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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, 2008

Commission file number 0-11330

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**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 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

Smaller reporting company

(Do not check if a 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 .

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

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Common Stock, \$0.01 Par Value

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360,795,137 Shares

CLASS

OUTSTANDING AS OF AUGUST 31, 2008

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## PART I. FINANCIAL INFORMATION

## Item 1. Financial Statements

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

	For the three months ended	
	August 31, 2008	August 31, 2007
<b>Revenue:</b>		
Service revenue	\$ 509,867	\$ 474,815
Interest on funds held for clients	24,218	32,315
<b>Total revenue</b>	<b>534,085</b>	<b>507,130</b>
<b>Expenses:</b>		
Operating expenses	168,468	159,315
Selling, general and administrative expenses	144,032	137,227
<b>Total expenses</b>	<b>312,500</b>	<b>296,542</b>
<b>Operating income</b>	<b>221,585</b>	<b>210,588</b>
Investment income, net	3,051	12,237
<b>Income before income taxes</b>	<b>224,636</b>	<b>222,825</b>
Income taxes	75,927	71,750
<b>Net income</b>	<b>\$ 148,709</b>	<b>\$ 151,075</b>
<b>Basic earnings per share</b>	<b>\$ 0.41</b>	<b>\$ 0.40</b>
<b>Diluted earnings per share</b>	<b>\$ 0.41</b>	<b>\$ 0.40</b>
<b>Weighted-average common shares outstanding</b>	<b>360,629</b>	<b>380,539</b>
<b>Weighted-average common shares outstanding, assuming dilution</b>	<b>361,040</b>	<b>382,255</b>
<b>Cash dividends per common share</b>	<b>\$ 0.31</b>	<b>\$ 0.30</b>

See Notes to Consolidated Financial Statements.

**PAYCHEX, INC.**  
**CONSOLIDATED BALANCE SHEETS (UNAUDITED)**  
 In thousands, except per share amounts

	August 31, 2008	May 31, 2008
<b>ASSETS</b>		
Cash and cash equivalents	\$ 61,582	\$ 164,237
Corporate investments	402,553	228,727
Interest receivable	29,529	34,435
Accounts receivable, net of allowance for doubtful accounts	197,128	184,686
Deferred income taxes	—	7,274
Prepaid income taxes	—	11,236
Prepaid expenses and other current assets	27,685	27,231
<b>Current assets before funds held for clients</b>	<b>718,477</b>	<b>657,826</b>
Funds held for clients	3,656,923	3,808,085
<b>Total current assets</b>	<b>4,375,400</b>	<b>4,465,911</b>
Long-term corporate investments	55,011	41,798
Property and equipment, net of accumulated depreciation	275,628	275,297
Intangible assets, net of accumulated amortization	70,952	74,500
Goodwill	433,316	433,316
Deferred income taxes	14,499	13,818
Other long-term assets	4,804	5,151
<b>Total assets</b>	<b>\$ 5,229,610</b>	<b>\$ 5,309,791</b>
<b>LIABILITIES</b>		
Accounts payable	\$ 35,041	\$ 40,251
Accrued compensation and related items	107,629	132,589
Deferred revenue	10,216	10,326
Deferred income taxes	2,056	—
Accrued income taxes	55,227	—
Litigation reserve	22,934	22,968
Other current liabilities	47,434	47,457
<b>Current liabilities before client fund obligations</b>	<b>280,537</b>	<b>253,591</b>
Client fund obligations	3,623,145	3,783,681
<b>Total current liabilities</b>	<b>3,903,682</b>	<b>4,037,272</b>
Accrued income taxes	19,750	17,728
Deferred income taxes	10,772	9,600
Other long-term liabilities	45,281	48,549
<b>Total liabilities</b>	<b>3,979,485</b>	<b>4,113,149</b>
<b>COMMITMENTS AND CONTINGENCIES — NOTE I</b>		
<b>STOCKHOLDERS' EQUITY</b>		
Common stock, \$0.01 par value; Authorized: 600,000 shares; Issued and outstanding: 360,795 shares as of August 31, 2008 and 360,500 shares as of May 31, 2008, respectively	3,608	3,605
Additional paid-in capital	443,644	431,639
Retained earnings	780,570	745,351
Accumulated other comprehensive income	22,303	16,047
<b>Total stockholders' equity</b>	<b>1,250,125</b>	<b>1,196,642</b>
<b>Total liabilities and stockholders' equity</b>	<b>\$ 5,229,610</b>	<b>\$ 5,309,791</b>

See Notes to Consolidated Financial Statements.

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

	For the three months ended	
	August 31, 2008	August 31, 2007
<b>OPERATING ACTIVITIES</b>		
Net income	\$ 148,709	\$ 151,075
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization on property and equipment and intangible assets	20,687	19,131
Amortization of premiums and discounts on available-for-sale securities	6,537	3,965
Stock-based compensation costs	6,922	6,322
Provision for deferred income taxes	6,422	5,634
Provision for allowance for doubtful accounts	464	700
Net realized gains on sales of available-for-sale securities	(300)	(143)
Changes in operating assets and liabilities:		
Interest receivable	4,906	18,251
Accounts receivable	(12,906)	(25,409)
Prepaid expenses and other current assets	10,782	7,262
Accounts payable and other current liabilities	23,275	66,542
Net change in other assets and liabilities	(947)	(117)
<b>Net cash provided by operating activities</b>	<b>214,551</b>	<b>253,213</b>
<b>INVESTING ACTIVITIES</b>		
Purchases of available-for-sale securities	(13,140,530)	(33,300,803)
Proceeds from sales and maturities of available-for-sale securities	12,508,552	34,381,101
Net change in funds held for clients' money market securities and other cash equivalents	599,586	(331,244)
Purchases of property and equipment	(16,207)	(20,775)
Proceeds from sales of property and equipment	—	708
Acquisition of businesses, net of cash acquired	—	(32,596)
Purchases of other assets	(1,274)	(1,684)
<b>Net cash (used in)/provided by investing activities</b>	<b>(49,873)</b>	<b>694,707</b>
<b>FINANCING ACTIVITIES</b>		
Net change in client fund obligations	(160,536)	(453,957)
Repurchases of common stock	—	(396,484)
Dividends paid	(111,904)	(114,988)
Proceeds from exercise of stock options	4,809	44,402
Excess tax benefit related to exercise of stock options	298	4,368
<b>Net cash used in financing activities</b>	<b>(267,333)</b>	<b>(916,659)</b>
<b>(Decrease)/increase in cash and cash equivalents</b>	<b>(102,655)</b>	<b>31,261</b>
Cash and cash equivalents, beginning of period	164,237	79,353
<b>Cash and cash equivalents, end of period</b>	<b>\$ 61,582</b>	<b>\$ 110,614</b>

See Notes to Consolidated Financial Statements.

**PAYCHEX, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**  
**August 31, 2008**

**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, 2008. Long-lived assets in Germany are insignificant in relation to total long-lived assets of the Company as of August 31, 2008.

**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, 2008 ("fiscal 2008"). Operating results and cash flows for the three months ended August 31, 2008 are not necessarily indicative of the results that may be expected for other interim periods or the full fiscal year ending May 31, 2009 ("fiscal 2009").

**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 \$635.7 million for both the three months ended August 31, 2008 and 2007, 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. Claims are paid as incurred and the Company's maximum individual claims liability is \$1,000,000 under both its fiscal 2009 policy and its fiscal 2008 policy.

The Company has recorded the following amounts on its Consolidated Balance Sheets for workers' compensation claims as of:

<u>In thousands</u>	<u>August 31,</u> <u>2008</u>	<u>May 31,</u> <u>2008</u>
Prepaid expense	\$ 2,597	\$ 2,612
Current liability	\$ 9,279	\$ 8,395
Long-term liability	\$ 14,929	\$ 18,294

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

The amount included in prepaid expense on the Consolidated Balance Sheets relates to the policy for the fiscal year ended May 31, 2004, which was a pre-funded policy.

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 social and 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 stock-based awards to employees consisting of stock options, restricted stock awards, and restricted stock units. The Company typically makes grants to its officers, directors, and management in July. The grants approved by the Board of Directors (the "Board") were as follows:

	For the three months ended August 31,			
	2008		2007	
In thousands, except per share amounts	Shares granted	Weighted- average fair value per share	Shares granted	Weighted- average fair value per share
Stock options	536	\$ 7.29	472	\$ 11.77
Restricted stock	134	\$ 31.95	134	\$ 43.91
Restricted stock units	606	\$ 28.30	499	\$ 40.60

The Company accounts for all stock-based awards to employees, including grants of employee stock options, 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 \$6.9 million and \$6.3 million for the three months ended August 31, 2008 and 2007, respectively. As of August 31, 2008, the total unrecognized compensation cost related to all unvested stock-based awards was \$78.2 million and is expected to be recognized over a weighted-average period of 2.7 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 restricted stock units 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.

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

The fair value of stock option grants was 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,	
	2008	2007
Risk-free interest rate	3.5%	5.0%
Dividend yield	3.3%	2.7%
Volatility factor	.28	.27
Expected option term life in years	6.5	6.5

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 and implied market volatility, both over a period equal to the expected option life. The expected option life is based on historical exercise behavior.

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.

**Fair value of financial instruments:** Effective June 1, 2008, the Company adopted Financial Accounting Standards Board Statement of Financial Accounting Standard ("SFAS") No. 157, "Fair Value Measurements." This statement clarifies the definition of fair value, establishes a framework for measuring fair value and expands the disclosures on fair value measurements; however, does not require any new fair value measurements. The adoption of this standard has not had a material effect on the Company's results of operations or financial position.

In determining the fair value of its assets and liabilities, the Company uses various valuation approaches, predominately the market and income approaches. In determining the fair value of its available-for-sale securities, the Company utilizes the Interactive Data Pricing service, a market approach. SFAS No. 157 establishes a hierarchy for information and valuations used in measuring fair value that is broken down into three levels based on its reliability. Level 1 valuations are based on quoted prices in active markets for identical assets or liabilities that the Company has the ability to access. Level 2 valuations are based on quoted prices in markets that are not active or for which all significant inputs are observable, directly or indirectly. Level 3 valuations are based on information that is unobservable and significant to the overall fair value measurement.



[Table of Contents](#)**Note A: Description of Business and Significant Accounting Policies — continued**

The following table presents information on the Company's financial assets and liabilities measured at fair value on a recurring basis under SFAS No. 157 as of August 31, 2008:

In thousands	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	\$ 3,988,937	\$ 75	\$ 3,988,862	\$ —
Other securities	10,230	10,230	—	—
Liabilities:				
Other long-term liabilities	10,263	10,263	—	—

As of August 31, 2008, the Company did not have any assets or liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3).

**Note B: Reclassification Within Consolidated Statements of Cash Flows**

Client fund obligations represent the Company's contractual obligation to remit funds to satisfy clients' payroll and tax payment obligations. To better reflect the nature of these activities, the Company has reclassified the net change in client fund obligations in the Consolidated Statements of Cash Flows from investing activities to financing activities for all periods presented. The impact of the reclassification to the prior year period is as follows:

	For the three months ended August 31, 2007
Net cash provided by investing activities — as previously reported	\$ 240,750
Impact of reclassification — net change in client fund obligations	453,957
Net cash provided by investing activities — as reclassified	<u>\$ 694,707</u>
Net cash used in financing activities — as previously reported	\$ (462,702)
Impact of reclassification — net change in client fund obligations	(453,957)
Net cash used in financing activities — as reclassified	<u>\$ (916,659)</u>

This reclassification had no impact on the net change in cash and cash equivalents or cash flows from operating activities for the period presented.

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**Note C: Basic and Diluted Earnings Per Share**

Basic and diluted earnings per share were calculated as follows:

In thousands, except per share amounts	For the three months ended	
	August 31,	
	2008	2007
<b>Basic earnings per share:</b>		
Net income	\$ 148,709	\$ 151,075
Weighted-average common shares outstanding	360,629	380,539
Basic earnings per share	\$ 0.41	\$ 0.40
<b>Diluted earnings per share:</b>		
Net income	\$ 148,709	\$ 151,075
Weighted-average common shares outstanding	360,629	380,539
Dilutive effect of common share equivalents at average market price	411	1,716
Weighted-average common shares outstanding, assuming dilution	361,040	382,255
Diluted earnings per share	\$ 0.41	\$ 0.40
Weighted-average anti-dilutive common share equivalents	11,387	5,126

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, 2008, 0.3 million shares of the Company's common stock were issued for stock option exercises and vesting of restricted stock compared with 1.5 million shares issued for stock option exercises and vesting of restricted stock for the three months ended August 31, 2007. During the three months ended August 31, 2007, the Company repurchased 8.9 million shares for \$396.5 million under its stock repurchase program completed in fiscal 2008.

**Note D: Funds Held for Clients and Corporate Investments**

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

In thousands	August 31, 2008			
	Cost	Gross unrealized gains	Gross unrealized losses	Fair value
<b>Type of issue:</b>				
Money market securities and other cash equivalents	\$ 115,320	\$ —	\$ —	\$ 115,320
Available-for-sale securities:				
General obligation municipal bonds	827,459	16,833	(10)	844,282
Pre-refunded municipal bonds	509,139	10,800	(13)	519,926
Revenue municipal bonds	404,080	6,863	(64)	410,879
Variable rate demand notes	2,103,815	3	—	2,103,818
U.S. agency securities	110,000	28	(71)	109,957
Other equity securities	20	55	—	75
Total available-for-sale securities	3,954,513	34,582	(158)	3,988,937
Other	10,839	169	(778)	10,230
<b>Total funds held for clients and corporate investments</b>	<b>\$ 4,080,672</b>	<b>\$ 34,751</b>	<b>\$ (936)</b>	<b>\$ 4,114,487</b>

In thousands	May 31, 2008			
	Cost	Gross unrealized gains	Gross unrealized losses	Fair value
<b>Type of issue:</b>				
Money market securities and other cash equivalents	\$ 714,907	\$ —	\$ —	\$ 714,907
Available-for-sale securities:				
General obligation municipal bonds	812,611	12,732	(287)	825,056
Pre-refunded municipal bonds	504,377	7,724	(489)	511,612
Revenue municipal bonds	444,852	5,298	(295)	449,855
Variable rate demand notes	1,536,911	67	—	1,536,978
U.S. agency securities	30,000	—	(36)	29,964
Other equity securities	20	59	—	79
Total available-for-sale securities	3,328,771	25,880	(1,107)	3,353,544
Other	10,143	426	(410)	10,159
<b>Total funds held for clients and corporate investments</b>	<b>\$ 4,053,821</b>	<b>\$ 26,306</b>	<b>\$ (1,517)</b>	<b>\$ 4,078,610</b>

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

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

<b>In thousands</b>	<b>August 31, 2008</b>	<b>May 31, 2008</b>
Funds held for clients	\$ 3,656,923	\$ 3,808,085
Corporate investments	402,553	228,727
Long-term corporate investments	55,011	41,798
Total funds held for clients and corporate investments	\$ 4,114,487	\$ 4,078,610

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 attempts to mitigate these risks by investing primarily in high credit quality securities with AAA and AA ratings and short-term securities with A-1/P-1 ratings, limiting amounts that can be invested in any single issuer, and by investing in short- to intermediate-term instruments whose fair value is less sensitive to interest rate changes. The Company's variable rate demand notes ("VRDNs") are rated A-1/P-1 and must have a liquidity facility issued by highly rated financial institutions.

As of September 22, 2008, the Company has sold substantially all of its VRDNs. The Company expects to be fully divested of VRDNs by the end of September 2008. Funds from the VRDNs are being reinvested in agency discount notes. The Company does not hold any auction rate securities. The Company exited the auction rate market in the early fall of 2007 and has never experienced a failed auction. The Company has no exposure to any 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). The Company has not and does not utilize derivative financial instruments to manage interest rate risk. As of September 22, 2008, the Company does not have any position in prime money market funds.

The Company's available-for-sale securities reflected a net unrealized gain of \$34.4 million as of August 31, 2008 compared with a net unrealized gain of \$24.8 million as of May 31, 2008. The gross unrealized gains as of August 31, 2008 were comprised of 18 available-for-sale securities, which had a total fair value of \$93.9 million. The gross unrealized losses as of May 31, 2008 were comprised of 76 available-for-sale securities, which had a total fair value of \$243.6 million.

The Company periodically 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, 2008 were not other-than-temporarily impaired. While certain available-for-sale securities had fair values that were below cost, the Company believes that it is probable that the principal and interest will be collected in accordance with contractual terms, and that the decline in the fair value was due to changes in interest rates and was not due to increased credit risk. As of August 31, 2008 and May 31, 2008, substantially all of the securities with an unrealized loss held an AA rating or better. The Company currently believes that it has the ability and intent to hold these investments until the earlier of market price recovery or maturity. 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.

[Table of Contents](#)**Note D: Funds Held for Clients and Corporate Investments — continued**

The cost and fair value of available-for-sale securities that have stated maturities as of August 31, 2008 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 thousands	August 31, 2008	
	Cost	Fair value
<b>Maturity date:</b>		
Due in one year or less	\$ 293,168	\$ 295,312
Due after one year through three years	697,129	708,783
Due after three years through five years	540,526	553,623
Due after five years	2,423,669	2,431,144
Total	\$ 3,954,492	\$ 3,988,862

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 E: Property and Equipment, Net of Accumulated Depreciation**

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

In thousands	August 31, 2008	May 31, 2008
Land and improvements	\$ 4,117	\$ 3,617
Buildings and improvements	84,758	84,723
Data processing equipment	169,381	166,893
Software	100,280	98,513
Furniture, fixtures, and equipment	138,598	136,330
Leasehold improvements	79,506	76,244
Construction in progress	55,972	52,078
Total property and equipment, gross	632,612	618,398
Less: Accumulated depreciation and amortization	356,984	343,101
Property and equipment, net of accumulated depreciation	\$ 275,628	\$ 275,297

Depreciation expense was \$15.9 million and \$15.0 million for the three months ended August 31, 2008 and 2007, respectively.

Within construction in progress, there are costs for software being developed for internal use of \$55.1 million and \$51.6 million as of August 31, 2008 and May 31, 2008, respectively. Capitalization of costs ceases when the software is ready for its intended use, at which time the Company begins amortization of the costs.

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

The Company had goodwill balances on its Consolidated Balance Sheets of \$433.3 million as of August 31, 2008 and May 31, 2008.

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

In thousands	August 31, 2008	May 31, 2008
Client lists and associate office license agreements	\$ 172,258	\$ 170,984
Other intangible assets	5,675	5,675
Total intangible assets, gross	177,933	176,659
Less: Accumulated amortization	106,981	102,159
<b>Intangible assets, net of accumulated amortization</b>	<b>\$ 70,952</b>	<b>\$ 74,500</b>

Amortization expense relating to intangible assets was \$4.8 million and \$4.1 million for the three months ended August 31, 2008 and 2007, respectively.

As of August 31, 2008, the estimated amortization expense relating to intangible asset balances for the full fiscal year 2009 and the following four fiscal years is as follows:

In thousands Year ended May 31,	Estimated amortization expense
2009	\$ 19,654
2010	\$ 17,014
2011	\$ 14,414
2012	\$ 12,105
2013	\$ 6,705

**Note G: Business Acquisition Reserves**

During the fiscal year ended May 31, 2003, the Company recorded reserves related to acquisitions in the amounts of \$10.0 million for severance and \$5.9 million for redundant lease costs. Activity for the three months ended August 31, 2008 for these reserves is summarized as follows:

In thousands	Balance as of May 31, 2008	Utilization of reserve	Balance as of August 31, 2008
Severance costs	\$ 149	\$ —	\$ 149
Redundant lease costs	\$ 742	\$ (74)	\$ 668

The remaining severance payments are expected to be complete during the fiscal year ending May 31, 2010. Redundant lease payments are expected to be completed during the fiscal year ending May 31, 2016. Payments of \$0.4 million extend beyond one year and are included in other long-term liabilities on the Consolidated Balance Sheets as of August 31, 2008.

**Note H: 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 thousands	For the three months ended	
	August 31,	
	2008	2007
Net income	\$ 148,709	\$ 151,075
Change in unrealized gains and losses of available-for-sale securities, net of taxes	6,256	5,565
Total comprehensive income	\$ 154,965	\$ 156,640

As of August 31, 2008, the accumulated other comprehensive income was \$22.3 million, which was net of taxes of \$12.1 million. As of May 31, 2008, the accumulated other comprehensive income was \$16.0 million, which was net of taxes of \$8.8 million.

**Note I: Commitments and Contingencies**

**Commitments:** As of August 31, 2008, the Company has 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 2009
Bank of America, N.A.	\$250 million	February 2009
PNC Bank, National Association	\$150 million	February 2009
Wells Fargo Bank, National Association	\$150 million	February 2009

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, 2008.

As of August 31, 2008 and May 31, 2008, the Company had irrevocable standby letters of credit outstanding totaling \$65.5 million, and \$71.5 million, respectively, required to secure commitments for certain insurance policies and bonding requirements. These letters of credit expire at various dates between November 2008 and December 2012 and are secured by securities held in the Company's investment portfolio. No amounts were outstanding on these letters of credit as of or during the three months ended August 31, 2008.

The Company enters into various purchase commitments with vendors in the ordinary course of business. As of August 31, 2008, the Company had outstanding commitments to purchase approximately \$11.0 million of capital assets.

**Note I: Commitments and Contingencies — continued**

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. 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. Historically, there have been no material losses related to such guarantees and indemnifications.

The Company 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 its business. These include disputes or potential disputes related to breach of contract, employment-related claims, tax claims, and other matters.

In August 2001, the Company's wholly owned subsidiary, Rapid Payroll, Inc. ("Rapid Payroll") informed 76 licensees that it intended to stop supporting their payroll processing software in August of 2002. Thereafter, lawsuits were commenced by licensees asserting various claims, including breach of contract and related tort and fraud causes of action. As previously reported in the Company's prior periodic reports, these lawsuits sought compensatory damages, punitive damages, and injunctive relief against Rapid Payroll, the Company, the Company's former Chief Executive Officer, and its Senior Vice President of Sales and Marketing. In accordance with the Company's indemnification agreements with its senior executives, the Company has agreed to defend and, if necessary, indemnify them in connection with these pending matters.

