

**Strong. Confident. Focused on the Future.**



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**Automatic Data Processing, Inc. (ADP) is one of the world's leading providers of technology-based outsourcing solutions to employers, the brokerage and financial services community, vehicle retailers and their manufacturers and the property and casualty insurance, auto collision repair and auto recycling industries.**

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# financial highlights

(In thousands, except per share amounts)  
Years ended June 30,

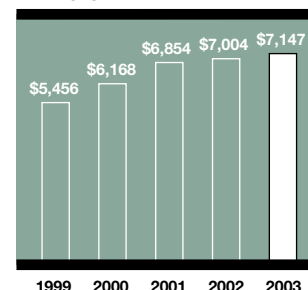
	2003	2002	Change
Total revenues	<b>\$ 7,147,017</b>	\$ 7,004,263	2%
Net earnings	<b>\$ 1,018,150</b>	\$ 1,100,770	(8%)
Basic earnings per share	<b>\$ 1.70</b>	\$ 1.78	(4%)
Diluted earnings per share	<b>\$ 1.68</b>	\$ 1.75	(4%)
Cash dividends	<b>\$ 284,605</b>	\$ 276,860	3%
Cash dividends per share	<b>\$ .4750</b>	\$ .4475	6%

Basic average shares outstanding	<b>600,071</b>	618,857
Diluted average shares outstanding	<b>605,917</b>	630,579
Return on equity	<b>19.4%</b>	22.4%

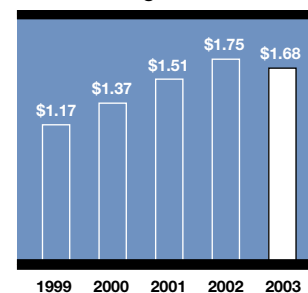
At year end:

Cash, cash equivalents and marketable securities	<b>\$ 2,344,343</b>	\$ 2,749,583
Working capital	<b>\$ 1,676,718</b>	\$ 1,406,155
Total assets before funds held for clients	<b>\$ 8,025,922</b>	\$ 7,051,251
Long-term debt	<b>\$ 84,674</b>	\$ 90,648
Shareholders' equity	<b>\$ 5,371,473</b>	\$ 5,114,205
Number of employees	<b>41,000</b>	40,000

**Total Revenues**  
in millions

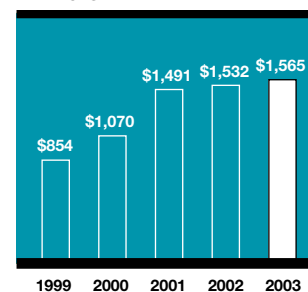


**Diluted Earnings Per Share**



The 2001, 2000 and 1999 data reflects the proforma impact relating to the July 1, 2001 adoption of Statement of Financial Accounting Standards No. 142, which eliminated goodwill amortization.

**Operating Cash Flow**  
in millions



Gary C. Butler

Arthur F. Weinbach



## Dear Shareholders,

**B**y ADP standards, fiscal 2003 was a difficult year. To help put that into perspective, in fiscal 2003, ADP had revenues in excess of \$7 billion, net earnings of \$1 billion, a return on equity of almost 20% and we continued our AAA financial rating by Standard & Poor's and Moody's. Strong results compared to most standards. For fiscal 2004, our forecast is for mid single-digit revenue growth and a decline of 5 to 10% in earnings per share. Our decision to make significant investments in future growth combined with the current interest rate environment are the primary reasons for the earnings per share decline.

The questions are:

1. Why was this a difficult period?
2. Why has ADP chosen to invest more now?
3. How does this affect the long-term outlook for ADP?

We will answer these questions in the text of this letter.

### *Why was this a difficult period?*

The continued weak economy has impacted Employer Services, Brokerage Services and interest rates in a significant way.

Employer Services has been impacted by the weakened economy with fewer new company formations, fewer decisions to change methods of processing, fewer employees employed by our clients and minimal growth in

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**OUR BUSINESS MODEL  
and financial strength  
provide us the ability to  
pursue opportunities even in  
times of economic  
uncertainty.**

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## **WE ARE INCREASING our investments in our most promising growth areas, particularly in Employer Services.**

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our clients' employees compensation (especially in bonus dollars and stock option profits). These factors clearly affect our ability to sell services to new clients and to grow revenues from existing clients.

Brokerage Services has felt the repercussions of the malaise in the stock market. There have been (i) reduced retail investor trades, (ii) consolidation of brokerage industry firms (with ADP's more retail-oriented clients more frequently the acquiree than the acquirer), (iii) no growth in street name shareholders, (iv) fewer IPOs and related one-time events, and (v) less discretionary spending, in general, by the industry. All of these items negatively affect our primarily volume-based back-office processing and investor communications activities.

Interest rates continued their decline to multi-decade lows with a 50-basis point decline in November and a 25-basis point decline in June on top of a 200-basis point drop in fiscal 2002. Since ADP's average daily balance of investable funds exceeded \$12 billion in fiscal 2003, the interest rate reductions caused a significant reduction in our interest income.

### *Why has ADP chosen to invest more now?*

At the same time that we are facing these difficulties, which are ongoing into fiscal 2004, we see exciting investment opportunities to enhance our leadership position in a number of our most critical markets and to reinforce our Employer of Choice relationship with our associates.

We are seeing growth opportunities where positive early market reaction to our new offerings clearly justifies an increased level of investment. Our business model and financial strength provide us the ability to pursue these opportunities even in times of economic uncertainty.

We've been tightening our belts long enough. Our markets are too good and our associates are too valuable to hold off on further investment. So, while the timing of the recovery remains unclear, now is the time to take aggressive steps to position us for the future. We understand that this bucks the trend of continuing cutbacks in the face of weakness, but we believe ADP's long-term opportunities and the value of our franchise justifies the short-term impact. We are taking actions along three critical paths: (i) increasing our investments in attractive growth opportunities; (ii) continued cost focus in selected areas; and (iii) reinvigorating our Employer of Choice initiatives. We started these actions toward the end of fiscal 2003.

**1. Growth** — We are increasing our investments in our most promising growth areas, particularly in Employer Services. These investments include both product development and product launch initiatives. Some of the Employer Services areas we have targeted include improved and increased use of Web front ends for payroll and benefits, a new 100% Web-native payroll offering targeted at companies with in-house systems, a new payroll platform for large companies and broadly increasing our sales coverage. In addition, we are increasing our investment in growth opportunities in each of our other core businesses.

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## **ADP IS A VERY STRONG company with solid results even in difficult periods and with excellent future growth prospects.**

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**2. Continued Cost Focus**—In areas where our growth has been short of our expectations, we have reduced or frozen headcount. In a limited number of cases, we are exiting non-performing product lines to focus our resources on more promising areas. Many of these actions took place in the 4th quarter of fiscal 2003 with some product exits still in process.

**3. Employer of Choice**—Retaining our *quality* associates is one of our most important objectives and we are committed to accomplishing this goal. We will restore full bonus plans in fiscal 2004, continue efforts to improve our competitive compensation and benefits and increase our focus on associate training.

We estimate we will invest about \$150 million in these initiatives in fiscal 2004.

### ***How does this affect the long-term outlook for ADP?***

ADP is a very strong company with solid results even in difficult periods and with excellent future growth prospects. The actions we are taking (which will contribute to fiscal 2004's forecasted 5 - 10% decline in earnings per share) will strengthen our powerful market posi-

tions and position us well for the inevitable rebound in our largest markets. If you believe as we do that the economy and related employment will grow, brokerage markets will rebound and interest rates will rise *and* if you combine these beliefs with (i) our market positions, financial strength, and powerful sales and service and (ii) the commitment of our many long-term associates, you should share our confidence in the future.

### **Acquisitions and Dispositions**

We supplement our internal growth with strategic acquisitions that extend our markets or add applications to our product sets. In fiscal 2003, we acquired 11 businesses with about \$270 million of revenues for an aggregate of approximately \$650 million.

The largest transactions were in Employer Services:

In June, we acquired ProBusiness Services, Inc., a leading provider of comprehensive payroll and human resource processing solutions to large employers (primarily Employer Services National Accounts) in the United States. This was our largest transaction with revenues approximating \$170 million; the aggregate purchase price was approximately \$500 million.

In May, we acquired the retirement services recordkeeping operations of Scudder Investments, a 401(k) and defined contribution plan recordkeeping business that fits with our Employer Services retirement services business.

In January, we acquired SMS, a market leader in the highly fragmented job tax credit market (an added application across our Small Business, Major Accounts and National Accounts Employer Services markets).

We also review each business and product line and dispose of those businesses that are no longer strategically relevant. In fiscal 2003, we sold or announced the intention to exit businesses with approximately \$65 million of revenues.

#### Major Initiatives

We remain focused on three major initiatives, which are important throughout economic cycles.

We are committed to providing *World Class Service* to our clients.

We must provide *Product Leadership* within our markets.

We cannot succeed unless we attract and retain knowledgeable and committed associates so we must be an *Employer of Choice*.

While the journey is not always a straight line, we are proud of our progress in each of these areas.

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**THE MOST CRITICAL  
element in ADP's success  
and future is our team  
of 41,000 associates who  
make the services we  
deliver every day superior.**

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#### Our Associates

The most critical element in ADP's success and future is our team of 41,000 associates who make the services we deliver every day superior. We are fortunate to attract and retain motivated, talented people who are committed to our aspirations and who help us win in the marketplace. We particularly want to thank our ADP associates whose efforts and results make our success possible.

#### The Future

We are confident about ADP's long-term prospects for good internal growth supplemented by selective acquisitions. We have the businesses, core competencies and most important the will, focus, commitment and dedication to succeed.



**Arthur F. Weinbach**  
Chairman and  
Chief Executive Officer



**Gary C. Butler**  
President and Chief  
Operating Officer

# strong. confident. focus

In fiscal 2003, ADP strengthened its market leadership position by continuing to invest in innovative products, services and processes through a down business cycle — confident that robust growth opportunities will return as the economy improves.

While many businesses followed conventional wisdom and opted to wait for the economy to rebound, ADP's decision was to invest and compete:

- We focused on our core businesses, consistently seeking to leverage their strengths.
- We brought to market a new generation of reliable, efficient and creative solutions in each of our major businesses.
- We supplemented our internal growth through selective acquisitions.
- We made a commitment to accelerate investment in high-growth parts of our business.
- We renewed our long-term commitment to provide World Class Service, ensuring that the client remains at the focal point of everything we do.
- We reinforced our Employer of Choice initiatives, enabling us to attract and retain the best-qualified associates.

Our clients rewarded our performance this year with some of the highest satisfaction scores in almost a decade. Despite the difficult economy, more clients are staying with us and expanding their relationship with ADP. Market acceptance of outsourcing solutions remains positive and future growth opportunities are present in all of our core business markets.

Three specific market differentiators, amplified by current economic conditions, continue to distinguish ADP from the competition: *our financial strength*, *our premier products* and *our associates*.

*Our financial strength* gives us the freedom and flexibility to remain on course with key investments in new products and services that help us to extend the reach and penetration of our core businesses. We are proud to be one of the most financially stable public companies in the world. Rated AAA by Standard & Poor's and Moody's, ADP is one of just seven U.S. industrial companies to earn these highest ratings of financial confidence.

*Our premier products* provide reliable solutions that are accompanied by responsive support and service. Many of our products and services are Web-driven to deliver the

high levels of functionality and flexibility that clients of every size and across every industry increasingly expect.

*Our associates* are the engine of our success and embody our commitment to World Class Service. Each and every day, they serve the needs of thousands of our clients all around the world with knowledge, skill, reliability and dedication — professional traits that are essential to a World Class Service environment. Our associates are ADP's most precious resource because they create, sell and service the business solutions that enable our clients to focus more time on their own core businesses.

## building and leveraging our core business strength.



**Clients in 26 countries rely on ADP's payroll and other employer-related services.**

Core businesses are the heart of any enterprise and are the primary source of a company's revenues. They gain their strength from core competencies — what a company does best. Successful core businesses build brand recognition, create value-added services and serve as a portal to new opportunities in adjacent markets.

ADP leverages its core business strengths to gain access to higher growth markets, develop opportunities to increase revenue-per-client, initiate new relationships and enhance our ability to increase client satisfaction and retention.



Even in an uncertain economy, ADP's vision remains focused on implementing innovative solutions — and investing in the future.

**Employer Services** continued to grow core payroll, which is ADP's oldest and largest business. In fiscal 2003, our key metrics for core payroll — revenues, margins and client population — all increased, despite less-than-ideal market conditions.

Core payroll strength is vital to our future growth, because the payroll process interfaces with many widely used employer-related functions that require extensive processing and recordkeeping, such as benefits and retirement plan administration and COBRA management. With so many companies choosing to outsource the administrative aspects of these requirements, we have built successful, growth-oriented businesses to address these opportunities, which we refer to as "Beyond Payroll."

This year, our Beyond Payroll businesses represent about one-third of total Employer Services North America revenues. Many of these payroll-related businesses had a successful year:

- **ADP Screening and Selection Services**, which provides pre-employment background checks, grew its revenue over 50%.
- **TotalSource®**, ADP's professional employer organization (PEO), opened five new offices and increased its revenue 37%.
- **Time and labor management revenue increased 18%.**

**Brokerage Services**, in a very difficult sales environment, continued to have success marketing the combined strength and synergies of our back-office processing and investor communications businesses to premier brokerage and financial services companies. This year, we signed a 10-year outsourcing agreement with E\*Trade Group to provide the firm with our integrated back-office processing and investor communications solution.

