UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended August 31, 2010

Commission file number 0-11330

PAYCHEX, INC.

911 Panorama Trail South
Rochester, New York 14625-2396
(585) 385-6666
A Delaware Corporation

IRS Employer Identification Number: 16-1124166

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☑ No ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☑ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ☑	Accelerated filer ☐	Non-accelerated filer ☐ (Do not check if a smaller reporting company)	Smaller reporting company ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☑

The number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

Common Stock, $0.01 Par Value	361,670,988 Shares
CLASS	OUTSTANDING AS OF August 31, 2010

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

PAYCHEX, INC.
CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)
In millions, except per share amounts

	For the three months ended August 31, 2010	For the three months ended August 31, 2009
Revenue:		
Service revenue	$ 506.2	$ 486.5
Interest on funds held for clients	12.1	13.7
Total revenue	**518.3**	**500.2**
Expenses:		
Operating expenses	160.2	163.3
Selling, general and administrative expenses	157.3	147.0
Total expenses	**317.5**	**310.3**
Operating income	**200.8**	**189.9**
Investment income, net	1.4	0.9
Income before income taxes	**202.2**	**190.8**
Income taxes	70.3	67.2
Net income	**$ 131.9**	**$ 123.6**
Basic earnings per share	**$ 0.36**	**$ 0.34**
Diluted earnings per share	**$ 0.36**	**$ 0.34**
Weighted-average common shares outstanding	**361.6**	**361.2**
Weighted-average common shares outstanding, assuming dilution	**362.0**	**361.4**
Cash dividends per common share	**$ 0.31**	**$ 0.31**

See Notes to Consolidated Financial Statements.

PAYCHEX, INC.
CONSOLIDATED BALANCE SHEETS (UNAUDITED)
In millions, except per share amount

	August 31, 2010	May 31, 2010
ASSETS		
Cash and cash equivalents	$ 272.9	$ 284.3
Corporate investments	177.2	82.5
Interest receivable	22.8	28.7
Accounts receivable, net of allowance for doubtful accounts	208.6	186.6
Deferred income taxes	—	3.8
Prepaid income taxes	—	6.7
Prepaid expenses and other current assets	28.3	25.5
Current assets before funds held for clients	**709.8**	**618.1**
Funds held for clients	3,290.1	3,541.0
Total current assets	**3,999.9**	**4,159.1**
Long-term corporate investments	266.3	290.1
Property and equipment, net of accumulated depreciation	268.0	267.6
Intangible assets, net of accumulated amortization	58.4	63.3
Goodwill	421.6	421.6
Deferred income taxes	21.3	21.1
Other long-term assets	3.5	3.5
Total assets	**$ 5,039.0**	**$ 5,226.3**
LIABILITIES		
Accounts payable	$ 34.4	$ 37.3
Accrued compensation and related items	148.8	163.2
Deferred revenue	2.9	3.5
Accrued income taxes	54.8	—
Deferred income taxes	24.3	17.0
Other current liabilities	41.4	41.2
Current liabilities before client fund obligations	**306.6**	**262.2**
Client fund obligations	3,213.6	3,480.0
Total current liabilities	**3,520.2**	**3,742.2**
Accrued income taxes	27.9	27.4
Deferred income taxes	8.1	7.8
Other long-term liabilities	45.8	46.9
Total liabilities	**3,602.0**	**3,824.3**
COMMITMENTS AND CONTINGENCIES — NOTE H		
STOCKHOLDERS' EQUITY		
Common stock, $0.01 par value; Authorized: 600.0 shares; Issued and outstanding: 361.7 shares as of August 31, 2010 and 361.5 shares as of May 31, 2010, respectively.	3.6	3.6
Additional paid-in capital	506.2	499.7
Retained earnings	873.0	856.3
Accumulated other comprehensive income	54.2	42.4
Total stockholders' equity	**1,437.0**	**1,402.0**
Total liabilities and stockholders' equity	**$ 5,039.0**	**$ 5,226.3**

See Notes to Consolidated Financial Statements.

PAYCHEX, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
In millions

	For the three months ended August 31, 2010	2009
OPERATING ACTIVITIES		
Net income	$ 131.9	$ 123.6
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization on property and equipment and intangible assets	20.9	21.6
Amortization of premiums and discounts on available-for-sale securities	9.4	8.0
Stock-based compensation costs	7.1	6.7
Provision for deferred income taxes	3.6	4.2
Provision for allowance for doubtful accounts	0.2	1.0
Net realized gains on sales of available-for-sale securities	(0.1)	(0.3)
Changes in operating assets and liabilities:		
Interest receivable	5.9	4.5
Accounts receivable	(22.2)	(24.3)
Prepaid expenses and other current assets	3.9	1.6
Accounts payable and other current liabilities	33.8	41.3
Net change in other assets and liabilities	(0.1)	(1.3)
Net cash provided by operating activities	**194.3**	**186.6**
INVESTING ACTIVITIES		
Purchases of available-for-sale securities	(1,958.4)	(336.6)
Proceeds from sales and maturities of available-for-sale securities	1,549.8	175.2
Net change in funds held for clients' money market securities and other cash equivalents	598.3	423.1
Purchases of property and equipment	(16.6)	(10.1)
Purchases of other assets	(0.6)	(4.1)
Net cash provided by investing activities	**172.5**	**247.5**
FINANCING ACTIVITIES		
Net change in client fund obligations	(266.4)	(485.4)
Dividends paid	(112.0)	(112.1)
Proceeds from and excess tax benefit related to exercise of stock options	0.2	5.9
Net cash used in financing activities	**(378.2)**	**(591.6)**
Decrease in cash and cash equivalents	**(11.4)**	**(157.5)**
Cash and cash equivalents, beginning of period	284.3	472.8
Cash and cash equivalents, end of period	**$ 272.9**	**$ 315.3**

See Notes to Consolidated Financial Statements.

Note A: Description of Business and Significant Accounting Policies

Description of business: Paychex, Inc. and its wholly owned subsidiaries (collectively, the "Company" or "Paychex") is a leading provider of comprehensive payroll and integrated human resource and employee benefits outsourcing solutions for small- to medium-sized businesses in the United States ("U.S."). The Company also has a subsidiary in Germany.

Paychex, a Delaware corporation formed in 1979, reports as one segment. Substantially all of the Company's revenue is generated within the U.S. The Company also generates revenue within Germany, which was less than one percent of its total revenue for the three months ended August 31, 2010 and 2009. Long-lived assets in Germany are insignificant in relation to total long-lived assets of the Company as of August 31, 2010 and May 31, 2010.

Basis of presentation: The accompanying consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP") for interim financial information and with the instructions to the Quarterly Report on Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statement presentation. The consolidated financial statements include the consolidated accounts of the Company with all significant intercompany transactions eliminated. In the opinion of management, the information furnished herein reflects all adjustments (consisting of items of a normal recurring nature), which are necessary for a fair presentation of the results for the interim period. These financial statements should be read in conjunction with the Company's consolidated financial statements and related Notes to Consolidated Financial Statements presented in the Company's Annual Report on Form 10-K as of and for the year ended May 31, 2010 ("fiscal 2010"). Operating results and cash flows for the three months ended August 31, 2010 are not necessarily indicative of the results that may be expected for other interim periods or the full fiscal year ending May 31, 2011 ("fiscal 2011"). The Company has evaluated subsequent events for potential recognition and/or disclosure through the date of issuance of these financial statements.

PEO revenue recognition: Professional Employer Organization ("PEO") revenue is included in service revenue and is reported net of direct costs billed and incurred which include wages, taxes, benefit premiums, and claims of PEO worksite employees. Direct costs billed and incurred were $950.9 million and $708.4 million for the three months ended August 31, 2010, and 2009, respectively.

PEO workers' compensation insurance: Workers' compensation insurance for PEO worksite employees is provided under a deductible workers' compensation policy with a national insurance company. Reserves are established to provide for the estimated costs of paying claims underwritten by the Company. The Company's maximum individual claims liability is $1.0 million under both its fiscal 2011 and fiscal 2010 policies. As of August 31, 2010 and May 31, 2010, the Company had current liabilities of $6.8 million and $5.8 million, respectively, and long-term liabilities of $18.8 million and $20.1 million, respectively, on its Consolidated Balance Sheets.

Note A: Description of Business and Significant Accounting Policies — *continued*

Estimating the ultimate cost of future claims is an uncertain and complex process based upon historical loss experience and actuarial loss projections, and is subject to change due to multiple factors, including economic trends, changes in legal liability law, and damage awards, all of which could materially impact the reserves as reported. Adjustments to previously established reserves are reflected in the results of operations for the period in which the adjustment is identified. Such adjustments could possibly be significant, reflecting any variety of new and adverse or favorable trends.

Stock-based compensation costs: The Company has issued stock-based awards to employees and directors consisting of stock options, restricted stock awards, restricted stock units ("RSUs"), and performance shares. The Company accounts for all stock-based awards to employees and directors as compensation costs in the consolidated financial statements based on the fair value measured as of the date of grant. These costs are recognized as an expense in the Consolidated Statements of Income over the requisite service period and increase additional paid-in capital. Stock-based compensation costs recognized were $7.1 million for the three months ended August 31, 2010, compared to $6.7 million for the respective prior year period. As of August 31, 2010, the total unrecognized compensation cost related to all unvested stock-based awards was $56.5 million and is expected to be recognized over a weighted-average period of 3.0 years.

The fair value of restricted stock awards is equal to the closing market price of the underlying common stock as of the date of grant. The fair value of RSUs is equal to the closing market price of the underlying common stock as of the date of grant, adjusted for the present value of expected dividends over the vesting period, as these awards do not earn dividend equivalents. The fair value of performance shares is equal to the closing market price as of the measurement date, adjusted for the present value of the expected dividends over the performance period.

The fair value of stock option grants is estimated as of the date of grant using a Black-Scholes option pricing model. The weighted-average assumptions used for valuation under the Black-Scholes model were as follows:

	For the three months ended August 31,	
	2010	2009
Risk-free interest rate	2.5%	3.0%
Dividend yield	4.2%	4.5%
Volatility factor	.24	.28
Expected option life in years	6.5	6.4

Risk-free interest rates are yields for zero-coupon U.S. Treasury notes maturing approximately at the end of the expected option life. The estimated volatility factor is based on a combination of historical volatility, using weekly stock prices over a period equal to the expected option life, and implied market volatility. The expected option life is based on historical exercise behavior.

Note A: Description of Business and Significant Accounting Policies — *continued*

The Company has determined that the Black-Scholes option pricing model, as well as the underlying assumptions used in its application, is appropriate in estimating the fair value of its stock option grants. The Company periodically assesses its assumptions as well as its choice of valuation model, and will reconsider use of this model if additional information becomes available in the future indicating that another model would provide a more accurate estimate of fair value, or if characteristics of future grants would warrant such a change.

Recently adopted accounting pronouncements: Effective June 1, 2010, the Company adopted the following Financial Accounting Standards Board ("FASB") authoritative guidance, neither of which had a material impact on its consolidated financial statements:

- Guidance amending the accounting and reporting standards for transfers and servicing of financial assets, including the removal of the concept of a qualifying special purpose entity; and
- Guidance to require a qualitative analysis rather than a quantitative-based risks and rewards calculation to determine the primary beneficiary of a variable interest entity ("VIE") for consolidation purposes. This qualitative approach focuses on identifying which entity has the power to direct the activities of a VIE with the most significant impact on the VIE's economic performance.