As of August 31, 2008, the Company has fully resolved its licensing responsibility and settled all litigation with 75 of the 76 licensees who were provided services by Rapid Payroll. In 2007, a verdict was issued in the *Brunskill Associates, Inc. v. Rapid Payroll, Inc. et al.* case, which was pending in California Superior Court, Los Angeles County, in which a jury awarded to the plaintiff \$15.0 million in compensatory damages and subsequently awarded an additional \$11.0 million in punitive damages. The Company is pursuing an appeal of that verdict.

The Company has a reserve for pending litigation matters. The litigation reserve has been adjusted in fiscal 2009 for incurred litigation expenditures. The Company's reserve for all pending litigation totaled \$22.9 million as of August 31, 2008, and is included in current liabilities on the Consolidated Balance Sheets.

In light of the reserve for all pending litigation matters, the Company's management currently believes that resolution of 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 the results of operations in the period in which any such effect is recorded.



**Note J: Supplemental Cash Flow Information**

Income taxes paid were \$0.5 million and \$0.4 million for the three months ended August 31, 2008 and 2007, respectively.

**Note K: Related Party Transactions**

During the three months ended August 31, 2008 and 2007, the Company purchased approximately \$0.3 million and \$2.2 million, respectively, 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.

**Note L: Subsequent Event**

On September 22, 2008, Paychex of New York LLC (the "Borrower"), a subsidiary of the Company entered into a one-year revolving credit facility with JPMorgan Chase Bank, National Association and Bank of America, National Association, which is collateralized by the long-term securities of the Borrower, to the extent of any borrowing (the "Credit Agreement"). Under the facility, the Borrower may, subject to certain restrictions, borrow up to \$400 million, to meet short-term funding requirements on client fund obligations. The obligations under this facility have been guaranteed by the Company and certain of its subsidiaries.

The Lenders commitments under the Credit Agreement will expire on September 20, 2009 and any borrowings outstanding will mature and be payable on such date. The revolving loans under the Credit Agreement will bear interest, at the Borrower's election, at an annual rate equal to one of the following:

- alternate base rate — the greatest of (i) JPMorgan Chase Bank's prime rate; (ii) Base CD rate plus 1%; or (iii) the federal funds effective rate plus .50%; or
- JPMorgan Chase Bank's money market-based rate; or
- LIBOR-based rate.

The Borrower will also pay a facility fee at a rate of .05% per annum on the average daily unused amount of the commitment.

The Credit Agreement includes various financial and other customary covenants with which the Borrower must comply in order to maintain borrowing availability and avoid penalties, including a limitation on the Borrower's ability to incur additional indebtedness, create liens, enter into consolidations or mergers, dispose of assets, make investments, pay dividends, or enter into transactions with affiliates. The Credit Agreement (and collateral security agreements executed in connection therewith) also contains customary events of default including, but not limited to, payment defaults, covenant defaults, cross-defaults to other indebtedness, material judgment defaults, inaccuracy of representations and warranties, bankruptcy and insolvency events, defects in the Lenders' security interest, change in control events, and material adverse changes.

Certain of the Lenders under the Credit Agreement, and their respective affiliates, have performed, and may in the future perform for the Company and its subsidiaries, various commercial banking, investment banking, underwriting, and other financial advisory services, for which they have received, and will receive, customary fees and expenses.

The foregoing description is qualified in its entirety by reference to the Credit Agreement, which is filed as Exhibit 10.1 hereto and incorporated herein by reference.

## 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, 2008 and August 31, 2007, and our financial condition as of August 31, 2008. 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, 2008 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, 2008 ("fiscal 2008"). 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 management 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 that are described in our filings with the Securities and Exchange Commission ("SEC"): general market and economic conditions including, among others, changes in United States employment and wage levels, changes in new hiring trends, changes in short- and long-term interest rates, and changes in the fair value and the credit rating of securities held by us; 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 possibility of penalties and losses resulting from errors and omissions in performing services; the possible inability of our clients to meet their payroll obligations; 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.

**Overview**

We are a leading provider of comprehensive payroll and integrated human resource and employee benefits outsourcing solutions for small- to medium-sized businesses. Our Payroll and Human Resource Services offer a portfolio of services and products that allow our clients to meet their diverse payroll and human resource needs.

Our Payroll services are provided through either our core payroll or Major Market Services, which is utilized by clients that have more sophisticated payroll and benefit needs, and include:

- payroll processing;
- payroll tax administration services;
- employee payment services; and
- regulatory compliance services (new-hire reporting and garnishment processing).

Our Human Resource Services primarily include:

- comprehensive human resource outsourcing services, which include Paychex Premier® Human Resources and our Professional Employer Organization (“PEO”);
- retirement services administration;
- workers’ compensation insurance services;
- health and benefits services;
- time and attendance solutions; and
- other human resource services and products.

We mainly earn revenue through recurring fees for services performed. Service revenue is primarily driven by the number of clients, checks or transactions per client per pay period, and utilization of ancillary services. We also earn interest on funds held for clients between the time of collection from our clients and remittance to the applicable tax or regulatory agencies or client employees. Our strategy is focused on achieving strong long-term financial performance by providing high-quality, timely, accurate, and affordable services; growing our client base; increasing utilization of our ancillary services; leveraging our technological and operating infrastructure; and expanding our service offerings.

Our financial results for the three months ended August 31, 2008 as compared to the three months ended August 31, 2007 include the following:

- Diluted earnings per share increased 3% to \$0.41 per share.
- Total revenue increased 5% to \$534.1 million.
- Payroll service revenue increased 5% to \$378.5 million.
- Human Resource Services revenue increased 16% to \$131.4 million.
- Operating income increased 5% to \$221.6 million.
- Operating income, net of certain items, increased 11% to \$197.4 million.

Refer to the discussion below for further information on this non-GAAP measure, operating income, net of certain items.

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Our financial performance during the three months ended August 31, 2008 was due to service revenue growth of 7% over the same period last year, and leveraging of expenses. The growth in service revenue was attributable to client base growth, price increases, and growth in the utilization of our ancillary services. The weak economy continues to impact revenue growth as new client payroll sales have slowed, losses due to clients going out of business have increased, and to a lesser extent, transaction volumes (such as checks per client which have decreased slightly over 1% in the last 12 months) have declined.

In addition to reporting operating income, a 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 11% to \$197.4 million for the three months ended August 31, 2008, as compared to \$178.3 million for the same period last year.

As of August 31, 2008, we maintained a strong financial position with cash and total corporate investments of \$519.1 million. Our primary source of cash is from our ongoing operations. Cash flows from operations were \$214.6 million for the three months ended August 31, 2008, as compared with \$253.2 million for the three months ended August 31, 2007. Cash flows from operations were higher for the three months ended August 31, 2007 due to the stock repurchase program. Historically, we have funded our operations, capital purchases, and dividend payments from our operating activities. It is anticipated that cash and total corporate investments as of August 31, 2008, 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 three months ended August 31, 2008, and our financial position as of August 31, 2008, refer to the analysis and discussion in the "Results of Operations," "Liquidity and Capital Resources," and "Critical Accounting Policies" sections of this review.

### **Investment Portfolio Overview**

We maintain a conservative investment strategy within our portfolio of available-for-sale securities to maximize liquidity and protect principal. Our exposure has been limited in the current investment environment as the result of our policies of investing in high credit quality securities with AAA and AA ratings and short-term securities with A-1/P-1 ratings and by limiting the amounts that can be invested in any single issuer.

As of September 22, 2008, we have sold substantially all of our variable rate demand notes ("VRDNs"). The VRDNs are money market securities held at par. No losses have resulted from these sales. We expect to be fully divested of VRDNs by the end of September 2008. Funds from VRDNs are being reinvested in agency discount notes. We have no auction rate securities in our investment portfolio. We had exited the auction rate market in the early fall of 2007 and have never experienced a failed auction. We have no exposure to sub-prime mortgage securities, asset-

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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. As of September 22, 2008, we do not have any position in prime money market funds.

### Outlook

Our outlook for the full fiscal year ending May 31, 2009 ("fiscal 2009") 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. We estimate the earnings effect of a 25-basis-point increase or decrease in the Federal Funds rate at the present time would be approximately \$4.5 million, after taxes, for the next twelve-month period. Projected revenue and net income growth for fiscal 2009 are as follows:

Payroll service revenue	5%	—	7%
Human Resource Services revenue	18%	—	21%
Total service revenue	8%	—	10%
Interest on funds held for clients	(25%)	—	(20%)
Total revenue	6%	—	8%
Investment income, net	(55%)	—	(50%)
Net income	2%	—	4%

Human Resource Services revenue growth is expected to accelerate slightly during the second half of fiscal 2009 as the second half of fiscal 2008 had been impacted by lower revenue from our time and attendance solutions and from the asset values from our retirement services funds.

Growth in operating income, net of certain items, is expected to approximate 11% to 13% for fiscal 2009. The effective income tax rate is expected to be approximately 34% throughout fiscal 2009.

Interest on funds held for clients and investment income are expected to be impacted by interest rate volatility. Based upon current interest rate and economic conditions, we expect interest on funds held for clients and investment income, net, to (decrease)/increase by the following amounts in the remaining respective quarters of fiscal 2009:

Fiscal 2009	Interest on funds held for clients	Investment income, net
Second quarter	(30%) — (25%)	(60%) — (55%)
Third quarter	(30%) — (25%)	(20%) — (15%)
Fourth quarter	(20%) — (15%)	0 — 5%

Remaining unchanged, purchases of property and equipment for fiscal 2009 are expected to be in the range of \$80 million to \$85 million, in line with our growth rates. Fiscal 2009 depreciation expense is projected to be approximately \$68 million, and we project amortization of intangible assets to be approximately \$20 million.

**RESULTS OF OPERATIONS****Summary of Results of Operations**

\$ in millions	For the three months ended		Change
	August 31,		
	2008	2007	
<b>Revenue:</b>			
Payroll service revenue	\$ 378.5	\$ 361.5	5%
Human Resource Services revenue	131.4	113.3	16%
Total service revenue	509.9	474.8	7%
Interest on funds held for clients	24.2	32.3	(25%)
<b>Total revenue</b>	<b>534.1</b>	<b>507.1</b>	<b>5%</b>
Combined operating and SG&A expenses	312.5	296.5	5%
<b>Operating income</b>	<b>221.6</b>	<b>210.6</b>	<b>5%</b>
As a % of total revenue	41%	42%	
Investment income, net	3.0	12.2	(75%)
<b>Income before income taxes</b>	<b>224.6</b>	<b>222.8</b>	<b>1%</b>
As a % of total revenue	42%	44%	
Income taxes	75.9	71.7	6%
<b>Net income</b>	<b>\$ 148.7</b>	<b>\$ 151.1</b>	<b>(2%)</b>
As a % of total revenue	28%	30%	
<b>Diluted earnings per share</b>	<b>\$ 0.41</b>	<b>\$ 0.40</b>	<b>3%</b>

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Details regarding our combined funds held for clients and corporate investment portfolios are as follows:

<b>\$ in millions</b>	<b>For the three months ended</b>	
	<b>August 31,</b>	
	<b>2008</b>	<b>2007</b>
<b>Average investment balances:</b>		
Funds held for clients	\$ 3,220.1	\$ 3,094.6
Corporate investments	484.5	1,227.6
Total	<u>\$ 3,704.6</u>	<u>\$ 4,322.2</u>
<b>Average interest rates earned (exclusive of net realized gains):</b>		
Funds held for clients	3.0%	4.2%
Corporate investments	2.6%	4.0%
Combined funds held for clients and corporate investments	2.9%	4.1%
<b>Net realized gains:</b>		
Funds held for clients	\$ 0.3	\$ 0.1
Corporate investments	—	—
Total	<u>\$ 0.3</u>	<u>\$ 0.1</u>
<b>As of :</b>		
<b>\$ in millions</b>	<b>August 31,</b>	<b>May 31,</b>
	<b>2008</b>	<b>2008</b>
Net unrealized gains on available-for-sale securities(1)	\$ 34.4	\$ 24.8
Federal Funds rate	2.00%	2.00%
Three-year “AAA” municipal securities yield	2.46%	2.65%
Total fair value of available-for-sale securities	\$ 3,988.9	\$ 3,353.5
Average duration of available-for-sale securities in years(2)	2.7	2.7
Weighted-average yield-to-maturity of available-for-sale securities(2)	3.3%	3.4%

(1) The net unrealized gain of our investment portfolio was approximately \$19.6 million as of September 22, 2008.

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

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**Revenue:** The 5% increase in Payroll service revenue for the three months ended August 31, 2008 compared with the same period last year was attributable to client base growth, price increases, and growth in utilization of our ancillary payroll services. The weak economy continues to impact growth through lower client payroll sales, lower transaction volume (checks per client decreased slightly over 1% in the last 12 months) and increases in clients going out of business.

Our payroll tax administration services were utilized by 93% of all clients as of August 31, 2008 and 2007. Our employee payment services were utilized by 73% of all clients as of August 31, 2008, compared with 72% as of August 31, 2007. Nearly all new clients purchase our payroll tax administration services and more than 80% of new clients select a form of our employee payment services.

Human Resource Services revenue increased 16% to \$131.4 million for the three months ended August 31, 2008. The following factors contributed to Human Resource Services revenue growth:

As of August 31,	2008	Change	2007	Change
Comprehensive human resource outsourcing services client employees served	446,000	17%	381,000	22%
Workers' compensation insurance clients	74,000	15%	65,000	19%
Retirement services clients	49,000	9%	45,000	18%
Asset value of retirement services client employees' funds (in billions)	\$ 9.4	7%	\$ 8.8	30%

For the three months ended August 31, 2008, interest on funds held for clients decreased primarily due to a lower average interest rates earned, partially offset by higher realized gains on sales of available-for-sale securities and higher average investment balances. The increase in average invested balances was driven by client base growth and wage inflation within our current 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		Change
	August 31,		
	2008	2007	
Compensation-related expenses	\$ 201.6	\$ 190.2	6%
Stock-based compensation costs	6.9	6.3	10%
Facilities expense	15.0	13.7	10%
Depreciation of property and equipment	15.9	15.0	6%
Amortization of intangible assets	4.8	4.1	17%
Other expenses	68.3	67.2	2%
Total operating and SG&A expenses	\$ 312.5	\$ 296.5	5%

Combined operating and SG&A expenses for the three months ended August 31, 2008 increased 5% as a result of increases in personnel and other costs related to selling and retaining clients, and promoting new services. As of August 31, 2008, we had approximately 12,500 employees compared with approximately 11,900 employees as of August 31, 2007.



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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. The increase in amortization was mainly due to intangibles from acquisitions during the three months ended August 31, 2007. Other expenses include such items as delivery, forms and supplies, communications, travel and entertainment, professional services, and other costs incurred to support our business.

**Operating income:** Operating income growth was 5% for the three months ended August 31, 2008, as compared with the same period last year. The increase in operating income was attributable to the factors previously discussed.

Operating income, net of certain items, excludes interest on funds held for clients. Refer to the discussion of operating income, net of certain items, in the "Overview" section on page 19 of this review. Operating income, net of certain items, is summarized as follows:

\$ in millions	For the three months ended		Change
	August 31,		
	2008	2007	
Operating income	\$ 221.6	\$ 210.6	5%
Excluding interest on funds held for clients	(24.2)	(32.3)	(25%)
Operating income, net of certain items	\$ 197.4	\$ 178.3	11%

**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. The decrease in investment income for the three months ended August 31, 2008 as compared to the same period last year is due to lower average investment balances resulting from the funding of the stock repurchase program commenced at the beginning of August 2007, and lower average interest rates earned.

**Income taxes:** Our effective income tax rate was 33.8% for the three months ended August 31, 2008 compared with 32.2% for the same period last year. The increase in the effective income tax rate is a result of lower levels of tax-exempt income derived from municipal debt securities held in our investment portfolios.

**Net income and earnings per share:** The decrease in net income was 2% for the three months ended August 31, 2008, as compared with the three months ended August 31, 2007. The decrease in net income was attributable to the factors previously discussed. Additionally, changes in interest rates since the same period last year unfavorably impacted net income by \$7.4 million, or 5%. Diluted earnings per share for the three months ended August 31, 2008 of \$0.41 per share increased 3% over \$0.40 per share for the same period last year. Diluted earnings per share increased at a greater rate than the net income change due to a lower number of weighted-average shares outstanding as a result of purchases under the stock repurchase program completed in fiscal 2008.

## LIQUIDITY AND CAPITAL RESOURCES

As of August 31, 2008, we had \$519.1 million in cash and total corporate investments. Cash and total corporate investments as of August 31, 2008, along with projected operating cash flows, are expected to support our normal business operations, capital purchases, and dividend payments for the foreseeable future.

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As of August 31, 2008, we have unused borrowing capacity available under four uncommitted, secured, short-term lines of credit at market rates of interest with financial institutions as follows:

<b>Financial institution</b>	<b>Amount available</b>	<b>Expiration date</b>
JP Morgan Chase Bank, N.A.	\$350 million	February 2009
Bank of America, N.A.	\$250 million	February 2009
PNC Bank, National Association	\$150 million	February 2009
Wells Fargo Bank, National Association	\$150 million	February 2009

The primary uses of the lines of credit would be to meet short-term funding requirements related to deposit account overdrafts and client fund deposit 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, 2008.

As of August 31, 2008, we had irrevocable standby letters of credit outstanding totaling \$65.5 million, required to secure commitments for certain of our insurance policies and bonding requirements. These letters of credit expire at various dates between November 2008 and December 2012 and are secured 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, 2008.

We enter into various purchase commitments with vendors in the ordinary course of business. As of August 31, 2008, we had outstanding commitments to purchase approximately \$11.0 million of capital assets.

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 our services under service arrangements with clients. 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 claims as they relate to their services provided to us. Historically, there have been no material losses related to such guarantees and indemnifications.

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.

**Reclassification Within Consolidated Statements of Cash Flows**

Client fund obligations represent our contractual obligation to remit funds to satisfy clients' payroll and tax payment obligations. To better reflect the nature of these activities, we have reclassified the net change in client fund obligations in the Consolidated Statements of Cash Flows from investing activities to financing activities for all periods presented. This reclassification had no impact on the net change in cash and cash equivalents or cash flows from operating activities for any periods presented. Refer to Note B in the Notes to Consolidated Financial Statements for more information on this reclassification.

**Operating Cash Flow Activities**

<b>In millions</b>	<b>For the three months ended</b>	
	<b>August 31,</b>	
	<b>2008</b>	<b>2007</b>
Net income	\$ 148.7	\$ 151.1
Non-cash adjustments to net income	40.7	35.6
Cash provided by changes in operating assets and liabilities	25.2	66.5
Net cash provided by operating activities	\$ 214.6	\$ 253.2

The decrease in our operating cash flows for the three months ended August 31, 2008 related primarily to changes in operating assets and liabilities. The fluctuation in operating assets and liabilities between periods was primarily the result of lower interest receivable balances and timing of collections and payments for compensation, PEO payroll, income tax, and other liabilities. During the three months ended August 31, 2007, other operating liabilities increased as a result of timing of payments for our stock repurchase program.

**Investing Cash Flow Activities**

<b>In millions</b>	<b>For the three months ended</b>	
	<b>August 31,</b>	
	<b>2008</b>	<b>2007</b>
Net change in funds held for clients and corporate investment activities	\$ (32.4)	\$ 749.0
Purchases of property and equipment, net of proceeds from the sale of property and equipment	(16.2)	(20.0)
Acquisition of businesses, net of cash acquired	—	(32.6)
Purchases of other assets	(1.3)	(1.7)
Net cash (used in)/provided by investing activities	\$ (49.9)	\$ 694.7

**Funds held for clients and corporate investments** : 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. The portfolio of funds held for clients and corporate investments is detailed in Note D of the Notes to Consolidated Financial Statements.

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 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. During the three months ended August 31, 2007, proceeds from sales and maturities of available-for-sale securities were not reinvested in

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anticipation of the \$1.0 billion stock repurchase program commenced in August 2007. Additional discussion of interest rates and related risks is included in the "Market Risk Factors" section of this review.

**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. We purchased approximately \$0.3 million and \$2.2 million of data processing equipment and software from EMC Corporation during the three months ended August 31, 2008 and 2007, respectively. The Chairman, President, and Chief Executive Officer of EMC Corporation is a member of our Board of Directors (the "Board").

Construction in progress totaled \$56.0 million as of August 31, 2008 and \$52.1 million as of May 31, 2008. Of these costs, \$55.1 million and \$51.6 million represent software being developed for internal use as of August 31, 2008 and May 31, 2008, respectively. Capitalization of costs ceases when software is ready for its intended use, at which time we will begin amortization of the costs. We expect amortization of a significant portion of the internal use software costs in construction in progress to begin in fiscal 2009, and to be amortized over fifteen years.

During the three months ended August 31, 2007, we paid \$32.6 million related to an immaterial acquisition.

### Financing Cash Flow Activities

In millions, except per share amounts	For the three months ended	
	August 31,	
	2008	2007
Net change in client fund obligations	\$ (160.5)	\$ (454.0)
Repurchases of common stock	—	(396.5)
Dividends paid	(111.9)	(115.0)
Proceeds from and excess tax benefit related to exercise of stock options	5.1	48.8
Net cash used in financing activities	\$ (267.3)	\$ (916.7)
Cash dividends per common share	\$ 0.31	\$ 0.30

**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.

**Repurchases of common stock:** During the three months ended August 31, 2007, we repurchased 8.9 million shares for a total of \$396.5 million under our stock repurchase program completed in fiscal 2008.

**Dividends paid:** In July 2008, our Board approved an increase of 3% in the quarterly dividend payment to \$0.31 per share from \$0.30 per share. The quarterly dividend of \$0.31 per share was paid August 15, 2008 to stockholders of record as of August 1, 2008. 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 the exercise of stock options and the excess tax benefit related to exercise of stock options is due to a decrease in the number of shares exercised to 0.2 million shares during the three months ended August 31, 2008 from 1.4 million shares during the three months ended August 31, 2007, and an decrease in the average exercise price per share.