**Dealer Services** utilized the reliability of its traditional systems and service model to introduce a growing number of auto retailers to a new generation of advanced technology that efficiently provides business applications and service over the Internet. ADP's DealerSuite.com e-business portal gives these clients ready access to an array of Web-based products, services and tools, including links to consumer financial sources, as well as ADP client service.

**Claims Services** leveraged the market's confidence in our core estimatics products, enabling us to expand into new and promising geographical venues. For example, this year Audatex®, our international claims processing business, entered a joint venture with an organization of top insurers to improve the auto repair process throughout Mexico.

**ADP provides brokerage transaction processing and investor communications services worldwide.**



delivering  
**reliable and  
innovative solutions.**

**T**echnology — particularly Internet technology — and globalization have changed the way that businesses do business. As a leading provider of information services, our biggest strategic challenge is to continually find new and better ways to apply the increased functionality and flexibility of technology in order to improve business applications — and then deliver those solutions to wherever they are needed, across town or the other side of the world.

One way that ADP is responding to these new requirements is through the delivery of Web-based services:

**Employer Services** provides Web-based solutions in each of its market segments. All of these products are exceeding sales expectations. EasyPayNet<sup>SM</sup> is our Web-based payroll for small business employers. Pay eXpert<sup>®</sup> is part of a suite of Web-driven, employer-related services that serve mid-sized businesses, while Enterprise Payroll addresses the payroll needs of larger companies that desire a Web-based or hosted payroll solution.

In addition, TotalChoice<sup>SM</sup> Solutions, a Web-native, ADP-hosted human resources (HR) and payroll offering for mid-market employers, allows in-house users to retain direct control over their processing needs, connect with other ADP value-added services, and off-load the normal in-house burdens of performing system upgrades and maintenance.

**Brokerage Services** used the Internet to electronically deliver more than 17 million investor communications. Also, by consolidating or electronically delivering 30% of all proxies this year, we added significant value to our services by saving our clients about \$300 million in printing and postage expenses.

**Dealer Services** doubled the number of dealerships that use the ADP Customer Relationship Management (CRM) system, which helps our clients find, sell and keep their customers. We more than doubled the number of locations that utilize our Application Service Provider (ASP) Offsite Managed Services. Here, auto retailers outsource their IT infrastructure and management as well as technology decisions and system support to ADP. In addition, our Web-Enabled Business offering provides solution suites that empower vehicle dealers of any size to utilize the power and functionality of leading technology to run their businesses.

**Claims Services** introduced three new Web-based claims management applications — Claim Manager, Dispatch and Estimate Sharing — that automate manual processes and increase productivity for insurance companies, repair facilities and other businesses in the auto damage claims processing cycle.

## supplementing internal growth with selective acquisitions.

**W**e invested in our future by acquiring businesses that will augment internal growth, expand existing services and strengthen our leadership positions.

**Employer Services:** ProBusiness Services, Inc. — Serves large U.S. employers with comprehensive payroll, tax filing and HR processing services. This acquisition provides a strong strategic fit with our National Account Services and Benefit Services businesses.

Scudder Investments — ADP became the fourth-largest recordkeeper of retirement plans in the U.S. (based on number of plans) with the acquisition of Scudder Investments' 401(k) and defined contribution plan record-keeping operations.

SMS — ADP acquired the federal and state job tax credit business of SMS, making ADP the first major company in the payroll processing industry to offer these services.

eLabor®, Inc. — Provides hosted time and labor management solutions that serve small and lower mid-market businesses.

**Brokerage Services:** Vantra Group, Inc. — ADP acquired the assets of Vantra Group, Inc., specializing in Web-based solutions to brokerage clients.

Power Securities Systems, Inc. — Offers leading back-office software for niche market firms.

Dataphile Software Ltd. — Furnishes real-time, straight-through-processing solutions for brokerage firms and mutual fund securities dealers in Canada.

**Dealer Services:** LeaseStar, Ltd. — Supports auto dealerships with Web-driven lease quote services.

Automotive Directions, Inc. — Specializes in e-Customer Relationship Management solutions for auto retailers, adding significant value to our CRM and front-office solutions.

## making incremental investments in high-growth areas.



**More than 16,000 auto and truck retailers in North America and Europe are ADP clients.**

**W**hile most businesses are passive in times of uncertainty, market leaders take well-calculated, forward-looking actions in down markets in order to be fully prepared for the next economic upturn.

With that proactive mindset, we decided to increase our investment in attractive, high-growth, market-leading products that are built on new technology platforms. We are also exiting certain underperforming or non-strategic businesses and product lines.

By accelerating the rollout of product offerings such as TotalChoice Solutions (our Web-native product that targets in-house HR and payroll prospects), Enterprise (our payroll platform for large employers that require a comprehensive Web-based or hosted payroll solution), and the eXpert Services<sup>SM</sup> suite of Web-driven outsourcing solutions for mid-market employers, ADP is in a far more favorable position to accelerate growth rates much earlier than originally planned.

## renewing our commitment to world class service.



**ADP is a leading provider of automated claims solutions for the auto insurance, collision repair and auto recycling industries.**

**W**e know that our long-term success ultimately depends on how well we succeed in meeting our clients' expectations. Satisfied clients not only provide us with a steady flow of revenues, but are also historically the best source for new business referrals.

Six years ago, we began investing in an important company-wide initiative — a commitment to provide World Class Service. We invested in new tools, processes and training to consistently increase our overall service quality. Our product lines offer wide choice and access to reliable, leading technologies. New service models across our enterprise are meeting established goals and expectations by utilizing proven, high-tech tools that allow us to respond to client inquiries more accurately and rapidly.

ADP's strategic commitment empowers all of our associates to constantly improve our performance, to always strive to exceed client expectations and to work toward ever-higher levels of proficiency and service excellence. The yardsticks of our success include increased client satisfaction and improved client retention rates.

Our substantial, long-term investment in World Class Service is yielding significant results. Employer Services, Brokerage Services, Dealer Services and Claims Services all saw their client satisfaction scores reach record levels. Client retention also held strong or improved within each of our businesses.

These positive results, achieved in a tough economic climate, reinforce our belief that World Class Service is the foundation for our long-term success. We also know that a commitment to World Class Service is by definition a work-in-progress, because striving for excellence and leadership — especially in a competitive service environment — involves a continuous and rigorous journey, during which we anticipate market expectations will always grow higher.

## attracting and retaining results-oriented associates.

**I**n fiscal 2003, ADP reaffirmed its Employer of Choice commitment with plans to improve competitive compensation, associate training, career development and work environments. These plans, which we will expand in fiscal 2004, are a key component of our initiatives that will accelerate business growth.

Knowledgeable, results-oriented associates have always been important to ADP's success. Today, as the development and delivery of business solutions rely increasingly on the application of advanced technology, associates with high-tech skills are a critical core asset.

To keep succeeding, ADP must continue to attract and retain associates who have the skills we need, are driven by a passion for excellence and quality and share our vision to provide superior products and services.

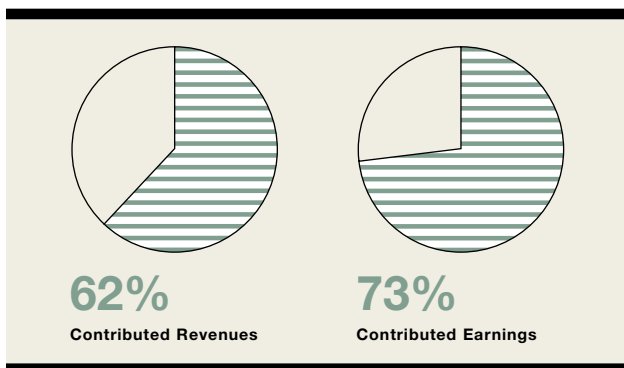
**A**t ADP, proven business principles — precepts that have served us well in prior economic downturns as well as periods of prosperity — fundamentally guide our actions. Notwithstanding a soft economy, ADP accomplished much in fiscal 2003. Even more important is all that we bring across the threshold into fiscal 2004.

ADP is strong, confident and focused on the future.

## ADP at-a-glance

# employer services

**ADP Employer Services is the leading full-service provider of a comprehensive range of human resource services, including traditional and Web-based outsourcing solutions that help over 460,000 employers staff, manage, pay and retain their employees.**



**ADP EMPLOYER SERVICES earned the highest client satisfaction scores and achieved the best retention rates in our history.**

## Major Markets

Employer Services focuses on client needs in three distinct market segments: National Account Services (employers with 1,000 or more employees); Major Accounts (50-999 employees); and Small Business Services (fewer than 50 employees). Geographical markets include: North America, Europe, Australia, Asia and Brazil.

## Products & Services

- Human resource information systems
- Benefits administration
- Payroll processing
- Payroll and business tax filing and reporting
- Money Movement – Full Service Direct Deposit, ADPCheck™, TotalPay® Card
- Regulatory compliance management services (including new hire reporting, wage garnishment processing, COBRA administration)
- Pre-employment screening and selection services
- Retirement plan services (primarily 401(k) Plans and SIMPLE IRAs)
- Section 529 College Plan administration
- Professional Employer Organization (PEO) – assisting small and mid-sized companies with comprehensive employment administration outsourcing solutions. These include: payroll, tax filing, employee background checks, HR guidance, 401(k) Plan administration, benefits administration, regulatory compliance services, workers' compensation insurance and supplemental benefits for employees.
- Time and labor management
- Comprehensive outsourcing of payroll and personnel administration services (i.e., managed services) worldwide including: data gathering, data entry, payroll control and other administrative tasks, depending on the client's needs and each country's regulations
- Job tax credit services that help employers file for special tax credits based upon geography, demographics and other criteria

## ADP PAYS 1 in 6 private sector workers in the U.S.

### FY '03 Employer Services Highlights

- Earned the highest client satisfaction scores in our history.
- Increased our client retention rate a full percentage point to record levels.
- Improved our associate retention levels.
- Brought more new products and services to market than in any prior year.
- Completed more acquisitions than in recent years.

### FY '03 Payroll Highlights

- Paid 1 in 6 private sector workers in the U.S. — 29 million worldwide.
- Prepared nearly 40 million Form W-2s.
- Grew our new Web-based solution for mid-sized companies, Pay eXpert®, to nearly 2,500 clients.
- Increased clients of our EasyPayNet<sup>SM</sup> Web-based small business payroll solution over the prior year by nearly 50% to 11,000.
- Launched PayForce<sup>SM</sup>, a comprehensive Web-based payroll solution for large employers.
- Provided payroll solutions in 26 countries to many of the world's largest multinational companies.
- Sustained our market-leading position as the largest provider of outsourced payroll services in the combined global markets we serve.
- Increased revenues in our Enterprise Payroll/HR product for larger clients by over 45%.
- Initiated the nationwide rollout of TotalChoice<sup>SM</sup>, our Web-native, full-featured HR solution for mid-sized companies that currently use in-house HR and payroll systems.
- Posted revenue growth of over 35% in our standalone tax services business.

### FY '03 Beyond Payroll Highlights

- Grew our TotalPay® direct deposit and payroll check product by 14% — the 7th consecutive year of substantial growth for this product.
- Achieved revenue growth of 37% in our PEO business, opened five new offices and served 13% more PEO worksite employees than during the prior year.
- Increased revenues more than 50% in ADP Screening and Selection Services, our business which provides clients with pre-employment background checks.
- Launched our TotalPay® Card electronic payroll product, an additional way for clients to pay their employees without using traditional paper checks.
- Increased revenues in our time and labor management business by 18%.
- Printed and delivered more than 72 million checks in our Print Services Division, which serves clients that have their own in-house payroll systems.
- Grew revenues over 15% in the portion of our 401(k) business that serves smaller plans.
- Entered agreements that made Merrill Lynch and Scudder Investments alliance partners for our retirement services business, complementing our existing alliances with Morgan Stanley, Bank of America and AIG SunAmerica.
- Gained a new recordkeeping platform, product capabilities and service model for our 401(k) and defined contribution National Account Services' clients as a result of our alliance with Scudder Investments.

## ADP at-a-glance

# brokerage services

**ADP Brokerage Services is a leading provider of transaction processing systems, desktop productivity applications and investor communications services to the financial services industry worldwide. Our clients include: retail and institutional brokerage firms, global banks, mutual funds, annuity companies, institutional investors, specialty trading firms, clearing firms and hedge funds, as well as publicly owned corporations.**

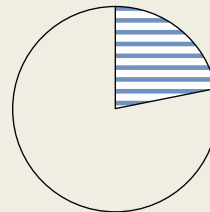
## Major Markets

Brokerage Services provides securities transaction processing of equities, fixed-income, mutual funds, derivatives, foreign exchange, and money market instruments, as well as the printing and distribution of investor communications, proxy voting and other services to clients in: North America, Europe, Asia, South America and Australia.