Recently issued accounting pronouncements: Recent authoritative guidance issued by the FASB (including technical corrections to the Codification), the American Institute of Certified Public Accountants, and the Securities and Exchange Commission did not, or are not expected to have a material effect on the Company's consolidated financial statements.

Note B: Basic and Diluted Earnings Per Share

Basic and diluted earnings per share were calculated as follows:

In millions, except per share amounts	For the three months ended August 31, 2010	2009
Basic earnings per share:		
Net income	$ 131.9	$ 123.6
Weighted-average common shares outstanding	361.6	361.2
Basic earnings per share	$ 0.36	$ 0.34
Diluted earnings per share:		
Net income	$ 131.9	$ 123.6
Weighted-average common shares outstanding	361.6	361.2
Dilutive effect of common share equivalents at average market price	0.4	0.2
Weighted-average common shares outstanding, assuming dilution	362.0	361.4
Diluted earnings per share	$ 0.36	$ 0.34
Weighted-average anti-dilutive common share equivalents	14.2	14.6

Weighted-average common share equivalents that have an anti-dilutive impact are excluded from the computation of diluted earnings per share.

For the three months ended August 31, 2010, 0.2 million shares of the Company's common stock were issued for stock option exercises and vesting of restricted stock and RSUs, compared with 0.5 million shares for the three months ended August 31, 2009.

Note C: Funds Held for Clients and Corporate Investments

Funds held for clients and corporate investments consisted of the following:

	August 31, 2010			
In millions	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
Type of issue:				
Money market securities and other cash equivalents	$ 1,156.3	$ —	$ —	$ 1,156.3
Available-for-sale securities:				
General obligation municipal bonds	1,021.2	46.2	—	1,067.4
Pre-refunded municipal bonds(1)	503.8	21.5	—	525.3
Revenue municipal bonds	354.0	17.4	—	371.4
Variable rate demand notes	605.6	—	—	605.6
Total available-for-sale securities	2,484.6	85.1	—	2,569.7
Other	7.9	0.1	(0.4)	7.6
Total funds held for clients and corporate investments	$ 3,648.8	$ 85.2	$ (0.4)	$ 3,733.6

	May 31, 2010			
In millions	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
Type of issue:				
Money market securities and other cash equivalents	$ 1,754.5	$ —	$ —	$ 1,754.5
Available-for-sale securities:				
General obligation municipal bonds	951.1	33.7	(0.3)	984.5
Pre-refunded municipal bonds(1)	539.8	19.5	—	559.3
Revenue municipal bonds	368.0	13.8	(0.1)	381.7
Variable rate demand notes	226.3	—	—	226.3
Total available-for-sale securities	2,085.2	67.0	(0.4)	2,151.8
Other	7.5	—	(0.2)	7.3
Total funds held for clients and corporate investments	$ 3,847.2	$ 67.0	$ (0.6)	$ 3,913.6

(1) Pre-refunded municipal bonds are secured by an escrow fund of U.S. government obligations.

Note C: Funds Held for Clients and Corporate Investments — ***continued***

Included in money market securities and other cash equivalents as of August 31, 2010 and May 31, 2010 are U.S. agency discount notes, government money market funds, and bank demand deposit accounts.

Classification of investments on the Consolidated Balance Sheets is as follows:

In millions	August 31, 2010	May 31, 2010
Funds held for clients	$ 3,290.1	$ 3,541.0
Corporate investments	177.2	82.5
Long-term corporate investments	266.3	290.1
Total funds held for clients and corporate investments	$ 3,733.6	$ 3,913.6

The Company is exposed to credit risk in connection with these investments through the possible inability of borrowers to meet the terms of their bonds. In addition, the Company is exposed to interest rate risk, as rate volatility will cause fluctuations in the fair value of held investments and in the earnings potential of future investments. The Company follows a conservative investment strategy of optimizing liquidity and protecting principal. The Company invests primarily in high credit quality securities with AAA and AA ratings and short-term securities with A-1/P-1 ratings. The Company limits the amounts that can be invested in any single issuer and invests in short- to intermediate-term instruments whose fair value is less sensitive to interest rate changes. All the investments held as of August 31, 2010 are traded in active markets. The Company has not and does not utilize derivative financial instruments to manage interest rate risk.

The Company's available-for-sale securities reflected a net unrealized gain of $85.1 million as of August 31, 2010 compared with a net unrealized gain of $66.6 million as of May 31, 2010. There were no securities held as of August 31, 2010 that were in an unrealized loss position. As of May 31, 2010, there were 23 available-for-sale securities in an unrealized loss position as follows:

	Less than 12 months		More than 12 months		Total	
In millions	Gross unrealized loss	Fair value	Gross unrealized loss	Fair value	Gross unrealized loss	Fair value
Type of issue:						
General obligation municipal bonds	$ (0.3)	$ 44.0	$ —	$ —	$ (0.3)	$ 44.0
Pre-refunded municipal bonds	—	4.1	—	—	—	4.1
Revenue municipal bonds	(0.1)	25.5	—	—	(0.1)	25.5
Total	$ (0.4)	$ 73.6	$ —	$ —	$ (0.4)	$ 73.6

Note C: Funds Held for Clients and Corporate Investments — ***continued***

The Company regularly reviews its investment portfolios to determine if any investment is other-than-temporarily impaired due to changes in credit risk or other potential valuation concerns. The Company believes that the investments it held as of August 31, 2010 were not other-than-temporarily impaired, as none of the securities held had fair values that were below amortized cost. All of the securities in an unrealized loss position as of May 31, 2010 held an AA rating or better. The Company's assessment that an investment is not other-than-temporarily impaired could change in the future due to new developments or changes in the Company's strategies or assumptions related to any particular investment.

Realized gains and losses on the sales of securities are determined by specific identification of the amortized cost basis of each security. On the Consolidated Statements of Income, realized gains and losses from funds held for clients are included in interest on funds held for clients and realized gains and losses from corporate investments are included in investment income, net. Realized gains and losses were as follows:

In millions	For the three months ended August 31, 2010	For the three months ended August 31, 2009
Gross realized gains	$ 0.1	$ 0.3
Gross realized losses	—	—
Net realized gains	$ 0.1	$ 0.3

The amortized cost and fair value of available-for-sale securities that had stated maturities as of August 31, 2010 are shown below by contractual maturity. Expected maturities can differ from contractual maturities because borrowers may have the right to prepay obligations without prepayment penalties.

In millions	August 31, 2010 Amortized cost	August 31, 2010 Fair value
Maturity date:		
Due in one year or less	$ 391.2	$ 395.9
Due after one year through three years	750.2	785.1
Due after three years through five years	456.6	484.1
Due after five years	886.6	904.6
Total	$ 2,484.6	$ 2,569.7

Variable rate demand notes ("VRDNs") are primarily categorized as due after five years in the table above as the contractual maturities on these securities are typically 20 to 30 years. Although these securities are issued as long-term securities, they are priced and traded as short-term instruments because of the liquidity provided through the tender feature.

Note D: Fair Value Measurements

The carrying values of cash and cash equivalents, accounts receivable, net of allowance for doubtful accounts, and accounts payable approximate fair value due to the short maturities of these instruments. Marketable securities included in funds held for clients and corporate investments consist primarily of securities classified as available-for-sale and are recorded at fair value on a recurring basis.

The accounting standards related to fair value measurements include a hierarchy for information and valuations used in measuring fair value that is broken down into three levels based on reliability, as follows:

- Level 1 valuations are based on quoted prices in active markets for identical instruments that the Company has the ability to access.
- Level 2 valuations are based on quoted prices for similar, but not identical, instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; or other significant observable inputs besides quoted prices.
- Level 3 valuations are based on information that is unobservable and significant to the overall fair value measurement.

The Company's financial assets and liabilities measured at fair value on a recurring basis were as follows:

	August 31, 2010			
In millions	**Carrying value (Fair value)**	**Quoted prices in active markets (Level 1)**	**Significant other observable inputs (Level 2)**	**Significant unobservable inputs (Level 3)**
Assets:				
Available-for-sale securities:				
General obligation municipal bonds	$ 1,067.4	$ —	$ 1,067.4	$ —
Pre-refunded municipal bonds	525.3	—	525.3	—
Revenue municipal bonds	371.4	—	371.4	—
Variable rate demand notes	605.6	—	605.6	—
Total available-for-sale securities	$ 2,569.7	$ —	$ 2,569.7	$ —
Other securities	$ 7.6	$ 7.6	$ —	$ —
Liabilities:				
Other long-term liabilities	$ 7.6	$ 7.6	$ —	$ —

Note D: Fair Value Measurements — ***continued***

	May 31, 2010			
In millions	**Carrying value (Fair value)**	**Quoted prices in active markets (Level 1)**	**Significant other observable inputs (Level 2)**	**Significant unobservable inputs (Level 3)**
Assets:				
Available-for-sale securities:				
General obligation municipal bonds	$ 984.5	$ —	$ 984.5	$ —
Pre-refunded municipal bonds	559.3	—	559.3	—
Revenue municipal bonds	381.7	—	381.7	—
Variable rate demand notes	226.3	—	226.3	—
Total available-for-sale securities	$ 2,151.8	$ —	$ 2,151.8	$ —
Other securities	$ 7.3	$ 7.3	$ —	$ —
Liabilities:				
Other long-term liabilities	$ 7.3	$ 7.3	$ —	$ —

In determining the fair value of its assets and liabilities, the Company predominately uses the market approach. In determining the fair value of its available-for-sale securities, the Company utilizes the Interactive Data Pricing service. Other securities are comprised of mutual fund investments, which are valued based on quoted market prices. Other long-term liabilities include the liability for the Company's non-qualified and unfunded deferred compensation plans, and are valued based on the quoted market prices for various mutual fund investment choices.

The preceding methods described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although the Company believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

Note E: Property and Equipment, Net of Accumulated Depreciation

The components of property and equipment, at cost, consisted of the following:

In millions	August 31, 2010	May 31, 2010
Land and improvements	$ 4.2	$ 4.2
Buildings and improvements	85.6	84.1
Data processing equipment	190.4	186.8
Software	186.2	178.8
Furniture, fixtures, and equipment	147.0	147.1
Leasehold improvements	91.8	91.4
Construction in progress	17.1	17.9
Total property and equipment, gross	722.3	710.3
Less: Accumulated depreciation and amortization	454.3	442.7
Property and equipment, net of accumulated depreciation	$ 268.0	$ 267.6

Depreciation expense was $16.2 million and $16.4 million for the three months ended August 31, 2010 and 2009, respectively.

Note F: Goodwill and Intangible Assets, Net of Accumulated Amortization

The Company had goodwill balances on its Consolidated Balance Sheets of $421.6 million as of both August 31, 2010 and May 31, 2010.

The Company has certain intangible assets with finite lives. The components of intangible assets, at cost, consisted of the following:

In millions	August 31, 2010	May 31, 2010
Client lists	$ 195.0	$ 194.4
Other intangible assets	4.9	4.9
Total intangible assets, gross	199.9	199.3
Less: Accumulated amortization	141.5	136.0
Intangible assets, net of accumulated amortization	$ 58.4	$ 63.3

Amortization expense relating to intangible assets was $4.7 million and $5.2 million for the three months ended August 31, 2010 and 2009, respectively.