#### **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 effect 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. In seeking to minimize the risks and/or costs associated with such activities, we generally direct investments towards high credit quality securities with AAA and AA ratings and short-term securities with A-1/P-1 ratings. We manage the available-for-sale securities to a benchmark duration of two and one-half to three years.

As of September 22, 2008, we have sold substantially all of our VRDNs. We expect to be fully divested of VRDNs by the end of September 2008. Funds from VRDNs are being reinvested in agency discount notes. We have no auction rate securities in our investment portfolio. We had exited the auction rate market in the early fall of 2007 and have never experienced a failed auction. We have no exposure to 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. As of September 22, 2008, we do not have any position in prime money market funds.

During the three months ended August 31, 2008, the average interest rate earned on our combined funds held for clients and corporate investment portfolios was 2.9% compared with 4.1% for the same period last year. 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 long- and short-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 will decrease earnings from our longer-term available-for-sale securities. Earnings from the available-for-sale-securities, which as of August 31, 2008 had an average duration of 2.7 years, excluding the impact of VRDNs tied to short-term interest rates, would not reflect decreases in interest rates until the investments are sold or mature and the proceeds are reinvested at lower rates.

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The cost and fair value of available-for-sale securities that had stated maturities as of August 31, 2008 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, 2008	
	Cost	Fair value
<b>Maturity date:</b>		
Due in one year or less	\$ 293.2	\$ 295.3
Due after one year through three years	697.1	708.8
Due after three years through five years	540.5	553.6
Due after five years	2,423.7	2,431.2
Total	\$ 3,954.5	\$ 3,988.9

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, 2008	Fiscal year ended May 31, 2008	Fiscal year ended May 31, 2007
Federal Funds rate — beginning of period	2.00%	5.25%	5.00%
Rate increase:			
First quarter	—	—	0.25
Second quarter	NA	(0.75)	—
Third quarter	NA	(1.50)	—
Fourth quarter	NA	(1.00)	—
Federal Funds rate — end of period	2.00%	2.00%	5.25%
Three-year “AAA” municipal securities yield — end of period	2.46%	2.65%	3.71%

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, a 25-basis-point change generally affects our tax-exempt interest rates by approximately 17 basis points.

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Our total investment portfolio (funds held for clients and corporate investments) is expected to average approximately \$4.0 billion for fiscal 2009. Our normal and anticipated allocation is approximately 55% invested in short-term and available-for-sale securities with an average duration of 35 days and 45% 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 \$34.4 million as of August 31, 2008, compared with a net unrealized gain of \$24.8 million as of May 31, 2008. During the three months ended August 31, 2008, the net unrealized gain ranged from \$4.4 million to \$34.8 million. Our investment portfolios reflected a net unrealized gain of approximately \$19.6 million as of September 22, 2008.

As of August 31, 2008 and May 31, 2008, we had \$4.0 billion and \$3.4 billion, respectively, invested in available-for-sale securities at fair value. The weighted-average yield-to-maturity was 3.3% and 3.4% as of August 31, 2008 and May 31, 2008, 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 as of August 31, 2008 would be in the range of \$12.5 million to \$13.0 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.

**Credit Risk:** We are exposed to credit risk in connection with these investments from the possible inability of the borrowers to meet the terms of their bonds. We attempt to mitigate this risk by investing primarily in high credit quality securities with AAA and AA ratings and short-term securities with an A-1/P-1 ratings, and by limiting amounts that can be invested in any single issuer.

We periodically 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, 2008 were not other-than-temporarily impaired. While certain available-for-sale securities had fair values that were below cost, we believe that it is probable that the principal and interest will be collected in accordance with contractual terms, and that the decline in the fair value was due to changes in interest rates and was not due to increased credit risk. As of August 31, 2008 and May 31, 2008, substantially all of the securities with an unrealized loss held an AA rating or better. We currently believe that we have the ability and intent to hold these investments until the earlier of market price recovery or maturity. 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 2008, filed with the SEC on July 18, 2008. 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;
- valuation of investments;
- goodwill and other intangible assets;
- accrual for client fund losses;
- contingent liabilities;
- stock-based compensation costs; and
- income taxes.

There have been no material changes in these aforementioned critical accounting policies, other than as required by adoption of new accounting pronouncements as described below.

Effective June 1, 2008, we adopted Financial Accounting Standards Board Statement of Financial Accounting Standard ("SFAS") No. 157, "Fair Value Measurements." This statement clarifies the definition of fair value, establishes a framework for measuring fair value and expands the disclosures on fair value measurements; however, does not require any new fair value measurements. The adoption of this standard has not had a material effect on our results of operations or financial position.

In determining the fair value of our assets and liabilities, we use various valuation approaches, predominately the market and income approaches. In determining the fair value of our available-for-sale securities, we utilize the Interactive Data Pricing service, a market approach. SFAS No. 157 establishes a hierarchy for information and valuations used in measuring fair value that is broken down into three levels based on its reliability. Level 1 valuations are based on quoted prices in active markets for identical assets or liabilities that we have the ability to access. Level 2 valuations are based on quoted prices in markets that are not active or for which all significant inputs are observable, directly or indirectly. Level 3 valuations are based on information that is unobservable and significant to the overall fair value measurement.



**Item 3. Quantitative and Qualitative Disclosures 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 our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

**Evaluation 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 Chief Executive Officer 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 Chief Executive Officer 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, 2008, that materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**PART II. OTHER INFORMATION**

**Item 1. Legal Proceedings**

See Note I of the Notes to Consolidated Financial Statements, which is incorporated herein by reference thereto, for information regarding legal proceedings.

**Item 5. Other Information**

On July 10, 2008, 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.

Additional information regarding compensation awarded to our directors for the year ended May 31, 2008 was provided in our Proxy Statement for our 2008 Annual Meeting of Stockholders, which was filed with the SEC on August 29, 2008.

**Item 6. Exhibits**

- 10.1 Credit Agreement dated as of September 22, 2008 among Paychex of New York LLC, as Borrower, and JPMorgan Chase Bank, National Association, as Administrative Agent, J.P. Morgan Securities Inc., as Co-Bookrunner and Co-Arranger, Bank of America, National Association, as Co-Arranger and Co-Bookrunner, and the Lenders Party Hereto, filed herewith.
- 10.2 Paychex, Inc. 2002 Stock Incentive Plan (as amended and restated effective October 12, 2005) Restricted Stock Award Agreement, incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed with the Commission on July 16, 2008.
- 10.3 Paychex, Inc. 2002 Stock Incentive Plan (as amended and restated effective October 12, 2005) Form of Non-Qualified Stock Option Award Agreement, incorporated by reference to Exhibit 10.2 to the Company's Form 8-K filed with the Commission on July 16, 2008.
- 10.4 Paychex, Inc. 2002 Stock Incentive Plan (as amended and restated effective October 12, 2005) 2008-2009 Officer Performance Incentive Award Agreement, incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed with the Commission on September 5, 2008.
- 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.

**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 24, 2008

/s/ Jonathan J. Judge

Jonathan J. Judge  
President and Chief Executive Officer

Date: September 24, 2008

/s/ John M. Morphy

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



CREDIT AGREEMENT

dated as of September 22, 2008

among

PAYCHEX OF NEW YORK LLC

as Borrower

and

JPMORGAN CHASE BANK,  
NATIONAL ASSOCIATION  
as Administrative Agent

J.P. MORGAN SECURITIES INC.,  
as Co-Bookrunner and Co-Arranger

BANK OF AMERICA,  
NATIONAL ASSOCIATION  
as Co-Arranger and Co-Bookrunner

and

The Lenders Party Hereto

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**SCHEDULES:**

- Schedule 2.01 — Commitments
- Schedule 4.06 — Disclosed Matters
- Schedule 7.01 — Existing Indebtedness
- Schedule 7.02 — Existing Liens
- Schedule 7.07 — Existing Restrictions

**EXHIBITS:**

The Registrant has omitted from this filing the Exhibits listed below. The Registrant will furnish supplementally to the Commission, upon request, a copy of any omitted exhibit.

- Exhibit A — Form of Assignment and Assumption
  - Exhibit B — Form of Collateral Spreadsheet
  - Exhibit C — Investment Policy
  - Exhibit D — Form of Borrowing Request
  - Exhibit E — Form of Interest Election Request
  - Exhibit F — Form of Opinion of Borrower's Counsel
  - Exhibit G — Form of Compliance Certificate
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CREDIT AGREEMENT dated as of September 22, 2008, among PAYCHEX OF NEW YORK LLC, the LENDERS party hereto, JPMORGAN CHASE BANK, NATIONAL ASSOCIATION, as Administrative Agent, and BANK OF AMERICA, N.A., as Co-Arranger and Co-Bookrunner.

The parties hereto agree as follows:

**ARTICLE I.**  
**DEFINITIONS**

SECTION 1.01. Defined Terms. As used in this Agreement, the following terms have the meanings specified below:

“ABR”, when used in reference to any Loan or Borrowing, refers to whether such Loan, or the Loans comprising such Borrowing, are bearing interest at a rate determined by reference to the Alternate Base Rate.

“Accounts” means the Accounts as defined in the Intercreditor Agreement.

“Adjusted LIBO Rate” means, with respect to any Eurodollar Borrowing for any day, an interest rate per annum equal to (a) the Overnight LIBO Rate for such day multiplied by (b) the Statutory Reserve Rate.

“Administrative Agent” means JPMorgan Chase Bank, in its capacity as administrative agent for the Lenders hereunder.

“Administrative Questionnaire” means an Administrative Questionnaire in a form supplied by the Administrative Agent.

“Affiliate” means, with respect to a specified Person, another Person that directly, or indirectly through one or more intermediaries, Controls or is Controlled by or is under common Control with the Person specified.

“Alternate Base Rate” means, for any day, a rate per annum equal to the greatest of (a) the Prime Rate in effect on such day, (b) the Base CD Rate in effect on such day plus 1% and (c) the Federal Funds Effective Rate in effect on such day plus  $\frac{1}{2}$  of 1%. Any change in the Alternate Base Rate due to a change in the Prime Rate, the Base CD Rate or the Federal Funds Effective Rate shall be effective from and including the effective date of such change in the Prime Rate, the Base CD Rate or the Federal Funds Effective Rate, respectively.

“Applicable Percentage” means, with respect to any Lender, the percentage of the total Commitments represented by such Lender’s Commitment. If the Commitments have terminated or expired, the Applicable Percentages shall be determined based upon the Commitments most recently in effect, giving effect to any assignments.

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“Applicable Rate” means, for any day, (a) with respect to any Money Market Revolving Loan, 0.18% per annum, and (b) with respect to any Eurodollar Revolving Loan, 0.18% per annum.

“Approved Fund” has the meaning assigned to such term in Section 10.04.

“Assessment Rate” means, for any day, the annual assessment rate in effect on such day that is payable by a member of the Bank Insurance Fund classified as “well-capitalized” and within supervisory subgroup “B” (or a comparable successor risk classification) within the meaning of 12 C.F.R. Part 327 (or any successor provision) to the Federal Deposit Insurance Corporation for insurance by such Corporation of time deposits made in dollars at the offices of such member in the United States; provided that if, as a result of any change in any law, rule or regulation, it is no longer possible to determine the Assessment Rate as aforesaid, then the Assessment Rate shall be such annual rate as shall be determined by the Administrative Agent to be representative of the cost of such insurance to the Lenders.

“Assignment and Assumption” means an assignment and assumption entered into by a Lender and an assignee (with the consent of any party whose consent is required by Section 10.04), and accepted by the Administrative Agent, in the form of Exhibit A or any other form approved by the Administrative Agent.

“Authorized Person” means any of the following, acting individually: (a) Jonathan J. Judge, (b) John M. Murphy, (c) Melinda Janik, or (d) such other persons who may be designated in writing by Borrower as an Authorized Person.

“Availability Period” means the period from and including the Effective Date to but excluding the earlier of the Maturity Date and the date of termination of the Commitments.

“Base CD Rate” means the sum of (a) the Three-Month Secondary CD Rate multiplied by the Statutory Reserve Rate plus (b) the Assessment Rate.

“Board” means the Board of Governors of the Federal Reserve System of the United States of America.

“Borrower” means Paychex of New York LLC, a Delaware limited liability company.

“Borrowing” means Revolving Loans of the same Type, made, converted or continued on the same date.

“Borrowing Request” means a request by the Borrower for a Revolving Borrowing in accordance with Section 2.03.

“Business Day” means any day that is not a Saturday, Sunday or other day on which commercial banks in New York City are authorized or required by law to remain closed; provided that, when used in connection with a Eurodollar Loan, the term “Business Day” shall also exclude any day on which banks are not open for dealings in dollar deposits in the London interbank market.

“Capital Lease Obligations” of any Person means the obligations of such Person to pay rent or other amounts under any lease of (or other arrangement conveying the right to use) real or personal property, or a combination thereof, which obligations are required to be classified and accounted for as capital leases on a balance sheet of such Person under GAAP, and the amount of such obligations shall be the capitalized amount thereof determined in accordance with GAAP.

“Change in Control” means (a) the acquisition of ownership, directly or indirectly, beneficially or of record, by any Person or group (within the meaning of the Securities Exchange Act of 1934 and the rules of the Securities and Exchange Commission thereunder as in effect on the date hereof) other than an Affiliate of the Borrower of Equity Interests representing more than 50% of the aggregate ordinary voting power represented by the issued and outstanding Equity Interests of any Parent Entity; (b) occupation of a majority of the seats (other than vacant seats) on the board of directors of any Parent Entity or the Borrower by Persons who were neither (i) nominated by the board of directors of such Parent Entity or the Borrower nor (ii) appointed by directors so nominated; or (c) the acquisition of direct or indirect Control of the Borrower by any Person or group other than a Parent Entity.

“Change in Law” means (a) the adoption of any law, rule or regulation after the date of this Agreement, (b) any change in any law, rule or regulation or in the interpretation or application thereof by any Governmental Authority after the date of this Agreement or (c) compliance by any Lender (or, for purposes of Section 2.12(b), by any lending office of such Lender or by such Lender’s holding company, if any) with any request, guideline or directive (whether or not having the force of law) of any Governmental Authority made or issued after the date of this Agreement.

“Code” means the Internal Revenue Code of 1986, as amended from time to time.

“Collateral” has the meaning given to such term in the Pledge Security Agreement.

“Collateral Account” has the meaning given such term in the Pledge Security Agreement.

“Collateral Spreadsheet” means a spreadsheet provided by the Borrower showing the Net Market Value of the Collateral in each of the Accounts and, if any of the Collateral has been segregated, the Collateral Account (each as defined in the Pledge Security Agreement), a form of which is attached hereto as Exhibit B.

“Commitment” means, with respect to each Lender, the commitment of such Lender to make Revolving Loans hereunder, expressed as an amount representing the maximum aggregate amount of such Lender’s Revolving Credit Exposure hereunder, as such commitment may be (a) reduced from time to time pursuant to Section 2.06 and (b) reduced or increased from time to time pursuant to assignments by or to such Lender pursuant to Section 10.04. The initial amount of each Lender’s Commitment is set forth on Schedule 2.01, or in the Assignment and Assumption pursuant to which such Lender shall have assumed its Commitment, as applicable. The initial aggregate amount of the Lenders’ Commitments is \$400,000,000.

“Control” means the possession, directly or indirectly, of the power to direct or cause the direction of the management or policies of a Person, whether through the ability to exercise

voting power, by contract or otherwise. “Controlling” and “Controlled” have meanings correlative thereto.

“Credit Documents” means this Agreement, the Guarantee Agreement, the Intercreditor Agreement, the Security Documents, and any other documents entered into by any of the parties hereto in connection with the foregoing, and as the same may be amended, modified, restated, or extended from time to time.

“Default” means any event or condition which constitutes an Event of Default or which upon notice, lapse of time or both would, unless cured or waived, become an Event of Default.

“Disclosed Matters” means the actions, suits and proceedings and the environmental matters disclosed in Schedule 4.06.

“dollars” or “\$” refers to lawful money of the United States of America.

“Effective Date” means the date on which the conditions specified in Section 5.01 are satisfied (or waived in accordance with Section 10.02).

“Environmental Laws” means all laws, rules, regulations, codes, ordinances, orders, decrees, judgments, injunctions, notices or binding agreements issued, promulgated or entered into by any Governmental Authority, relating in any way to the environment, preservation or reclamation of natural resources, the management, release or threatened release of any Hazardous Material or to health and safety matters.

“Environmental Liability” means any liability, contingent or otherwise (including any liability for damages, costs of environmental remediation, fines, penalties or indemnities), of the Borrower or any Subsidiary directly or indirectly resulting from or based upon (a) violation of any Environmental Law, (b) the generation, use, handling, transportation, storage, treatment or disposal of any Hazardous Materials, (c) exposure to any Hazardous Materials, (d) the release or threatened release of any Hazardous Materials into the environment or (e) any contract, agreement or other consensual arrangement pursuant to which liability is assumed or imposed with respect to any of the foregoing.

“Equity Interests” means shares of capital stock, partnership interests, membership interests in a limited liability company, beneficial interests in a trust or other equity ownership interests in a Person, and any warrants, options or other rights entitling the holder thereof to purchase or acquire any such equity interest.

“ERISA” means the Employee Retirement Income Security Act of 1974, as amended from time to time.

“ERISA Affiliate” means any trade or business (whether or not incorporated) that, together with the Borrower, is treated as a single employer under Section 414(b) or (c) of the Code or, solely for purposes of Section 302 of ERISA and Section 412 of the Code, is treated as a single employer under Section 414 of the Code.

“ERISA Event” means (a) any “reportable event”, as defined in Section 4043 of ERISA or the regulations issued thereunder with respect to a Plan (other than an event for which the 30-day notice period is waived); (b) the existence with respect to any Plan of an “accumulated funding deficiency” (as defined in Section 412 of the Code or Section 302 of ERISA), whether or not waived; (c) the filing pursuant to Section 412(d) of the Code or Section 303(d) of ERISA of an application for a waiver of the minimum funding standard with respect to any Plan; (d) the incurrence by the Borrower or any of its ERISA Affiliates of any liability under Title IV of ERISA with respect to the termination of any Plan; (e) the receipt by the Borrower or any ERISA Affiliate from the PBGC or a plan administrator of any notice relating to an intention to terminate any Plan or Plans or to appoint a trustee to administer any Plan; (f) the incurrence by the Borrower or any of its ERISA Affiliates of any liability with respect to the withdrawal or partial withdrawal from any Plan or Multiemployer Plan; or (g) the receipt by the Borrower or any ERISA Affiliate of any notice, or the receipt by any Multiemployer Plan from the Borrower or any ERISA Affiliate of any notice, concerning the imposition of Withdrawal Liability or a determination that a Multiemployer Plan is, or is expected to be, insolvent or in reorganization, within the meaning of Title IV of ERISA.

“Eurodollar”, when used in reference to any Loan or Borrowing, refers to whether such Loan, or the Loans comprising such Borrowing, are bearing interest at a rate determined by reference to the Adjusted LIBO Rate.

“Event of Default” has the meaning assigned to such term in ARTICLE VIII.

“Excluded Taxes” means, with respect to the Administrative Agent, any Lender, or any other recipient of any payment to be made by or on account of any obligation of the Borrower hereunder, (a) income or franchise taxes imposed on (or measured by) its net income by the United States of America, or by the jurisdiction under the laws of which such recipient is organized or in which its principal office is located or, in the case of any Lender, in which its applicable lending office is located, (b) any branch profits taxes imposed by the United States of America or any similar tax imposed by any other jurisdiction in which the Borrower is located and (c) in the case of a Foreign Lender (other than an assignee pursuant to a request by the Borrower under Section 2.15(b)), any withholding tax that is imposed on amounts payable to such Foreign Lender at the time such Foreign Lender becomes a party to this Agreement (or designates a new lending office) or is attributable to such Foreign Lender’s failure to comply with Section 2.13(e), except to the extent that such Foreign Lender (or its assignor, if any) was entitled, at the time of designation of a new lending office (or assignment), to receive additional amounts from the Borrower with respect to such withholding tax pursuant to Section 2.13(a).

“Federal Funds Effective Rate” means, for any day, the weighted average (rounded upwards, if necessary, to the next 1/100 of 1%) of the rates on overnight Federal funds transactions with members of the Federal Reserve System arranged by Federal funds brokers, as published on the next succeeding Business Day by the Federal Reserve Bank of New York, or, if such rate is not so published for any day that is a Business Day, the average (rounded upwards, if necessary, to the next 1/100 of 1%) of the quotations for such day for such transactions received by the Administrative Agent from three Federal funds brokers of recognized standing selected by it.

“Financial Officer” means the chief financial officer, principal accounting officer, treasurer or controller of the Borrower.

“Foreign Lender” means any Lender that is organized under the laws of a jurisdiction other than that in which the Borrower is located. For purposes of this definition, the United States of America, each State thereof and the District of Columbia shall be deemed to constitute a single jurisdiction.

“GAAP” means generally accepted accounting principles in the United States of America.

“Governmental Authority” means the government of the United States of America, any other nation or any political subdivision thereof, whether state or local, and any agency, authority, instrumentality, regulatory body, court, central bank or other entity exercising executive, legislative, judicial, taxing, regulatory or administrative powers or functions of or pertaining to government.

“Guarantee” of or by any Person (the “guarantor”) means any obligation, contingent or otherwise, of the guarantor guaranteeing or having the economic effect of guaranteeing any Indebtedness or other obligation of any other Person (the “primary obligor”) in any manner, whether directly or indirectly, and including any obligation of the guarantor, direct or indirect, (a) to purchase or pay (or advance or supply funds for the purchase or payment of) such Indebtedness or other obligation or to purchase (or to advance or supply funds for the purchase of) any security for the payment thereof, (b) to purchase or lease property, securities or services for the purpose of assuring the owner of such Indebtedness or other obligation of the payment thereof, (c) to maintain working capital, equity capital or any other financial statement condition or liquidity of the primary obligor so as to enable the primary obligor to pay such Indebtedness or other obligation or (d) as an account party in respect of any letter of credit or letter of guaranty issued to support such Indebtedness or obligation; provided, that the term Guarantee shall not include endorsements for collection or deposit in the ordinary course of business.