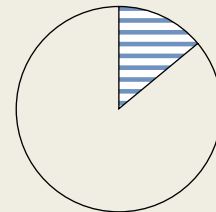
## Products & Services

- Global order entry, trade processing and settlement systems that enable firms to trade virtually any financial instrument, in any market, at any time
- Comprehensive Global Processing Solution that provides a best-of-breed product set over one platform, allowing firms to outsource all of their transaction processing worldwide
- Full-service investor communications services including: electronic delivery and Internet solutions; workflow services; financial, offset, and on-demand printing; proxy distribution and vote processing; householding; regulatory mailings; fulfillment; and customized communications
- Easy-to-use, browser-based desktop tools that increase the efficiency and productivity of financial consultants and back-office personnel, enabling firms to gather and retain more assets
- Internet trading and portfolio management solutions for brokerage firms to offer to their clients

**ADP DELIVERED OVER  
17 million investor  
communications via the  
Internet.**



**22%**  
Contributed Revenues



**14%**  
Contributed Earnings

## CLIENT SATISFACTION increased to record levels.

### FY '03 Brokerage Services Highlights

- Served the North American processing needs of most global banks.
- Signed a 10-year outsourcing agreement with E\*Trade Group to provide the firm with our integrated back-office processing and investor communications solution.
- Entered into an agreement with HSBC Brokerage (USA) Inc. to provide equities processing and broker desktop, statement, trade confirmation and proxy services.
- Expanded the strategic role of our operations in Hyderabad, India, as an offshore center for development and business process outsourcing services.
- Initiated global trade processing relationships with BNP Paribas, Mizuho Securities Co. Ltd. and Lazard Frères & Co.
- Signed an outsourcing agreement with WestLB AG to process international fixed-income instruments and support its treasury processing operations in London.
- Created a new trust processing system for Canadian banks that is fully integrated with the back-office processing system; Scotia Trust, a division of The Bank of Nova Scotia, is the system's first client.
- Delivered a major functional upgrade to our international brokerage capability to comply with the latest international standards (ISO 15022) well ahead of industry deadlines.
- Provided investor communication services to approximately 14,000 publicly traded companies and 450 mutual funds and annuity companies on behalf of more than 800 brokerage firms and banks.
- Distributed more than 750 million proxy and interim mailings, and 70 million prospectuses, enrollment kits and other pre- and post-sale documents; and processed the votes of over 465 billion shares.
- Consolidated or electronically delivered 30% of all proxies, saving clients about \$300 million in printing and postage costs.
- Extended the use of ProxyEdge®, ADP's proprietary electronic management system for institutional investors, to the mutual fund market to help that business community meet new SEC requirements concerning vote disclosure.
- Served more than 1,300 global institutions with ICS Global, our global proxy service, which provides a single platform for receiving and voting consolidated ballots for positions in over 90 countries.
- Enhanced our ReorgPlus® service, which delivers reorganization materials via paper and the Web, to include mailing of Bankruptcy, Default and Class Action notices.
- Increased the number of clients who use our ICSSOne® single-source solution, which combines regulatory and proxy processing distribution, vote tabulation and printing services for corporations and mutual funds. New ICSSOne clients include Outback Steakhouse, Agere Systems and Avaya.
- Provided mutual fund distribution services to MFS Investment Management, enabling it to reduce its mailing costs through the use of our sophisticated householding system and e-delivery of investor materials.
- Selected by MetLife Retirement & Savings to provide on-demand print services that create and produce 401(k) Plan participant enrollment materials for small and mid-sized employers. This comprehensive solution is designed to allow MetLife to reduce production costs, increase efficiency and incorporate customization into enrollment kits.
- Printed more than 8.5 billion document pages for the financial services industry this year through our financial printing business, as well as 1.4 billion statement and confirmation images for bank, broker and mutual fund clients — 38% more than last year.

## ADP at-a-glance

# dealer services

**ADP Dealer Services is a leading provider of integrated dealer management systems (DMS) and business solutions for automotive (car and heavy truck) retailers and their manufacturers.**

## Major Markets

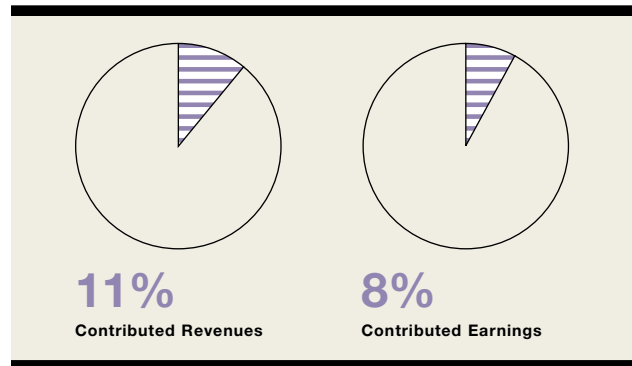
Dealer Services provides business solutions to new and used vehicle franchise retailers, heavy truck retailers and service centers, consolidators, and automotive and heavy truck manufacturers. Geographical markets include: North America and Europe.

## Products & Services

- Integrated hardware and software solutions that help automotive and truck retailers sell cars, parts and service more profitably
- Networking and telecommunications systems that link and improve communications between automotive retailers and their manufacturers, business partners and consumers
- Integrated information systems that help dealerships and manufacturers collect, manage and use customer, vehicle and third-party data to make well-informed business decisions
- Integrated Customer Relationship Management (CRM) solutions that enable retailers to increase sales and service revenues and decrease advertising costs
- Training and consulting services to help retailers and manufacturers improve employee productivity and maximize their return on technology investments
- High-speed Computerized Vehicle Registration (CVR<sup>®</sup>) system that electronically transmits documents, such as vehicle registration and title information, between dealerships and government agencies

## FY '03 Dealer Services Highlights

- Provided core dealer management systems to more than 16,000 automobile and truck dealers throughout North America and Europe.
- Sustained record-level client satisfaction scores for a fourth consecutive year.
- Maintained a client retention rate of 95%.



- Doubled the number of dealerships that are using our CRM application, which gives clients an integrated way to find, sell and keep customers.
- Served over 630 locations and 31,000 user connections with our ASP Offsite Managed Services, generating twice the revenue as last year.
- Increased our Networking Solutions revenues 55% as a result of greater market penetration and by helping manufacturers achieve key connectivity initiatives.
- Launched Web-Enabled Business — our comprehensive, next-generation dealer management system that is customizable to accommodate specific dealer size and technology needs.
- Added to our Internet offerings with the acquisition of LeaseStar, Ltd., which provides dealerships with Web-based automotive lease quoting applications.
- Introduced the “ADP Network Phone” which integrates voice and data. The IP (Internet Protocol) Telephony product suite will fully integrate with our CRM and other core dealer management system applications.
- Doubled revenues in our Digital Motorworks<sup>®</sup> data integration business which provides any dealership group, original equipment manufacturer (OEM) or third party with the ability to collect and utilize more accurate market data from which they can make better business decisions.
- Increased CVR electronic vehicle registration to 19 states.



ADP at-a-glance

# claims services

**ADP Claims Services is a leading international provider of integrated business solutions for clients in the property and casualty insurance, auto collision repair and auto recycling industries. Our products help clients manage costs and improve efficiency, and accelerate the claim review and settlement process.**

## Major Markets

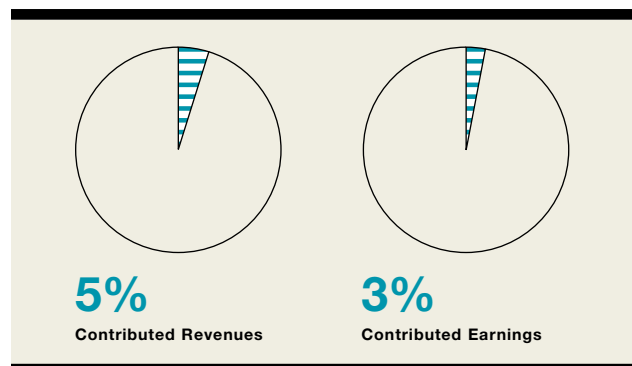
ADP Claims Services focuses on several market segments: auto insurance claims, auto insurance appraisers, auto collision repair centers, auto recyclers and other claims-related businesses. Geographical markets include: North America, Europe, Brazil, Israel and South Africa.

## Products & Services

- Claims management applications such as automated repair estimating, total loss vehicle valuation, first notice of loss, dispatch and assignment, claims audit, parts exchange and workflow applications that streamline the end-to-end claims process
- Body shop and auto recycler management systems
- Other applications, databases and services that enhance and optimize the claims process

## FY '03 Claims Services Highlights

- Processed claims for over one-third of all property and casualty insurance companies in North America and Europe.
- Provided our 10 millionth Autosource® total loss valuation transaction in February 2003, demonstrating the confidence that clients have in our ability to provide accurate valuations.
- Achieved a client retention rate of 94% in our North American markets.
- Released a robust new version of Shoplink®, ADP's collision repair estimating software, which presents fully integrated imaging.



- Launched three new Web-based claims management applications — Claim Manager, Dispatch and Estimate Sharing. These products provide insurance companies, collision repair facilities and other parties to the claims process with a smarter way to work by automating manual processes to reduce overall cycle time, deliver increased productivity and create higher customer satisfaction.
- Introduced a new management reporting application for insurers, Autosource Reporting Manager, and an enhanced version of our auditing application, Claimsflo® Passport.
- Achieved 3% annual growth in transactions in our Autosource total loss valuation product.
- Increased North American Direct Repair Program (DRP) transactions between collision repair facilities and insurance companies by 4% in fiscal 2003 compared to a year ago.
- Announced a joint venture in October 2002 between Audatex®, our international business line, and an organization of top insurance carriers to form Audatex Mexico. The mission of this joint venture is to improve the automotive repair process in Mexico.

## Selected Financial Data

(In thousands, except per share amounts)  
Years ended June 30,

	2003	2002	2001	2000	1999
Total revenues	<b>\$ 7,147,017</b>	\$ 7,004,263	\$ 6,853,652	\$ 6,168,432	\$ 5,455,707
Earnings before income taxes	<b>\$ 1,645,200</b>	\$ 1,786,970	\$ 1,525,010	\$ 1,289,600	\$ 1,084,500
Net earnings	<b>\$ 1,018,150</b>	\$ 1,100,770	\$ 924,720	\$ 840,800	\$ 696,840
Pro forma net earnings*			\$ 971,680	\$ 881,890	\$ 739,260
Basic earnings per share	<b>\$ 1.70</b>	\$ 1.78	\$ 1.47	\$ 1.34	\$ 1.13
Diluted earnings per share	<b>\$ 1.68</b>	\$ 1.75	\$ 1.44	\$ 1.31	\$ 1.10
Pro forma basic earnings per share*			\$ 1.54	\$ 1.41	\$ 1.20
Pro forma diluted earnings per share*			\$ 1.51	\$ 1.37	\$ 1.17
Basic average shares outstanding	<b>600,071</b>	618,857	629,035	626,766	615,630
Diluted average shares outstanding	<b>605,917</b>	630,579	645,989	646,098	636,892
Cash dividends per share	<b>\$ .4750</b>	\$ .4475	\$ .3950	\$ .3388	\$ .2950
Return on equity	<b>19.4%</b>	22.4%	19.9%	19.7%	18.7%
At year end:					
Cash, cash equivalents and marketable securities	<b>\$ 2,344,343</b>	\$ 2,749,583	\$ 2,596,964	\$ 2,452,549	\$ 2,169,040
Working capital	<b>\$ 1,676,718</b>	\$ 1,406,155	\$ 1,747,187	\$ 1,767,784	\$ 907,864
Total assets before funds held for clients	<b>\$ 8,025,922</b>	\$ 7,051,251	\$ 6,549,980	\$ 6,429,927	\$ 5,824,820
Total assets	<b>\$19,833,671</b>	\$18,276,522	\$17,889,090	\$16,850,816	\$12,839,553
Long-term debt	<b>\$ 84,674</b>	\$ 90,648	\$ 110,227	\$ 132,017	\$ 145,765
Shareholders' equity	<b>\$ 5,371,473</b>	\$ 5,114,205	\$ 4,700,997	\$ 4,582,818	\$ 4,007,941

\*Pro forma net earnings and earnings per share reflect the impact relating to the July 1, 2001 adoption of Statement of Financial Accounting Standards No. 142, which eliminated goodwill amortization.

## Management's Discussion and Analysis

### Critical Accounting Policies

Our Consolidated Financial Statements and accompanying notes have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires management to make estimates, judgments and assumptions that affect reported amounts of assets, liabilities, revenues and expenses. We continually evaluate the accounting policies and estimates used to prepare the consolidated financial statements. The estimates are based on historical experience and assumptions believed to be reasonable under current facts and circumstances. Actual amounts and results could differ from these estimates made by management. Certain accounting policies that require significant management estimates and are deemed critical to our results of operations or financial position are discussed below.

**Revenue Recognition.** Our revenues are primarily attributable to fees for providing services (e.g., Employer Services' payroll processing fees and Brokerage Services' trade processing fees) as well as investment income on payroll funds, tax filing funds and other Employer Services client-related funds. We typically enter into agreements for a fixed fee per transaction (e.g., number of payees). Fees associated with services are recognized in the period services are rendered and earned under service arrangements with clients where service fees are fixed or determinable and collectibility is reasonably assured. Interest income on collected but not yet remitted funds held for clients is recognized in revenues as earned.

We also recognize revenues associated with the sale of software systems and associated software licenses. For a majority of our software sales arrangements, which provide hardware, software licenses, installation and post customer support, revenues are recognized ratably over the software license term as objective evidence of the fair values of the individual elements in the sales arrangement does not exist.

The majority of our revenues are generated from a fee for service model (e.g., fixed-fee per transaction processed) in which revenue is recognized when the related services have been rendered under written price quotations or service agreements having stipulated terms and conditions which do not require management to make any significant judgments or assumptions regarding any potential uncertainties.