As of August 31, 2010, the estimated amortization expense relating to intangible asset balances for the full fiscal year 2011 and the following four fiscal years is as follows:

In millions	Estimated amortization expense
Fiscal year ending May 31,	
2011	$ 19.3
2012	$ 16.3
2013	$ 11.5
2014	$ 7.3
2015	$ 4.7

Note G: Comprehensive Income

Comprehensive income is comprised of two components: net income and other comprehensive income. Comprehensive income includes all changes in equity during a period except those resulting from transactions with owners of the Company. The change in unrealized gains and losses, net of applicable taxes, related to available-for-sale securities is the primary component reported in accumulated other comprehensive income in the Consolidated Balance Sheets.

Comprehensive income, net of related tax effects, is as follows:

In millions	For the three months ended August 31, 2010	2009
Net income	$ 131.9	$ 123.6
Other comprehensive income:		
Unrealized gains on available-for-sale securities, net of taxes	11.9	1.5
Reclassification adjustment for the net gain on sale of available-for-sale securities realized in net income, net of tax	(0.1)	(0.2)
Total other comprehensive income	11.8	1.3
Total comprehensive income	$ 143.7	$ 124.9

As of August 31, 2010, accumulated other comprehensive income was $54.2 million, which was net of taxes of $30.8 million. As of May 31, 2010, accumulated other comprehensive income was $42.4 million, which was net of taxes of $24.1 million.

Note H: Commitments and Contingencies

Lines of credit: As of August 31, 2010, the Company had unused borrowing capacity available under four uncommitted, secured, short-term lines of credit at market rates of interest with financial institutions as follows:

Financial institution	Amount available	Expiration date
JP Morgan Chase Bank, N.A.	$350 million	February 2011
Bank of America, N.A.	$250 million	February 2011
PNC Bank, National Association	$150 million	February 2011
Wells Fargo Bank, National Association	$150 million	February 2011

The primary uses of the lines of credit would be to meet short-term funding requirements related to deposit account overdrafts and client fund obligations arising from electronic payment transactions on behalf of clients in the ordinary course of business, if necessary. No amounts were outstanding against these lines of credit as of, or during the three months ended, August 31, 2010.

JP Morgan Chase Bank, N.A. and Bank of America, N.A. are also parties to the Company's irrevocable standby letters of credit, which arrangements are discussed next.

Note H: Commitments and Contingencies — *continued*

Letters of credit: As of August 31, 2010, the Company also had irrevocable standby letters of credit available totaling $47.5 million required to secure commitments for certain insurance policies. The letters of credit expire at various dates between December 2010 and July 2011, and are collateralized by securities held in the Company's investment portfolios. No amounts were outstanding on these letters of credit as of, or during the three months ended, August 31, 2010.

Other commitments: The Company enters into various purchase commitments with vendors in the ordinary course of business. The Company had outstanding commitments to purchase approximately $9.6 million and $8.9 million of capital assets as of August 31, 2010 and May 31, 2010, respectively.

The Company guarantees performance of service on annual maintenance contracts for clients who financed their service contracts through a third party. In the normal course of business, the Company makes representations and warranties that guarantee the performance of its services under service arrangements with clients. Historically, there have been no material losses related to such guarantees. In addition, the Company has entered into indemnification agreements with its officers and directors, which require it to defend and, if necessary, indemnify these individuals for certain pending or future claims as they relate to their services provided to the Company.

Paychex currently self-insures the deductible portion of various insured exposures under certain employee benefit plans. The Company's estimated loss exposure under these insurance arrangements is recorded in other current liabilities on the Consolidated Balance Sheets. Historically, the amounts accrued have not been material. The Company also maintains insurance coverage in addition to its purchased primary insurance policies for gap coverage for employment practices liability, errors and omissions, warranty liability, and acts of terrorism; and capacity for deductibles and self-insured retentions through its captive insurance company.

Contingencies: The Company is subject to various claims and legal matters that arise in the normal course of business. These include disputes or potential disputes related to breach of contract, breach of fiduciary duty, employment-related claims, tax claims, and other matters.

The Company's management currently believes that resolution of any outstanding legal matters will not have a material adverse effect on the Company's financial position or results of operations. However, legal matters are subject to inherent uncertainties and there exists the possibility that the ultimate resolution of these matters could have a material adverse impact on the Company's financial position and results of operations in the period in which any such effect is recorded.

Note I: Related Party Transactions

During the three months ended August 31, 2010 and 2009, the Company purchased approximately $0.8 million and $1.5 million of data processing equipment and software from EMC Corporation. The Chairman, President, and Chief Executive Officer of EMC Corporation is a member of the Company's Board of Directors (the "Board").

During both the three months ended August 31, 2010 and 2009, the Company purchased approximately $0.4 million of services from Dun & Bradstreet Corporation. Jonathan J. Judge, the Company's former President and Chief Executive Officer, and a current member of the Company's Board, is a member of the Board of Directors of Dun & Bradstreet Corporation.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Management's Discussion and Analysis of Financial Condition and Results of Operations reviews the operating results of Paychex, Inc. and its wholly owned subsidiaries ("we," "our," or "us") for the three months ended August 31, 2010 (the "first quarter") and August 31, 2009, and our financial condition as of August 31, 2010. The focus of this review is on the underlying business reasons for significant changes and trends affecting our revenue, expenses, net income, and financial condition. This review should be read in conjunction with the August 31, 2010 Consolidated Financial Statements and the related Notes to Consolidated Financial Statements contained in this Quarterly Report on Form 10-Q ("Form 10-Q"). This review should also be read in conjunction with our Annual Report on Form 10-K ("Form 10-K") for the year ended May 31, 2010 ("fiscal 2010"). Forward-looking statements in this review are qualified by the cautionary statement included in this review under the next sub-heading, "Safe-Harbor Statement under the Private Securities Litigation Reform Act of 1995."

"Safe Harbor" Statement Under the Private Securities Litigation Reform Act of 1995: Certain written and oral statements made by us may constitute "forward-looking statements" as defined in the Private Securities Litigation Reform Act of 1995 (the "Reform Act"). Forward-looking statements are identified by such words and phrases as "we expect," "expected to," "estimates," "estimated," "current outlook," "we look forward to," "would equate to," "projects," "projections," "projected to be," "anticipates," "anticipated," "we believe," "could be," and other similar phrases. All statements addressing operating performance, events, or developments that we expect or anticipate will occur in the future, including statements relating to revenue growth, earnings, earnings-per-share growth, or similar projections, are forward-looking statements within the meaning of the Reform Act. Because they are forward-looking, they should be evaluated in light of important risk factors. These risk factors include, but are not limited to, the following risks as well as those described in our periodic filings with the Securities and Exchange Commission ("SEC"):

- general market and economic conditions including, among others, changes in United States ("U.S.") employment and wage levels, changes in new hiring trends, legislative changes to stimulate the economy, changes in short- and long-term interest rates, changes in the fair value and the credit rating of securities held by us, and accessibility of financing;
- changes in demand for our services and products, ability to develop and market new services and products effectively, pricing changes and the impact of competition, and the availability of skilled workers;
- changes in the laws regulating collection and payment of payroll taxes, professional employer organizations, and employee benefits, including retirement plans, workers' compensation, health insurance, state unemployment, and section 125 plans;
- changes in workers' compensation rates and underlying claims trends;
- the possibility of failure to keep pace with technological changes and provide timely enhancements to services and products;
- the possibility of failure of our operating facilities, computer systems, and communication systems during a catastrophic event;
- the possibility of third-party service providers failing to perform their functions;

- the possible failure of internal controls or our inability to implement business processing improvements; and
- potentially unfavorable outcomes related to pending legal matters.

Any of these factors could cause our actual results to differ materially from our anticipated results. The information provided in this Form 10-Q is based upon the facts and circumstances known at this time. We undertake no obligation to update these forward-looking statements after the date of filing of this Form 10-Q with the SEC to reflect events or circumstances after such date, or to reflect the occurrence of unanticipated events.

Business

We are a leading provider of payroll, human resource, and benefits outsourcing solutions for small- to medium-sized businesses. Our business strategy is focused on achieving strong long-term financial performance by providing high quality, timely, accurate, and affordable services; growing our client base; continually improving client service to maximize client retention; increasing utilization of our ancillary services; leveraging our technological and operating infrastructure; and expanding our service and product offerings to continually add value for our clients.

We offer a comprehensive portfolio of services and products that allow our clients to meet their diverse payroll and human resource needs. Our payroll services are the foundation of our service portfolio. They are provided through either our core payroll or Major Market Services (“MMS”), which is utilized by clients that have more sophisticated payroll and benefit needs. In addition to the services described below, our software-as-a-service solution through the MMS platform provides human resource management, employee benefits management, time and attendance systems, online expense reporting, and applicant tracking. Our services and products are as follows:

Service	Description
Payroll:	
Payroll processing	Includes the calculation, preparation, and delivery of employee payroll checks; production of internal accounting records and management reports; preparation of federal, state, and local payroll tax returns; and collection and remittance of clients’ payroll obligations.
Payroll tax administration services	Provides accurate preparation and timely filing of quarterly and year-end tax returns, as well as the electronic transfer of funds to the applicable federal, state, and local tax or regulatory agencies.
Employee payment services	Provides the employer the option of paying their employees by direct deposit, payroll debit card, a check drawn on a Paychex, Inc. account (Readychex®), or a check drawn on the employer’s account and electronically signed by us.
Regulatory compliance services	Includes new-hire reporting and garnishment processing, which allow employers to comply with legal requirements and reduce the risk of penalties.

Service	Description
Human Resource Services:	
Paychex HR Solutions	Is available as an administrative services organization (“ASO”) and a professional employer organization (“PEO”). Both offer a package that includes payroll and compliance, human resource and employee benefits administration, risk management outsourcing, and the on-site availability of a professionally trained human resource representative, among other services. Our PEO differs from the ASO in that we serve as co-employer of the clients’ employees, assume the risks and rewards of workers’ compensation insurance, and provide more sophisticated health care offerings to PEO clients.
Retirement services administration	Offers a variety of retirement plan options to employers, as well as recordkeeping services, which include plan implementation, ongoing compliance with government regulations, employee and employer reporting, participant and employer access online, electronic funds transfer, and other administrative services.
Insurance services	Our licensed insurance agency, Paychex Insurance Agency, Inc., provides insurance through a variety of carriers. Insurance offerings include property and casualty coverage, such as workers’ compensation; business-owner policies; commercial auto; and health and benefits coverage, including health, dental, vision, and life.
eServices	Offers online software products for employee benefits management and administration and time and attendance solutions.
Other human resource services and products	Includes section 125 plans, state unemployment insurance services, employee handbooks, management manuals, and personnel and required regulatory forms.

Overview

Our financial results for the first quarter of the fiscal year ending May 31, 2011 (“fiscal 2011”) reflected year-over-year growth. Checks per client increased 1.2% for the first quarter of fiscal 2011 compared to the same period last year, whereas for the first quarter of fiscal 2010 checks per client had declined 5.0% year over year. Checks per client for the fiscal fourth quarter ended May 31, 2010 had increased 1.1%.

Our financial results continue to be adversely impacted by the interest rate environment. The equity markets hit a low in March 2009, with interest rates available on high-quality instruments remaining low since then. The Federal Funds rate has been at a range of zero to 0.25% since December 2008. Our combined funds held for clients and corporate investment portfolios earned an average rate of return of 1.5% for the first quarter of fiscal 2011 compared to 1.7% for the same period last year.