“Guarantee Agreement” means the Guarantee Agreement dated on or about the date hereof made by the Guarantors in favor of the Administrative Agent and the Lenders, and as the same may be amended, modified, restated, or extended from time to time.

“Guarantors” means, collectively, Paychex Inc., Paychex Investment Partnership LP, Paychex of North America, Inc., Advantage Payroll Services, Inc., Paychex Recordkeeping Services, Inc., and Paychex Benefit Technologies Inc.

“Hazardous Materials” means all explosive or radioactive substances or wastes and all hazardous or toxic substances, wastes or other pollutants, including petroleum or petroleum distillates, asbestos or asbestos containing materials, polychlorinated biphenyls, radon gas, infectious or medical wastes and all other substances or wastes of any nature regulated pursuant to any Environmental Law.

“Indebtedness” of any Person means, without duplication, (a) all obligations of such Person for borrowed money or with respect to deposits or advances of any kind, (b) all obligations of such Person evidenced by bonds, debentures, notes or similar instruments, (c) all

obligations of such Person upon which interest charges are customarily paid, (d) all obligations of such Person under conditional sale or other title retention agreements relating to property acquired by such Person, (e) all obligations of such Person in respect of the deferred purchase price of property or services (excluding current accounts payable incurred in the ordinary course of business), (f) all Indebtedness of others secured by (or for which the holder of such Indebtedness has an existing right, contingent or otherwise, to be secured by) any Lien on property owned or acquired by such Person, whether or not the Indebtedness secured thereby has been assumed, (g) all Guarantees by such Person of Indebtedness of others, (h) all Capital Lease Obligations of such Person, (i) all obligations, contingent or otherwise, of such Person as an account party in respect of letters of credit and letters of guaranty and (j) all obligations, contingent or otherwise, of such Person in respect of bankers' acceptances. The Indebtedness of any Person shall include the Indebtedness of any other entity (including any partnership in which such Person is a general partner) to the extent such Person is liable therefor as a result of such Person's ownership interest in or other relationship with such entity, except to the extent the terms of such Indebtedness provide that such Person is not liable therefor.

“Indemnified Taxes” means Taxes other than Excluded Taxes.

“Index Debt” means senior, unsecured, long-term indebtedness for borrowed money of the Borrower that is not guaranteed by any other Person or subject to any other credit enhancement.

“Intercreditor Agreement” means the Amended and Restated Intercreditor Agreement dated on or about the date hereof among the Administrative Agent, Bank of America, N.A., Wells Fargo Bank, N.A., and other financial institutions offering discretionary advised lines of credit to the Borrower from time to time, and as the same may be amended, modified, restated, or extended from time to time.

“Interest Election Request” means a request by the Borrower to convert or continue a Revolving Borrowing in accordance with Section 2.05.

“Interest Payment Date” means with respect to any Loan the last day of each calendar month.

“Lenders” means the Persons listed on Schedule 2.01 and any other Person that shall have become a party hereto pursuant to an Assignment and Assumption, other than any such Person that ceases to be a party hereto pursuant to an Assignment and Assumption.

“Lien” means, with respect to any asset, (a) any mortgage, deed of trust, lien, pledge, hypothecation, encumbrance, charge or security interest in, on or of such asset, (b) the interest of a vendor or a lessor under any conditional sale agreement, capital lease or title retention agreement (or any financing lease having substantially the same economic effect as any of the foregoing) relating to such asset and (c) in the case of securities, any purchase option, call or similar right of a third party with respect to such securities.

“Loans” means the loans made by the Lenders to the Borrower pursuant to this Agreement.

“Material Adverse Effect” means a material adverse effect on (a) the business, assets, operations, prospects or condition, financial or otherwise, of the Borrower and its Subsidiaries taken as a whole or (b) the validity or enforceability of any of the Credit Documents or the rights or remedies of the Administrative Agent and the Lenders thereunder.

“Material Indebtedness” means Indebtedness (other than the Loans), or obligations in respect of one or more Swap Agreements, of any one or more of the Borrower and its Subsidiaries in an aggregate principal amount exceeding \$500,000,000. For purposes of determining Material Indebtedness, the “principal amount” of the obligations of the Borrower or any Subsidiary in respect of any Swap Agreement at any time shall be the maximum aggregate amount (giving effect to any netting agreements) that the Borrower or such Subsidiary would be required to pay if such Swap Agreement were terminated at such time.

“Maturity Date” means September 20, 2009.

“Money Market”, when used in reference to any Loan or Borrowing, refers to whether such Loan, or the Loans comprising such Borrowing, are bearing interest at a rate determined by reference to the Money Market Rate.

“Money Market Rate” means, for any day, a rate per annum equal to the rate quoted by the Administrative Agent as its money market rate for such day.

“Moody’s” means Moody’s Investors Service, Inc.

“Multiemployer Plan” means a multiemployer plan as defined in Section 4001(a)(3) of ERISA.

“Net Market Value” shall have the meaning given to such term in the Pledge Security Agreement.

“Obligations” means all advances to, and debts, liabilities, obligations, covenants and duties of, the Borrower arising under any Credit Document or otherwise with respect to any Loan, whether direct or indirect (including those acquired by assumption), absolute or contingent, due or to become due, now existing or hereafter arising and including interest and fees that accrue after the commencement by or against the Borrower or any Affiliate thereof of any proceeding under any bankruptcy or insolvency laws naming such Person as the debtor in such proceeding, regardless of whether such interest and fees are allowed claims in such proceeding.

“Other Taxes” means any and all present or future stamp or documentary taxes or any other excise or property taxes, charges or similar levies arising from any payment made hereunder or from the execution, delivery or enforcement of, or otherwise with respect to, this Agreement.

“Overnight LIBO Rate” means, with respect to any Eurodollar Borrowing for any day, the rate appearing on Page 3750 of the Dow Jones Market Service (or on any successor or substitute page of such Service, or any successor to or substitute for such Service, providing rate quotations comparable to those currently provided on such page of such Service, as determined



by the Administrative Agent from time to time for purposes of providing quotations of interest rates applicable to dollar deposits in the London interbank market), as the rate for overnight dollar deposits for delivery on such day. In the event that such rate is not available at such time for any reason, then the “Overnight LIBO Rate” with respect to such Eurodollar Borrowing on such day shall be the rate at which overnight dollar deposits for delivery on such day are offered by the principal London office of the Administrative Agent in immediately available funds in the London interbank market.

“Parent Entity” means Paychex, Inc. and/or PXC Inc., as applicable.

“Participant” has the meaning set forth in Section 10.04.

“PBGC” means the Pension Benefit Guaranty Corporation referred to and defined in ERISA and any successor entity performing similar functions.

“Permitted Acquisitions” means any acquisition consummated after the Effective Date, by the Borrower, any Guarantor, or any Subsidiary thereof, so long as, in each case, (a) no Default or Event of Default exists or would result from the acquisition immediately after such acquisition, and (b) in the event (i) the purchase price in the acquisition equals or exceeds \$75,000,000, and (ii) there are any outstanding Loans or the Borrower intends to borrow any Loans at such time, the Borrower shall provide the Agent and the Lenders prior written notice of any such proposed acquisition, including a reasonably detailed description thereof, such notice to be given on the date such acquisition becomes public. On the date such notice is required to be given, the Lenders shall be deemed to have requested segregation in accordance with section 3.2 of the Pledge Security Agreement and the Borrower shall immediately take all actions necessary to segregate Collateral sufficient to cover the outstanding and requested Loans.

“Permitted Encumbrances” means:

- (a) Liens imposed by law for taxes that are not yet due or are being contested in compliance with Section 6.04;
- (b) carriers’, warehousemen’s, mechanics’, materialmen’s, repairmen’s and other like Liens imposed by law, arising in the ordinary course of business and securing obligations that are not overdue by more than 30 days or are being contested in compliance with Section 6.04;
- (c) pledges and deposits made in the ordinary course of business in compliance with workers’ compensation, unemployment insurance and other social security laws or regulations;
- (d) deposits to secure the performance of bids, trade contracts, leases, statutory obligations, surety and appeal bonds, performance bonds and other obligations of a like nature, in each case in the ordinary course of business;
- (e) judgment liens in respect of judgments that do not constitute an Event of Default under clause (k) of ARTICLE VIII; and

(f) easements, zoning restrictions, rights-of-way and similar encumbrances on real property imposed by law or arising in the ordinary course of business that do not secure any monetary obligations and do not materially detract from the value of the affected property or interfere with the ordinary conduct of business of the Borrower or any Subsidiary;

provided that the term “Permitted Encumbrances” shall not include any Lien securing Indebtedness.

“Permitted Investments” means investments in accordance with the Investment Policy approved by the Board of Directors of Paychex, Inc. attached hereto as Exhibit C, as modified from time to time, provided that any such modifications conform in quality to the then current Investment Policy, and the Administrative Agent is promptly informed of all such modifications as set forth in Section 10.01.

“Person” means any natural person, corporation, limited liability company, trust, joint venture, association, company, partnership, Governmental Authority or other entity.

“Plan” means any employee pension benefit plan (other than a Multiemployer Plan) subject to the provisions of Title IV of ERISA or Section 412 of the Code or Section 302 of ERISA, and in respect of which the Borrower or any ERISA Affiliate is (or, if such plan were terminated, would under Section 4069 of ERISA be deemed to be) an “employer” as defined in Section 3(5) of ERISA.

“Pledge Security Agreement” means that certain Pledge Security Agreement dated on or about the date hereof among the Borrower, the Administrative Agent and each Lender, and as the same may be amended, modified, restated, or extended from time to time.

“Primary Obligations” shall have the meaning given to such term in the Pledge Security Agreement.

“Prime Rate” means the rate of interest per annum publicly announced from time to time by JPMorgan Chase Bank as its prime rate in effect at its office located at 270 Park Avenue, New York, New York; each change in the Prime Rate shall be effective from and including the date such change is publicly announced as being effective.

“Register” has the meaning set forth in Section 10.04.

“Related Parties” means, with respect to any specified Person, such Person’s Affiliates and the respective directors, officers, employees, agents and advisors of such Person and such Person’s Affiliates.

“Required Lenders” means, at any time that there are three or fewer Lenders, Lenders having Revolving Credit Exposures and unused Commitments representing more than 75% of the sum of the total of the total Revolving Credit Exposures and unused Commitments at such time, and at any time that there are four or more Lenders, Lenders having Revolving Credit Exposures and unused Commitments representing more than 66 2/3% of the sum of the total of the total Revolving Credit Exposures and unused Commitments at such time.

“Restricted Payment” means any dividend or other distribution (whether in cash, securities or other property) with respect to any Equity Interests in the Borrower or any Subsidiary, or any payment (whether in cash, securities or other property), including any sinking fund or similar deposit, on account of the purchase, redemption, retirement, acquisition, cancellation or termination of any such Equity Interests in the Borrower or any option, warrant or other right to acquire any such Equity Interests in the Borrower.

“Revolving Credit Exposure” means, with respect to any Lender at any time, the sum of the outstanding principal amount of such Lender’s Revolving Loans at such time.

“Revolving Loan” means a Loan made pursuant to Section 2.03.

“S&P” means Standard & Poor’s.

“Securities Intermediary” means JPMorgan Chase Bank, N.A., in its capacity as securities intermediary pursuant to the Security Documents.

“Security Documents” means the Pledge Security Agreement and any and all control agreements and any other documentation entered into by the Borrower, any Guarantor and/or the Secured Parties evidencing or perfecting the Secured Parties’ rights in the Collateral.

“Secured Party” shall have the meaning given to such term in Section 3.02.

“Statutory Reserve Rate” means a fraction (expressed as a decimal), the numerator of which is the number one and the denominator of which is the number one minus the aggregate of the maximum reserve percentages (including any marginal, special, emergency or supplemental reserves) expressed as a decimal established by the Board to which the Administrative Agent is subject (a) with respect to the Base CD Rate, for new negotiable nonpersonal time deposits in dollars of over \$100,000 with maturities approximately equal to three months and (b) with respect to the Adjusted LIBO Rate, for eurocurrency funding (currently referred to as “Eurocurrency Liabilities” in Regulation D of the Board). Such reserve percentages shall include those imposed pursuant to such Regulation D. Eurodollar Loans shall be deemed to constitute eurocurrency funding and to be subject to such reserve requirements without benefit of or credit for proration, exemptions or offsets that may be available from time to time to any Lender under such Regulation D or any comparable regulation. The Statutory Reserve Rate shall be adjusted automatically on and as of the effective date of any change in any reserve percentage.

“subsidiary” means, with respect to any Person (the “parent”) at any date, any corporation, limited liability company, partnership, association or other entity the accounts of which would be consolidated with those of the parent in the parent’s consolidated financial statements if such financial statements were prepared in accordance with GAAP as of such date, as well as any other corporation, limited liability company, partnership, association or other entity (a) of which securities or other ownership interests representing more than 50% of the equity or more than 50% of the ordinary voting power or, in the case of a partnership, more than 50% of the general partnership interests are, as of such date, owned, controlled or held, or (b) that is, as of such date, otherwise Controlled, by the parent or one or more subsidiaries of the parent or by the parent and one or more subsidiaries of the parent.

“Subsidiary” means any subsidiary of the Borrower.

“Swap Agreement” means any agreement with respect to any swap, forward, future or derivative transaction or option or similar agreement involving, or settled by reference to, one or more rates, currencies, commodities, equity or debt instruments or securities, or economic, financial or pricing indices or measures of economic, financial or pricing risk or value or any similar transaction or any combination of these transactions; provided that no phantom stock or similar plan providing for payments only on account of services provided by current or former directors, officers, employees or consultants of the Borrower or the Subsidiaries shall be a Swap Agreement.

“Taxes” means any and all present or future taxes, levies, imposts, duties, deductions, charges or withholdings imposed by any Governmental Authority.

“Three-Month Secondary CD Rate” means, for any day, the secondary market rate for three-month certificates of deposit reported as being in effect on such day (or, if such day is not a Business Day, the next preceding Business Day) by the Board through the public information telephone line of the Federal Reserve Bank of New York (which rate will, under the current practices of the Board, be published in Federal Reserve Statistical Release H.15(519) during the week following such day) or, if such rate is not so reported on such day or such next preceding Business Day, the average of the secondary market quotations for three-month certificates of deposit of major money center banks in New York City received at approximately 10:00 a.m., New York City time, on such day (or, if such day is not a Business Day, on the next preceding Business Day) by the Administrative Agent from three negotiable certificate of deposit dealers of recognized standing selected by it.

“Transactions” means the execution, delivery and performance by the Borrower of this Agreement, the borrowing of Loans, and the use of the proceeds thereof hereunder.

“Type”, when used in reference to any Loan or Borrowing, refers to whether the rate of interest on such Loan, or on the Loans comprising such Borrowing, is determined by reference to the Adjusted LIBO Rate, the Money Market Rate or the Alternate Base Rate.

“Withdrawal Liability” means liability to a Multiemployer Plan as a result of a complete or partial withdrawal from such Multiemployer Plan, as such terms are defined in Part I of Subtitle E of Title IV of ERISA.

SECTION 1.02. Classification of Loans and Borrowings. For purposes of this Agreement, Loans may be classified and referred to by class e.g., a “Revolving Loan”) or by Type (e.g., a “Eurodollar Loan”) or by class and Type (e.g., a “Eurodollar Revolving Loan”). Borrowings also may be classified and referred to by class e.g., a “Revolving Borrowing”) or by Type (e.g., a “Eurodollar Borrowing”) or by class and Type (e.g., a “Eurodollar Revolving Borrowing”).

SECTION 1.03. Terms Generally. The definitions of terms herein shall apply equally to the singular and plural forms of the terms defined. Whenever the context may require, any pronoun shall include the corresponding masculine, feminine and neuter forms. The words “include”, “includes” and “including” shall be deemed to be followed by the phrase “without limitation”. The word “will” shall be construed to have the same meaning and effect as the word “shall”. Unless the context

requires otherwise (a) any definition of or reference to any agreement, instrument or other document herein shall be construed as referring to such agreement, instrument or other document as from time to time amended, supplemented or otherwise modified (subject to any restrictions on such amendments, supplements or modifications set forth herein), (b) any reference herein to any Person shall be construed to include such Person's successors and assigns, (c) the words "herein", "hereof" and "hereunder", and words of similar import, shall be construed to refer to this Agreement in its entirety and not to any particular provision hereof, (d) all references herein to Articles, Sections, Exhibits and Schedules shall be construed to refer to Articles and Sections of, and Exhibits and Schedules to, this Agreement and (e) the words "asset" and "property" shall be construed to have the same meaning and effect and to refer to any and all tangible and intangible assets and properties, including cash, securities, accounts and contract rights.

SECTION 1.04. Accounting Terms: GAAP. Except as otherwise expressly provided herein, all terms of an accounting or financial nature shall be construed in accordance with GAAP, as in effect from time to time; provided that, if the Borrower notifies the Administrative Agent that the Borrower requests an amendment to any provision hereof to eliminate the effect of any change occurring after the date hereof in GAAP or in the application thereof on the operation of such provision (or if the Administrative Agent notifies the Borrower that the Required Lenders request an amendment to any provision hereof for such purpose), regardless of whether any such notice is given before or after such change in GAAP or in the application thereof, then such provision shall be interpreted on the basis of GAAP as in effect and applied immediately before such change shall have become effective until such notice shall have been withdrawn or such provision amended in accordance herewith.

## **ARTICLE II. THE CREDITS**

SECTION 2.01. Commitments. Subject to the terms and conditions set forth herein, each Lender agrees to make Revolving Loans to the Borrower from time to time during the Availability Period in an aggregate principal amount that will not result in such Lender's Revolving Credit Exposure exceeding such Lender's Commitment set forth in Schedule 2.01, as may be modified, supplemented or amended from time to time. Within the foregoing limits and subject to the terms and conditions set forth herein, the Borrower may borrow, prepay and reborrow Revolving Loans.

SECTION 2.02. Loans and Borrowings. (a) Each Revolving Loan shall be made as part of a Borrowing consisting of Revolving Loans made by the Lenders ratably in accordance with their respective Commitments. The failure of any Lender to make any Loan required to be made by it shall not relieve any other Lender of its obligations hereunder; provided that the Commitments are several and no Lender shall be responsible for any other Lender's failure to make Loans as required.

(a) Subject to Section 2.11, (i) each Revolving Borrowing shall be comprised entirely of ABR Loans, Money Market Loans or Eurodollar Loans as the Borrower may request in accordance herewith. Each Lender at its option may make any Eurodollar Loan by causing any domestic or foreign branch or Affiliate of such Lender to make such Loan; provided that any exercise of such option shall not affect the obligation of the Borrower to repay such Loan in accordance with the terms of this Agreement.

(b) At the time that each Eurodollar Revolving Borrowing is made, such Borrowing shall be in an aggregate amount that is an integral multiple of \$500,000 and not less than \$1,000,000. At the time that each ABR Revolving Borrowing or Money Market Revolving Borrowing is made, such Borrowing shall be in an aggregate amount that is an integral multiple of \$500,000 and not less than \$1,000,000; provided that an ABR Revolving Borrowing or Money Market Revolving Borrowing may be in an aggregate amount that is equal to the entire unused balance of the total Commitments. Borrowings of more than one Type may be outstanding at the same time.

SECTION 2.03. Requests for Revolving Borrowings. (a) To request a Revolving Borrowing, an Authorized Person shall notify the Administrative Agent of such request by telephone (i) in the case of a Eurodollar Borrowing, not later than 11:00 a.m., New York City time, three Business Days before the date of the proposed Borrowing, or (ii) in the case of an ABR Borrowing or a Money Market Borrowing, not later than 11:00 a.m., New York City time, on the date of the proposed Borrowing. Each such telephonic Borrowing Request shall be irrevocable and shall be confirmed promptly by hand delivery or telecopy to the Administrative Agent of a written Borrowing Request in the form attached hereto as Exhibit D which shall be accompanied by a Collateral Spreadsheet, each signed by the Borrower.

(b) Each such telephonic and written Borrowing Request shall specify the following information in compliance with Section 2.02:

- (i) the aggregate amount of the requested Borrowing;
- (ii) the date of such Borrowing, which shall be a Business Day;
- (iii) whether such Borrowing is to be an ABR Borrowing, a Money Market Borrowing or a Eurodollar Borrowing;
- (iv) whether Collateral is, at the time of such Borrowing, segregated in favor of any Secured Party, Wells Fargo Bank, N.A. or PNC Bank, N.A.; and
- (v) the location and number of the Borrower's account to which funds are to be disbursed, which shall comply with the requirements of Section 2.04.

(c) In the event that the segregation of Collateral is required pursuant to Section 3.2 of the Pledge Security Agreement, the Administrative Agent shall inform the Borrower that such segregation is required by 12:00 p.m. and the Borrower shall cause such Collateral to be segregated and shall provide the Administrative Agent with a revised Collateral Spreadsheet reflecting the segregation of such Collateral by 12:30 p.m. as a condition precedent to any Loans being advanced.

(d) If no election as to the Type of Revolving Borrowing is specified, then the requested Revolving Borrowing shall be an ABR Borrowing. Promptly following receipt of a Borrowing Request in accordance with this Section, the Administrative Agent shall advise each Lender of the details thereof and of the amount of such Lender's Loan to be made as part of the requested Borrowing.

SECTION 2.04. Funding of Borrowings. (a) Each Lender shall make each Loan to be made by it hereunder on the proposed date thereof by wire transfer of immediately available funds by 2:00, New York City time, to the account of the Administrative Agent most recently designated by it for such purpose by notice to the Lenders. The Administrative Agent will make such Loans available to the Borrower by promptly crediting the amounts so received, in like funds, to an account of the Borrower maintained with the Administrative Agent in New York City and designated by the Borrower in the applicable Borrowing Request.