**Goodwill.** We review the carrying value of all our goodwill in accordance with Statement of Financial Accounting Standards (SFAS) No. 142, "Goodwill and Other Intangible Assets," by comparing the carrying value of our reporting units to their fair values. We are required to perform this comparison at least annually or more frequently if circumstances indicate possible

impairment. When determining fair value, we utilize various assumptions, including projections of future cash flows, our weighted average cost of capital and long-term growth rates for our businesses. Any significant adverse changes in key assumptions about our businesses and their prospects or an adverse change in market conditions may cause a change in the estimation of fair value and could result in an impairment charge. We have approximately \$2.0 billion of goodwill that is not impaired, based on our impairment testing as of June 30, 2003. Given the significance of our goodwill, an adverse change to the fair value could result in an impairment charge, which could be material to our financial statements.

**Income taxes.** We account for income taxes in accordance with SFAS No. 109, "Accounting for Income Taxes," which establishes financial accounting and reporting standards for the effect of income taxes. The objectives of accounting for income taxes are to recognize the amount of taxes payable or refundable for the current year and deferred tax liabilities and assets for the future tax consequences of events that have been recognized in an entity's financial statements or tax returns. Judgment is required in addressing the future tax consequences of events that have been recognized in our financial statements or tax returns (e.g., realization of deferred tax assets, results of IRS and other tax authorities' examinations of our tax returns). Fluctuations in the actual outcome of these future tax consequences could materially impact our financial statements.

### Results of Operations

#### Analysis of Consolidated Operations

(In millions, except per share amounts)

	Years Ended June 30,			Change		
	2003	2002	2001	2003	2002	2001
Total revenues	\$7,147	\$7,004	\$6,854	2%	2%	11%
Total expenses	\$5,502	\$5,217	\$5,329	5%	(2%)	9%
Earnings before income taxes	\$1,645	\$1,787	\$1,525	(8%)	17%	18%
Margin	23.0%	25.5%	22.3%			
Provision for income taxes	\$ 627	\$ 686	\$ 600	(9%)	14%	34%
Effective tax rate	38.1%	38.4%	39.4%			
Net earnings	\$1,018	\$1,101	\$ 925	(8%)	19%	10%
Diluted earnings per share	\$ 1.68	\$ 1.75	\$ 1.44	(4%)	22%	10%

## Management's Discussion and Analysis

### 2003

Our consolidated revenues grew 2% to \$7.1 billion in fiscal 2003, primarily due to an increase in Employer Services of 5% to \$4.4 billion and an increase in Dealer Services of 12% to \$788 million. These increases were offset by a decrease in our Brokerage Services business of 9%, or \$165 million. Interest income on client funds decreased due to lower interest yields, despite 7% growth in our average client balances during the year to \$8.9 billion. The average interest rate earned on both client funds and corporate funds, exclusive of realized gains/(losses) in fiscal 2003 was 3.9% compared to 4.9% in fiscal 2002. Our revenue growth was impacted primarily by continued weak economic conditions impacting our Employer Services and Brokerage Services businesses and our interest income.

Earnings before income taxes in fiscal 2003 decreased 8% to \$1.6 billion as total expenses grew at a faster rate than revenues. This decrease primarily reflects the 35% decrease in earnings before income taxes in Brokerage Services. While we have focused on cost containment initiatives throughout the fiscal years ended June 30, 2002 and 2003 in order to bring our expense structure in line with our slower revenue growth, our Brokerage Services' cost reductions did not offset the 9% decline in revenues in this business. In March 2003, we announced plans to reduce costs in underperforming or non-strategic businesses. Selling, general and administrative expenses grew 9% to \$1.8 billion and include approximately \$60 million of incremental restructuring charges relating to exiting of certain businesses and cost reduction efforts in certain slow growth businesses, most of which occurred in the fourth quarter of 2003. The restructuring is primarily severance costs, including charges to exit our medical claims business within Claims Services and a small payroll business servicing primarily government agencies, separate from our core payroll business, in the United Kingdom. Operating expenses increased 4% to \$3.1 billion, primarily driven by revenue growth in Employer Services and Dealer Services. Systems development and programming costs increased 5% to \$499 million due to continued investment in our products, primarily in our Employer Services business, and the maintenance of our existing technology throughout all of our businesses. Depreciation and amortization expense decreased 2% to \$275 million due to a decrease in capital expenditures of approximately \$12 million in fiscal 2003 and \$40 million in fiscal 2002. Other income for the year increased to \$127 million, or 12%, from the prior year due to an increase in our net realized gains associated with our investment portfolio of \$13.1 million.

Our effective tax rate for fiscal 2003 was 38.1%, a decrease of 0.3% from fiscal 2002. The decrease is attributable to a favorable mix in income among tax jurisdictions.

Fiscal 2003 net earnings decreased 8% to \$1.0 billion and the related diluted earnings per share decreased 4% to \$1.68. The decrease in net earnings primarily reflects the decrease in earnings before income taxes, slightly offset by a lower effective tax rate. The decrease in diluted earnings per share reflects the decrease in net earnings, partially offset by fewer shares outstanding due to the repurchase of approximately 27.4 million shares for approximately \$940 million during the year and the lower impact of stock options on dilution during fiscal 2003. The total share repurchases in fiscal 2003 is a reflection of our confidence in the long-term growth prospects of our businesses.

For fiscal 2004, we are forecasting mid-single digit revenue growth and diluted earnings per share of \$1.50 - \$1.60. This reflects our anticipation of the ongoing impact of the continued weak economy on Employer Services and Brokerage Services, and lower interest rates, causing a decline in interest income on corporate and client funds of \$60 - \$80 million from 2003. We expect to invest an incremental \$90 - \$100 million in our highest growth opportunities, primarily in Employer Services. We also expect to spend \$40 - \$45 million on our Employer of Choice initiatives aimed at retaining our quality associates.

### 2002

In fiscal 2002, our consolidated revenues increased 2% to \$7.0 billion compared to fiscal 2001. The increase was primarily due to an increase in Employer Services of 5% to \$4.2 billion offset by a decrease in interest income. Interest income decreased due to lower interest yields, despite higher average client fund balances. Revenue growth in fiscal 2002 was impacted by weak economic conditions resulting in slower sales, lower client retention and fewer employees on our clients' payrolls in our Employer Services business and reductions in discretionary spending in the financial services industry, particularly in research and implementation services.

Fiscal 2002 earnings before income taxes increased 17% to \$1.8 billion, primarily due to growth in revenue, declines in selling, general and administrative expenses and systems development and programming costs and a significant increase in other income. Operating expenses increased 2% to \$3.0 billion compared to fiscal 2001 primarily driven by revenue growth in Employer Services, Brokerage Services and Dealer Services. Selling, general and administrative expenses

decreased 4% to \$1.6 billion as a result of our cost containment initiatives during the year, to bring our expense structure in line with our slower revenue growth. Systems development and programming costs decreased 8% to \$475 million as a result of our cost containment initiatives during the year, primarily related to the maintenance of existing applications, while funding of investments in new products continued. Depreciation and amortization expense decreased 13% to \$279 million compared to the prior year due to the adoption of SFAS No. 142 which resulted in the elimination of goodwill amortization. Other income increased 58% to \$114 million, primarily due to the \$90 million write-off of our investment in Bridge Information Systems, Inc. (Bridge) in fiscal 2001 which was a non-cash, non-recurring write-off of our total investment in Bridge offset by a \$45 million decrease in interest income attributable to a 1.3% decrease in the average interest rates earned on corporate funds in fiscal 2002.

Our effective tax rate for fiscal 2002 was 38.4%, a decrease of 1% from fiscal 2001. The decrease in the effective tax rate was primarily due to the impact of adopting SFAS No. 142 and the resulting elimination of goodwill amortization expense in fiscal 2002. Adjusting fiscal 2001 for the pro forma impact of SFAS No. 142, the effective income tax rate was 38.5%.

Net earnings in fiscal 2002 increased 19% to \$1.1 billion and the related diluted earnings per share increased 22% to \$1.75. The increase in net earnings primarily reflected the increase in earnings before income taxes. The increase in diluted earnings per share primarily reflected the increase in net earnings, as well as fewer shares outstanding due to the repurchase of 17.4 million shares during fiscal 2002.

## Analysis of Business Segments

### Revenues

(In millions)	Years Ended June 30,			Change		
	2003	2002	2001	2003	2002	2001
Employer Services	\$4,401	\$4,180	\$3,964	5%	5%	12%
Brokerage Services	1,593	1,758	1,742	(9)	1	19
Dealer Services	788	706	683	12	3	(4)
Other	420	425	412	(1)	4	7
Reconciling items:						
Foreign exchange	119	8	23	-	-	-
Client fund interest	(174)	(73)	30	-	-	-
Total revenues	\$7,147	\$7,004	\$6,854	2%	2%	11%

### Earnings Before Income Taxes

(In millions)	Years Ended June 30,			Change		
	2003	2002	2001	2003	2002	2001
Employer Services	\$1,193	\$1,110	\$ 937	7%	18%	21%
Brokerage Services	230	354	332	(35)	7	(1)
Dealer Services	132	116	99	14	17	(12)
Other	143	157	60	(9)	162	84
Reconciling items:						
Foreign exchange	12	1	3	-	-	-
Client fund interest	(174)	(73)	30	-	-	-
Cost of capital charge	109	122	64	-	-	-
Total earnings before income taxes	\$1,645	\$1,787	\$1,525	(8%)	17%	18%

### Major Business Units

Certain revenues and expenses are charged to the business units at a standard rate for management and motivational reasons. Other costs are recorded based on management responsibility. As a result, various income and expense items, including certain non-recurring gains and losses, are recorded at the corporate level and certain shared costs are not allocated. The prior years' business unit revenues and earnings before income taxes have been adjusted to reflect fiscal 2003 budgeted foreign exchange rates.

### Employer Services

Employer Services' revenues grew 5% in fiscal 2003. Despite the continued negative impacts of the weak economy, Employer Services continued to grow primarily due to the increases in our North America payroll and tax businesses, as well as strong growth in our beyond payroll products including our Professional Employer Organization (PEO) business. Client retention improved 1% from the prior year, however, new business sales declined 2% for the year and pays per control, which represents the number of employees on our clients' payrolls, also decreased 1% for the year. Employer Services' revenues include interest earned on collected but not yet remitted funds held for clients at a standard rate of 6%, or \$543 million, an increase of 7% over fiscal 2002. Earnings before income taxes grew 7% as a result of increased revenues and our continued cost containment efforts.

## Management's Discussion and Analysis

On June 20, 2003, we acquired all of the outstanding shares of ProBusiness Services, Inc. for cash of approximately \$517 million, net of cash acquired. ProBusiness Services, Inc., which has become a part of our Employer Services segment, is expected to generate approximately \$150 million in revenue in fiscal 2004.

In fiscal 2002, Employer Services' revenues grew 5%, compared to 12% in 2001. Revenue growth was impacted by weak economic conditions, which resulted in slower sales, lower client retention due primarily to bankruptcies, and fewer pays per control. Employer Services' revenues shown above include interest earned on collected but not yet remitted funds held for clients at a standard rate of 6%, or \$505 million, an increase of 3% over fiscal 2001. Earnings before income taxes grew 18% as a result of increased revenues and continued cost containment efforts.

### Brokerage Services

Brokerage Services' revenues declined 9% in fiscal 2003 when compared to fiscal 2002 primarily due to continued industry consolidations which impact trades per day, reduced discretionary spending and reduced mutual fund and equity proxy mailings. Trade processing revenues declined due to a 13% decline in trades per day from 1.5 million in fiscal 2002 to 1.3 million in fiscal 2003. Revenue per trade also declined due to the change in the mix of retail vs. institutional trades, industry consolidations and pricing pressures. Proxy revenues declined due to a 6% decline in pieces delivered from 806 million in fiscal 2002 to 754 million in fiscal 2003. Stock record growth, which is a measure of how many shareholders own a security compared with the prior year and a key factor in the number of pieces delivered, decreased 1% in fiscal 2003 as compared to 10% growth in fiscal 2002. Earnings before income taxes declined 35% primarily due to the decline in revenues. We have continued to focus on cost reductions in our under-performing businesses in order to properly align our cost structure with the slower growth levels.

In fiscal 2002, revenues increased 1% compared to 19% in fiscal 2001. Excluding acquisitions, revenues would have decreased 4% primarily due to consolidations within the financial services industry affecting trade volumes and lower revenue per trade due to pricing pressures. A reduction in discretionary spending in the financial services industry, particularly in research and implementation services also contributed to the decline in fiscal 2002 revenue growth. Earnings before income taxes increased 7% as a result of operating efficiencies, the impact of our cost containment initiatives and the transition of the proxy mailings and voting process to electronic delivery.

### Dealer Services

Dealer Services' revenues increased 12% in fiscal 2003 when compared to fiscal 2002. Excluding acquisitions, revenue growth increased approximately 8%. Revenue growth was generated by strong client retention and increased revenues in the traditional core business as well as from new services, primarily Application Service Provider (ASP) managed services, Networking and Computer Vehicle Registration. Sales of our Customer Relationship Management Systems continue to be strong. Earnings before income taxes grew 14% as a result of increased revenues and continued cost containment efforts.

Fiscal 2002 revenues increased 3% compared to fiscal 2001. This revenue growth compares to a 4% revenue decline in fiscal 2001. Earnings before income taxes grew 17% due to operating efficiencies and cost containment efforts, offset by investments in new products and acquisitions.

### Other

The primary components of "Other" revenues are Claims Services, miscellaneous processing services and corporate expenses.