Our operating income, net of certain items, as a percent of service revenue was 37.3% for the first quarter, up from 36.2% for the same period last year. We continue to manage our expenses while still investing in our business, particularly in areas related to selling and servicing our clients and the technological infrastructure to support these areas. These investments are critical to our success. Looking to the future, we continue to focus on investing in our products, people, and service capabilities, positioning us to capitalize on opportunities for long-term growth.

Highlights of the financial results for the first quarter as compared to the same period last year are as follows:

- Payroll service revenue increased 2% to $360.7 million.
- Human Resource Services revenue increased 10% to $145.5 million.
- Interest on funds held for clients decreased 12% to $12.1 million.
- Total revenue increased 4% to $518.3 million.
- Operating income increased 6% to $200.8 million and operating income, net of certain items, increased 7% to $188.7 million. Refer to the "Non-GAAP Financial Measure" section below for further information on this non-GAAP measure.
- Net income increased 7% to $131.9 million and diluted earnings per share increased 6% to $0.36 per share.
- Cash flow from operations increased 4% to $194.3 million.

Non-GAAP Financial Measure

In addition to reporting operating income, a U.S. generally accepted accounting principle ("GAAP") measure, we present operating income, net of certain items, which is a non-GAAP measure. We believe operating income, net of certain items, is an appropriate additional measure, as it is an indicator of our core business operations performance period over period. It is also the measure used internally for establishing the following year's targets and measuring management's performance in connection with certain performance-based compensation payments and awards. Operating income, net of certain items, excludes interest on funds held for clients. Interest on funds held for clients is an adjustment to operating income due to the volatility of interest rates which are not within the control of management. Operating income, net of certain items, is not calculated through the application of GAAP and is not the required form of disclosure by the SEC. As such, it should not be considered as a substitute for the GAAP measure of operating income and, therefore, should not be used in isolation, but in conjunction with the GAAP measure. The use of any non-GAAP measure may produce results that vary from the GAAP measure and may not be comparable to a similarly defined non-GAAP measure used by other companies. Operating income, net of certain items, increased 7% to $188.7 million for the three months ended August 31, 2010 as compared to the same period last year. Refer to the reconciliation of operating income to operating income, net of certain items, in the "Results of Operations" section of this Form 10-Q.

Financial Position and Liquidity

The current credit crisis has resulted in unprecedented volatility in the global financial markets, which has curtailed available liquidity and limited investment choices. Despite this macroeconomic environment, as of August 31, 2010, our financial position remained strong with cash and total corporate investments of $716.4 million and no debt.

We continue to follow our conservative investment strategy of optimizing liquidity and protecting principal. During the past two years, this has translated to significantly lower yields on high quality instruments, negatively impacting our income earned on funds held for clients and corporate investments. We invest predominantly in municipal bonds — general obligation bonds; pre-refunded bonds, which are secured by a U.S. government escrow; and essential services revenue bonds. During the first quarter of fiscal 2010, our primary short-term investment vehicle was U.S. agency discount notes. Starting in November 2009, we began to invest in select A-1/P-1-rated variable rate demand notes ("VRDNs"). We have gradually increased our investments in VRDNs to $605.6 million as of August 31, 2010, up from $226.3 million as of May 31, 2010. During the first quarter, we earned an after-tax rate of approximately 0.22% on VRDNs compared to approximately 0.08% on U.S. agency discount notes.

We invest primarily in high credit quality securities with AAA and AA ratings and short-term securities with A-1/P-1 ratings, with more than 95% of our portfolio rated AA or better. We limit the amounts that can be invested in any single issuer and invest in short-to intermediate-term instruments whose fair value is less sensitive to interest rate changes. We believe that our investments as of August 31, 2010 were not other-than-temporarily impaired, nor has any event occurred subsequent to that date that would indicate any other-than-temporary impairment. All investments held as of August 31, 2010 are traded in active markets.

Our primary source of cash is our ongoing operations. Cash flow from operations was $194.3 million for the first quarter of fiscal 2011. Historically, we have funded our operations, capital purchases, and dividend payments from our operating activities. Our positive cash flows have allowed us to support our business and to pay substantial dividends to our stockholders. It is anticipated that cash and total corporate investments as of August 31, 2010, along with projected operating cash flows, will support our normal business operations, capital purchases, and dividend payments for the foreseeable future.

For further analysis of our results of operations for the first quarter and our financial position as of August 31, 2010, refer to the analysis and discussion in the "Results of Operations" and "Liquidity and Capital Resources" sections of this Form 10-Q.

Outlook

Our outlook for fiscal 2011 is based upon current economic and interest rate conditions continuing with no significant changes. Consistent with our policy regarding guidance, our projections do not anticipate or speculate on future changes to interest rates. Although our first quarter results were slightly better than anticipated, we remain cautiously optimistic about the economic recovery and will watch how fiscal 2011 evolves before determining if we should revise the fiscal 2011 guidance issued in June 2010. Our guidance at that time was as follows:

- We project that payroll service revenue for fiscal 2011 will be flat compared to fiscal 2010. Human Resource Services revenue is anticipated to increase in the range of 10% to 13%. Interest on funds held for clients is expected to decrease in the range of 12% to 17%, while investment income, net is expected to increase in the range of 24% to 27%.

- Operating income, net of certain items, as a percentage of service revenue is expected to range from 34% to 35% for fiscal 2011. The effective income tax rate is expected to approximate 35% for fiscal 2011. Net income is expected to improve slightly over fiscal 2010.

Interest on funds held for clients and investment income for fiscal 2011 are expected to be impacted by the low interest rate environment. The average rate of return on our combined funds held for clients and corporate investment portfolios is expected to be 1.4% for fiscal 2011. As of August 31, 2010, the long-term investment portfolio, which excludes VRDNs, had an average yield-to-maturity of 2.8% and an average duration of 2.5 years. In the next twelve months, slightly over 20% of this portfolio will mature, and it is currently anticipated that these proceeds will be reinvested at a lower average interest rate of approximately 1.0%. Investment income is expected to benefit from ongoing investment of cash generated from operations.

Under normal financial market conditions, the impact to our earnings from a 25-basis-point increase or decrease in short-term interest rates would be approximately $3.5 million, after taxes, for a twelve-month period. Such a basis point change may or may not be tied to changes in the Federal Funds rate.

Purchases of property and equipment for fiscal 2011, revised for infrastructure investments, are expected to be in the range of $90 million to $95 million, as we continue to invest in technology and infrastructure. Fiscal 2011 depreciation expense is projected to be in the range of $65 million to $70 million, and we project amortization of intangible assets for fiscal 2011 to be approximately $20 million.

RESULTS OF OPERATIONS

Summary of Results of Operations:

$ in millions	For the three months ended August 31, 2010	2009	Change
Revenue:			
Payroll service revenue	$ 360.7	$ 354.4	2%
Human Resource Services revenue	145.5	132.1	10%
Total service revenue	506.2	486.5	4%
Interest on funds held for clients	12.1	13.7	(12%)
Total revenue	**518.3**	**500.2**	**4%**
Combined operating and SG&A expenses	317.5	310.3	2%
Operating income	**200.8**	**189.9**	**6%**
As a % of total revenue	39%	38%	
Investment income, net	1.4	0.9	57%
Income before income taxes	**202.2**	**190.8**	**6%**
As a % of total revenue	39%	38%	
Income taxes	70.3	67.2	5%
Effective income tax rate	34.8%	35.2%	
Net income	**$ 131.9**	**$ 123.6**	**7%**
As a % of total revenue	25%	25%	
Diluted earnings per share	**$ 0.36**	**$ 0.34**	**6%**

We invest in highly liquid, investment-grade fixed income securities and do not utilize derivative instruments to manage interest rate risk. As of August 31, 2010, we had no exposure to high-risk or illiquid investments. Details regarding our combined funds held for clients and corporate investment portfolios are as follows:

$ in millions	For the three months ended August 31, 2010	2009	Change
Average investment balances:			
Funds held for clients	$ 2,949.1	$ 2,907.2	1%
Corporate investments	665.7	618.4	8%
Total	$ 3,614.8	$ 3,525.6	3%
Average interest rates earned (exclusive of net realized gains):			
Funds held for clients	1.6%	1.8%	
Corporate investments	0.9%	0.7%	
Combined funds held for clients and corporate investments	1.5%	1.7%	
Net realized gains:			
Funds held for clients	$ 0.1	$ 0.3	
Corporate investments	—	—	
Total	$ 0.1	$ 0.3	

As of: $ in millions	August 31, 2010	May 31, 2010
Net unrealized gain on available-for-sale securities(1)	$ 85.1	$ 66.6
Federal Funds rate (2)	0.25%	0.25%
Three-year "AAA" municipal securities yield	0.48%	0.99%
Total fair value of available-for-sale securities	$ 2,569.7	$ 2,151.8
Weighted-average duration of available-for-sale securities in years(3)	2.5	2.5
Weighted-average yield-to-maturity of available-for-sale securities(3)	2.8%	2.9%

(1) The net unrealized gain of our investment portfolio was approximately $77.3 million as of September 22, 2010.

(2) The Federal Funds rate was a range of 0% to 0.25% as of August 31, 2010 and May 31, 2010.

(3) These items exclude the impact of VRDNs as they are tied to short-term interest rates.

Payroll service revenue: Payroll service revenue increased 2% to $360.7 million for the first quarter compared to the same period last year. Positively contributing to payroll service revenue was an increase in checks per client of 1.2% for the first quarter and annual price increases. Client retention reflected improvement as client losses decreased 12% for the first quarter compared to the prior year period. New client sales were down slightly for the first quarter compared to the same period last year.

Our payroll tax administration services were utilized by 94% of all clients as of August 31, 2010 compared with 93% as of August 31, 2009. Our employee payment services were utilized by 77% of all clients as of August 31, 2010, compared with 75% as of August 31, 2009.

Human Resource Services revenue: Human Resource Services revenue increased 10% to $145.5 million for the first quarter compared to the same period last year. Human Resource Services revenue growth was impacted by the sale of Stromberg time and attendance operations ("Stromberg") in October 2009. Excluding Stromberg, Human Resource Services revenue would have increased 13% for the first quarter. This growth was generated from the following:

As of: $ in billions	August 31, 2010	Change	August 31, 2009	Change(1)
Paychex HR Solutions client employees served	522,000	13%	463,000	4%
Paychex HR Solutions clients	20,000	8%	18,000	10%
Insurance services clients (2)	94,000	7%	88,000	8%
Retirement services clients	51,000	4%	49,000	1%
Asset value of retirement services client employees' funds	$ 11.5	20%	$ 9.6	2%

(1) Percent change compared to balances as of August 31, 2008.

(2) Includes workers' compensation insurance clients and health and benefits services clients.

Human Resource Services revenue growth reflects modest improvements in economic conditions and annual price increases. The asset value of retirement services client employees' funds increased 20% as a result of recovery in the financial markets and increased levels of larger plans converting to Paychex. This positive contribution to revenue was offset somewhat by the impact of a shift in the mix of assets to investments earning lower fees from investment managers. In addition, Paychex HR Solutions revenue was positively impacted by increases in clients and client employees and the related checks per client for the first quarter compared to the same period last year. This was largely attributed to the nationwide expansion of our PEO.