(b) Unless the Administrative Agent shall have received notice from a Lender prior to the proposed date of any Borrowing that such Lender will not make available to the Administrative Agent such Lender's share of such Borrowing, the Administrative Agent may assume that such Lender has made such share available on such date in accordance with paragraph (a) of this Section and may, in reliance upon such assumption, make available to the Borrower a corresponding amount. In such event, if a Lender has not in fact made its share of the applicable Borrowing available to the Administrative Agent, then the applicable Lender and the Borrower severally agree to pay to the Administrative Agent forthwith on demand such corresponding amount with interest thereon, for each day from and including the date such amount is made available to the Borrower to but excluding the date of payment to the Administrative Agent, at (i) in the case of such Lender, the greater of the Federal Funds Effective Rate and a rate determined by the Administrative Agent in accordance with banking industry rules on interbank compensation or (ii) in the case of the Borrower, the interest rate applicable to ABR Loans. If such Lender pays such amount to the Administrative Agent, then such amount shall constitute such Lender's Loan included in such Borrowing.

SECTION 2.05. Interest Elections. (a) Each Revolving Borrowing initially shall be of the Type specified in the applicable Borrowing Request and interest thereon shall be payable in accordance with Section 2.10. Thereafter, the Borrower may elect to convert such Borrowing to a different Type or to continue such Borrowing, all as provided in this Section. The Borrower may elect different options with respect to different portions of the affected Borrowing, in which case each such portion shall be allocated ratably among the Lenders holding the Loans comprising such Borrowing, and the Loans comprising each such portion shall be considered a separate Borrowing.

(b) To make an election pursuant to this Section, the Borrower shall notify the Administrative Agent of such election by telephone by the time that a Borrowing Request would be required under Section 2.03 if the Borrower were requesting a Revolving Borrowing of the Type resulting from such election to be made on the effective date of such election. Each such telephonic Interest Election Request shall be irrevocable and shall be confirmed promptly by hand delivery or telecopy to the Administrative Agent of a written Interest Election Request in the form attached hereto as Exhibit E signed by the Borrower.

(c) Each telephonic and written Interest Election Request shall specify the following information in compliance with Section 2.02:

(i) the Borrowing to which such Interest Election Request applies and, if different options are being elected with respect to different portions thereof, the portions thereof to be allocated to each resulting Borrowing (in which case the information to be specified pursuant to clauses (iii) and (iv) below shall be specified for each resulting Borrowing);

(ii) the effective date of the election made pursuant to such Interest Election Request, which shall be a Business Day; and

(iii) whether the resulting Borrowing is to be an ABR Borrowing, a Money Market Borrowing or a Eurodollar Borrowing.

(d) Promptly following receipt of an Interest Election Request, the Administrative Agent shall advise each Lender of the details thereof and of such Lender's portion of each resulting Borrowing.

SECTION 2.06. Termination and Reduction of Commitments. (a) Unless previously terminated, the Commitments shall terminate on the Maturity Date.

(b) The Borrower may at any time terminate, or from time to time reduce, the Commitments provided that (i) each reduction of the Commitments shall be in an amount that is an integral multiple of \$500,000 and not less than \$1,000,000 and (ii) the Borrower shall not terminate or reduce the Commitments if, after giving effect to any concurrent prepayment of the Loans in accordance with Section 2.08, the Revolving Credit Exposures would exceed the total Commitments.

(c) The Borrower shall notify the Administrative Agent of any election to terminate or reduce the Commitments under paragraph (b) of this Section at least three Business Days prior to the effective date of such termination or reduction, specifying such election and the effective date thereof. Promptly following receipt of any notice, the Administrative Agent shall advise the Lenders of the contents thereof. Each notice delivered by the Borrower pursuant to this Section shall be irrevocable; provided that a notice of termination of the Commitments delivered by the Borrower may state that such notice is conditioned upon the effectiveness of other credit facilities, in which case such notice may be revoked by the Borrower (by notice to the Administrative Agent on or prior to the specified effective date) if such condition is not satisfied. Any termination or reduction of the Commitments shall be permanent. Each reduction of the Commitments shall be made ratably among the Lenders in accordance with their respective Commitments.

SECTION 2.07. Repayment of Loans at Maturity; Evidence of Debt (a) The Borrower hereby unconditionally promises to pay to the Administrative Agent for the account of each Lender the then unpaid principal amount of each Revolving Loan on the Maturity Date.

(b) Each Lender shall maintain in accordance with its usual practice an account or accounts evidencing the indebtedness of the Borrower to such Lender resulting from each Loan made by such Lender, including the amounts of principal and interest payable and paid to such Lender from time to time hereunder.



(c) The Administrative Agent shall maintain accounts in which it shall record (i) the amount of each Loan made hereunder and the Type thereof, (ii) the amount of any principal or interest due and payable or to become due and payable from the Borrower to each Lender hereunder and (iii) the amount of any sum received by the Administrative Agent hereunder for the account of the Lenders and each Lender's share thereof.

(d) The entries made in the accounts maintained pursuant to paragraph (b) or (c) of this Section shall be prima facie evidence of the existence and amounts of the obligations recorded therein; provided that the failure of any Lender or the Administrative Agent to maintain such accounts or any error therein shall not in any manner affect the obligation of the Borrower to repay the Loans in accordance with the terms of this Agreement.

(e) Any Lender may request that Loans made by it be evidenced by a promissory note. In such event, the Borrower shall prepare, execute and deliver to such Lender a promissory note payable to the order of such Lender (or, if requested by such Lender, to such Lender and its registered assigns) and in a form approved by the Administrative Agent. Thereafter, the Loans evidenced by such promissory note and interest thereon shall at all times (including after assignment pursuant to Section 10.04) be represented by one or more promissory notes in such form payable to the order of the payee named therein (or, if such promissory note is a registered note, to such payee and its registered assigns).

**SECTION 2.08. Optional Repayment of Loans.** (a) The Borrower shall have the right at any time and from time to time to repay any Borrowing in whole or in part, subject to prior notice in accordance with paragraph (b) of this Section.

(b) The Borrower shall notify the Administrative Agent of any repayment hereunder either (i) as a date certain indicated on the Borrowing Request, or (ii) by telephone (confirmed by telecopy) not later than 11:00 a.m., New York City time, on the date of repayment, (in either case, such date being a Business Day). Each such notice shall be irrevocable and shall specify the repayment date and the principal amount of each Borrowing or portion thereof to be repaid. Promptly following receipt of any such notice relating to a Revolving Borrowing, the Administrative Agent shall advise the Lenders of the contents thereof. Each partial repayment of any Revolving Borrowing shall be in an amount that would be permitted in the case of an advance of a Revolving Borrowing of the same Type as provided in Section 2.02. Each repayment of a Revolving Borrowing shall be applied ratably to the Loans included in the repaid Borrowing. Repayments shall be accompanied by accrued interest to the extent required by Section 2.10.

**SECTION 2.09. Fees.** (a) The Borrower agrees to pay to the Administrative Agent for the account of each Lender a facility fee, which shall accrue at a rate of 5.0 basis points per annum on the average daily unused amount of the Commitment of such Lender during the period from and including the Effective Date to but excluding the date on which such Commitment terminates. Accrued facility fees shall be payable in arrears on the last day of each calendar month and on the

date on which the Commitments terminate, commencing on the first such date to occur after the date hereof. All facility fees shall be computed on the basis of a year of 360 days and shall be payable for the actual number of days elapsed (including the first day but excluding the last day).

(b) The Borrower agrees to pay to the Administrative Agent, for its own account, fees payable in the amounts and at the times separately agreed upon between the Borrower and the Administrative Agent.

(c) All fees payable hereunder shall be paid on the dates due, in immediately available funds, to the Administrative Agent for distribution, in the case of facility fees, to the Lenders. Fees paid shall not be refundable under any circumstances.

SECTION 2.10. Interest. (a) The Loans comprising each ABR Borrowing shall bear interest for each day outstanding at the Alternate Base Rate in effect on such day.

(b) The Loans comprising each Money Market Borrowing shall bear interest for each day outstanding at the Money Market Rate in effect on such day plus the Applicable Rate.

(c) The Loans comprising each Eurodollar Borrowing shall bear interest for each day outstanding at the Adjusted LIBO Rate in effect for such day plus the Applicable Rate.

(d) Notwithstanding the foregoing, if any principal of or interest on any Loan or any fee or other amount payable by the Borrower hereunder is not paid when due, whether at stated maturity, upon acceleration or otherwise, such overdue amount shall bear interest, after as well as before judgment, at a rate per annum equal to (i) in the case of overdue principal of any Loan, 2% plus the rate otherwise applicable to such Loan as provided in the preceding paragraphs of this Section or (ii) in the case of any other amount, 2% plus the rate applicable to ABR Loans as provided in paragraph (a) of this Section.

(e) Accrued interest on each Loan shall be payable in arrears on each Interest Payment Date for such Loan and, in the case of Revolving Loans, upon termination of the Commitments; provided that interest accrued pursuant to paragraph (e) of this Section shall be payable on demand.

(f) All interest hereunder shall be computed on the basis of a year of 360 days, except that interest computed by reference to the Alternate Base Rate at times when the Alternate Base Rate is based on the Prime Rate shall be computed on the basis of a year of 365 days (or 366 days in a leap year), and in each case shall be payable for the actual number of days elapsed (including the first day but excluding the last day). The applicable Alternate Base Rate, Money Market Rate, Adjusted LIBO Rate or Overnight LIBO Rate shall be determined by the Administrative Agent, and such determination shall be conclusive absent manifest error.

SECTION 2.11. Alternate Rate of Interest. If prior to the commencement of any Borrowing of or conversion into a Eurodollar Loan:

(a) the Administrative Agent determines (which determination shall be conclusive absent manifest error) that adequate and reasonable means do not exist for ascertaining the Adjusted LIBO Rate or the Overnight LIBO Rate, as applicable, for such day; or

(b) the Administrative Agent is advised by the Required Lenders that the Adjusted LIBO Rate or the Overnight LIBO Rate, as applicable, for such day will not adequately and fairly reflect the cost to such Lenders (or Lender) of making or maintaining their Loans (or its Loan) included in such Borrowing for such day;

then the Administrative Agent shall give notice thereof to the Borrower and the Lenders by telephone or teletype as promptly as practicable thereafter and, until the Administrative Agent notifies the Borrower and the Lenders that the circumstances giving rise to such notice no longer exist, (i) any Interest Election Request that requests the conversion of any Revolving Borrowing to, or continuation of any Revolving Borrowing as, a Eurodollar Borrowing shall be ineffective and (ii) if any Borrowing Request requests a Eurodollar Revolving Borrowing, such Borrowing shall be made as an ABR Borrowing or Money Market Borrowing, at Borrower's request; provided that if the circumstances giving rise to such notice affect only one Type of Borrowings, then the other Type of Borrowings shall be permitted.

SECTION 2.12. Increased Costs. (a) If any Change in Law shall:

(i) impose, modify or deem applicable any reserve, special deposit or similar requirement against assets of, deposits with or for the account of, or credit extended by, any Lender (except any such reserve requirement reflected in the Adjusted LIBO Rate); or

(ii) impose on any Lender or the London interbank market any other condition affecting this Agreement or Eurodollar Loans made by such Lender;

and the result of any of the foregoing shall be to increase the cost to such Lender of making or maintaining any Eurodollar Loan (or of maintaining its obligation to make any such Loan) or to reduce the amount of any sum received or receivable by such Lender hereunder (whether of principal, interest or otherwise), then the Borrower will pay to such Lender, such additional amount or amounts as will compensate such Lender, for such additional costs incurred or reduction suffered.

(b) If any Lender determines that any Change in Law regarding capital requirements has or would have the effect of reducing the rate of return on such Lender's capital or on the capital of such Lender's holding company, if any, as a consequence of this Agreement or the Loans made by such Lender to a level below that which such Lender or such Lender's holding company could have achieved but for such Change in Law (taking into consideration such Lender's policies and the policies of such Lender's holding company with respect to capital adequacy), then from time to time the Borrower will pay to such Lender such additional amount or amounts as will compensate such Lender or such Lender's holding company for any such reduction suffered.

(c) A certificate of a Lender setting forth the amount or amounts necessary to compensate such Lender or its holding company, as the case may be, as specified in paragraph (a) or (b) of this Section shall be delivered to the Borrower and shall be conclusive absent manifest error. The Borrower shall pay such Lender the amount shown as due on any such certificate within 10 days after receipt thereof.

(d) Failure or delay on the part of any Lender to demand compensation pursuant to this Section shall not constitute a waiver of such Lender's right to demand such compensation; provided that the Borrower shall not be required to compensate a Lender pursuant to this Section for any increased costs or reductions incurred more than 270 days prior to the date that such Lender notifies the Borrower of the Change in Law giving rise to such increased costs or reductions and of such Lender's intention to claim compensation therefor; provided further that, if the Change in Law giving rise to such increased costs or reductions is retroactive, then the 270-day period referred to above shall be extended to include the period of retroactive effect thereof.

SECTION 2.13. Taxes. (a) Any and all payments by or on account of any obligation of the Borrower hereunder shall be made free and clear of and without deduction for any Indemnified Taxes or Other Taxes; provided that if the Borrower shall be required to deduct any Indemnified Taxes or Other Taxes from such payments, then (i) the sum payable shall be increased as necessary so that after making all required deductions (including deductions applicable to additional sums payable under this Section) the Administrative Agent or Lender (as the case may be) receives an amount equal to the sum it would have received had no such deductions been made, (ii) the Borrower shall make such deductions and (iii) the Borrower shall pay the full amount deducted to the relevant Governmental Authority in accordance with applicable law.

(b) In addition, the Borrower shall pay any Other Taxes to the relevant Governmental Authority in accordance with applicable law.

(c) The Borrower shall indemnify the Administrative Agent and each Lender, within 10 days after written demand therefor, for the full amount of any Indemnified Taxes or Other Taxes paid by the Administrative Agent or such Lender, as the case may be, on or with respect to any payment by or on account of any obligation of the Borrower hereunder (including Indemnified Taxes or Other Taxes imposed or asserted on or attributable to amounts payable under this Section) and any penalties, interest and reasonable expenses arising therefrom or with respect thereto, whether or not such Indemnified Taxes or Other Taxes were correctly or legally imposed or asserted by the relevant Governmental Authority. A certificate as to the amount of such payment or liability delivered to the Borrower by a Lender, or by the Administrative Agent on its own behalf or on behalf of a Lender, shall be conclusive absent manifest error.

(d) As soon as practicable after any payment of Indemnified Taxes or Other Taxes by the Borrower to a Governmental Authority, the Borrower shall deliver to the Administrative Agent the original or a certified copy of a receipt issued by such Governmental Authority evidencing such payment, a copy of the return reporting such

payment or other evidence of such payment reasonably satisfactory to the Administrative Agent.

(e) Any Foreign Lender that is entitled to an exemption from or reduction of withholding tax under the law of the jurisdiction in which the Borrower is located, or any treaty to which such jurisdiction is a party, with respect to payments under this Agreement shall deliver to the Borrower (with a copy to the Administrative Agent), at the time or times prescribed by applicable law, such properly completed and executed documentation prescribed by applicable law or reasonably requested by the Borrower as will permit such payments to be made without withholding or at a reduced rate.

(f) If the Administrative Agent or a Lender determines, in its sole discretion, that it has received a refund of any Taxes or Other Taxes as to which it has been indemnified by the Borrower or with respect to which the Borrower has paid additional amounts pursuant to this Section 2.13, it shall pay over such refund to the Borrower (but only to the extent of indemnity payments made, or additional amounts paid, by the Borrower under this Section 2.13 with respect to the Taxes or Other Taxes giving rise to such refund), net of all out-of-pocket expenses of the Administrative Agent or such Lender and without interest (other than any interest paid by the relevant Governmental Authority with respect to such refund); provided, that the Borrower, upon the request of the Administrative Agent or such Lender, agrees to repay the amount paid over to the Borrower (plus any penalties, interest or other charges imposed by the relevant Governmental Authority) to the Administrative Agent or such Lender in the event the Administrative Agent or such Lender is required to repay such refund to such Governmental Authority. This Section shall not be construed to require the Administrative Agent or any Lender to make available its tax returns (or any other information relating to its taxes which it deems confidential) to the Borrower or any other Person.

SECTION 2.14. Payments Generally; Pro Rata Treatment; Sharing of Set-offs. (a) The Borrower shall make each payment required to be made by it hereunder (whether of principal, interest, fees, or of amounts payable under Section 2.12 or Section 2.13, or otherwise) prior to 12:00 noon, New York City time, on the date when due, in immediately available funds, without set-off or counterclaim. Any amounts received after such time on any date may, in the discretion of the Administrative Agent, be deemed to have been received on the next succeeding Business Day for purposes of calculating interest thereon. All such payments shall be made to the Administrative Agent at its offices at 270 Park Avenue, New York, New York, except that payments pursuant to Section 2.12, Section 2.13 and Section 10.03 shall be made directly to the Persons entitled thereto. The Administrative Agent shall distribute any such payments received by it for the account of any other Person to the appropriate recipient promptly following receipt thereof. If any payment hereunder shall be due on a day that is not a Business Day, the date for payment shall be extended to the next succeeding Business Day, and, in the case of any payment accruing interest, interest thereon shall be payable for the period of such extension. All payments hereunder shall be made in dollars.

(b) If at any time insufficient funds are received by and available to the Administrative Agent to pay fully all amounts of principal, interest and fees then due hereunder, such funds shall be applied (i) first, towards payment of interest and fees

then due hereunder, ratably among the parties entitled thereto in accordance with the amounts of interest and fees then due to such parties, and (ii) second, towards payment of principal then due hereunder, ratably among the parties entitled thereto in accordance with the amounts of principal then due to such parties.

(c) If any Lender shall, by exercising any right of set-off or counterclaim or otherwise, obtain payment in respect of any principal of or interest on any of its Revolving Loans resulting in such Lender receiving payment of a greater proportion of the aggregate amount of its Revolving Loans and accrued interest thereon than the proportion received by any other Lender, then the Lender receiving such greater proportion shall purchase (for cash at face value) participations in the Revolving Loans of other Lenders to the extent necessary so that the benefit of all such payments shall be shared by the Lenders ratably in accordance with the aggregate amount of principal of and accrued interest on their respective Revolving Loans; provided that (i) if any such participations are purchased and all or any portion of the payment giving rise thereto is recovered, such participations shall be rescinded and the purchase price restored to the extent of such recovery, without interest, and (ii) the provisions of this paragraph shall not be construed to apply to any payment made by the Borrower pursuant to and in accordance with the express terms of this Agreement or any payment obtained by a Lender as consideration for the assignment of or sale of a participation in any of its Loans to any assignee or participant, other than to the Borrower or any Subsidiary or Affiliate thereof (as to which the provisions of this paragraph shall apply). The Borrower consents to the foregoing and agrees, to the extent it may effectively do so under applicable law, that any Lender acquiring a participation pursuant to the foregoing arrangements may exercise against the Borrower rights of set-off and counterclaim with respect to such participation as fully as if such Lender were a direct creditor of the Borrower in the amount of such participation.

(d) Unless the Administrative Agent shall have received notice from the Borrower prior to the date on which any payment is due to the Administrative Agent for the account of the Lenders hereunder that the Borrower will not make such payment, the Administrative Agent may assume that the Borrower has made such payment on such date in accordance herewith and may, in reliance upon such assumption, distribute to the Lenders the amount due. In such event, if the Borrower has not in fact made such payment, then each of the Lenders severally agrees to repay to the Administrative Agent forthwith on demand the amount so distributed to such Lender with interest thereon, for each day from and including the date such amount is distributed to it to but excluding the date of payment to the Administrative Agent, at the greater of the Federal Funds Effective Rate and a rate determined by the Administrative Agent in accordance with banking industry rules on interbank compensation.

(e) If any Lender shall fail to make any payment required to be made by it pursuant to Section 2.04(b), Section 2.14(d) or Section 10.03(c), then the Administrative Agent may, in its discretion (notwithstanding any contrary provision hereof), apply any amounts thereafter received by the Administrative Agent for the account of such Lender to satisfy such Lender's obligations under such Sections until all such unsatisfied obligations are fully paid.

SECTION 2.15. Mitigation Obligations; Replacement of Lenders. (a) If any Lender requests compensation under Section 2.12, or if the Borrower is required to pay any additional amount to any Lender or any Governmental Authority for the account of any Lender pursuant to Section 2.13, then such Lender shall use reasonable efforts to designate a different lending office for funding or booking its Loans hereunder or to assign its rights and obligations hereunder to another of its offices, branches or affiliates, if, in the judgment of such Lender, such designation or assignment (i) would eliminate or reduce amounts payable pursuant to Section 2.12 or Section 2.13, as the case may be, in the future and (ii) would not subject such Lender to any unreimbursed cost or expense and would not otherwise be disadvantageous to such Lender. The Borrower hereby agrees to pay all reasonable costs and expenses incurred by any Lender in connection with any such designation or assignment.

(b) If any Lender requests compensation under Section 2.12, or if the Borrower is required to pay any additional amount to any Lender or any Governmental Authority for the account of any Lender pursuant to Section 2.13, or if any Lender defaults in its obligation to fund Loans hereunder, then the Borrower may, at its sole expense and effort, upon notice to such Lender and the Administrative Agent, require such Lender to assign and delegate, without recourse (in accordance with and subject to the restrictions contained in Section 10.04), all its interests, rights and obligations under this Agreement to an assignee that shall assume such obligations (which assignee may be another Lender, if a Lender accepts such assignment); provided that (i) the Borrower shall have received the prior written consent of the Administrative Agent, which consent shall not unreasonably be withheld, (ii) such Lender shall have received payment of an amount equal to the outstanding principal of its Loans, accrued interest thereon, accrued fees and all other amounts payable to it hereunder, from the assignee (to the extent of such outstanding principal and accrued interest and fees) or the Borrower (in the case of all other amounts) and (iii) in the case of any such assignment resulting from a claim for compensation under Section 2.12 or payments required to be made pursuant to Section 2.13, such assignment will result in a reduction in such compensation or payments. A Lender shall not be required to make any such assignment and delegation if, prior thereto, as a result of a waiver by such Lender or otherwise, the circumstances entitling the Borrower to require such assignment and delegation cease to apply.