Reconciling items for revenues and earnings before income taxes include foreign exchange differences between the actual and the fiscal year 2003 budgeted foreign exchange rates and the adjustment for the difference between actual interest income earned on invested funds held for clients and interest credited to Employer Services at a standard rate of 6%.

The business unit results also include an internal cost of capital charge related to the funding of acquisitions and other investments. This charge is eliminated in consolidation and as such, represents a reconciling item to earnings before income taxes.

## Financial Condition

Our financial condition and balance sheet remain exceptionally strong. At June 30, 2003, cash and marketable securities approximated \$2.3 billion. Shareholders' equity was approximately \$5.4 billion and return on average equity for the year was over 19%. The ratio of long-term debt to equity at June 30, 2003 was 1.6%.

In fiscal 2003, zero coupon convertible subordinated notes were converted to 0.5 million shares of common stock.

On June 20, 2003, we purchased ProBusiness Services, Inc. for a total of approximately \$517 million, net of cash acquired, of which \$351 million was paid as of June 30, 2003 and the remaining \$166 million will be paid as former ProBusiness shareholders tender their shares. We also acquired ten other businesses during 2003 for approximately \$118 million, net of cash acquired. The cost of acquisitions in 2002 and 2001 aggregated \$232 million (including \$12 million in common stock) and \$75 million, respectively. The cash used in all of our acquisitions was generated from our cash flows from operations. See Note 3 to the Consolidated Financial Statements for more information regarding acquisitions.

Capital expenditures during 2003 were \$134 million following investments of \$146 million in 2002 and \$185 million in 2001. Capital expenditures in fiscal 2004 should approximate \$150 to \$175 million.

The following table provides a summary of our contractual obligations as of June 30, 2003:

(In thousands)	Payments due by period					Total
	Less than 1 year	1-3 years	3-5 years	More than 5 years		
<b>Contractual Obligations</b>						
<b>Debt Obligations<sup>(1)</sup></b>	\$ 825	\$ 574	\$ 1,017	\$ 83,083	\$ 85,499	
<b>Operating Lease Obligations<sup>(2)</sup></b>	296,258	366,042	168,298	99,057	929,655	
<b>Purchase Obligations<sup>(3)</sup></b>	40,109	19,817	6,394	101	66,421	
<b>Total</b>	<b>\$337,192</b>	<b>\$386,433</b>	<b>\$175,709</b>	<b>\$182,241</b>	<b>\$1,081,575</b>	

(1) These amounts are included in our Consolidated Balance Sheets. See Note 7 to the Consolidated Financial Statements for additional information about our debt and related matters.

(2) Included in these amounts are various facilities and equipment leases, and software license agreements. We enter into operating leases in the normal course of business relating to facilities and equipment. The majority of our lease agreements have fixed payment terms based on the passage of time. Certain leases require payment of maintenance and real estate taxes and contain escalation provisions based on future adjustments in price indices. Our future operating lease obligations could change if we exit certain contracts and if we enter into additional operating lease agreements.

(3) Purchase obligations primarily relate to maintenance agreements on our software, equipment and other assets.

It is not our business practice to enter into off-balance sheet arrangements. However, in the normal course of business, we do enter into contracts in which we make certain representations and warranties that guarantee the performance of our products and services as well as other indemnifications in the normal course of business. There have historically been no material losses related to such guarantees and indemnifications and we do not expect there to be any in the future.

## Liquidity and Capital Resources

The primary source of our liquidity is our net earnings of \$1.0 billion in fiscal 2003. Cash flows generated from operations were approximately \$1.6 billion for the year ended June 30, 2003, supporting our strong cash position. This amount compares to cash flows from operations of \$1.5 billion in fiscal 2002 and 2001.

Cash flows provided by investing activities in fiscal 2003 totaled \$177 million compared to cash flows used in investing activities in fiscal 2002 of approximately \$1.1 billion. This fluctuation between periods is primarily due to the timing of purchases and proceeds of marketable securities and client fund money market securities, the net change in client funds obligations and an increase in acquisitions in fiscal 2003.

Cash flows used in financing activities in fiscal 2003 totaled \$1.1 billion compared to \$928 million in fiscal 2002. This increase reflects higher repurchases of common stock of approximately \$63 million and lower proceeds from stock purchase plan and exercises of stock options of approximately \$135 million. In fiscal 2003, we purchased approximately 27.4 million shares of common stock at an average price per share of approximately \$34. As of June 30, 2003, we had remaining Board of Directors' authorization to purchase up to 43.5 million additional shares.

During fiscal 2003, approximately twenty percent of our overall investment portfolio was invested in cash and cash equivalents, which are therefore impacted almost immediately by changes in short-term interest rates. The other eighty percent of our investment portfolio was invested in fixed-income securities, with varying maturities of less than ten years, which are also subject to interest rate risk including reinvestment risk. We have historically had the ability to hold most of these investments until maturity, and therefore, fluctuations in interest rates have not had an adverse impact on income or cash flows.

## Management's Discussion and Analysis

Details regarding our corporate investments and funds held for clients are as follows:

(In millions)		2003	2002	2001
Years ended June 30,				
Average investment balances at cost:				
Corporate investments	\$	3,374.4	\$ 2,752.3	\$ 2,598.9
Funds held for clients		8,936.8	8,376.6	8,188.6
Total	\$	12,311.2	\$ 11,128.9	\$ 10,787.5
Average interest rates earned exclusive of realized gains/(losses) on corporate investments and funds held for clients		3.9%	4.9%	6.2%
Realized gains on available-for-sale securities	\$	34.5	\$ 22.7	\$ 15.0
Realized losses on available-for-sale securities	\$	(4.9)	\$ (6.2)	\$ (92.6)*
As of June 30:				
Unrealized pre-tax gains on available-for-sale securities	\$	375.9	\$ 208.8	\$ 140.2
Total available-for-sale securities	\$	9,875.9	\$ 9,856.4	\$ 7,729.4

\*Includes a \$90 million (\$54 million after-tax) non-cash, non-recurring write-off of our investment in Bridge Information Systems, Inc. See Note 2 to the Consolidated Financial Statements.

The earnings impact of future interest rate changes is based on many factors, which influence the return on our portfolio. These factors include, among others, the amount of invested funds and the overall portfolio mix between short-term and long-term investments. This mix varies during the year and is impacted by daily interest rate changes. A hypothetical change in interest rates of 25 basis points applied to estimated average investment balances in fiscal 2004 would result in approximately an \$11.0 million impact to earnings before income taxes over the twelve-month period.

In October 2002, we entered into a new \$4.0 billion unsecured revolving credit agreement with certain financial institutions, replacing an existing \$4.0 billion credit agreement. The interest rate applicable to the borrowings is tied to LIBOR or prime rate depending on the notification provided to the syndicated financial institutions prior to borrowing. We are also required to pay a facility fee on the credit agreement. The primary uses of the credit facility are to provide liquidity to the unsecured commercial paper program and to fund normal business operations, if necessary. There have been no borrowings through June 30, 2003 under the credit agreement, which expires in October 2003.

In April 2002, we initiated a short-term commercial paper program providing for the issuance of up to \$4.0 billion in aggregate maturity value of commercial paper at our discretion. Our commercial paper program is rated A-1+ by Standard and Poor's and Prime 1 by Moody's. These ratings denote the highest quality investment grade securities. Maturities of commercial paper can range from overnight to 270 days. We use the commercial paper issuances as a primary instrument to meet short-term financing requirements related to client funds obligations. At June 30, 2003 and 2002, there was no commercial paper outstanding. For the year ended June 30, 2003, we had average borrowings of \$879 million at an effective weighted average interest rate of 1.5%. From the inception of the commercial paper program in April 2002 through the fiscal year ended June 30, 2002, we had average borrowings of \$667 million at an effective weighted average interest rate of 1.8%.

Our short-term financing is sometimes obtained on a secured basis through the use of repurchase agreements, which are collateralized principally by U.S. government securities. These agreements generally have terms ranging from overnight up to ten days. At June 30, 2003 and 2002, there were no outstanding repurchase agreements. For the fiscal years ended June 30, 2003 and 2002, we had average outstanding borrowings of \$6 million and \$361 million, respectively, at an average interest rate of 3.0% and 2.6%, respectively.

In June 2003, we formed a new wholly-owned subsidiary, ADP Indemnity, Inc. The primary purpose of this subsidiary is to provide workers' compensation insurance coverage for our PEO worksite employees. This insurance was previously provided by a third party. At June 30, 2003, ADP Indemnity, Inc. had a cash balance of approximately \$62.1 million to cover potential future insurance claims.



### Market Price, Dividend Data and Other

The market price of our common stock (symbol: ADP) based on New York Stock Exchange composite transactions and cash dividends per share declared during the past two years have been:

	Price Per Share		Dividends
	High	Low	Per Share
<b>Fiscal 2003 quarter ended</b>			
<b>June 30</b>	<b>\$36.08</b>	<b>\$30.80</b>	<b>\$.1200</b>
<b>March 31</b>	<b>\$40.81</b>	<b>\$27.24</b>	<b>\$.1200</b>
<b>December 31</b>	<b>\$45.96</b>	<b>\$33.76</b>	<b>\$.1200</b>
<b>September 30</b>	<b>\$43.75</b>	<b>\$31.15</b>	<b>\$.1150</b>
Fiscal 2002 quarter ended			
June 30	\$58.00	\$42.35	\$.1150
March 31	\$59.53	\$51.00	\$.1150
December 31	\$60.37	\$46.70	\$.1150
September 30	\$53.97	\$41.00	\$.1025

As of June 30, 2003, there were approximately 35,884 holders of record of our common stock. Approximately 316,607 additional holders have their stock in "street name."

### New Accounting Pronouncements

In March 2003, the Emerging Issues Task Force (EITF) published EITF Issue No. 00-21 "Accounting for Revenue Arrangements with Multiple Deliverables" (EITF 00-21). EITF 00-21 addresses certain aspects of the accounting by a vendor for arrangements under which it performs multiple revenue-generating activities and how to determine whether such an arrangement involving multiple deliverables contains more than one unit of accounting for purposes of revenue recognition. The guidance in EITF 00-21 is effective for revenue arrangements entered into in fiscal periods beginning after June 15, 2003. Accordingly, we have adopted EITF 00-21 effective July 1, 2003. We do not expect EITF 00-21 to have a material impact on our Consolidated Financial Statements.

### Forward-Looking Statements

This report and other written or oral statements made from time to time by ADP may contain "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Statements that are not historical in nature and which may be identified by the use of words like "expects," "projects," "anticipates," "estimates," "we believe," "could be" and other words of similar meaning, are forward-looking statements. These statements are based on management's expectations and assumptions and are subject to risks and uncertainties that may cause actual results to differ materially from those expressed. Factors that could cause actual results to differ materially from those contemplated by the forward-looking statements include: ADP's success in obtaining, retaining and selling additional services to clients; the pricing of products and services; changes in laws regulating payroll taxes, professional employer organizations and employee benefits; overall market and economic conditions, including interest rate and foreign currency trends; competitive conditions; stock market activity; auto sales and related industry changes; employment and wage levels; changes in technology; availability of skilled technical associates and the impact of new acquisitions and divestitures. ADP disclaims any obligation to update any forward-looking statements, whether as a result of new information, future events or otherwise.

## Statements of Consolidated Earnings

Automatic Data Processing, Inc. and Subsidiaries

(In thousands, except per share amounts)  
Years Ended June 30,

	2003	2002	2001
Revenues other than interest on funds held for clients and PEO revenues	<b>\$6,412,059</b>	\$6,305,206	\$6,100,112
Interest on funds held for clients	<b>368,727</b>	431,236	518,956
PEO revenues <sup>(A)</sup>	<b>366,231</b>	267,821	234,584
Total revenues	<b>7,147,017</b>	7,004,263	6,853,652
Operating expenses	<b>3,096,719</b>	2,970,645	2,900,124
Selling, general and administrative expenses	<b>1,758,353</b>	1,606,690	1,665,447
Systems development and programming costs	<b>499,192</b>	474,843	514,279
Depreciation and amortization	<b>274,682</b>	279,077	320,856
Other income, net	<b>(127,129)</b>	(113,962)	(72,064)
	<b>5,501,817</b>	5,217,293	5,328,642
Earnings before income taxes	<b>1,645,200</b>	1,786,970	1,525,010
Provision for income taxes	<b>627,050</b>	686,200	600,290
Net earnings	<b>\$1,018,150</b>	\$1,100,770	\$ 924,720
Basic earnings per share	<b>\$ 1.70</b>	\$ 1.78	\$ 1.47
Diluted earnings per share	<b>\$ 1.68</b>	\$ 1.75	\$ 1.44
Basic average shares outstanding	<b>600,071</b>	618,857	629,035
Diluted average shares outstanding	<b>605,917</b>	630,579	645,989

(A) Net of pass-through costs of \$3,462,783, \$2,648,321 and \$2,446,768, respectively.

See notes to consolidated financial statements.