Health and benefits services revenue increased 41% to $9.7 million for the first quarter, driven primarily by a 35% increase in the number of applicants. Growth in certain products that primarily support our MMS clients has also positively contributed to Human Resource Services revenue growth.

Total service revenue: Total service revenue increased 4% to $506.2 for the first quarter of fiscal 2011 compared to the same period last year, attributable to the factors previously discussed.

Interest on funds held for clients: The decrease of 12% to $12.1 million in interest on funds held for clients for the first quarter compared to the same period last year was the result of lower average interest rates earned, offset slightly by a 1% increase in average investment balances. The increase in average invested balances was due to an increase in state unemployment insurance rates for the 2010 calendar year, offset by lingering effects of the difficult economic conditions on our client base.

Combined operating and SG&A expenses: The following table summarizes total combined operating and selling, general and administrative ("SG&A") expenses:

$ in millions	For the three months ended August 31, 2010	For the three months ended August 31, 2009	Change
Compensation-related expenses	$ 207.2	$ 203.1	2%
Stock-based compensation costs	7.1	6.7	6%
Facilities expense	15.1	15.1	—
Depreciation of property and equipment	16.2	16.4	(1%)
Amortization of intangible assets	4.7	5.2	(10%)
Other expenses	67.2	63.8	5%
Total operating and SG&A expenses	$ 317.5	$ 310.3	2%

Total expenses increased 2% to $317.5 million for the first quarter compared to the same period last year. This increase is primarily due to costs related to continued investment in our sales force, customer service, and technological infrastructure. Improvements in productivity within operations with related lower headcount have offset this increase somewhat. Sales representatives are in line with our expected growth of 2% for fiscal 2011. As of August 31, 2010, we had approximately 12,300 employees compared to approximately 12,400 employees as of August 31, 2009. One-time costs related to the separation agreement entered into during the first quarter with Jonathan J. Judge, former President and Chief Executive Officer, are reflected in compensation-related expenses and stock-based compensation costs.

Depreciation expense is primarily related to buildings, furniture and fixtures, data processing equipment, and software. Amortization of intangible assets is primarily related to client list acquisitions, which are amortized using either straight-line or accelerated methods. Other expenses include items such as delivery, forms and supplies, communications, travel and entertainment, professional services, and other costs incurred to support our business.

Operating income: Operating income increased 6% to $200.8 million for the first quarter, as compared with the same period last year. The change in operating income is attributable to the factors previously discussed.

Operating income, net of certain items, is summarized as follows:

$ in millions	For the three months ended August 31, 2010	2009	Change
Operating income	$ 200.8	$ 189.9	6%
Excluding interest on funds held for clients	(12.1)	(13.7)	(12%)
Operating income, net of certain items	$ 188.7	$ 176.2	7%
Operating income, net of certain items, as a % of total service revenue	37.3%	36.2%	

Refer to the previous discussion of operating income, net of certain items, in the "Non-GAAP Financial Measure" section of this Form 10-Q.

Investment income, net: Investment income, net primarily represents earnings from our cash and cash equivalents and investments in available-for-sale securities. Investment income does not include interest on funds held for clients, which is included in total revenue. Investment income increased 57% to $1.4 million for the first quarter of fiscal 2011. The increase was a result of higher average invested balances resulting from investment of cash generated from operations and slightly higher average interest rates earned. The increase in average interest rates earned resulted from the allocation of funds from short-term to higher-rate longer-term investments late in the first quarter of fiscal 2010.

Income taxes: Our effective income tax rate was 34.8% for the first quarter of fiscal 2011 compared with 35.2% for the respective prior year period. The decrease in the effective income tax rate for the three months was primarily the result of lower overall state effective tax rate offset by lower levels of tax-exempt income derived from municipal debt securities in the funds held for clients and corporate investment portfolios.

Net income and earnings per share: Net income increased 7% to $131.9 million for the first quarter as compared with the same period last year. Diluted earnings per share increased 6% to $0.36 per share for the first quarter as compared with the same period last year. These fluctuations were attributable to the factors previously discussed.

LIQUIDITY AND CAPITAL RESOURCES

The volatility in the global financial markets that began in September 2008 has curtailed available liquidity and limited investment choices. Despite this macroeconomic environment, our financial position as of August 31, 2010 remained strong with cash and total corporate investments of $716.4 million and no debt. We also believe that our investments as of August 31, 2010 were not other-than-temporarily impaired, nor has any event occurred subsequent to that date to indicate any other-than-temporary impairment. It is anticipated that cash and total corporate investments as of August 31, 2010 along with projected operating cash flows, will support our normal business operations, capital purchases, and dividend payments for the foreseeable future.

Lines of credit: As of August 31, 2010, we had unused borrowing capacity available under four uncommitted, secured, short-term lines of credit at market rates of interest with financial institutions as follows:

Financial institution	Amount available	Expiration date
JP Morgan Chase Bank, N.A.	$350 million	February 2011
Bank of America, N.A.	$250 million	February 2011
PNC Bank, National Association	$150 million	February 2011
Wells Fargo Bank, National Association	$150 million	February 2011

The primary uses of the lines of credit would be to meet short-term funding requirements related to deposit account overdrafts and client fund obligations arising from electronic payment transactions on behalf of our clients in the ordinary course of business, if necessary. No amounts were outstanding against these lines of credit as of, or during the three months ended, August 31, 2010.

JP Morgan Chase Bank, N.A. and Bank of America, N.A. are also parties to our irrevocable standby letters of credit, which arrangements are discussed below.

Letters of credit: As of August 31, 2010, we had irrevocable standby letters of credit available totaling $47.5 million, required to secure commitments for certain insurance policies. The letters of credit expire at various dates between December 2010 and July 2011, and are collateralized by securities held in our investment portfolios. No amounts were outstanding on these letters of credit as of, or during the three months ended, August 31, 2010.

Other commitments: We enter into various purchase commitments with vendors in the ordinary course of business. We had outstanding commitments to purchase approximately $9.6 million of capital assets as of August 31, 2010.

We guarantee performance of service on annual maintenance contracts for clients who financed their service contracts through a third party. In the normal course of business, we make representations and warranties that guarantee the performance of services under service arrangements with clients. Historically, there have been no material losses related to such guarantees. In addition, we have entered into indemnification agreements with our officers and directors, which require us to defend and, if necessary, indemnify these individuals for certain pending or future legal claims as they relate to their services provided to us.

We currently self-insure the deductible portion of various insured exposures under certain employee benefit plans. Our estimated loss exposure under these insurance arrangements is recorded in other current liabilities on our Consolidated Balance Sheets. Historically, the amounts accrued have not been material. We also maintain insurance coverage in addition to our purchased primary insurance policies for gap coverage for employment practices liability, errors and omissions, warranty liability, and acts of terrorism; and capacity for deductibles and self-insured retentions through our captive insurance company.

Off-Balance Sheet Arrangements

As part of our ongoing business, we do not participate in transactions with unconsolidated entities such as special purpose entities or structured finance entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other limited purposes. We do maintain investments as a limited partner in low-income housing projects that are not considered part of our ongoing operations. These investments are accounted for under the equity method of accounting and are less than 1% of our total assets as of August 31, 2010.

Operating Cash Flow Activities

In millions	For the three months ended August 31, 2010	2009
Net income	$ 131.9	$ 123.6
Non-cash adjustments to net income	41.1	41.2
Cash provided by changes in operating assets and liabilities	21.3	21.8
Net cash provided by operating activities	$ 194.3	$ 186.6

The increase in our operating cash flows for the first three months of fiscal 2011 was a result of higher net income.

Investing Cash Flow Activities

In millions	For the three months ended August 31, 2010	2009
Net change in funds held for clients and corporate investment activities	$ 189.7	$ 261.7
Purchases of property and equipment	(16.6)	(10.1)
Purchases of other assets	(0.6)	(4.1)
Net cash provided by investing activities	$ 172.5	$ 247.5

Funds held for clients and corporate investments **:** Funds held for clients consist of short-term funds and available-for-sale securities. Corporate investments are primarily comprised of available-for-sale securities. The portfolio of funds held for clients and corporate investments is detailed in Note C of the Notes to Consolidated Financial Statements.

In general, fluctuations in net funds held for clients and corporate investment activities primarily relate to timing of purchases, sales, or maturities of investments. The amount of funds held for clients will also vary based upon the timing of collecting client funds, and the related remittance of funds to applicable tax or regulatory agencies for payroll tax administration services and to employees of clients utilizing employee payment services. Additional discussion of interest rates and related risks is included in the “Market Risk Factors” section of this Form 10-Q.

Purchases of long-lived assets: To support our continued client and ancillary product growth, purchases of property and equipment were made for data processing equipment and software, and for the expansion and upgrade of various operating facilities. The increase in purchases of property and equipment for the first quarter of fiscal 2011 is related to additional investment in our technological infrastructure.

We purchased approximately $0.8 million and $1.5 million of data processing equipment and software from EMC Corporation during the three months ended August 31, 2010 and 2009, respectively. The Chairman, President, and Chief Executive Officer of EMC Corporation is a member of our Board of Directors (the "Board").

The decrease in purchases of other assets for the first quarter of fiscal 2011 compared to the same period last year relates to purchases of customer lists for the three months ended August 31, 2009.

Financing Cash Flow Activities

In millions, except per share amounts	For the three months ended August 31, 2010	2009
Net change in client fund obligations	$ (266.4)	$ (485.4)
Dividends paid	(112.0)	(112.1)
Proceeds from and excess tax benefit related to exercise of stock options	0.2	5.9
Net cash used in financing activities	$ (378.2)	$ (591.6)
Cash dividends per common share	$ 0.31	$ 0.31

Net change in client fund obligations: The client fund obligations liability will vary based on the timing of collecting client funds and the related required remittance of funds to applicable tax or regulatory agencies for payroll tax administration services and to employees of clients utilizing employee payment services. Collections from clients are typically remitted from one to 30 days after receipt, with some items extending to 90 days. The net change in client fund obligations for the three months ended August 31, 2009 was adversely impacted by a decline in average invested balances for our funds held for clients resulting from the effect of difficult economic conditions on our client base during that time period.

Dividends paid: A quarterly dividend of $0.31 per share, unchanged since July 2008, was paid August 16, 2010 to stockholders of record as of August 2, 2010. The payment of future dividends is dependent on our future earnings and cash flow and is subject to the discretion of our Board.

Exercise of stock options: The decrease in proceeds from and excess tax benefit related to exercise of stock options is due to minimal stock option exercises during the first quarter of fiscal 2011 compared to 0.3 million shares exercised during the same period last year.

MARKET RISK FACTORS

Changes in interest rates and interest rate risk: Funds held for clients are primarily comprised of short-term funds and available-for-sale securities. Corporate investments are primarily comprised of available-for-sale securities. As a result of our operating and investing activities, we are exposed to changes in interest rates that may materially affect our results of operations and financial position. Changes in interest rates will impact the earnings potential of future investments and will cause fluctuations in the fair value of our longer-term available-for-sale securities. We follow a conservative investment strategy of optimizing liquidity and protecting principal. We invest primarily in high credit quality securities with AAA and AA ratings and short-term securities with A-1/P-1 ratings, with more than 95% of our portfolio rated AA or better. We invest predominantly in municipal bonds — general obligation bonds; pre-refunded bonds, which are secured by a U.S. government escrow; and essential services revenue bonds. We limit the amounts that can be invested in any single issuer and invest in short- to intermediate-term instruments whose fair value is less sensitive to interest rate changes. We manage the available-for-sale securities to a benchmark duration of two and one-half to three years. All investments held as of August 31, 2010 are traded in active markets.