### **ARTICLE III. GUARANTEES AND COLLATERAL SECURITY**

SECTION 3.01. Guarantee of Obligations. The Borrower will cause each of the Guarantors to continue to jointly and severally Guarantee the Obligations hereunder pursuant to the Guarantee Agreement executed and delivered by such Guarantors until such time as the Administrative Agent has confirmed that all Commitments have been terminated and all Obligations have been indefeasibly paid in full.

SECTION 3.02. Security for Obligations. The Borrower will, and will cause each Guarantor to, maintain in force the Pledge Security Agreement executed and delivered by the Borrower and such Guarantors on the date hereof to the Administrative Agent and the Lenders (each a "Secured Party" and together with the other secured parties party to the Intercreditor Agreement, the "Secured Parties"), provided that the Borrower and the Guarantors must, at all times that any Commitment or Loan remains outstanding, maintain securities (i) in the Accounts at the Securities Intermediary, such

securities having a Net Market Value of not less than the aggregate amount of the "Primary Obligations" as defined in the Intercreditor Agreement, and (ii) in the Collateral Account and the Accounts, such securities having a Net Market Value of not less than the aggregate amount of the Primary Obligations (as defined in the Pledge Security Agreement). On each Business Day that any Loan is outstanding, the Borrower shall deliver a Collateral Spreadsheet to the Administrative Agent by 12:00 p.m. New York time. The Borrower will, and will cause each Guarantor to, enter into a control agreement or agreements and any other documentation that the Secured Parties or any of them determine is necessary or desirable to perfect, evidence or protect the security interest granted pursuant to the Pledge Security Agreement.

**ARTICLE IV.**  
**REPRESENTATIONS AND WARRANTIES**

The Borrower represents and warrants to the Lenders that:

SECTION 4.01. Organization; Powers. Each of the Borrower and its Subsidiaries is duly organized, validly existing and in good standing under the laws of the jurisdiction of its organization, has all requisite power and authority to carry on its business as now conducted and, except where the failure to do so, individually or in the aggregate, could not reasonably be expected to result in a Material Adverse Effect, is qualified to do business in, and is in good standing in, every jurisdiction where such qualification is required.

SECTION 4.02. Authorization; Enforceability. The Transactions are within the Borrower's corporate powers and have been duly authorized by all necessary corporate and, if required, stockholder action. This Agreement has been duly executed and delivered by the Borrower and constitutes a legal, valid and binding obligation of the Borrower, enforceable in accordance with its terms, subject to applicable bankruptcy, insolvency, reorganization, moratorium or other laws affecting creditors' rights generally and subject to general principles of equity, regardless of whether considered in a proceeding in equity or at law.

SECTION 4.03. Governmental Approvals; No Conflicts. The Transactions (a) do not require any consent or approval of, registration or filing with, or any other action by, any Governmental Authority, except that this Agreement must be filed with the Securities and Exchange Commission, and except such as have been obtained or made and are in full force and effect, (b) will not violate any applicable law or regulation or the charter, by-laws or other organizational documents of the Borrower or any of its Subsidiaries or any order of any Governmental Authority, (c) will not violate or result in a default under any indenture, agreement or other instrument binding upon the Borrower or any of its Subsidiaries or its assets, or give rise to a right thereunder to require any payment to be made by the Borrower or any of its Subsidiaries, and (d) will not result in the creation or imposition of any Lien on any asset of the Borrower or any of its Subsidiaries.

SECTION 4.04. Financial Condition; No Material Adverse Change. (a) The Borrower has heretofore furnished to the Lenders consolidated balance sheet and statements of income, stockholders equity and cash flows of Paychex, Inc. (i) as of and for the fiscal year ended May 31, 2008, reported on by Ernst & Young LLP, independent public accountants, and certified by its chief financial officer. Such financial statements present fairly, in all material respects, the financial position and results of operations and cash flows of Paychex, Inc. and its consolidated Subsidiaries as



of such dates and for such periods in accordance with GAAP, subject to year-end audit adjustments and the absence of footnotes in the case of the statements referred to in clause (ii) above.

(b) Since May 31, 2008, there has been no material adverse change in the business, assets, operations, prospects or condition, financial or otherwise, of the Borrower and its Subsidiaries, taken as a whole.

SECTION 4.05. Properties. (a) Each of the Borrower and its Subsidiaries has good title to, or valid leasehold interests in, all its real and personal property material to its business, except for minor defects in title that do not interfere with its ability to conduct its business as currently conducted or to utilize such properties for their intended purposes.

(b) Each of the Borrower and its Subsidiaries owns, or is licensed to use, all trademarks, tradenames, copyrights, patents and other intellectual property material to its business, and the use thereof by the Borrower and its Subsidiaries does not infringe upon the rights of any other Person, except for any such infringements that, individually or in the aggregate, could not reasonably be expected to result in a Material Adverse Effect.

SECTION 4.06. Litigation and Environmental Matters. (a) There are no actions, suits or proceedings by or before any arbitrator or Governmental Authority pending against or, to the knowledge of the Borrower, threatened against or affecting the Borrower or any of its Subsidiaries (i) as to which there is a reasonable possibility of an adverse determination and that, if adversely determined, could reasonably be expected, individually or in the aggregate, to result in a Material Adverse Effect (other than as described in Schedule 4.06 (“the Disclosed Matters”)) or (ii) that involve this Agreement or the Transactions.

(b) Except for the Disclosed Matters and except with respect to any other matters that, individually or in the aggregate, could not reasonably be expected to result in a Material Adverse Effect, neither the Borrower nor any of its Subsidiaries (i) has failed to comply with any Environmental Law or to obtain, maintain or comply with any permit, license or other approval required under any Environmental Law, (ii) has become subject to any Environmental Liability, (iii) has received notice of any claim with respect to any Environmental Liability or (iv) knows of any basis for any Environmental Liability.

(c) Since the date of this Agreement, there has been no change in the status of the Disclosed Matters that, individually or in the aggregate, has resulted in, or materially increased the likelihood of, a Material Adverse Effect.

SECTION 4.07. Compliance with Laws and Agreements. Each of the Borrower and its Subsidiaries is in compliance with all laws, regulations and orders of any Governmental Authority applicable to it or its property and all indentures, agreements and other instruments binding upon it or its property, except where the failure to do so, individually or in the aggregate, could not reasonably be expected to result in a Material Adverse Effect. No Default has occurred and is continuing.

SECTION 4.08. Investment and Holding Company Status. Neither the Borrower nor any of its Subsidiaries is (a) an “investment company” as defined in, or subject to regulation under, the

Investment Company Act of 1940 or (b) a “holding company” as defined in, or subject to regulation under, the Public Utility Holding Company Act of 1935.

SECTION 4.09. Taxes. Each of the Borrower and its Subsidiaries has timely filed or caused to be filed all Tax returns and reports required to have been filed and has paid or caused to be paid all Taxes required to have been paid by it, except (a) Taxes that are being contested in good faith by appropriate proceedings and for which the Borrower or such Subsidiary, as applicable, has set aside on its books adequate reserves or (b) to the extent that the failure to do so could not reasonably be expected to result in a Material Adverse Effect.

SECTION 4.10. ERISA. Neither the Borrower nor any ERISA Affiliate maintains any Plan or any Multiemployer Plan.

SECTION 4.11. Disclosure. The Borrower has disclosed to the Lenders all agreements, instruments and corporate or other restrictions to which it or any of its Subsidiaries is subject, and all other matters known to it, that, individually or in the aggregate, could reasonably be expected to result in a Material Adverse Effect. Neither the information memorandum nor any of the other reports, financial statements, certificates or other information furnished by or on behalf of the Borrower to the Administrative Agent or any Lender in connection with the negotiation of this Agreement or delivered hereunder (as modified or supplemented by other information so furnished) contains any material misstatement of fact or omits to state any material fact necessary to make the statements therein, in the light of the circumstances under which they were made, not misleading; provided that, with respect to projected financial information, the Borrower represents only that such information was prepared in good faith based upon assumptions believed to be reasonable at the time.

## **ARTICLE V.** **CONDITIONS**

SECTION 5.01. Effective Date. The obligations of the Lenders to make Loans hereunder shall not become effective until the date on which each of the following conditions is satisfied (or waived in accordance with Section 10.02):

- (a) The Administrative Agent (or its counsel) shall have received from each party hereto either (i) a counterpart of this Agreement signed on behalf of such party or (ii) written evidence satisfactory to the Administrative Agent (which may include telecopy transmission of a signed signature page of this Agreement) that such party has signed a counterpart of this Agreement.
- (b) The Administrative Agent (or its counsel) shall have received from each party thereto either (i) a counterpart of each Credit Document (other than this Agreement and including the Intercreditor Agreement) signed on behalf of such party or (ii) written evidence satisfactory to the Administrative Agent (which may include telecopy transmission of a signed signature page of such Credit Document) that such party has signed a counterpart of such Credit Document.
- (c) The Administrative Agent shall have received a favorable written opinion (addressed to the Administrative Agent and the Lenders and dated the Effective Date) of Nixon Peabody, LLP, counsel for the Borrower, substantially in the form of

Exhibit F, and covering such other matters relating to the Borrower, this Agreement or the Transactions as the Required Lenders shall reasonably request. The Borrower hereby requests such counsel to deliver such opinion.

(d) The Administrative Agent shall have received such documents and certificates as the Administrative Agent or its counsel may reasonably request relating to the organization, existence and good standing of the Borrower, the authorization of the Transactions and any other legal matters relating to the Borrower, this Agreement or the Transactions, all in form and substance satisfactory to the Administrative Agent and its counsel.

(e) The Administrative Agent shall have received evidence satisfactory to it that all governmental and third party approvals necessary or, in the discretion of the Administrative Agent, advisable, in connection with the Transactions contemplated hereby have been obtained.

(f) The Administrative Agent shall have received (i) satisfactory audited consolidated financial statements of the Borrower for the two most recent fiscal years ended prior to the Effective Date as to which such financial statements are available and (ii) satisfactory unaudited interim financial statements of the Borrower for each fiscal quarterly period ended subsequent to the date of the latest financial statements delivered pursuant to clause (i) hereof as to which financial statements are available.

(g) The Administrative Agent shall have received all fees and other amounts due and payable on or prior to the Effective Date, including, to the extent invoiced, reimbursement or payment of all out-of-pocket expenses required to be reimbursed or paid by the Borrower hereunder.

The Administrative Agent shall notify the Borrower and the Lenders of the Effective Date, and such notice shall be conclusive and binding. Notwithstanding the foregoing, the obligations of the Lenders to make Loans hereunder shall not become effective unless each of the foregoing conditions is satisfied (or waived pursuant to Section 10.02).

SECTION 5.02. Each Credit Event. The obligation of each Lender to make a Loan on the occasion of any Borrowing is subject to the satisfaction of the following conditions:

(a) The representations and warranties of the Borrower set forth in this Agreement shall be true and correct on and as of the date of such Borrowing.

(b) The Net Market Value of the Collateral shall be greater than or equal to the aggregate amount of each of (i) the Primary Obligations (as defined in the Pledge

Security Agreement) and (ii) the “Primary Obligations” as defined in the Intercreditor Agreement, on and as of the date of such Borrowing and after giving effect thereto, as set forth on the Collateral Spreadsheet provided to the Administrative Agent simultaneously with the Borrowing Request.

(c) At the time of and immediately after giving effect to such Borrowing, no Default or Event of Default shall have occurred and be continuing.

Each Borrowing shall be deemed to constitute a representation and warranty by the Borrower on the date thereof as to the matters specified in paragraphs (a), (b) and (c) of this Section.

**ARTICLE VI.**  
**AFFIRMATIVE COVENANTS**

Until the Commitments have expired or been terminated and the principal of and interest on each Loan and all fees payable hereunder shall have been paid in full the Borrower covenants and agrees with the Lenders that:

SECTION 6.01. Financial Statements; Ratings Change and Other Information. The Borrower will furnish to the Administrative Agent and each Lender:

(a) within 90 days after the end of each fiscal year of Paychex, Inc., its audited consolidated balance sheet and related statements of operations, stockholders’ equity and cash flows as of the end of and for such year, setting forth in each case in comparative form the figures for the previous fiscal year, all reported on by Ernst & Young LLP or other independent public accountants of recognized national standing (without a “going concern” or like qualification or exception and without any qualification or exception as to the scope of such audit) to the effect that such consolidated financial statements present fairly in all material respects the financial condition and results of operations of Paychex, Inc. and its consolidated Subsidiaries on a consolidated basis in accordance with GAAP consistently applied;

(b) within 45 days after the end of each of the first three fiscal quarters of each fiscal year of Paychex, Inc., its consolidated balance sheet and related statements of operations, stockholders’ equity and cash flows as of the end of and for such fiscal quarter and the then elapsed portion of the fiscal year, setting forth in each case in comparative form the figures for the corresponding period or periods of (or, in the case of the balance sheet, as of the end of) the previous fiscal year, all certified by one of Paychex, Inc.’s Financial Officers as presenting fairly in all material respects the financial condition and results of operations of Paychex, Inc. and its consolidated Subsidiaries on a consolidated basis in accordance with GAAP consistently applied, subject to normal year-end audit adjustments and the absence of footnotes;

(c) concurrently with any delivery of financial statements under clause (a) or (b) above, a certificate of a Financial Officer of the Borrower (i) certifying as to whether a Default has occurred and, if a Default has occurred, specifying the details thereof and any action taken or proposed to be taken with respect thereto, and (ii) stating whether any change in GAAP or in the application thereof has occurred since the date of the

audited financial statements referred to in Section 4.04 and, if any such change has occurred, specifying the effect of such change on the financial statements accompanying such certificate, a form of which is attached hereto as Exhibit G;

(d) promptly after the same become publicly available, copies of all periodic and other reports, proxy statements and other materials filed by Paychex, Inc. or any Subsidiary with the Securities and Exchange Commission, or any Governmental Authority succeeding to any or all of the functions of said Commission, or with any national securities exchange, or distributed by Paychex, Inc. to its shareholders generally, as the case may be;

(e) promptly after Moody's or S&P shall have announced a change in the rating established or deemed to have been established for the Index Debt, written notice of such rating change; and

(f) promptly following any request therefor, such other information regarding the operations, business affairs and financial condition of the Borrower or any Subsidiary, or compliance with the terms of this Agreement, as the Administrative Agent or any Lender may reasonably request.

SECTION 6.02. Notices of Material Events. The Borrower will furnish to the Administrative Agent and each Lender prompt written notice of the following:

(a) the occurrence of any Default;

(b) the filing or commencement of any action, suit or proceeding by or before any arbitrator or Governmental Authority against or affecting the Borrower or any Affiliate thereof that, if adversely determined, could reasonably be expected to result in a Material Adverse Effect;

(c) the occurrence of any ERISA Event that, alone or together with any other ERISA Events that have occurred, could reasonably be expected to have a Material Adverse Effect; and

(d) any other development that results in, or could reasonably be expected to result in, a Material Adverse Effect.

Each notice delivered under this Section shall be accompanied by a statement of a Financial Officer or other executive officer of the Borrower setting forth the details of the event or development requiring such notice and any action taken or proposed to be taken with respect thereto.

SECTION 6.03. Existence; Conduct of Business. The Borrower will, and will cause each of its Subsidiaries to, do or cause to be done all things necessary to preserve, renew and keep in full force and effect its legal existence and the rights, licenses, permits, privileges and franchises material to the conduct of its business; provided that the foregoing shall not prohibit any merger, consolidation, liquidation or dissolution permitted under Section 7.03.

SECTION 6.04. Payment of Obligations. The Borrower will, and will cause each of its Subsidiaries to, pay its obligations, including Tax liabilities, that, if not paid, could result in a Material Adverse Effect before the same shall become delinquent or in default, except where (a) the validity or amount thereof is being contested in good faith by appropriate proceedings, (b) the Borrower or such Subsidiary has set aside on its books adequate reserves with respect thereto in accordance with GAAP and (c) the failure to make payment pending such contest could not reasonably be expected to result in a Material Adverse Effect.

SECTION 6.05. Maintenance of Properties; Insurance. The Borrower will, and will cause each of its Subsidiaries to, (a) keep and maintain all property material to the conduct of its business in good working order and condition, ordinary wear and tear excepted, and (b) maintain, with financially sound and reputable insurance companies, insurance in such amounts and against such risks as are customarily maintained by companies engaged in the same or similar businesses operating in the same or similar locations.

SECTION 6.06. Books and Records; Inspection Rights. The Borrower will, and will cause each of its Subsidiaries to, keep proper books of record and account in which full, true and correct entries are made of all dealings and transactions in relation to its business and activities. Upon reasonable prior notice and, in any event, not more than two times in any twelve month period, the Borrower will, and will cause each of its Subsidiaries to, permit any representatives designated by the Administrative Agent or any Lender to visit and inspect the properties, to discuss its affairs, finances and condition with its officers and independent accountants; provided however, that upon the occurrence and during the continuation of an Event of Default, at such reasonable times and as often as reasonably requested, the Borrower will, and will cause each of its Subsidiaries to, permit any representatives designated by the Administrative Agent or any Lender to visit and inspect its properties, to examine and make extracts from its books and records, and to discuss its affairs, finances and condition with its officers and independent accountants.

SECTION 6.07. Compliance with Laws. The Borrower will, and will cause each of its Subsidiaries to, comply with all laws, rules, regulations and orders of any Governmental Authority and any material contractual obligations applicable to it or its property, except where the failure to do so, individually or in the aggregate, could not reasonably be expected to result in a Material Adverse Effect.

SECTION 6.08. Use of Proceeds. The proceeds of the Loans will be used only for short term liquidity in lieu of liquidation of the Borrower's investment portfolio for the benefit of clients in the normal course of business. No part of the proceeds of any Loan will be used, whether directly or indirectly, for any purpose that entails a violation of any of the Regulations of the Board, including Regulations T, U and X.

SECTION 6.09. Environmental Laws. The Borrower will, and will cause each of its Subsidiaries to, comply with any Environmental Law and to obtain, maintain or comply with any permit, license or other approval required under any Environmental Law, applicable to it or its property, except where the failure to do so, individually or in the aggregate, could not reasonably be expected to result in a Material Adverse Effect, and to provide prompt notice to the Administrative Agent of any claim with respect to any Environmental Liability for which notice has been received by the Borrower or any of its Subsidiaries.

**ARTICLE VII.**  
**NEGATIVE COVENANTS**

Until the Commitments have expired or terminated and the principal of and interest on each Loan and all fees payable hereunder have been paid in full the Borrower covenants and agrees with the Lenders that:

SECTION 7.01. Indebtedness. The Borrower will not, and will not permit any Subsidiary to, create, incur, assume or permit to exist any Indebtedness, except:

- (a) Indebtedness created hereunder;
- (b) Indebtedness existing on the date hereof and set forth in Schedule 7.01 and extensions, renewals and replacements of any such Indebtedness that do not materially increase the outstanding principal amount thereof;
- (c) Indebtedness of the Borrower to any Subsidiary and of any Subsidiary to the Borrower or any other Subsidiary, provided, that any loans and advances by the Borrower or a Guarantor to a non-Guarantor Subsidiary are made in compliance with section 7.04(c);
- (d) Guarantees by the Borrower of Indebtedness of any Subsidiary and by any Subsidiary of Indebtedness of the Borrower or any other Subsidiary;
- (e) Indebtedness of the Borrower or any Subsidiary incurred to finance the acquisition, construction or improvement of any fixed or capital assets, including Capital Lease Obligations and any Indebtedness assumed in connection with the acquisition of any such assets or secured by a Lien on any such assets prior to the acquisition thereof, and extensions, renewals and replacements of any such Indebtedness that do not increase the outstanding principal amount thereof; provided that the aggregate principal amount of Indebtedness permitted by this clause (e) shall not exceed \$50,000,000 at any time outstanding;
- (f) Indebtedness of any Person that becomes a Subsidiary after the date hereof; provided that (i) such Indebtedness exists at the time such Person becomes a Subsidiary and is not created in contemplation of or in connection with such Person becoming a Subsidiary and (ii) the aggregate principal amount of Indebtedness permitted by this clause (f) shall not exceed \$100,000,000 at any time outstanding; and
- (g) other unsecured Indebtedness in an aggregate principal amount not exceeding \$500,000,000 at any time outstanding.

SECTION 7.02. Liens. The Borrower will not, and will not permit any Subsidiary to, create, incur, assume or permit to exist any Lien on any material property or asset now owned or hereafter acquired by it (provided that no Lien shall be permitted to exist on any Collateral at any time), or assign or sell any income or revenues (including accounts receivable) or rights in respect of any thereof, except:

(a) Permitted Encumbrances;

(b) any Lien on any property or asset of the Borrower or any Subsidiary existing on the date hereof and set forth in Schedule 7.02 provided that (i) such Lien shall not apply to any other property or asset of the Borrower or any Subsidiary and (ii) such Lien either is covered by the Intercreditor Agreement or shall secure only those obligations which it secures on the date hereof and extensions, renewals and replacements thereof that do not increase the outstanding principal amount thereof;

(c) any Lien existing on any property or asset prior to the acquisition thereof by the Borrower or any Subsidiary or existing on any property or asset of any Person that becomes a Subsidiary after the date hereof prior to the time such Person becomes a Subsidiary; provided that (i) such Lien is not created in contemplation of or in connection with such acquisition or such Person becoming a Subsidiary, as the case may be, (ii) such Lien shall not apply to any other property or assets of the Borrower or any Subsidiary and (iii) such Lien shall secure only those obligations which it secures on the date of such acquisition or the date such Person becomes a Subsidiary, as the case may be and extensions, renewals and replacements thereof that do not increase the outstanding principal amount thereof;

(d) Liens on fixed or capital assets acquired, constructed or improved by the Borrower or any Subsidiary; provided that (i) such security interests secure Indebtedness permitted by clause (e) of Section 7.01, (ii) such security interests and the Indebtedness secured thereby are incurred prior to or within 90 days after such acquisition or the completion of such construction or improvement, (iii) the Indebtedness secured thereby does not exceed 100% of the cost of acquiring, constructing or improving such fixed or capital assets and (iv) such security interests shall not apply to any other property or assets of the Borrower or any Subsidiary; and

(e) Liens in favor of the Lenders securing the Obligations.