# Consolidated Balance Sheets

Automatic Data Processing, Inc. and Subsidiaries

(In thousands, except per share amounts)  
June 30,

	2003	2002
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 1,410,218	\$ 798,810
Short-term marketable securities	595,166	677,005
Accounts receivable, net	1,005,833	1,045,170
Other current assets	664,284	296,272
Total current assets	3,675,501	2,817,257
Long-term marketable securities	338,959	1,273,768
Long-term receivables	180,354	192,769
Property, plant and equipment:		
Land and buildings	477,682	458,478
Data processing equipment	780,044	696,829
Furniture, leaseholds and other	603,451	540,217
	1,861,177	1,695,524
Less accumulated depreciation	(1,246,476)	(1,099,073)
	614,701	596,451
Other assets	565,385	293,808
Goodwill	1,981,131	1,375,654
Intangible assets, net	669,891	501,544
Total assets before funds held for clients	8,025,922	7,051,251
Funds held for clients	11,807,749	11,225,271
Total assets	<b>\$19,833,671</b>	<b>\$18,276,522</b>
<b>Liabilities and Shareholders' Equity</b>		
Current liabilities:		
Accounts payable	\$ 173,988	\$ 148,694
Accrued expenses and other current liabilities	1,609,665	1,035,389
Income taxes payable	215,130	227,019
Total current liabilities	1,998,783	1,411,102
Long-term debt	84,674	90,648
Other liabilities	270,267	233,671
Deferred income taxes	320,796	237,633
Deferred revenues	338,763	138,893
Total liabilities before client funds obligations	3,013,283	2,111,947
Client funds obligations	11,448,915	11,050,370
Total liabilities	14,462,198	13,162,317
Shareholders' equity:		
Preferred stock, \$1.00 par value: Authorized, 300 shares; issued, none	—	—
Common stock, \$.10 par value: Authorized, 1,000,000 shares; issued, 638,702 shares at June 30, 2003 and 2002	63,870	63,870
Capital in excess of par value	211,339	333,371
Retained earnings	6,710,863	5,977,318
Treasury stock - at cost: 43,863 and 22,385 shares, respectively	(1,773,418)	(1,142,041)
Accumulated other comprehensive income (loss)	158,819	(118,313)
Total shareholders' equity	5,371,473	5,114,205
Total liabilities and shareholders' equity	<b>\$19,833,671</b>	<b>\$18,276,522</b>

See notes to consolidated financial statements.

## Statements of Consolidated Shareholders' Equity

Automatic Data Processing, Inc. and Subsidiaries

(In thousands, except per share amounts)	Common Stock		Capital in Excess of Par Value	Retained Earnings	Treasury Stock	Comprehensive Income	Accumulated Other Comprehensive Income (Loss)
	Shares	Amount					
Balance at June 30, 2000	631,443	\$63,144	\$402,767	\$4,477,141	\$ (130,800)		\$(229,434)
Net earnings	—	—	—	924,720	—	\$ 924,720	—
Currency translation adjustments						(80,816)	(80,816)
Unrealized net gain on securities, net of tax						77,286	77,286
Comprehensive income						\$ 921,190	
Employee stock plans and related tax benefits	6,878	688	163,464	—	187,058		
Treasury stock acquired (16,558 shares)	—	—	—	—	(935,064)		
Acquisitions (22 shares)	—	—	234	—	839		
Debt conversion (1,303 shares)	381	38	(12,538)	—	40,723		
Dividends (\$.3950 per share)	—	—	—	(248,453)	—		
Balance at June 30, 2001	638,702	63,870	553,927	5,153,408	(837,244)		(232,964)
Net earnings	—	—	—	1,100,770	—	\$ 1,100,770	—
Currency translation adjustments						73,504	73,504
Unrealized net gain on securities, net of tax						41,147	41,147
Comprehensive income						\$ 1,215,421	
Employee stock plans and related tax benefits	—	—	(197,083)	—	515,729		
Treasury stock acquired (17,412 shares)	—	—	—	—	(875,449)		
Acquisitions (226 shares)	—	—	(423)	—	12,848		
Debt conversion (705 shares)	—	—	(23,050)	—	42,075		
Dividends (\$.4475 per share)	—	—	—	(276,860)	—		
Balance at June 30, 2002	638,702	63,870	333,371	5,977,318	(1,142,041)		(118,313)
<b>Net earnings</b>	—	—	—	<b>1,018,150</b>	—	<b>\$ 1,018,150</b>	—
<b>Currency translation adjustments</b>						<b>174,046</b>	<b>174,046</b>
<b>Unrealized net gain on securities, net of tax</b>						<b>108,562</b>	<b>108,562</b>
<b>Minimum pension liability adjustment, net of tax</b>						<b>(5,476)</b>	<b>(5,476)</b>
<b>Comprehensive income</b>						<b>\$ 1,295,282</b>	
Employee stock plans and related tax benefits	—	—	(103,593)	—	268,938		
Treasury stock acquired (27,413 shares)	—	—	—	—	(938,545)		
Acquisitions (294 shares)	—	—	(3,056)	—	14,883		
Debt conversion (462 shares)	—	—	(15,383)	—	23,347		
Dividends (\$.4750 per share)	—	—	—	(284,605)	—		
<b>Balance at June 30, 2003</b>	<b>638,702</b>	<b>\$63,870</b>	<b>\$211,339</b>	<b>\$6,710,863</b>	<b>\$(1,773,418)</b>		<b>\$ 158,819</b>

See notes to consolidated financial statements.

# Statements of Consolidated Cash Flows

Automatic Data Processing, Inc. and Subsidiaries

(In thousands) Years Ended June 30,	2003	2002	2001
<b>Cash Flows From Operating Activities</b>			
Net earnings	\$ 1,018,150	\$ 1,100,770	\$ 924,720
Adjustments to reconcile net earnings to net cash flows provided by operating activities:			
Depreciation and amortization	274,682	279,077	320,856
Write-off of investment in Bridge Information Systems, Inc.	—	—	90,000
Deferred income taxes	(15,775)	8,680	29,450
Increase in receivables and other assets	(94,422)	(73,511)	(70,699)
Increase in accounts payable and accrued expenses	287,174	138,141	182,634
Other	95,280	78,547	14,063
Net cash flows provided by operating activities	<u>1,565,089</u>	<u>1,531,704</u>	<u>1,491,024</u>
<b>Cash Flows From Investing Activities</b>			
Purchases of marketable securities	(3,451,554)	(6,243,228)	(6,864,707)
Proceeds from sale of marketable securities	4,014,300	4,167,028	3,087,406
Net proceeds from client fund money market securities	1,501,286	1,645,908	2,891,273
Net change in client funds obligations	(967,797)	(188,484)	818,082
Capital expenditures	(133,758)	(145,621)	(185,406)
Additions to intangibles	(144,728)	(109,799)	(97,448)
Acquisitions of businesses, net of cash acquired	(651,320)	(219,783)	(73,667)
Disposals of businesses	4,035	7,200	900
Other	6,609	6,286	(32,267)
Net cash flows provided by (used in) investing activities	<u>177,073</u>	<u>(1,080,493)</u>	<u>(455,834)</u>
<b>Cash Flows From Financing Activities</b>			
Payments of debt	(1,384)	(3,919)	(48,567)
Proceeds from issuance of notes	964	358	26,435
Repurchases of common stock	(938,545)	(875,449)	(935,064)
Proceeds from stock purchase plan and exercises of stock options	92,816	228,113	218,178
Dividends paid	(284,605)	(276,860)	(248,453)
Net cash flows used in financing activities	<u>(1,130,754)</u>	<u>(927,757)</u>	<u>(987,471)</u>
Net change in cash and cash equivalents	611,408	(476,546)	47,719
Cash and cash equivalents, at beginning of period	798,810	1,275,356	1,227,637
Cash and cash equivalents, at end of period	<u>\$ 1,410,218</u>	<u>\$ 798,810</u>	<u>\$ 1,275,356</u>

See notes to consolidated financial statements.

## Notes to Consolidated Financial Statements

Automatic Data Processing, Inc. and Subsidiaries

Years ended June 30, 2003, 2002 and 2001

(Unless otherwise noted, amounts in thousands, except per share amounts)

### NOTE 1 Summary of Significant Accounting Policies

**A. Consolidation and Basis of Preparation.** The consolidated financial statements include the financial results of Automatic Data Processing, Inc. and its majority-owned subsidiaries (the "Company" or "ADP"). Intercompany balances and transactions have been eliminated in consolidation.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from these estimates.

**B. Revenue Recognition.** A majority of the Company's revenues are attributable to fees for providing services (e.g., Employer Services' payroll processing fees and Brokerage Services' trade processing fees) as well as investment income on payroll funds, tax filing funds and other Employer Services' client-related funds. The Company typically enters into agreements for a fixed fee per transaction (e.g., number of payees). Fees associated with services are recognized in the period services are rendered and earned under service arrangements with clients where service fees are fixed or determinable and collectibility is reasonably assured. Interest income on collected but not yet remitted funds held for clients is recognized in revenues as earned.

The Company also recognizes revenues associated with the sale of software systems and associated software licenses. For a majority of the Company's software sales arrangements, which provide hardware, software licenses, installation and post customer support, revenues are recognized ratably over the software license term as objective evidence of the fair values of the individual elements in the sales arrangement does not exist. As part of the sale of software systems, the Company recognizes revenues from the sale of hardware, which is recorded net of the associated costs.

Postage fees for client mailings are included in revenues and the associated postage expenses are included in operating expenses. Professional Employer Organization (PEO) service revenues are included in revenues and are reported net of direct costs billed and incurred for PEO worksite employees, which primarily include payroll wages and payroll taxes.

**C. Cash and Cash Equivalents.** Highly-liquid investments with a maturity of ninety days or less at the time of purchase are considered cash equivalents.

**D. Investments.** Corporate investments and funds held for clients at June 30, 2003 and 2002.

	2003		2002	
	Cost	Fair Value	Cost	Fair Value
Money market securities and other cash equivalents:				
Corporate investments	\$ 1,410,218	\$ 1,410,218	\$ 798,810	\$ 798,810
Funds held for clients	2,865,957	2,865,957	3,319,646	3,319,646
Total money market securities and other cash equivalents	4,276,175	4,276,175	4,118,456	4,118,456
Available-for-sale securities:				
Corporate investments	917,026	934,125	1,916,896	1,950,773
Funds held for clients	8,582,958	8,941,792	7,730,724	7,905,625
Total available-for-sale securities	9,499,984	9,875,917	9,647,620	9,856,398
Total corporate investments and funds held for clients	\$13,776,159	\$14,152,092	\$13,766,076	\$13,974,854

All of the Company's marketable securities are considered to be "available-for-sale" at June 30, 2003 and, accordingly, are carried on the Consolidated Balance Sheets at fair value.

Expected maturities of available-for-sale securities for both corporate investments and funds held for clients at June 30, 2003 are as follows:

Maturity Dates:	
Due in one year or less	\$2,732,443
Due after one year through two years	3,402,876
Due after two years through three years	1,882,764
Due after three years through four years	779,654
Due after four years through ten years	1,078,180
Total available-for-sale securities	\$9,875,917

**E. Property, Plant and Equipment.** Property, plant and equipment is stated at cost and depreciated over the estimated useful lives of the assets using the straight-line method. Leasehold improvements are amortized over the shorter of the term of the lease or the estimated useful lives of the improvements.

The estimated useful lives of assets are primarily as follows:

Data processing equipment	2 to 3 years
Buildings	20 to 40 years
Furniture and fixtures	3 to 7 years

**F. Goodwill and Intangibles.** In July 2001, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 142 "Goodwill and Other Intangible Assets" (SFAS No. 142), which requires that goodwill no longer be amortized, but instead tested for impairment at least annually at the reporting unit level. If impairment is indicated, a write-down to fair value (normally measured by discounting estimated future cash flows) is recorded. Intangible assets with finite lives continue to be amortized primarily on the straight-line basis over their estimated useful lives. Prior to fiscal 2002, the Company amortized goodwill over periods from 10 to 40 years. Proforma net income and diluted earnings per share for the year ended June 30, 2001, would have been \$972 million and \$1.51, respectively, had the Company applied the non-amortization methodology of SFAS No. 142.

**G. Foreign Currency Translation.** The net assets of the Company's foreign subsidiaries are translated into U.S. dollars based on exchange rates in effect at the end of each period, and revenues and expenses are translated at average exchange rates during the periods. Currency transaction gains or losses, which are included in the results of operations, are immaterial for all periods presented. Gains or losses from balance sheet translation are included in accumulated other comprehensive income on the balance sheet.

**H. Earnings Per Share (EPS).** The calculations of basic and diluted EPS are as follows:

Years ended June 30,	Basic	Effect of Zero Coupon Subordinated Notes	Effect of Stock Options	Diluted
<b>2003</b>				
Net earnings	\$1,018,150	\$1,207	\$ —	\$1,019,357
Average shares	600,071	1,693	4,153	605,917
EPS	\$ 1.70			\$ 1.68
<b>2002</b>				
Net earnings	\$1,100,770	\$1,611	\$ —	\$1,102,381
Average shares	618,857	2,352	9,370	630,579
EPS	\$ 1.78			\$ 1.75
<b>2001</b>				
Net earnings	\$ 924,720	\$2,340	\$ —	\$ 927,060
Average shares	629,035	3,472	13,482	645,989
EPS	\$ 1.47			\$ 1.44

**I. Internal Use Software.** The Company capitalizes certain costs associated with computer software developed or obtained for internal use in accordance with the provisions of Statement of Position No. 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use." The Company's policy provides for the capitalization of exter-

nal direct costs of materials and services associated with developing or obtaining internal use computer software. In addition, ADP also capitalizes certain payroll and payroll-related costs for employees who are directly associated with internal use computer software projects. The amount of capitalizable payroll costs with respect to these employees is limited to the time directly spent on such projects. Costs associated with preliminary project stage activities, training, maintenance and all other post implementation stage activities are expensed as incurred. The Company also expenses internal costs related to minor upgrades and enhancements, as it is impractical to separate these costs from normal maintenance activities. Capitalized costs related to computer software developed or obtained for internal use are amortized over a three- to five-year period on a straight-line basis.

