This dynamic puts employees in the absurd position of lending money to their employers. Payday lending and other short-term credit solutions draw oxygen from the continued existence of the payday.

Abolishing the payday might take time, as it will face resistance. No change is easy. However, the case for paying people for their work is too compelling to ignore. Paying employees late may be a legacy of the times of typewriters and cash chests carried by wagon to the worksite, but it can no longer be justified when effective payroll and money technologies exist. Many of the recent developments in Fintech suggest that the payday lives on borrowed time. It is perhaps time to call this loan.

[286] Barr, *supra* note 191, at 237 ("[N]etwork externalities in electronic payments systems and distribution networks suggest that net social benefit could be obtained through further expansion.")

[287] *See* Letter from Richard Cordray, Dir., CFPB, to Sen. Richard Blumenthal (Sept. 12, 2013), http://goo.gl/KOqFzB. CFPB Bulletin 2013-10: Payroll Accounts (Regulation E), CONSUMER FIN. PROTECTION BUREAU 1-2 (Sept. 12, 2013), http://goo.gl/98d8I6.

[288] N.Y. LAB. LAW § 191 (2018); *see also* N.Y. STATE DEP'T. OF LAB., OPINION LETTER RO-08-0001 (Oct. 29, 2009).