SECTION 7.03. Fundamental Changes. The Borrower will not, and will not permit any Guarantor to, merge into or consolidate with any other Person, or permit any other Person to merge into or consolidate with it, or sell, transfer, lease or otherwise dispose of (in one transaction or in a series of transactions) all or substantially all/any substantial part of its assets, or all or substantially all of the stock of any of its Subsidiaries (in each case, whether now owned or hereafter acquired), or liquidate or dissolve, except that, if at the time thereof and immediately after giving effect thereto no Default shall have occurred and be continuing (i) any Person may merge into the Borrower in a transaction in which the Borrower is the surviving corporation, (ii) any Person may merge into any Guarantor in a transaction in which the surviving entity is a Guarantor, (iii) any Subsidiary may sell, transfer, lease or otherwise dispose of its assets to the Borrower or to a Guarantor and (iv) any non-Guarantor may liquidate or dissolve if the Borrower determines in good faith that such liquidation or dissolution is in the best interests of the Borrower and is not materially disadvantageous to the Lenders; provided that any such merger involving a Person that is not a wholly owned Subsidiary immediately prior to such merger shall not be permitted unless also permitted by Section 7.04.



SECTION 7.04. Investments, Loans, Advances, Guarantees and Acquisitions. The Borrower will not, and will not permit any of its Subsidiaries to, purchase, hold or acquire (including pursuant to any merger with any Person that was not a wholly owned Subsidiary prior to such merger) any capital stock, evidences of indebtedness or other securities (including any option, warrant or other right to acquire any of the foregoing) of, make or permit to exist any loans or advances to, Guarantee any obligations of, or make or permit to exist any investment or any other interest in, any other Person, or purchase or otherwise acquire (in one transaction or a series of transactions) any assets of any other Person constituting a business unit, except:

(a) Permitted Investments;

(b) investments by the Borrower in the capital stock of its Subsidiaries, provided, that investments by the Borrower in the capital stock of non-Guarantor Subsidiaries, when aggregated with loans and advances to non-Guarantor Subsidiaries under section 7.04(c) shall not exceed \$100,000,000;

(c) loans or advances made by the Borrower to any Guarantor and made by any Guarantor to the Borrower, or any other Guarantor or any non-Guarantor Subsidiary to any other non-Guarantor Subsidiary and other loans or advances made by the Borrower or any Subsidiary in an aggregate amount not to exceed \$100,000,000;

(d) Guarantees constituting Indebtedness permitted by Section 7.01;

(e) investments consisting of Permitted Acquisitions.

SECTION 7.05. Restricted Payments. The Borrower will not, and will not permit any Guarantor to, declare or make, or agree to pay or make, directly or indirectly, any Restricted Payment, except that (a) any of the Borrower's Subsidiaries may pay dividends to the Borrower or other Subsidiaries, (b) the Borrower may pay dividends to Paychex Inc., and (c) Paychex Inc. may pay dividends to shareholders, provided that in the case of (c) above, the aggregate amount of all such dividends in any rolling four fiscal quarter period shall not exceed an amount equal to (i) one hundred percent of the current consolidated net income of Paychex, Inc. for such rolling four fiscal quarter period plus (ii) consolidated corporate cash on hand of Paychex, Inc., which for the avoidance of doubt, shall not include pledged securities or customer cash.

SECTION 7.06. Transactions with Affiliates. The Borrower will not, and will not permit any Guarantor to, sell, lease or otherwise transfer any property or assets to, or purchase, lease or otherwise acquire any property or assets from, or otherwise engage in any other transactions with, any of its non-Guarantor Affiliates, except in the ordinary course of business at prices and on terms and conditions not less favorable to the Borrower or such Subsidiary than could be obtained on an arm's-length basis from unrelated third parties and in an aggregate amount not to exceed \$50,000,000.

SECTION 7.07. Restrictive Agreements. The Borrower will not, and will not permit any of its Subsidiaries to, directly or indirectly, enter into, incur or permit to exist any agreement or other arrangement that prohibits, restricts or imposes any condition upon (a) the ability of the Borrower or any Subsidiary to create, incur or permit to exist any Lien upon any of its property or assets, or (b) the ability of any Subsidiary to pay dividends or other distributions with respect to any shares of its capital stock or to make or repay loans or advances to the Borrower or any other Subsidiary or to

Guarantee Indebtedness of the Borrower or any other Subsidiary; provided that (i) the foregoing shall not apply to restrictions and conditions imposed by law or by this Agreement, (ii) the foregoing shall not apply to restrictions and conditions existing on the date hereof identified on Schedule 7.07 (but shall apply to any extension or renewal of, or any amendment or modification expanding the scope of, any such restriction or condition), (iii) the foregoing shall not apply to customary restrictions and conditions contained in agreements relating to the sale of a Subsidiary pending such sale, provided such restrictions and conditions apply only to the Subsidiary that is to be sold and such sale is permitted hereunder, (iv) clause (a) of the foregoing shall not apply to restrictions or conditions imposed by any agreement relating to secured Indebtedness permitted by this Agreement if such restrictions or conditions apply only to the property or assets securing such Indebtedness and (v) clause (a) of the foregoing shall not apply to customary provisions in leases restricting the assignment thereof.

**ARTICLE VIII.**  
**EVENTS OF DEFAULT**

If any of the following events ("Events of Default") shall occur:

- (a) the Borrower shall fail to pay any principal of any Loan when and as the same shall become due and payable, whether at the due date thereof or at a date fixed for prepayment thereof or otherwise;
- (b) the Borrower shall fail to pay any interest on any Loan or any fee or any other amount (other than an amount referred to in clause (a) of this Article) payable under this Agreement, when and as the same shall become due and payable, and such failure shall continue unremedied for a period of three Business Days;
- (c) any representation or warranty made or deemed made by or on behalf of the Borrower or any Subsidiary in or in connection with this Agreement or any amendment or modification hereof or waiver hereunder, or in any report, certificate, financial statement or other document furnished pursuant to or in connection with this Agreement or any amendment or modification hereof or waiver hereunder, shall prove to have been materially incorrect when made or deemed made;
- (d) the Borrower shall fail to observe or perform any covenant, condition or agreement contained in Section 6.02, Section 6.03 (with respect to the Borrower's existence) or Section 6.08 or in ARTICLE III (provided, that with respect to failure to maintain the required Net Market Value of pledged securities, such failure continues beyond the one business day period for delivery of additional collateral set forth in section 3.2 of the Pledge Security Agreement), or ARTICLE VII or the Pledge Security Agreement or any Guarantor fails to perform or observe any term, covenant or agreement contained in Section 1, Section 2, Section 5 or Section 6 of the Guarantee Agreement;
- (e) the Borrower shall fail to observe or perform any covenant, condition or agreement contained in this Agreement or any of the Security Documents, or any Guarantor shall fail to observe or perform any other provision of the Guarantee

Agreement (other than those specified in clause (a), (b) or (d) of this Article), and such failure shall continue unremedied for a period of 30 days after notice thereof from the Administrative Agent to the Borrower (which notice will be given at the request of any Lender);

(f) the Borrower or any Subsidiary shall fail to make any payment (whether of principal or interest and regardless of amount) in respect of any Material Indebtedness, when and as the same shall become due and payable;

(g) any event or condition occurs that results in any Material Indebtedness becoming due prior to its scheduled maturity or that enables or permits (with or without the giving of notice, the lapse of time or both) the holder or holders of any Material Indebtedness or any trustee or agent on its or their behalf to cause any Material Indebtedness to become due, or to require the prepayment, repurchase, redemption or defeasance thereof, prior to its scheduled maturity; provided that this clause (g) shall not apply to secured Indebtedness that becomes due as a result of the voluntary sale or transfer of the property or assets securing such Indebtedness;

(h) an involuntary proceeding shall be commenced or an involuntary petition shall be filed seeking (i) liquidation, reorganization or other relief in respect of the Borrower or any Subsidiary or its debts, or of a substantial part of its assets, under any Federal, state or foreign bankruptcy, insolvency, receivership or similar law now or hereafter in effect or (ii) the appointment of a receiver, trustee, custodian, sequestrator, conservator or similar official for the Borrower or any Subsidiary or for a substantial part of its assets, and, in any such case, such proceeding or petition shall continue undismissed for 60 days or an order or decree approving or ordering any of the foregoing shall be entered;

(i) the Borrower or any Guarantor shall (i) voluntarily commence any proceeding or file any petition seeking liquidation, reorganization or other relief under any Federal, state or foreign bankruptcy, insolvency, receivership or similar law now or hereafter in effect, (ii) consent to the institution of, or fail to contest in a timely and appropriate manner, any proceeding or petition described in clause (h) of this Article, (iii) apply for or consent to the appointment of a receiver, trustee, custodian, sequestrator, conservator or similar official for the Borrower or any Subsidiary or for a substantial part of its assets, (iv) file an answer admitting the material allegations of a petition filed against it in any such proceeding, (v) make a general assignment for the benefit of creditors or (vi) take any action for the purpose of effecting any of the foregoing;

(j) the Borrower or any Guarantor shall become unable, admit in writing its inability or fail generally to pay its debts as they become due;

(k) one or more judgments for the payment of money in an aggregate amount in excess of \$25,000,000 shall be rendered against the Borrower, any Subsidiary or any combination thereof and the same shall remain undischarged, unbonded or otherwise unsecured for a period of 30 consecutive days (or the maximum period permitted under

the laws of the applicable jurisdiction) during which execution shall not be effectively stayed, or any action shall be legally taken by a judgment creditor to attach or levy upon any assets of the Borrower or any Subsidiary to enforce any such judgment;

(l) an ERISA Event shall have occurred that, in the opinion of the Required Lenders, when taken together with all other ERISA Events that have occurred, could reasonably be expected to result in a Material Adverse Effect; or

(m) a Change in Control shall occur;

then, and in every such event (other than an event with respect to the Borrower described in clause (h) or (i) of this Article), and at any time thereafter during the continuance of such event, the Administrative Agent may, and at the request of the Required Lenders shall, by notice to the Borrower, take either or both of the following actions, at the same or different times: (i) terminate the Commitments, and thereupon the Commitments shall terminate immediately, and (ii) declare the Loans then outstanding to be due and payable in whole (or in part, in which case any principal not so declared to be due and payable may thereafter be declared to be due and payable), and thereupon the principal of the Loans so declared to be due and payable, together with accrued interest thereon and all fees and other obligations of the Borrower accrued hereunder, shall become due and payable immediately, without presentment, demand, protest or other notice of any kind, all of which are hereby waived by the Borrower; and in case of any event with respect to the Borrower described in clause (h) or (i) of this Article, the Commitments shall automatically terminate and the principal of the Loans then outstanding, together with accrued interest thereon and all fees and other obligations of the Borrower accrued hereunder, shall automatically become due and payable, without presentment, demand, protest or other notice of any kind, all of which are hereby waived by the Borrower.

**ARTICLE IX.**  
**THE ADMINISTRATIVE AGENT**

Each of the Lenders hereby irrevocably appoints the Administrative Agent as its agent and authorizes the Administrative Agent to take such actions on its behalf and to exercise such powers as are delegated to the Administrative Agent by the terms hereof, together with such actions and powers as are reasonably incidental thereto including the authority, without the necessity of any notice to or further consent of the Lenders, from time to time to take any action on behalf of the Lenders with respect to any Collateral or the Security Documents which may be necessary to perfect, maintain perfected or insure the priority of the security interest in and liens upon the Collateral granted pursuant to the Security Documents.

The bank serving as the Administrative Agent hereunder shall have the same rights and powers in its capacity as a Lender as any other Lender and may exercise the same as though it were not the Administrative Agent, and such bank and its Affiliates may accept deposits from, lend money to and generally engage in any kind of business with the Borrower or any Subsidiary or other Affiliate thereof as if it were not the Administrative Agent hereunder.

As an independent contractor empowered by the Lenders to exercise certain rights and perform certain duties and responsibilities hereunder and under the other Credit Documents, the

Administrative Agent is nevertheless a “representative” of the Lenders, as that term is defined in Article 1 of the Uniform Commercial Code, for purposes of actions for the benefit of the Lenders and the Administrative Agent with respect to all Collateral security and Guarantees contemplated by the Credit Documents. Such actions include the designation of the Administrative Agent as “secured party”, “mortgagee” or the like on all financing statements and other documents and instruments, whether recorded or otherwise, relating to the attachment, perfection, priority or enforcement of any security interests, mortgages or deeds of trust in collateral security intended to secure the payment or performance of any of the Obligations, all for the benefit of the Lenders and the Administrative Agent.

The Administrative Agent shall not have any duties or obligations except those expressly set forth herein. Without limiting the generality of the foregoing, (a) the Administrative Agent shall not be subject to any fiduciary or other implied duties, regardless of whether a Default has occurred and is continuing, (b) the Administrative Agent shall not have any duty to take any discretionary action or exercise any discretionary powers, except discretionary rights and powers expressly contemplated hereby that the Administrative Agent is required to exercise in writing as directed by the Required Lenders (or such other number or percentage of the Lenders as shall be necessary under the circumstances as provided in Section 10.02), and (c) except as expressly set forth herein the Administrative Agent shall not have any duty to disclose, and shall not be liable for the failure to disclose, any information relating to the Borrower or any of its Subsidiaries that is communicated to or obtained by the bank serving as Administrative Agent or any of its Affiliates in any capacity. The Administrative Agent shall not be liable for any action taken or not taken by it with the consent or at the request of the Required Lenders (or such other number or percentage of the Lenders as shall be necessary under the circumstances as provided in Section 10.02) or in the absence of its own gross negligence or willful misconduct. The Administrative Agent shall not be deemed not to have knowledge of any Default unless and until written notice thereof is given to the Administrative Agent by the Borrower or a Lender, and the Administrative Agent shall not be responsible for or have any duty to ascertain or inquire into (i) any statement, warranty or representation made in or in connection with this Agreement, (ii) the contents of any certificate, report or other document delivered hereunder or in connection herewith, (iii) the performance or observance of any of the covenants, agreements or other terms or conditions set forth herein, (iv) the validity, enforceability, effectiveness or genuineness of this Agreement or any other agreement, instrument or document, or (v) the satisfaction of any condition set forth in ARTICLE V or elsewhere herein, other than to confirm receipt of items expressly required to be delivered to the Administrative Agent.

The Administrative Agent shall be entitled to rely upon, and shall not incur any liability for relying upon, any notice, request, certificate, consent, statement, instrument, document or other writing believed by it to be genuine and to have been signed or sent by the proper Person. The Administrative Agent also may rely upon any statement made to it orally or by telephone and believed by it to be made by the proper Person, and shall not incur any liability for relying thereon. The Administrative Agent may consult with legal counsel (who may be counsel for the Borrower), independent accountants and other experts selected by it, and shall not be liable for any action taken or not taken by it in accordance with the advice of any such counsel, accountants or experts.

The Administrative Agent may perform any and all their duties and exercise their rights and powers by or through any one or more sub-agents appointed by the Administrative Agent. The Administrative Agent and any such sub-agent may perform any and all their duties and exercise their rights and powers through their respective Related Parties. The exculpatory provisions of the preceding paragraphs shall apply to any such sub-agent and to the Related Parties of the Administrative Agent and any such sub-agent, and shall apply to their respective activities in connection with the syndication of the credit facilities provided for herein as well as activities as Administrative Agent.

Subject to the appointment and acceptance of a successor Administrative Agent as provided in this paragraph, the Administrative Agent may resign at any time by notifying the Lenders and the Borrower. Upon any such resignation, the Required Lenders shall have the right, in consultation with the Borrower, to appoint a successor. If no successor shall have been so appointed by the Required Lenders and shall have accepted such appointment within 30 days after the retiring Administrative Agent gives notice of its resignation, then the retiring Administrative Agent may, on behalf of the Lenders, appoint a successor Administrative Agent which shall be a bank with an office in New York, New York, or an Affiliate of any such bank. Upon the acceptance of its appointment as Administrative Agent hereunder by a successor, such successor shall succeed to and become vested with all the rights, powers, privileges and duties of the retiring Administrative Agent, and the retiring Administrative Agent shall be discharged from its duties and obligations hereunder. The fees payable by the Borrower to a successor Administrative Agent shall be the same as those payable to its predecessor unless otherwise agreed between the Borrower and such successor. After the Administrative Agent's resignation hereunder, the provisions of this Article and Section 10.03 shall continue in effect for the benefit of such retiring Administrative Agent, its sub-agents and their respective Related Parties in respect of any actions taken or omitted to be taken by any of them while it was acting as Administrative Agent.

Each Lender acknowledges that it has, independently and without reliance upon the Administrative Agent or any other Lender and based on such documents and information as it has deemed appropriate, made its own credit analysis and decision to enter into this Agreement. Each Lender also acknowledges that it will, independently and without reliance upon the Administrative Agent or any other Lender and based on such documents and information as it shall from time to time deem appropriate, continue to make its own decisions in taking or not taking action under or based upon this Agreement, any related agreement or any document furnished hereunder or thereunder.

**ARTICLE X.**  
**MISCELLANEOUS**

SECTION 10.01. Notices. (a) Except in the case of notices and other communications expressly permitted to be given by telephone (and subject to paragraph (b) below), all notices and other communications provided for herein shall be in writing and shall be delivered by hand or overnight courier service, mailed by certified or registered mail, as follows:

- (i) if to the Borrower, to it at 911 Panorama Trail South, Rochester, New York 14625, Attention of Secretary, with a copy to Paychex, Inc., 911

Panorama Trail South, Rochester, New York 14624, Attention of Chief Legal Officer;

(ii) if to the Administrative Agent, to JPMorgan Chase Bank, N.A., One Chase Square (T-9), Rochester, NY 14643, Attn: Hollie Calderon, Senior Vice President, Tel: (585) 797-0153, Fax: (585) 797-1880, with a copy to James Kibler, Senior Vice President, at the same address; and

(iii) if to any other Lender, to it at its address (or teletype number) set forth in its Administrative Questionnaire.

(b) Notices and other communications to the Lenders hereunder may be delivered or furnished by electronic communications pursuant to procedures approved by the Administrative Agent; provided that the foregoing shall not apply to notices pursuant to ARTICLE II unless otherwise agreed by the Administrative Agent and the applicable Lender. The Administrative Agent or the Borrower may, in its discretion, agree to accept notices and other communications to it hereunder by electronic communications pursuant to procedures approved by it; provided that approval of such procedures may be limited to particular notices or communications.

(c) Any party hereto may change its address or teletype number for notices and other communications hereunder by notice to the other parties hereto. All notices and other communications given to any party hereto in accordance with the provisions of this Agreement shall be deemed to have been given on the date of receipt.

SECTION 10.02. Waivers; Amendments. (a) No failure or delay by the Administrative Agent, or any Lender in exercising any right or power hereunder shall operate as a waiver thereof, nor shall any single or partial exercise of any such right or power, or any abandonment or discontinuance of steps to enforce such a right or power, preclude any other or further exercise thereof or the exercise of any other right or power. The rights and remedies of the Administrative Agent and the Lenders hereunder are cumulative and are not exclusive of any rights or remedies that they would otherwise have. No waiver of any provision of this Agreement or consent to any departure by the Borrower therefrom shall in any event be effective unless the same shall be permitted by paragraph (b) of this Section, and then such waiver or consent shall be effective only in the specific instance and for the purpose for which given. Without limiting the generality of the foregoing, the making of a Loan shall not be construed as a waiver of any Default, regardless of whether the Administrative Agent or any Lender may have had notice or knowledge of such Default at the time.

(b) Neither this Agreement nor any provision hereof may be waived, amended or modified except pursuant to an agreement or agreements in writing entered into by the Borrower and the Required Lenders or by the Borrower and the Administrative Agent with the consent of the Required Lenders; provided that no such agreement shall (i) increase the Commitment of any Lender without the written consent of such Lender, (ii) reduce the principal amount of any Loan or reduce the rate of interest thereon, or reduce any fees payable hereunder, without the written consent of each Lender affected thereby, (iii) postpone the scheduled date of payment of the principal amount of any Loan, or any interest thereon, or any fees payable hereunder, or

reduce the amount of, waive or excuse any such payment, or postpone the scheduled date of expiration of any Commitment, without the written consent of each Lender affected thereby, (iv) release all or a substantial portion of the Collateral or one or more significant Guarantors without the written consent of each Lender affected thereby, (v) change Section 2.14(b) or (c) in a manner that would alter the pro rata sharing of payments required thereby, without the written consent of each Lender, or (vi) change any of the provisions of this Section or the definition of "Required Lenders" or any other provision hereof specifying the number or percentage of Lenders required to waive, amend or modify any rights hereunder or make any determination or grant any consent hereunder, without the written consent of each Lender; provided further that no such agreement shall amend, modify or otherwise affect the rights or duties of the Administrative Agent hereunder without the prior written consent of the Administrative Agent.

SECTION 10.03. Expenses; Indemnity; Damage Waiver. (a) The Borrower shall pay (i) all reasonable out-of-pocket expenses incurred by the Administrative Agent and its Affiliates as more particularly set forth in the Fee Letter, including the reasonable fees, charges and disbursements of counsel for the Administrative Agent, in connection with the syndication of the credit facilities provided for herein, the preparation and administration of this Agreement or any amendments, modifications or waivers of the provisions hereof (whether or not the transactions contemplated hereby or thereby shall be consummated), (ii) all reasonable out-of-pocket expenses incurred by the Lenders, other than the Administrative Agent associated with review by their respective counsel of the definitive financing documentation, such expenses to be reimbursed by the Borrower up to an amount not to exceed \$5,000 per Lender (other than Administrative Agent), (iii) all out-of-pocket expenses incurred by the Administrative Agent or any Lender, including the fees, charges and disbursements of any counsel for the Administrative Agent or any Lender, in connection with the enforcement or protection of its rights in connection with this Agreement, including its rights under this Section, or in connection with the Loans made hereunder, including all such out-of-pocket expenses incurred during any workout or, restructuring.