**J. Computer Software to be Sold, Leased or Otherwise Marketed.** The Company capitalizes certain costs of computer software to be sold, leased or otherwise marketed in accordance with the provisions of SFAS No. 86, "Accounting for the Costs of Computer Software to be Sold, Leased or Otherwise Marketed." The Company's policy provides for the capitalization of all software production costs upon reaching technological feasibility for a specific product. Technological feasibility is attained when software products have a completed working model whose consistency with the overall product design has been confirmed by testing. Costs incurred prior to the establishment of technological feasibility are expensed as incurred. The establishment of technological feasibility requires considerable judgment by management and in many instances is only attained a short time prior to the general release of the software. Upon the general release of the software product to customers, capitalization ceases and such costs are amortized over a three-year period on a straight-line basis. Maintenance-related costs are expensed as incurred.

**K. Fair Value Accounting for Stock Plans.** In December 2002, the Financial Accounting Standards Board (FASB) issued SFAS No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure" (SFAS No. 148) which amends SFAS No. 123, "Accounting for Stock-Based Compensation" (SFAS No. 123). SFAS No. 148 provides alternative methods of transition for a voluntary change to the fair value-based method of accounting for stock-based employee compensation and requires disclosures in annual and interim financial statements of the effects of stock-based compensation as reflected below.

## Notes to Consolidated Financial Statements

The Company continues to account for its stock option and employee stock purchase plans under the recognition and measurement principles of Accounting Principles Board (APB) Opinion No. 25, "Accounting for Stock Issued to Employees," and related Interpretations. No stock-based employee compensation expense related to the Company's stock option and stock purchase plans is reflected in net earnings, as all options granted under the stock option plans had an exercise price equal to the market value of the underlying common stock on the date of grant, and for the stock purchase plan the discount does not exceed fifteen percent.

The following table illustrates the effect on net earnings and earnings per share if the Company had applied the fair value recognition provisions of SFAS No. 123 to stock-based employee compensation.

Years ended June 30,	2003	2002	2001
Net earnings, as reported	\$1,018,150	\$1,100,770	\$924,720
Deduct: Total stock-based employee compensation expense determined using the fair value-based method for all awards, net of related tax effects	(123,062)	(120,010)	(106,628)
Pro forma net earnings	\$ 895,088	\$ 980,760	\$818,092
Earnings per share:			
Basic - as reported	\$ 1.70	\$ 1.78	\$ 1.47
Basic - pro forma	\$ 1.49	\$ 1.58	\$ 1.30
Diluted - as reported	\$ 1.68	\$ 1.75	\$ 1.44
Diluted - pro forma	\$ 1.48	\$ 1.56	\$ 1.27

The fair value for these instruments was estimated at the date of grant using a Black-Scholes valuation model with the following weighted average assumptions:

Years ended June 30,	2003	2002	2001
Risk-free interest rate	3.2%-4.1%	4.3%-5.2%	5.3%-6.0%
Dividend yield	.8%-.9%	.7%-.8%	.7%-.8%
Volatility factor	29.5%-31.7%	25.9%-27.9%	27.9%-28.2%
Expected life:			
Options	6.4	6.3	6.3
Stock purchase plans	2.0	2.0	2.0
Weighted average fair value:			
Options	\$12.85	\$16.54	\$21.31
Stock purchase plans	\$12.94	\$21.55	\$20.58

See Note 9, Employee Benefit Plans, for additional information relating to the Company's stock plans.

**L. Reclassification of Prior Financial Statements.** Certain reclassifications have been made to previous years' financial statements to conform to the 2003 presentation.

**M. Income taxes.** The provisions for income taxes, income taxes payable and deferred income taxes are determined using the liability method. Deferred tax assets and liabilities are determined based on differences between the financial reporting and tax basis of assets and liabilities and are measured by applying enacted tax rates and laws to taxable years in which such differences are expected to reverse. A valuation allowance is provided when the Company determines that it is more likely than not that a portion of the deferred tax asset balance will not be realized.

**N. Adoption of New Accounting Pronouncements.** In November 2002, the FASB issued Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others," which elaborates on the disclosures to be made by a guarantor in its interim and annual financial statements about its obligations under certain guarantees that it has issued. It also clarifies that a guarantor is required to recognize, at the inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee. The initial recognition and measurement provisions of this Interpretation are applicable on a prospective basis to guarantees issued or modified after December 31, 2002. The disclosure requirements in this Interpretation are effective for financial statements of interim or annual periods ending after December 15, 2002. The Company has provided information regarding commitments and contingencies relating to guarantees in Note 11. There have been no material commitments and contingencies requiring recognition in the Consolidated Financial Statements since December 31, 2002.

In June 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" (SFAS No. 146), which nullifies Emerging Issues Task Force (EITF) Issue No. 94-3 (EITF 94-3), "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)." SFAS No. 146 requires that a liability for a cost associated with an exit or disposal activity be recognized when the liability is incurred. Under EITF 94-3, a liability for an exit cost as defined in EITF 94-3 was recognized at the date of an entity's commitment to an exit plan. The provisions of SFAS No. 146 are effective and are being applied to all exit or disposal activities initiated since December 31, 2002. These provisions affect the timing of the recognition of the Company's exit and disposal costs.



On July 1, 2002, we adopted SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" (SFAS No. 144). This standard supersedes SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of" (SFAS No. 121), and replaces the accounting and reporting provisions of APB Opinion No. 30, "Reporting Results of Operations - Reporting the Effects of Disposal of a Segment of a Business and Extraordinary, Unusual and Infrequently Occurring Events and Transactions," as it relates to the disposal of a segment of a business. SFAS No. 144 requires the use of a single accounting model for long-lived assets to be disposed of by sale, including discontinued operations, by requiring those long-lived assets to be measured at the lower of carrying amount or fair value less cost to sell. The impairment recognition and measurement provisions of SFAS No. 121 were retained for all long-lived assets to be held and used with the exception of goodwill. Accordingly, the Company periodically evaluates its long-lived assets for impairment by comparing the undiscounted cash flows to the carrying value of the related long-lived asset. If the undiscounted cash flows are less than the carrying value, the Company will write down the asset to its fair value.

**O. New Accounting Pronouncements.** In March 2003, the EITF published Issue No. 00-21 "Accounting for Revenue Arrangements with Multiple Deliverables" (EITF 00-21). EITF 00-21 addresses certain aspects of the accounting by a vendor for arrangements under which it performs multiple revenue-generating activities and how to determine whether such an arrangement involving multiple deliverables contains more than one unit of accounting for purposes of revenue recognition. The guidance in this Issue is effective for revenue arrangements entered in fiscal periods beginning after June 15, 2003. Accordingly, the Company has adopted EITF 00-21 effective July 1, 2003. The Company does not expect EITF 00-21 to have a material impact on the Consolidated Financial Statements.

## **NOTE 2 Other income, net consists of the following:**

Years ended June 30,	2003	2002	2001
Interest income on corporate funds	<b>\$(119,413)</b>	\$(118,672)	\$(163,918)
Interest expense	<b>21,838</b>	21,164	14,260
Realized gains on available-for-sale securities	<b>(34,491)</b>	(22,657)	(15,023)
Realized losses on available-for-sale securities	<b>4,937</b>	6,203	92,617
Total other income, net	<b>\$(127,129)</b>	\$(113,962)	\$(72,064)

Proceeds from the sale of available-for-sale securities were \$4.0 billion, \$4.2 billion and \$3.1 billion for the years-ended June 30, 2003, 2002 and 2001, respectively.

In fiscal 1999, the Company divested its Brokerage front-office business to Bridge Information Systems, Inc. (Bridge), and received \$90 million of Bridge convertible preferred stock as part of the proceeds. In fiscal 2001, Bridge filed for bankruptcy and the Company recorded a \$90 million (\$54 million net of tax) write-off of its investment.

## **NOTE 3 Acquisitions**

Assets acquired and liabilities assumed in business combinations were recorded on the Company's Consolidated Balance Sheets as of the respective acquisition dates based upon their estimated fair values at such dates. The results of operations of businesses acquired by the Company have been included in the Company's Statements of Consolidated Earnings since their respective dates of acquisition. The excess of the purchase price over the estimated fair values of the underlying assets acquired and liabilities assumed was allocated to goodwill. In certain circumstances, the allocations of the excess purchase price are based upon preliminary estimates and assumptions. Accordingly, the allocations are subject to revision when the Company receives final information, including appraisals and other analyses. Revisions to the fair values, which may be significant, will be recorded by the Company as further adjustments to the purchase price allocations.

On June 20, 2003, the Company acquired all of the outstanding common and preferred stock of ProBusiness Services, Inc. (ProBusiness) for \$17 per common share and \$26 per preferred share. The transaction was consummated in cash of approximately \$517 million, net of cash acquired, of which \$351 million was paid as of June 30, 2003. The remaining \$166 million will be paid to former ProBusiness shareholders as they tender their shares. ProBusiness Services, Inc. is a leading provider of comprehensive payroll and human resource processing solutions to larger employers within the United States. The acquisition resulted in approximately \$417 million of goodwill. Intangible assets acquired of approximately \$79.8 million consist of software, customer contracts and lists and other intangible assets which are being amortized over an average life of 8 years.

## Notes to Consolidated Financial Statements

The Company also acquired ten additional businesses in fiscal 2003 for approximately \$118 million, net of cash acquired. These acquisitions resulted in approximately \$90 million of goodwill. Intangible assets acquired of approximately \$27.9 million consist of software, customer contracts and lists and other intangible assets which are being amortized over an average life of 5 years.

In addition to goodwill recognized in these transactions noted above, ADP made contingent payments totaling \$28 million (including \$12 million in common stock), relating to previously consummated acquisitions. As of June 30, 2003, the Company has contingent consideration remaining for all transactions of approximately \$138 million, which is payable over the next three years, subject to the acquired entity's achievement of specified revenue, earnings and/or development targets.

The Company purchased several businesses in fiscal 2002 and 2001 in the amount of \$232 million (including \$12 million in common stock) and \$75 million, respectively, net of cash acquired.

The acquisitions discussed above for fiscal 2003, 2002 and 2001 were not material to the Company's operations, financial position or cash flows.

### NOTE 4 Receivables

Accounts receivable is net of an allowance for doubtful accounts of \$55 million and \$53 million at June 30, 2003 and 2002, respectively.

The Company finances the sale of computer systems to certain of its clients. These finance receivables, most of which are due from automobile and truck dealerships, are reflected in the consolidated balance sheets as follows:

June 30,	2003		2002	
	Current	Long-term	Current	Long-term
Receivables	\$167,328	\$209,177	\$181,609	\$227,422
Less:				
Allowance for doubtful accounts	(7,337)	(11,103)	(9,216)	(16,020)
Unearned income	(20,563)	(17,720)	(23,100)	(18,633)
	\$139,428	\$180,354	\$149,293	\$192,769

Unearned income from finance receivables represents the excess of gross receivables over the sales price of the computer systems financed. Unearned income is amortized using the effective interest method to maintain a constant rate of return on the net investment over the term of each contract.

Long-term receivables at June 30, 2003 mature as follows:

2005	\$107,176
2006	61,061
2007	30,708
2008	9,842
2009	298
Thereafter	92
	\$209,177

### NOTE 5 Goodwill and Intangible Assets, net

Changes in goodwill for the year ended June 30, 2003 are as follows:

	Employer Services	Brokerage Services	Dealer Services	Other	Total
Balance as of					
June 30, 2002	\$ 751,451	\$348,960	\$182,642	\$ 92,601	\$1,375,654
Additions	472,234	21,704	29,013	11,619	534,570
Other	(5,221)	(6,089)	2,434	-	(8,876)
Sale of businesses	(110)	-	-	(537)	(647)
Cumulative translation adjustments	68,774	2,200	1,045	8,411	80,430
<b>Balance as of</b>					
<b>  June 30, 2003</b>	<b>\$1,287,128</b>	<b>\$366,775</b>	<b>\$215,134</b>	<b>\$112,094</b>	<b>\$1,981,131</b>

No impairment losses were recognized during the year.

Components of intangible assets are as follows:

June 30,	2003	2002
Intangibles		
Software licenses	\$ 578,261	\$ 462,474
Customer contracts and lists	545,978	384,785
Other	405,860	373,978
	1,530,099	1,221,237
Less accumulated amortization	(860,208)	(719,693)
Intangible assets, net	\$ 669,891	\$ 501,544

Other intangibles consist primarily of purchased rights, covenants, patents and trademarks (acquired directly or through acquisitions). All of the intangible assets have finite lives and as such are subject to amortization. The weighted-average remaining useful life of the intangible assets is 11 years (2 years for software licenses, 15 years for customer contracts and lists and 14 years for other). Amortization of intangibles totaled \$114 million for fiscal 2003, \$115 million for 2002 and \$103 million for 2001. Estimated amortization expenses of the Company's existing intangible assets for the next five years are as follows:

2004	\$122,675
2005	\$103,026
2006	\$ 73,177
2007	\$ 56,196
2008	\$ 48,599

#### **NOTE 6 Short-term Financing**

In October 2002, the Company entered into a new \$4.0 billion, unsecured revolving credit agreement with certain financial institutions, replacing an existing \$4.0 billion credit agreement. The interest rate applicable to the borrowings is tied to LIBOR or prime rate depending on the notification provided to the syndicated financial institutions prior to borrowing. The Company is also required to pay a facility fee on the credit agreement. The primary uses of the credit facility are to provide liquidity to the unsecured commercial paper program and to fund normal business operations, if necessary. The Company has had no borrowings through June 30, 2003 under the credit agreement, which expires in October 2003.