During the first quarter of fiscal 2010, our primary short-term investment vehicle was U.S. agency discount notes. Starting in November 2009, we began to invest in select A-1/P-1-rated VRDNs. We have gradually increased our investments in VRDNs to $605.6 million as of August 31, 2010, up from $226.3 million as of May 31, 2010. During the first quarter, we earned an after-tax rate of approximately 0.22% on VRDNs as compared to approximately 0.08% on U.S. agency discount notes. We have no exposure to high-risk or illiquid investments such as auction rate securities, sub-prime mortgage securities, asset-backed securities or asset-backed commercial paper, collateralized debt obligations, enhanced cash or cash plus mutual funds, or structured investment vehicles (SIVs). We have not and do not utilize derivative financial instruments to manage our interest rate risk.

During the three months ending August 31, 2010, the average interest rate earned on our combined funds held for clients and corporate investment portfolios was 1.5% compared with 1.7% for the same period last year. With the turmoil in the financial markets, our conservative investment strategy has translated to significantly lower yields on high quality instruments. When interest rates are falling, the full impact of lower interest rates will not immediately be reflected in net income due to the interaction of short- and long-term interest rate changes. During a falling interest rate environment, the decreases in interest rates decrease earnings from our short-term investments, and over time decrease earnings from our longer-term available-for-sale securities. Earnings from the available-for-sale-securities, which as of August 31, 2010 had an average duration of 2.5 years, would not reflect decreases in interest rates until the investments are sold or mature and the proceeds are reinvested at lower rates. In the next twelve months, slightly over 20% of our long-term investment portfolio, which excludes VRDNs, will mature, and it is currently anticipated that these proceeds will be reinvested at a lower average interest rate of approximately 1.0%.

The amortized cost and fair value of available-for-sale securities that had stated maturities as of August 31, 2010 are shown below by contractual maturity. Expected maturities can differ from contractual maturities because borrowers may have the right to prepay obligations without prepayment penalties.

In millions	August 31, 2010 Amortized cost	Fair value
Maturity date:		
Due in one year or less	$ 391.2	$ 395.9
Due after one year through three years	750.2	785.1
Due after three years through five years	456.6	484.1
Due after five years	886.6	904.6
Total	$ 2,484.6	$ 2,569.7

VRDNs are primarily categorized as due after five years in the table above as the contractual maturities on these securities are typically 20 to 30 years. Although these securities are issued as long-term securities, they are priced and traded as short-term instruments because of the liquidity provided through the tender feature.

The following table summarizes recent changes in the Federal Funds rate:

	Fiscal year through August 31, 2010	Fiscal year ended May 31, 2010	Fiscal year ended May 31, 2009
Federal Funds rate — beginning of period	0.25%	0.25%	2.00%
Rate decrease:			
First quarter	—	—	—
Second quarter	NA	—	(1.00)
Third quarter	NA	—	(0.75)
Fourth quarter	NA	—	—
Federal Funds rate — end of period (1)	0.25%	0.25%	0.25%
Three-year “AAA” municipal securities yield — end of period	0.48%	0.99%	1.35%

(1) The Federal Funds rate was a range of 0% to 0.25% as of August 31, 2010 and May 31, 2010.

Calculating the future effects of changing interest rates involves many factors. These factors include, but are not limited to:

- daily interest rate changes;
- seasonal variations in investment balances;
- actual duration of short-term and available-for-sale securities;
- the proportional mix of taxable and tax-exempt investments;
- changes in tax-exempt municipal rates as compared to taxable investment rates, which are not synchronized or simultaneous; and

- financial market volatility and the resulting effect on benchmark and other indexing interest rates.

Subject to these factors, and under normal financial market conditions, a 25-basis-point change generally affects our tax-exempt interest rates by approximately 17 basis points.

Our total investment portfolio (funds held for clients and corporate investments) is expected to average approximately $3.9 billion for fiscal 2011. Our normal and anticipated allocation is approximately 50% invested in short-term and available-for-sale securities with an average duration of less than 30 days and 50% invested in available-for-sale securities with an average duration of two and one-half to three years.

The combined funds held for clients and corporate available-for-sale securities reflected a net unrealized gain of $85.1 million as of August 31, 2010, compared with a net unrealized gain of $66.6 million as of May 31, 2010. During the first quarter of fiscal 2011, the net unrealized gain on our investment portfolios ranged from $62.4 million to $86.2 million. Our investment portfolios reflected a net unrealized gain of approximately $77.3 million as of September 22, 2010.

As of August 31, 2010 and May 31, 2010, we had $2.6 billion and $2.2 billion, respectively, invested in available-for-sale securities at fair value. The weighted-average yield-to-maturity was 2.8% and 2.9% as of August 31, 2010 and May 31, 2010, respectively. The weighted-average yield-to-maturity excludes available-for-sale securities tied to short-term interest rates, such as VRDNs. Assuming a hypothetical decrease in both short-term and longer-term interest rates of 25 basis points, the resulting potential increase in fair value for our portfolio of available-for-sale securities held as of August 31, 2010 would be approximately $12.5 million. Conversely, a corresponding increase in interest rates would result in a comparable decrease in fair value. This hypothetical increase or decrease in the fair value of the portfolio would be recorded as an adjustment to the portfolio's recorded value, with an offsetting amount recorded in stockholders' equity. These fluctuations in fair value would have no related or immediate impact on the results of operations, unless any declines in fair value were considered to be other-than-temporary and an impairment loss recognized.

Credit Risk: We are exposed to credit risk in connection with these investments through the possible inability of the borrowers to meet the terms of their bonds. We regularly review our investment portfolios to determine if any investment is other-than-temporarily impaired due to changes in credit risk or other potential valuation concerns. We believe that the investments we held as of August 31, 2010 were not other-than-temporarily impaired, as none of our available-for-sale securities had fair values that were below amortized cost. Our assessment that an investment is not other-than-temporarily impaired could change in the future due to new developments or changes in our strategies or assumptions related to any particular investment.

CRITICAL ACCOUNTING POLICIES

Our critical accounting policies are described in Item 7 of our Form 10-K for fiscal 2010, filed with the SEC on July 16, 2010. On an ongoing basis, we evaluate the critical accounting policies used to prepare our consolidated financial statements, including, but not limited to, those related to:

- revenue recognition;
- PEO workers' compensation insurance;
- goodwill and other intangible assets;
- stock-based compensation costs; and
- income taxes.

There have been no material changes in these aforementioned critical accounting policies.

NEW ACCOUNTING PRONOUNCEMENTS

Recently adopted accounting pronouncements: Refer to Note A of the Notes to Consolidated Financial Statements for a discussion of recently adopted accounting pronouncements.

Recently issued accounting pronouncements: At this time, we do not anticipate that recently issued accounting guidance that has not yet been adopted will have a material impact on our consolidated financial statements. Refer to Note A of the Notes to Consolidated Financial Statements for a discussion of recently issued accounting pronouncements.

Item 3. Quantitative and Qualitative Disclosure of Market Risk

The information called for by this item is provided under the caption "Market Risk Factors" under Item 2 — Management's Discussion and Analysis of Financial Condition and Results of Operations and is incorporated herein by reference.

Item 4. Controls and Procedures

Disclosure Controls and Procedures and Internal Control Over Financial Reporting: Disclosure controls and procedures are designed with the objective of ensuring that information required to be disclosed in our reports filed under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), such as this report, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures are also designed with the objective of ensuring that such information is accumulated and communicated to our management, including the Executive Committee, consisting of our Chief Financial Officer, Senior Vice President of Operations, and Senior Vice President of Sales and Marketing, to allow timely decisions regarding required disclosure.

Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures: As of the end of the period covered by this report, we carried out an evaluation, under the supervision and with the participation of our Executive Committee and Chief Financial Officer, of the effectiveness of disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act. Based on such evaluation, the Executive Committee and Chief Financial Officer have concluded that as of the end of the period covered by this report, our disclosure controls and procedures were effective.

Changes in Internal Control over Financial Reporting: We also carried out an evaluation of the internal control over financial reporting to determine whether any changes occurred during the period covered by this report. Based on such evaluation, there has been no change in our internal control over financial reporting that occurred during the most recently completed fiscal quarter ended August 31, 2010, that materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 5. Other Information

On July 6, 2010, our Board approved the grant of restricted stock to outside members of the Board, as provided under our 2002 Stock Incentive Plan, as amended and restated effective October 12, 2005.

This and additional information regarding compensation awarded to our directors for the year ended May 31, 2010 was provided in our Proxy Statement for our 2010 Annual Meeting of Stockholders, which was filed with the SEC on September 3, 2010.

Item 6. Exhibits

Exhibit number	Description
10.1	Separation Agreement and Release between Jonathan J. Judge and Paychex, Inc. dated July 12, 2010.
31.1	Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS*	XBRL instance document.
101.SCH*	XBRL taxonomy extension schema document.
101.CAL*	XBRL taxonomy extension calculation linkbase document.
101.LAB*	XBRL taxonomy label linkbase document.
101.PRE*	XBRL taxonomy extension presentation linkbase document.
101.DEF*	XBRL taxonomy extension definition linkbase document.

* As provided in Rule 406T of Regulation S-T, this information is furnished and not filed for purposes of Sections 11 and 12 of the Securities Act of 1933 and Section 18 of the Exchange Act.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

PAYCHEX, INC.

Date: September 27, 2010

/s/ John M. Morphy
John M. Morphy
Senior Vice President, Chief
Financial Officer, and Secretary
(Principal Executive on behalf of Executive
Committee and Principal Financial Officer)

EXHIBIT 10.1

SEPARATION AGREEMENT AND RELEASE

THIS SEPARATION AGREEMENT AND RELEASE (" Agreement"), by and between Jonathan J. Judge (" Employee" or "you") and PAYCHEX, INC. (the "Company") and its parents, subsidiaries, divisions, affiliates, and/or related business entities, and with respect to each of them, their predecessors, successors and assigns, employee benefit plans or funds, and with respect to each such entity, all of its or their past and/or present shareholders, directors, officers, attorneys, fiduciaries, agents, trustees, administrators, employees and assigns, whether acting on behalf of the Company or in their individual capacities (collectively the "Company") is made on July 12, 2010.