(b) The Borrower shall indemnify the Administrative Agent and each Lender, and each Related Party of any of the foregoing Persons (each such Person being called an "Indemnitee") against, and hold each Indemnitee harmless from, any and all losses, liabilities, costs and related expenses, including the fees, charges and disbursements of any counsel for any Indemnitee, incurred by or asserted against any Indemnitee arising out of, in connection with, or as a result of (i) the execution or delivery of this Agreement or any agreement or instrument contemplated hereby, the performance by the parties hereto of their respective obligations hereunder or the consummation of the Transactions or any other transactions contemplated hereby, other than in connection with an assignment or other transfer by a Lender of all or any portion of its rights and obligations, (ii) any Loan or the use of the proceeds therefrom, (iii) any actual or alleged presence or release of Hazardous Materials on or from any property owned or operated by the Borrower or any of its Subsidiaries, or any Environmental Liability related in any way to the Borrower or any of its Subsidiaries, or (iv) any actual or prospective claim, litigation, investigation or proceeding relating to any of the foregoing, whether based on contract, tort or any other theory and regardless of whether



any Indemnitee is a party thereto; provided that such indemnity shall not, as to any Indemnitee, be available to the extent that such losses, claims, damages, liabilities or related expenses resulted from the gross negligence or willful misconduct of such Indemnitee.

(c) To the extent that the Borrower fails to pay any amount required to be paid by it to the Administrative Agent under paragraph (a) or (b) of this Section, each Lender severally agrees to pay to the Administrative Agent such Lender's Applicable Percentage (determined as of the time that the applicable unreimbursed expense or indemnity payment is sought) of such unpaid amount; provided that the unreimbursed expense or indemnified loss, claim, damage, liability or related expense, as the case may be, was incurred by or asserted against the Administrative Agent in its capacity as such.

(d) To the extent permitted by applicable law, the Borrower shall not assert, and hereby waives, any claim against any Indemnitee, on any theory of liability, for special, indirect, consequential or punitive damages (as opposed to direct or actual damages) arising out of, in connection with, or as a result of, this Agreement or any agreement or instrument contemplated hereby, the Transactions, any Loan or the use of the proceeds thereof.

(e) All amounts due under this Section shall be payable promptly after written demand therefor.

SECTION 10.04. Successors and Assigns. (a) The provisions of this Agreement shall be binding upon and inure to the benefit of the parties hereto and their respective successors and assigns permitted hereby except that (i) the Borrower may not assign or otherwise transfer any of its rights or obligations hereunder without the prior written consent of each Lender (and any attempted assignment or transfer by the Borrower without such consent shall be null and void) and (ii) no Lender may assign or otherwise transfer its rights or obligations hereunder except in accordance with this Section. Nothing in this Agreement, expressed or implied, shall be construed to confer upon any Person (other than the parties hereto, their respective successors and assigns permitted hereby (to the extent provided in paragraph (c) of this Section) and, to the extent expressly contemplated hereby, the Related Parties of each of the Administrative Agent and the Lenders) any legal or equitable right, remedy or claim under or by reason of this Agreement.

(b) (i) Subject to the conditions set forth in paragraph (b)(ii) below, any Lender may assign to one or more assignees all or a portion of its rights and obligations under this Agreement (including all or a portion of its Commitment and the Loans at the time owing to it) with the prior written consent (such consent not to be unreasonably withheld) of:

(A) the Borrower, provided that no consent of the Borrower shall be required for an assignment to a Lender, an Affiliate of a Lender, an Approved Fund or, if an Event of Default has occurred and is continuing, any other assignee;

(B) the Administrative Agent.

(ii) Assignments shall be subject to the following additional conditions:

(A) except in the case of an assignment to a Lender, an Affiliate of a Lender or an Approved Fund or an assignment of the entire remaining amount of the assigning Lender's Commitment, the amount of the Commitment or Loans of the assigning Lender subject to each such assignment (determined as of the date the Assignment and Assumption with respect to such assignment is delivered to the Administrative Agent) shall not be less than \$10,000,000 unless each of the Borrower and the Administrative Agent otherwise consent, provided that no such consent of the Borrower shall be required if an Event of Default has occurred and is continuing;

(B) each partial assignment shall be made as an assignment of a proportionate part of all the assigning Lender's rights and obligations under this Agreement;

(C) the parties to each assignment shall execute and deliver to the Administrative Agent an Assignment and Assumption, together with a processing and recordation fee of \$3,500; and

(D) the assignee, if it shall not be a Lender, shall deliver to the Administrative Agent an Administrative Questionnaire in which the assignee designates one or more Credit Contacts to whom all syndicate-level information (which may contain material non-public information about the Borrower, the Guarantors and their related parties or their respective securities) will be made available and who may receive such information in accordance with the assignee's compliance procedures and applicable laws, including Federal and state securities laws.

(E) the assignee hereby agrees to be bound by the terms of the Intercreditor Agreement as if it was an original signatory thereto.

For the purposes of this Section 10.04(b), the term "Approved Fund" has the following meaning:

"Approved Fund" means any Person (other than a natural person) that is engaged in making, purchasing, holding or investing in bank loans and similar extensions of credit in the ordinary course of its business and that is administered or managed by (a) a Lender, (b) an Affiliate of a Lender or (c) an entity or an Affiliate of an entity that administers or manages a Lender.

(iii) Subject to acceptance and recording thereof pursuant to paragraph (b)(iv) of this Section, from and after the effective date specified in each Assignment and Assumption the assignee thereunder shall be a party hereto and, to the extent of the interest assigned by such Assignment and Assumption, have the rights and obligations of a Lender under this Agreement, and the

assigning Lender thereunder shall, to the extent of the interest assigned by such Assignment and Assumption, be released from its obligations under this Agreement (and, in the case of an Assignment and Assumption covering all of the assigning Lender's rights and obligations under this Agreement, such Lender shall cease to be a party hereto but shall continue to be entitled to the benefits of Section 2.12, Section 2.13, and Section 10.03. Any assignment or transfer by a Lender of rights or obligations under this Agreement that does not comply with this Section 10.04 shall be treated for purposes of this Agreement as a sale by such Lender of a participation in such rights and obligations in accordance with paragraph (c) of this Section.

(iv) The Administrative Agent, acting for this purpose as an agent of the Borrower, shall maintain at one of its offices a copy of each Assignment and Assumption delivered to it and a register for the recordation of the names and addresses of the Lenders, and the Commitment of, and principal amount of the Loans owing to, each Lender pursuant to the terms hereof from time to time (the "Register"). The entries in the Register shall be conclusive, and the Borrower, the Administrative Agent and the Lenders may treat each Person whose name is recorded in the Register pursuant to the terms hereof as a Lender hereunder for all purposes of this Agreement, notwithstanding notice to the contrary. The Register shall be available for inspection by the Borrower and any Lender, at any reasonable time and from time to time upon reasonable prior notice.

(v) Upon its receipt of a duly completed Assignment and Assumption executed by an assigning Lender and an assignee, the assignee's completed Administrative Questionnaire (unless the assignee shall already be a Lender hereunder), the processing and recordation fee referred to in paragraph (b) of this Section and any written consent to such assignment required by paragraph (b) of this Section, the Administrative Agent shall accept such Assignment and Assumption and record the information contained therein in the Register; provided that if either the assigning Lender or the assignee shall have failed to make any payment required to be made by it pursuant to Section 2.04(b), Section 2.14(d) or Section 10.04(b)(ii)(C), the Administrative Agent shall have no obligation to accept such Assignment and Assumption and record the information therein in the Register unless and until such payment shall have been made in full, together with all accrued interest thereon. No assignment shall be effective for purposes of this Agreement unless it has been recorded in the Register as provided in this paragraph.

(c) (i) Any Lender may, without the consent of the Borrower or the Administrative Agent, sell participations to one or more banks or other entities (a "Participant") (other than an entity that could reasonably be considered to be a direct competitor of the Borrower) in all or a portion of such Lender's rights and obligations under this Agreement (including all or a portion of its Commitment and the Loans owing to it); provided that (A) such Lender's obligations under this Agreement shall remain unchanged, (B) such Lender shall remain solely responsible to the other parties hereto for the performance of such obligations and (C) the Borrower, the Administrative

Agent and the other Lenders shall continue to deal solely and directly with such Lender in connection with such Lender's rights and obligations under this Agreement. Any agreement or instrument pursuant to which a Lender sells such a participation shall provide that such Lender shall retain the sole right to enforce this Agreement and to approve any amendment, modification or waiver of any provision of this Agreement; provided that such agreement or instrument may provide that such Lender will not, without the consent of the Participant, agree to any amendment, modification or waiver described in Section 10.02(b) that affects such Participant. Subject to paragraph (c)(ii) of this Section, the Borrower agrees that each Participant shall be entitled to the benefits of Section 2.12 and Section 2.13 to the same extent as if it were a Lender and had acquired its interest by assignment pursuant to paragraph (b) of this Section. To the extent permitted by law, each Participant also shall be entitled to the benefits of Section 10.08 as though it were a Lender, provided such Participant agrees to be subject to Section 2.14(c) as though it were a Lender. Subject to Section 2.10(e), participants may request a promissory note evidencing the Loan.

(ii) A Participant shall not be entitled to receive any greater payment under Section 2.12 or Section 2.13 than the applicable Lender would have been entitled to receive with respect to the participation sold to such Participant, unless the sale of the participation to such Participant is made with the Borrower's prior written consent. A Participant that would be a Foreign Lender if it were a Lender shall not be entitled to the benefits of Section 2.13 unless the Borrower is notified of the participation sold to such Participant and such Participant agrees, for the benefit of the Borrower, to comply with Section 2.13(e) as though it were a Lender.

(d) Any Lender may at any time pledge or assign a security interest in all or any portion of its rights under this Agreement to secure obligations of such Lender, including without limitation any pledge or assignment to secure obligations to a Federal Reserve Bank, and this Section shall not apply to any such pledge or assignment of a security interest; provided that no such pledge or assignment of a security interest shall release a Lender from any of its obligations hereunder or substitute any such pledgee or assignee for such Lender as a party hereto.

SECTION 10.05. Survival. All covenants, agreements, representations and warranties made by the Borrower herein and in the certificates or other instruments delivered in connection with or pursuant to this Agreement shall be considered to have been relied upon by the other parties hereto and shall survive the execution and delivery of this Agreement and the making of any Loans, regardless of any investigation made by any such other party or on its behalf and notwithstanding that the Administrative Agent or any Lender may have had notice or knowledge of any Default or incorrect representation or warranty at the time any credit is extended hereunder, and shall continue in full force and effect as long as the principal of or any accrued interest on any Loan or any fee or any other amount payable under this Agreement is outstanding and unpaid and so long as the Commitments have not expired or terminated. The provisions of Section 2.12, Section 2.13, and Section 10.03 and ARTICLE IX shall survive and remain in full force and effect regardless of the consummation of the transactions contemplated hereby, the repayment of the Loans, the expiration or termination of the Commitments or the termination of this Agreement or any provision hereof.

SECTION 10.06. Counterparts; Integration; Effectiveness. This Agreement may be executed in counterparts (and by different parties hereto on different counterparts), each of which shall constitute an original, but all of which when taken together shall constitute a single contract. This Agreement and any separate letter agreements with respect to fees payable to the Administrative Agent constitute the entire contract among the parties relating to the subject matter hereof and supersede any and all previous agreements and understandings, oral or written, relating to the subject matter hereof. Except as provided in Section 5.01, this Agreement shall become effective when it shall have been executed by the Administrative Agent and when the Administrative Agent shall have received counterparts hereof which, when taken together, bear the signatures of each of the other parties hereto, and thereafter shall be binding upon and inure to the benefit of the parties hereto and their respective successors and assigns. Delivery of an executed counterpart of a signature page of this Agreement by telecopy shall be effective as delivery of a manually executed counterpart of this Agreement.

SECTION 10.07. Severability. Any provision of this Agreement held to be invalid, illegal or unenforceable in any jurisdiction shall, as to such jurisdiction, be ineffective to the extent of such invalidity, illegality or unenforceability without affecting the validity, legality and enforceability of the remaining provisions hereof; and the invalidity of a particular provision in a particular jurisdiction shall not invalidate such provision in any other jurisdiction.

SECTION 10.08. Right of Setoff. If an Event of Default shall have occurred and be continuing, each Lender and each of its Affiliates is hereby authorized at any time and from time to time, to the fullest extent permitted by law, to set off and apply any and all deposits (general or special, time or demand, provisional or final) at any time held and other obligations at any time owing by such Lender or Affiliate to or for the credit or the account of the Borrower against any of and all the obligations of the Borrower now or hereafter existing under this Agreement held by such Lender, irrespective of whether or not such Lender shall have made any demand under this Agreement and although such obligations may be unmaturred. The rights of each Lender under this Section are in addition to other rights and remedies (including other rights of setoff) which such Lender may have.

SECTION 10.09. Governing Law; Jurisdiction; Consent to Service of Process. (a) This Agreement shall be construed in accordance with and governed by the law of the State of New York.

(b) The Administrative Agent, each Lender and the Borrower hereby irrevocably and unconditionally submits, for itself and its property, to the exclusive jurisdiction of the Supreme Court of the State of New York sitting in Monroe County and of the United States District Court of the Western District of New York, and any appellate court from any thereof, in any action or proceeding arising out of or relating to this Agreement, or for recognition or enforcement of any judgment, and each of the parties hereto hereby irrevocably and unconditionally agrees that all claims in respect of any such action or proceeding may be heard and determined in such New York State or, to the extent permitted by law, in such Federal court. Each of the parties hereto agrees that a final judgment in any such action or proceeding shall be conclusive and may be enforced in other jurisdictions by suit on the judgment or in any other manner provided by law.

(c) The Administrative Agent, each Lender and the Borrower hereby irrevocably and unconditionally waives, to the fullest extent it may legally and effectively do so, any objection which it may now or hereafter have to the laying of venue of any suit, action or proceeding arising out of or relating to this Agreement in any court referred to in paragraph (b) of this Section. Each of the parties hereto hereby irrevocably waives, to the fullest extent permitted by law, the defense of an inconvenient forum to the maintenance of such action or proceeding in any such court.

(d) Each party to this Agreement irrevocably consents to service of process in the manner provided for notices in Section 10.01. Nothing in this Agreement will affect the right of any party to this Agreement to serve process in any other manner permitted by law.

SECTION 10.10. WAIVER OF JURY TRIAL. EACH PARTY HERETO HEREBY WAIVES, TO THE FULLEST EXTENT PERMITTED BY APPLICABLE LAW, ANY RIGHT IT MAY HAVE TO A TRIAL BY JURY IN ANY LEGAL PROCEEDING DIRECTLY OR INDIRECTLY ARISING OUT OF OR RELATING TO THIS AGREEMENT OR THE TRANSACTIONS CONTEMPLATED HEREBY (WHETHER BASED ON CONTRACT, TORT OR ANY OTHER THEORY). EACH PARTY HERETO (A) CERTIFIES THAT NO REPRESENTATIVE, AGENT OR ATTORNEY OF ANY OTHER PARTY HAS REPRESENTED, EXPRESSLY OR OTHERWISE, THAT SUCH OTHER PARTY WOULD NOT, IN THE EVENT OF LITIGATION, SEEK TO ENFORCE THE FOREGOING WAIVER AND (B) ACKNOWLEDGES THAT IT AND THE OTHER PARTIES HERETO HAVE BEEN INDUCED TO ENTER INTO THIS AGREEMENT BY, AMONG OTHER THINGS, THE MUTUAL WAIVERS AND CERTIFICATIONS IN THIS SECTION.

SECTION 10.11. Headings. Article and Section headings and the Table of Contents used herein are for convenience of reference only, are not part of this Agreement and shall not affect the construction of, or be taken into consideration in interpreting, this Agreement.

SECTION 10.12. Confidentiality. (a) Each of the Administrative Agent and the Lenders agrees to maintain the confidentiality of the Information (as defined below), except that Information may be disclosed (i) to its and its Affiliates' directors, officers, employees and agents, including accountants, legal counsel and other advisors (it being understood that the Persons to whom such disclosure is made will be informed of the confidential nature of such Information and instructed to keep such Information confidential) solely in connection with their relationships with each of the Borrower, the Guarantors, and affiliates thereof, (ii) to the extent requested by any regulatory authority, (iii) to the extent required by applicable laws or regulations or by any subpoena or similar legal process, (iv) to any other party to this Agreement, (v) in connection with the exercise of any remedies hereunder or any suit, action or proceeding relating to this Agreement or the enforcement of rights hereunder, (vi) subject to an agreement containing provisions substantially the same as those of this Section, to (A) any assignee of or Participant in, or any prospective assignee of or Participant in, any of its rights or obligations under this Agreement or (B) any actual or prospective counterparty (or its advisors) to any swap or derivative transaction relating to the Borrower and its obligations, (vii) with the consent of the Borrower or (viii) to the extent such Information (A) becomes publicly available other than as a result of a breach of this Section or (B) becomes available to the Administrative Agent or any Lender on a nonconfidential basis from a source other than the

Borrower. For the purposes of this Section, "Information" means all nonpublic information received from the Borrower relating to the Borrower or any affiliate of the Borrower or its or their business, other than any such information that is available to the Administrative Agent or any Lender on a nonconfidential basis prior to disclosure by the Borrower. Any Person required to maintain the confidentiality of Information as provided in this Section shall be considered to have complied with its obligation to do so if such Person has exercised the same degree of care to maintain the confidentiality of such Information as such Person would accord to its own confidential information, provided that such Person shall, at a minimum, exercise reasonable care.

(b) EACH LENDER ACKNOWLEDGES THAT INFORMATION AS DEFINED IN SECTION 10.12(a) FURNISHED TO IT PURSUANT TO THIS AGREEMENT MAY INCLUDE MATERIAL NON-PUBLIC INFORMATION CONCERNING THE BORROWER AND ITS RELATED PARTIES OR THEIR RESPECTIVE SECURITIES, AND CONFIRMS THAT IT HAS DEVELOPED COMPLIANCE PROCEDURES REGARDING THE USE OF MATERIAL NON-PUBLIC INFORMATION AND THAT IT WILL HANDLE SUCH MATERIAL NON-PUBLIC INFORMATION IN ACCORDANCE WITH THOSE PROCEDURES AND APPLICABLE LAW, INCLUDING FEDERAL AND STATE SECURITIES LAWS.

(c) ALL INFORMATION, INCLUDING REQUESTS FOR WAIVERS AND AMENDMENTS, FURNISHED BY THE BORROWER OR THE ADMINISTRATIVE AGENT PURSUANT TO, OR IN THE COURSE OF ADMINISTERING, THIS AGREEMENT WILL BE SYNDICATE-LEVEL INFORMATION, WHICH MAY CONTAIN MATERIAL NON-PUBLIC INFORMATION ABOUT THE BORROWER, AND ITS RELATED PARTIES OR SECURITIES. ACCORDINGLY, EACH LENDER REPRESENTS TO THE BORROWER AND THE ADMINISTRATIVE AGENT THAT IT HAS IDENTIFIED IN ITS ADMINISTRATIVE QUESTIONNAIRE A CREDIT CONTACT WHO MAY RECEIVE INFORMATION THAT MAY CONTAIN MATERIAL NON-PUBLIC INFORMATION IN ACCORDANCE WITH ITS COMPLIANCE PROCEDURES AND APPLICABLE LAW.

SECTION 10.13. Interest Rate Limitation. Notwithstanding anything herein to the contrary, if at any time the interest rate applicable to any Loan, together with all fees, charges and other amounts which are treated as interest on such Loan under applicable law (collectively the "Charges"), shall exceed the maximum lawful rate (the "Maximum Rate") which may be contracted for, charged, taken, received or reserved by the Lender holding such Loan in accordance with applicable law, the rate of interest payable in respect of such Loan hereunder, together with all Charges payable in respect thereof, shall be limited to the Maximum Rate and, to the extent lawful, the interest and Charges that would have been payable in respect of such Loan but were not payable as a result of the operation of this Section shall be cumulated and the interest and Charges payable to such Lender in respect of other Loans or periods shall be increased (but not above the Maximum Rate therefor) until such cumulated amount, together with interest thereon at the Federal Funds Effective Rate to the date of repayment, shall have been received by such Lender.

SECTION 10.14. USA PATRIOT Act. Each Lender that is subject to the requirements of the USA Patriot Act (Title III of Pub. L. 107-56 (signed into law October 26, 2001)) (the "Act") hereby notifies the Borrower that pursuant to the requirements of the Act, it is required to obtain, verify and record information that identifies the Borrower, which information includes the name and address of the Borrower and other information that will allow such Lender to identify the Borrower in accordance with the Act.

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IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be duly executed by their respective authorized officers as of the day and year first above written.

PAYCHEX OF NEW YORK LLC

By /s/ John M. Morphy  
Name: John M. Morphy  
Title: Senior Vice President, Chief Financial Officer, and Secretary

JPMORGAN CHASE BANK, N.A., as Lender and as Administrative Agent,

By /s/ Hollie E. Calderon  
Name: Hollie E. Calderon  
Title: Senior Vice President

BANK OF AMERICA, N.A., as Lender and as Co-Arranger and Co-Bookrunner

By /s/ Colleen M. O'Brien  
Name: Colleen M. O'Brien  
Title: Senior Vice President

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

I, JONATHAN J. JUDGE, 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 officer 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 officer 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 24, 2008

/s/ Jonathan J. Judge  
\_\_\_\_\_  
President and Chief Executive Officer

**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 officer 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 officer 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 24, 2008

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

**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, 2008 as filed with the Securities and Exchange Commission ("SEC") on the date hereof (the "Report"), I, JONATHAN J. JUDGE, Chief Executive 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 24, 2008

/s/ Jonathan J. Judge

Jonathan J. Judge

President and Chief Executive Officer

**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, 2008 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 24, 2008

/s/ John M. Morphy

John M. Morphy

Senior Vice President, Chief Financial Officer, and Secretary