1. SEPARATION DATE .

a. You have informed the Company that your voluntary separation date, which shall be your last day of employment with the Company, will be July 31, 2010 (the "Separation Date"). From the date hereof through the Separation Date (the " Notice Period"), you shall continue to be an employee of the Company, the Company will, during the Notice Period, continue to pay you your regular base pay, your fiscal year 2010 bonus (as previously determined by the Governance and Compensation Committee) and continue to provide you with those benefits that you were eligible to receive prior to the date hereof. During the Notice Period the Company may, at its sole discretion, choose to discontinue or otherwise limit your access to confidential information and/or elect to: (i) require you to continue to perform your regular and/or comparable alternative duties; (ii) require you to discontinue your duties, in whole or in part; and/or (iii) require you to aid and assist in a reasonable manner with the transition process associated with your departure.

b. After the Separation Date, you shall remain a member of the Board of Directors of the Company through your current term of service, but you shall no longer be an employee or an executive officer of the Company. The Separation Date shall be the termination date of your employment for purposes of your Employment Agreement dated November 30, 2007 and for purposes of participation in and coverage under all benefit/pension plans and programs sponsored by or through the Company. You agree to submit all requests for reimbursable business expenses incurred as an employee prior to the Separation Date for reimbursement no later than one month following the Separation Date (all such reimbursement requests shall otherwise be in accordance with Company's usual guidelines and practices).

c. Except as otherwise expressly provided for herein, you affirm that you have been paid and/or have received all base pay, bonuses, severance and/or benefits to which you may have been entitled during the period of employment with the Company, including any payments or benefits you may have been entitled to and you shall not be entitled to any other compensation, severance, equity or option payments, incentives, bonuses, awards or any other form of payment or benefits from any of the Company, either with respect to prior years or service or your employment in 2010. Notwithstanding the foregoing, you shall remain entitled to (i) your restricted stock and option awards to the extent vested as provided for under this Agreement or otherwise, and (ii) your accrued and vested balance in the Company's non qualified and unfunded deferred compensation plan (the "Deferral Plan"), and any other accrued and vested rights you may have under any other plans. Except as otherwise provided herein, your rights with respect to the exercise of any vested stock options shall be governed by the terms of the applicable option grant and plan. Amounts payable to you under the Deferral Plan shall be paid to you in accordance with your prior election and otherwise subject to the terms of such plan. For purposes of the Paychex, Inc. 401(k) Retirement Plan, you will be considered a terminated employee as of your Separation Date. All of the terms and conditions of the Company's benefit plans will continue to be governed by the controlling plan documents.

2. CONSIDERATION. In consideration of and exchange for your release and waiver of all claims against the Company and your compliance with all other terms and conditions of this Agreement (subject to written notice and an opportunity to cure any alleged breach), the Company agrees to provide you with the following "Consideration":

a. The Company shall pay you $1,900,000.00 (less applicable taxes and withholdings), payable within ten (10) business days following the expiration of six months after your Separation Date. The Payment shall not constitute compensation for any purpose under any retirement plan maintained by the Company. In the event of your death or incapacity, the Payment shall be made to your estate or personal representative, as applicable.

b. If you timely elect COBRA coverage for yourself and/or your eligible dependents, the Company will pay the premiums for such coverage for twelve (12) months following your Separation Date. In addition, following the twelve (12) month coverage period, you may be eligible to elect to continue health coverage on a self-pay basis in accordance with your rights and obligations under COBRA. Information regarding your rights under COBRA will be provided to you under separate cover.

c. Any options, restricted stock, or other equity granted to you prior to July 1, 2007 that have not previously vested shall vest and become immediately exercisable on the Separation Date. In addition, you will be vested in (i) an additional 11,111 shares of restricted stock associated with your July 17, 2007 award, and (ii) an additional 30,000 non-qualified stock options associated with your July 17, 2007 award. Your exercise period in connection with all vested options shall be one year from the Separation Date.

d. You acknowledge and agree that the payments provided to you under this Agreement represent good and valuable consideration for your General Release and your obligations hereunder.

3. a. GENERAL RELEASE OF ALL CLAIMS. You will execute and deliver to the Company on or before Separation Date a General Release in the form set forth in Annex A ("General Release").

b. Company's Release. The Company hereby forever releases and discharges Employee, his heirs, successors, and assigns, from any and all claims, charges, complaints, liens, demands, causes of action, obligations, damages, and liabilities, known or unknown, suspected or unsuspected, that the Company had or may now have, from the beginning of the world to the date of this release (the "Company's Release"). The Company's Release specifically extends to, without limitation, any and all claims or causes of action under common law as well as any claims under any applicable state, federal, or local statutes and regulations; provided, however, that the Company's Release does not waive, release, or otherwise discharge any claim or cause of action to enforce the Company's rights under (x) this Agreement or (y) any option or equity Award Agreement with respect to conduct arising after the date of this release.

c. The parties agree to execute and exchange mutual "bring down" releases upon the Employee's resignation from the Board of Directors of the Company.

4. RESIGNATIONS. Effective as of the Separation Date (or earlier if your employment is terminated), you agree to resign from all subsidiary board seats and any other positions that you hold in connection with your employment by or service in connection with any of the Company and to execute the omnibus resignation letter attached as Annex B and any implementing documentation that the Company may request in connection with such resignations.

5. RESPONSE TO LEGAL PROCESS. Nothing in this Agreement shall preclude you from providing truthful information to a government agency, or in response to a valid subpoena, or as otherwise required by law.

6. NO ADMISSION OF WRONGDOING. This Agreement is not intended, and shall not be construed, as an admission that you or the Company have violated any law (statutory or decisional), ordinance or regulation, breached any contract or policy, or committed any wrongdoing.

7. POST TERMINATION OBLIGATIONS.

a. Your Existing Contractual Obligations— You acknowledge that by virtue of your employment by the Company as President and CEO, you have had unfettered access to a range of sensitive and confidential information regarding the business operations, strategies, customers, prospects, employees and finances of the Company and its affiliates. You acknowledge that you are bound by the terms of paragraph 6 of your Employment Agreement as signed by you on November 30, 2007 ("Confidentiality Agreement") and that the provisions of the Confidentiality Agreement shall continue in full force and effect following the Separation Date. You also acknowledge that you continue to be bound by the Non-competition, Non-solicitation, Confidentiality, and Detrimental Conduct provisions of your 2008 and 2009 equity compensation agreements with the Company.

b. Non-Disparagement. The parties agree that they will not disparage or defame or encourage or induce others to disparage or defame the Employee or the Company, including comments that would adversely affect or damage in any manner (or otherwise portray in a false or negative light) the conduct of the business of, or business reputation of, the Company or any of its officers, directors, executives or personnel.

c. Indemnification/D&O Coverage. Nothing herein is intended to waive or extinguish any rights you have to coverage as a former executive under the Company's D&O policies, charter, by-laws or indemnification agreement(s).

8. RETURN OF PROPERTY. On or before the Separation Date you shall comply in all respects with the Confidentiality Agreement and shall immediately return to the Company all property belonging to the Company and/or the Company Entities, including but not limited to laptop, cell phone, keys, card access to the building and office floors, internal policies and other confidential business financial information and documents, such as files and material in your possession (including any computers, pagers, Blackberry, cellular phones, etc.), and all copies of computerized databases and related materials regarding the Company.

9. COOPERATION. You agree that it is an essential term and condition of this Agreement that during the three year period following your Separation Date, you cooperate with the Company and its counsel (i) with respect to all matters, for which you had responsibility or oversight while employed and (ii) any claims and/or lawsuits involving the Company of which you may have particular knowledge or in which you may be a witness, and following your termination of employment, you agree to cooperate with, and make yourself available on a reasonable basis to respond to inquiries from, representatives of any of the Company regarding any matters arising during the course of your employment or in connection with any investigation, administrative proceeding, arbitration, mediation or litigation (each, a "Proceeding") relating to any matter arising during the course of your employment or of which you have knowledge. Such cooperation includes meeting with Company representatives and counsel to disclose such facts as you may know, preparing with the Company's counsel for any deposition, trial, hearing or other proceeding; attending any deposition, trial, hearing or other proceeding to provide truthful testimony; and providing other assistance to the Company and to the Company's counsel as may, in the judgment of the Company's counsel, be necessary. You agree that, in the event you are subpoenaed or otherwise required by any person or entity (including, but not limited to, any government agency) to give testimony or produce documents (in a deposition, administrative or court proceeding or otherwise) which in any way relates to your employment by the Company, you will, to the extent not legally prohibited from doing so, give prompt notice of such request to the Chief Legal Officer of the Company so that the Company may contest the right of the requesting person or entity to such disclosure before making such disclosure. Nothing in this provision shall require you to violate your obligation to comply with valid legal process. The Company will not pay any consulting, per diem, or professional fees for cooperation in such matters; provided, however, the Company shall pay for or directly reimburse you for your reasonable out-of-pocket expenses incurred pursuant to this section 9 (including but not limited to reasonable travel expenses).

10. MATERIAL BREACH. Any breach of the provisions of Paragraphs 7, 8 and/or 9 above, shall be considered a material breach of this Agreement. In the event that you or the Company have committed a material breach of this Agreement, in addition to any remedies available to the Company under the Confidentiality Agreement or to you, the parties consent to the entry of injunctive relief, in addition to the right to pursue any and all of their remedies under the law. The parties further agree that you or the Company may obtain injunctive relief without the posting of a bond. The parties further agree that the prevailing party in any litigation shall be entitled to recover their attorneys' fees and costs incurred in any such action. The parties further agree that in the event of an alleged breach of this Agreement by either party, the non-breaching party shall provide written notice of such action and the section of the Agreement under which it constitutes a breach, and further will provide a reasonable opportunity to cure the breach.

11. REFERENCES; PUBLIC STATEMENTS. All reference inquiries relating to your employment with the Company shall be directed to the Vice President of Organizational Development. Any public statement by you or the Company shall be consistent with the Company's press release announcing your resignation, attached hereto as Annex C.

12. GOVERNING LAW AND ENFORCEMENT. This Agreement shall be construed and enforced in accordance with the laws of the State of New York without regard to the principles of conflicts of law. Additionally, any action concerning this Agreement shall be commenced exclusively in the state courts of Monroe Country, New York or United States District Court for the Western District of New York, in Rochester, New York. Both parties consent to the exclusive jurisdiction of such state and federal courts and waive any claim under the doctrine *of forum non conveniens.*

13. ENTIRE AGREEMENT. You understand that, except as otherwise provided herein, this Agreement constitutes the complete understanding between the Company and you, and, supersedes any and all agreements, understandings, and discussions, whether written or oral, between you and any of the Company Entities, except that any indemnification rights you were provided as an officer of the Company will survive this Agreement. No other promises or agreements, or modifications, waivers or amendments to this Agreement, shall be binding unless in writing and signed by both the Company and you after the execution of this Agreement. This Agreement may be executed in any number of counterparts and by different parties on separate counterparts, each of which counterparts, when executed together, shall constitute but one and the same Agreement. The parties further agree that if any part or any provision of this Agreement is determined to be invalid or unenforceable under applicable law by a court of competent jurisdiction, that part shall be ineffective to the extent of such invalidity only, without in any way affecting the remaining parts of said provision or the remaining provisions of the Agreement.

14. ACKNOWLEDGMENTS. You acknowledge that you: (a) have carefully read this Agreement in its entirety; (b) are hereby advised by the Company, in this writing, to consult with an attorney of your choice before signing this Agreement; (c) fully understand the significance of all of the terms and conditions of this Agreement and have discussed them with an attorney of your choice; and (d) are signing this Agreement voluntarily and of your own free will and agree to abide by all the terms and conditions contained herein.

15. 409A Considerations. The intent of the parties is that payments and benefits under this Agreement comply with Section 409A of the Internal Revenue Code of 1986, as amended (the "Code") and the regulations and guidance promulgated thereunder (collectively " Code Section 409A") and, accordingly, to the maximum extent permitted, this Agreement shall be interpreted to be in compliance therewith. In no event whatsoever shall the Company be liable for any additional tax, interest or penalties that may be imposed on Employee by Code Section 409A or any damages for failing to comply with Code Section 409A hereunder or otherwise. The reimbursement payment for costs, expenses or in-kind benefits provided for under Section 2(b) of this Agreement or otherwise, except as permitted by Code Section 409A, shall (i) be made no later than the end of the calendar year following the calendar year in which such costs, expenses or in-kind benefits were incurred or provided; (ii) the amount of expenses eligible for reimbursement, or in-kind benefits provided, during any taxable year shall not affect

the amounts of expenses eligible for reimbursement, or in-kind benefits to be provided, in any other taxable year (other than with regard to a limit related to the period in which an arrangement is in effect (other than with regard to a limit related to the period in which the arrangement is in effect with regard to an arrangement subject to Section 105(b) of the Code), and (iii) the reimbursement or in-kind benefit cannot be liquidated or exchanged for any other benefit.

IN WITNESS WHEREOF, the parties hereto have approved and executed this Agreement as of the dates set forth below:

PAYCHEX, INC.	**EMPLOYEE**
BY: /s/ John Morphy	BY: /s/ Jonathan J. Judge 7/10/2010
Name: John Morphy	Jonathan J. Judge
Title: Sr. Vice President, Chief Financial Officer, Secretary, Treasurer	

Annex A

GENERAL RELEASE

1. In consideration for the benefits to be provided pursuant to the Agreement entered into between the undersigned and the Company, dated as of July 12, 2010 (the "Agreement"), you, for yourself and for your heirs, executors, administrators, trustees, legal representatives and assigns (hereinafter referred to collectively as "Releasors"), forever release and discharge the Company from any and all claims, demands, causes of action, fees and liabilities of any kind whatsoever, whether known or unknown, which you ever had, now have, or may have against any of the Company Entities by reason of any act, omission, transaction, practice, plan, policy, procedure, conduct, occurrence, or other matter, up to and including the execution of this Agreement, including but not limited to claims for, under, or based on: (i) the Age Discrimination in Employment Act and the Older Workers' Benefit Protection Act; (ii) Title VII of the Civil Rights Act of 1964; (iii) the Americans with Disabilities Act; (iv) any claims under Sections 1981 through 1988 of Title 42 of the United States Code; (v) the Employee Retirement Income Security Act of 1974; (vi) the Family and Medical Leave Act; (vii) the National Labor Relations Act; (viii) Sections 503 and 504 of the Rehabilitation Act of 1973; (ix) the New York State Human Rights Law and the New York City Administrative Code; (ix) all other federal, state and local fair employment and civil rights laws; (x) breach of contract (express or implied), retaliation, wrongful discharge, detrimental reliance, defamation, emotional distress, and/or compensatory and/or punitive damages; (xi) claims of any character arising under any laws of any jurisdiction with respect to which the Company may conduct any business operations or otherwise have a place of business, and (x) attorneys' fees, costs, disbursements and/or the like; all of the above statutes as amended.

a. Claims Not Released. Notwithstanding the foregoing, you are not releasing claims that relate to: (i) any claims arising after the execution of this General Release; (ii) any claims for enforcement of the Agreement; (iii) claims for accrued, vested benefits under any employee benefit or welfare plan of the Company, or vested option or equity award granted by the Company, in accordance with the terms of such plans, award and applicable law; (iv) any claims or rights which cannot be waived by law; and/or (v) any claims for indemnification or contribution pursuant to Section 7(c) of the Agreement.

b. Waiver. By virtue of the foregoing, you agree that you have waived any damages and other relief available to you (including, without limitation, monetary damages, equitable relief and reinstatement) with respect to any claim or cause of action released in section 1, above. Therefore, you agree that you will not accept any award or settlement from any source or proceeding (including but not limited to any proceeding brought by any other person or by any governmental agency) with respect to any claim or right waived in this General Release. You further covenant not to commence any action with respect to any claims released under this General Release, and agree to indemnify the Company for any damages or expenses resulting from your breach of this release.

c. Rights. Nothing in this General Release shall be construed to prevent you from filing a charge with, or participating in an investigation conducted by any governmental agency, including any federal/state/city fair employment practices agency, to the extent required or permitted by law. Nevertheless, as set forth in (b) above, you acknowledge that you cannot benefit monetarily with respect to any of the claims released and waived in this General Release.

d. Defined Terms. Capitalized terms used herein shall have the meaning set forth in the Agreement.

e. Acknowledgments. You acknowledge that you: (a) have carefully read the Agreement and this General Release in its entirety and have had twenty-one (21) days in which to consider its terms; (b) are hereby advised by the Company, in this writing, to consult with an attorney of your choice before signing this General Release; (c) fully understand the significance of all of the terms and conditions of this General Release and have discussed them with an attorney of your choice, or have had a reasonable opportunity to do so; and (d) are signing this General Release voluntarily and of your own free will and agree to abide by all the terms and conditions contained herein.

f. Effective Date. After executing this General Release, you shall have seven (7) days (the "Revocation Period") to revoke this General Release by indicating your desire to do so in writing delivered to Paychex Vice President, Chief Legal Officer at 911 Panorama Trail South, Rochester, New York 14625-2396, by no later than 5:00 p.m. on the seventh (7th) day after the date you sign this General Release. The effective date of this General Release shall be the eighth (8th) day after you sign the General Release (the "Effective Date"). If the last day of the Revocation Period falls on a Saturday, Sunday or holiday, the last day of the Revocation Period shall be deemed to be the next business day. In the event you do not accept this General Release as set forth above, or in the event you revoke this General Release during the Revocation Period, this General Release, including but not limited to the obligation of the Company to provide the Consideration and other benefits referred to in section 2 of the Agreement, shall be deemed automatically null and void.

/s/ Jonathan J. Judge
Jonathan J. Judge

Dated: 7/31/2010

Annex B

Omnibus Resignation Letter

Paychex, Inc.

July 12, 2010

Ladies and Gentlemen:

Effective as of July 31, 2010, I hereby retire and resign from any and all positions, offices, board directorships and committee memberships that I may occupy or hold in connection with the Company (as defined in the Separation Agreement and Release dated July 12, 2010), with the exception of my membership on the Paychex, Inc. Board of Directors, for which I shall continue to serve the remainder of my existing term and for which my resignation shall be effective at the expiration of said term. My resignation is not due to any disagreement with the Company related to its operations, policies or practices.

Sincerely,

/s/ Jonathan J. Judge

Jonathan J. Judge

News from Paychex

911 Panorama Trail South • Rochester, NY 14625 • www.paychex.com

For Immediate Release

Paychex President and Chief Executive Officer Resigns

Rochester, NY (July 12, 2010) — The Board of Directors of Paychex, Inc. (NASDAQ: PAYX) today announced the resignation of Jonathan J. Judge as president and chief executive officer, effective July 31, 2010. Judge, who joined Paychex in October 2004 as the company's second president and CEO, said he is leaving to pursue other interests. He will complete his term as a member of the Paychex Board of Directors.

The Board of Directors immediately began the search for Judge's successor. In the interim, an executive committee has been formed to lead the company. Members of that committee include the following Paychex executives: Delbert Humenik, senior vice president of sales and marketing; John M. Morphy, senior vice president, chief financial officer, and secretary; and Martin Mucci, senior vice president of operations. Paychex Chairman B. Thomas Golisano and the Board of Directors will provide oversight for the executive committee.

"Jon joined Paychex as my successor, bringing with him experience and qualifications gained during his 25-year career with IBM," said Golisano, Paychex chairman and founder. "During his tenure with Paychex, Jon guided our company's revenue growth from $1.4 billion in fiscal 2005 to $2.0 billion in 2010. He also strengthened our management practices, oversaw key technology advances for our payroll and HR offerings, and led our successful entry into the health and benefits business. We thank Jon for his leadership over the last six years and wish him well as he pursues new interests."

"I have greatly enjoyed my time at Paychex, working with some of the most talented and dedicated employees in the payroll and HR services industry," said Judge. "We have accomplished a great deal together, and the company will continue to prosper. I have decided this is a good time for me to move on to my next challenge."

About Paychex

Paychex, Inc. (NASDAQ: PAYX) is a leading provider of payroll, human resource, and benefits outsourcing solutions for small- to medium-sized businesses. The company offers comprehensive payroll services, including payroll processing, payroll tax administration, and employee pay services, including direct deposit, check signing, and Readychex®. Human resource services include 401(k) plan recordkeeping, health insurance, workers' compensation administration, section 125 plans, a professional employer organization, time and attendance solutions, and other administrative services for business. Paychex was founded in 1971. With headquarters in Rochester, New York, the company has more than 100 offices serving approximately 536,000 payroll clients nationwide as of May 31, 2010. For more information about Paychex and our products, visit www.paychex.com.

# # #

Editor's note: To access a high-resolution photograph of Jonathan J. Judge, go to the Media Center of www.paychex.com and click on "photos."

Media Contact
Laura Saxby Lynch
Director, Corporate Communications
585-383-3074 (office)
585-354-3756 (mobile)
lsaxbylynch@paychex.com

EXHIBIT 31.1

**CERTIFICATION PURSUANT TO
SECTION 302
OF THE SARBANES-OXLEY ACT OF 2002**

We, the Executive Committee, consisting of the Chief Financial Officer, Senior Vice President, Operations and Senior Vice President of Sales and Marketing, (the "Committee") certify that:

1. We have reviewed this Quarterly Report on Form 10-Q of Paychex, Inc.;
2. Based on our knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on our knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and the Committee are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant’s other certifying officer and the Committee have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors:

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: September 27, 2010

/s/ John M. Morphy
Senior Vice President, Chief Financial Officer, and Secretary

Date: September 27, 2010

/s/ Martin Mucci
Senior Vice President, Operations

Date: September 27, 2010

/s/ Delbert M. Humenik
Senior Vice President of Sales and Marketing

EXHIBIT 31.2

**CERTIFICATION PURSUANT TO
SECTION 302
OF THE SARBANES-OXLEY ACT OF 2002**

I, JOHN M. MORPHY, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Paychex, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors:
   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: September 27, 2010

/s/ John M. Morphy
Senior Vice President, Chief Financial Officer, and Secretary

EXHIBIT 32.1

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Paychex, Inc. (the “Company”) on Form 10-Q for the period ended August 31, 2010 as filed with the Securities and Exchange Commission (“SEC”) on the date hereof (the “Report”), the Company’s Executive Committee, consisting of its Chief Financial Officer, Senior Vice President, Operations and Senior Vice President of Sales and Marketing, certify, pursuant to 18 U.S.C. section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

A signed original of this written statement has been provided to the Company and will be retained by the Company and furnished to the SEC upon request.

Date: September 27, 2010

/s/ John M. Morphy
Senior Vice President, Chief
Financial Officer, and Secretary

Date: September 27, 2010

/s/ Martin Mucci
Senior Vice President, Operations

Date: September 27, 2010

/s/ Delbert M. Humenik
Senior Vice President of Sales and Marketing

EXHIBIT 32.2

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Paychex, Inc. (the "Company") on Form 10-Q for the period ended August 31, 2010 as filed with the Securities and Exchange Commission ("SEC") on the date hereof (the "Report"), I, JOHN M. MORPHY, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

A signed original of this written statement has been provided to the Company and will be retained by the Company and furnished to the SEC upon request.

Date: September 27, 2010

/s/ John M. Morphy
John M. Morphy
Senior Vice President, Chief Financial Officer, and Secretary