In April 2002, the Company initiated a short-term commercial paper program providing for the issuance of up to \$4.0 billion in aggregate maturity value of commercial paper at the Company's discretion. The Company's commercial paper program is rated A-1+ by Standard and Poor's and Prime 1 by Moody's. These ratings denote the highest quality investment grade securities. Maturities of commercial paper can range from overnight to 270 days. The Company uses the commercial paper issuances as a primary instrument to meet short-term funding requirements related to client funds obligations. At June 30, 2003 and 2002, there was no commercial paper outstanding. For the year ended June 30, 2003, the Company had average borrowings of \$879 million at an effective weighted average interest rate of 1.5%. From the inception of the commercial paper program in April 2002 through the fiscal year ended June 30, 2002, the Company had average borrowings of \$667 million at an effective weighted average interest rate of 1.8%.

The Company's short-term financing is sometimes obtained on a secured basis through the use of repurchase agreements, which are collateralized principally by U.S. government securities. These agreements generally have terms ranging from overnight up to ten days. At June 30, 2003 and 2002, there were no outstanding repurchase agreements. For the fiscal years ended June 30, 2003 and 2002, the Company had average outstanding borrowings of \$6 million and \$361 million, respectively, at an average interest rate of 3.0% and 2.6%, respectively.

#### **NOTE 7 Debt**

Components of long-term debt are as follows:

June 30,	2003	2002
Zero coupon convertible subordinated notes (5.25% yield)	\$39,661	\$45,614
Industrial revenue bonds (with variable interest rates from 1.25% to 1.53%)	36,500	36,474
Other	9,338	8,685
	85,499	90,773
Less current portion	(825)	(125)
	\$84,674	\$90,648

The zero coupon convertible subordinated notes have a face value of approximately \$62 million at June 30, 2003 and mature February 20, 2012, unless converted or redeemed earlier. At June 30, 2003, the notes were convertible into approximately 1.6 million shares of the Company's common stock. The notes are callable at the option of the Company, and the holders of the notes can convert into common stock at any time or require redemption in fiscal 2007. During fiscal 2003 and 2002, approximately \$18 million and \$27 million face value of notes were converted, respectively. As of June 30, 2003 and 2002, the quoted market prices for the zero coupon notes were approximately \$55 million and \$90 million, respectively. The fair value of the other debt, included above, approximates its carrying value.

Long-term debt repayments at June 30, 2003 are due as follows:

2005	\$ 417
2006	157
2007	163
2008	854
2009	16,365
Thereafter	66,718
	\$84,674

Cash payments relating to interest were approximately \$20 million in fiscal 2003, \$18 million in fiscal 2002 and \$10 million in fiscal 2001.

## Notes to Consolidated Financial Statements

### NOTE 8 Funds Held for Clients and Client Funds Obligations

As part of its integrated payroll and payroll tax filing services, the Company impounds funds for federal, state and local employment taxes from approximately 364,000 clients; handles all regulatory payroll tax filings, correspondence, amendments, and penalty and interest disputes; remits the funds to the appropriate tax agencies; and handles other employer-related services.

In addition to fees paid by clients for these services, the Company receives interest during the interval between the receipt and disbursement of these funds by investing the funds primarily in fixed-income instruments. The amount of collected but not yet remitted funds for the Company's payroll and tax filing and certain other services varies significantly during the year and averaged approximately \$8.9 billion in fiscal 2003, \$8.4 billion in fiscal 2002 and \$8.2 billion in fiscal 2001.

### NOTE 9 Employee Benefit Plans

**A. Stock Plans.** The Company has stock option plans which provide for the issuance, to eligible employees, of incentive and non-qualified stock options, which may expire as much as 10 years from the date of grant, at prices not less than the fair market value on the date of grant. At June 30, 2003, there were

11,293 participants in the plans. The aggregate purchase price for options outstanding at June 30, 2003 was approximately \$2.5 billion. The options expire at various points between 2003 and 2013.

A summary of changes in the stock option plans for the three years ended June 30, 2003, is as follows:

Years ended June 30,	Number of Options			Weighted Average Price		
	2003	2002	2001	2003	2002	2001
Options outstanding, beginning of year	50,843	47,496	46,694	\$41	\$37	\$29
Options granted	15,867	12,325	10,740	\$37	\$49	\$57
Options exercised	(2,588)	(6,481)	(7,956)	\$19	\$22	\$18
Options canceled	(3,164)	(2,497)	(1,982)	\$48	\$47	\$38
Options outstanding, end of year	60,958	50,843	47,496	\$41	\$41	\$37
Options exercisable, end of year	27,617	21,626	19,929	\$36	\$31	\$25
Shares available for future grants, end of year	1,189	13,892	1,720			
Shares reserved for issuance under stock option plans	62,147	64,735	49,216			

Summarized information about stock options outstanding as of June 30, 2003 is as follows:

Exercise Price Range	Outstanding			Exercisable		
	Number of Options (In thousands)	Remaining Life (In years)	Weighted Average Price	Number of Options (In thousands)	Weighted Average Price	Weighted Average Price
Under \$15	2,012	1.0	\$13	1,994	\$13	\$13
\$15 to \$25	5,451	3.0	\$20	5,407	\$20	\$20
\$25 to \$35	13,523	7.6	\$32	4,857	\$29	\$29
\$35 to \$45	18,840	7.3	\$42	8,440	\$41	\$41
\$45 to \$55	15,309	8.1	\$50	4,620	\$51	\$51
Over \$55	5,823	7.2	\$60	2,299	\$60	\$60

The Company has stock purchase plans under which eligible employees have the ability to purchase shares of common stock at 85% of the lower of market value as of the date of purchase election or as of the end of the plans. Approximately 3.6 million and 2.2 million shares are scheduled for issuance on December 31, 2004 and 2003, respectively. Approximately 1.5 million and 2.3 million shares were issued during the years ended June 30, 2003 and 2002, respectively. At June 30, 2003 and 2002, there were approximately 0.6 million and 3.3 million shares, respectively, reserved for purchase under the plans. Included in liabilities as of June 30, 2003 and 2002 are employee stock purchase plan withholdings of approximately \$87 million and \$93 million, respectively.

The Company has a restricted stock plan under which shares of common stock have been sold for nominal consideration to certain key employees. These shares are restricted as to transfer and in certain circumstances must be resold to the Company at the original purchase price. The restrictions lapse over periods of up to six years. During the years ended June 30, 2003, 2002 and 2001, the Company issued 221 thousand, 144 thousand and 173 thousand restricted shares, respectively.

**B. Pension Plans.** The Company has a defined benefit cash balance pension plan covering substantially all U.S. employees, under which employees are credited with a percentage of base pay plus interest. The plan interest credit rate will vary from year-to-year based on the ten-year U.S. Treasury rate. Employees are fully vested on completion of five years of service. The Company's policy is to make contributions within the range determined by generally accepted actuarial principles. In addition, the Company has various retirement plans for its non-U.S. employees and maintains a Supplemental Officer Retirement Plan ("SORP"). The SORP is a defined benefit plan pursuant to which the Company will pay supplemental pension benefits to certain key officers upon retirement based upon the officer's years of service and compensation.

The plans' funded status as of June 30, 2003 and 2002 follows:

June 30,	2003	2002
Change in plan assets:		
Fair value of plan assets at beginning of year	\$444,500	\$477,800
Actual return on plan assets	20,400	(55,200)
Employer contributions	99,700	33,800
Benefits paid	(11,400)	(11,900)
Fair value of plan assets at end of year	\$553,200	\$444,500
Change in benefit obligation:		
Benefit obligation at beginning of year	\$484,600	\$409,700
Service cost	25,600	17,400
Interest cost	31,200	29,100
Actuarial and other losses	63,400	40,300
Benefits paid	(11,400)	(11,900)
Projected benefit obligation at end of year	\$593,400	\$484,600
Projected benefits in excess of plan assets	\$ (40,200)	\$ (40,100)
Unrecognized net actuarial loss due to different experience than assumed	279,800	183,500
Prepaid pension cost	\$239,600	\$143,400

The components of net pension expense were as follows:

Years ended June 30,	2003	2002	2001
Service cost - benefits earned during the period	\$ 25,600	\$ 17,400	\$ 31,400
Interest cost on projected benefits	31,200	29,100	23,600
Expected return on plan assets	(50,500)	(46,300)	(40,100)
Net amortization and deferral	1,100	(500)	200
	\$ 7,400	\$ (300)	\$ 15,100

Assumptions used to develop the actuarial present value of benefit obligations generally were:

Years ended June 30,	2003	2002
Discount rate	5.75%	6.75%
Expected long-term rate on assets	7.25%	8.50%
Increase in compensation levels	6.0%	6.0%

The projected benefit obligation, accumulated benefit obligation and fair value of plan assets for the Company's pension plans with accumulated benefit obligations in excess of plan assets were \$67 million, \$59 million and \$19 million, respectively, as of June 30, 2003, and \$69 million, \$61 million and \$26 million, respectively, as of June 30, 2002.

## Notes to Consolidated Financial Statements

**C. Retirement and Savings Plan.** The Company has a 401(k) retirement and savings plan, which allows eligible employees to contribute up to 20% of their compensation annually and allows highly compensated employees to contribute up to 10% of their compensation annually. The Company matches a portion of employee contributions, which amounted to approximately \$34 million, \$35 million and \$31 million for calendar years 2002, 2001 and 2000, respectively.

### NOTE 10 Income Taxes

Earnings before income taxes shown below are based on the geographic location to which such earnings are attributable.

Years ended June 30,	2003	2002	2001
Earnings before income taxes:			
U.S.	\$1,474,915	\$1,618,885	\$1,375,220
Non-U.S.	170,285	168,085	149,790
	<b>\$1,645,200</b>	\$1,786,970	\$1,525,010

The provision for income taxes consists of the following components:

Years ended June 30,	2003	2002	2001
Current:			
Federal	\$496,920	\$542,980	\$439,745
Non-U.S.	84,180	67,380	77,435
State	61,725	67,160	53,660
Total current	<b>642,825</b>	677,520	570,840
Deferred:			
Federal	430	6,525	24,895
Non-U.S.	(16,350)	(20)	(3,743)
State	145	2,175	8,298
Total deferred	<b>(15,775)</b>	8,680	29,450
Total provision	<b>\$627,050</b>	\$686,200	\$600,290

A reconciliation between the Company's effective tax rate and the U.S. federal statutory rate is as follows:

Years ended June 30,	2003	%	2002	%	2001	%
Provision for taxes at U.S. statutory rate	\$575,820	35.0	\$625,415	35.0	\$533,800	35.0
Increase (decrease) in provision from:						
State taxes, net of federal tax benefit	40,215	2.4	45,070	2.5	40,270	2.6
Other	11,015	0.7	15,715	0.9	26,220	1.8
	<b>\$627,050</b>	<b>38.1</b>	\$686,200	38.4	\$600,290	39.4

The significant components of deferred income tax assets and liabilities and their balance sheet classifications are as follows:

June 30,	2003	2002
Deferred tax assets:		
Accrued expenses not currently deductible	\$178,893	\$135,604
Net operating losses	58,178	30,861
Other	29,023	18,320
	<b>266,094</b>	184,785
Less: Valuation allowances	(32,220)	(40,140)
Deferred tax assets – net	<b>\$233,874</b>	\$144,645
Deferred tax liabilities:		
Unrealized investment gains	\$142,102	\$83,512
Accrued retirement benefits	90,730	81,883
Depreciation and amortization	188,943	164,160
Other	49,244	50,660
Deferred tax liabilities	<b>\$471,019</b>	\$380,215
Net deferred tax liabilities	<b>\$237,145</b>	\$235,570

There are \$83.7 million and \$2.1 million net current deferred tax assets included in other current assets in the balance sheet at June 30, 2003 and June 30, 2002, respectively.

Income taxes have not been provided on undistributed earnings of foreign subsidiaries as the Company considers such earnings to be permanently reinvested as of June 30, 2003 and June 30, 2002.

The Company has estimated domestic and foreign net operating loss carry forwards of approximately \$103.2 million and \$66.9 million, respectively, at June 30, 2003 and approximately \$0 and \$85.2 million, respectively, at June 30, 2002.

The Company has recorded valuation allowances of \$32.2 million and \$40.1 million at June 30, 2003 and June 30, 2002, respectively, to reflect the estimated amount of foreign deferred tax assets that may not be realized. A portion of the valuation allowances in the amounts of approximately \$11.6 million and \$17.7 million at June 30, 2003 and June 30, 2002, respectively, relate to net deferred tax assets which were recorded in purchase accounting. The recognition of such amounts in future years will be allocated to reduce the excess purchase price over the net assets acquired.

Income tax payments were approximately \$686 million in 2003, \$518 million in 2002 and \$437 million in 2001.

### **NOTE 11 Contractual Commitments, Contingencies and Off-Balance Sheet Arrangements**

The Company has obligations under various facilities and equipment leases and software license agreements. Total expense under these agreements was approximately \$319 million in 2003, \$272 million in 2002 and \$269 million in 2001, with minimum commitments at June 30, 2003 as follows:

Years ending June 30,	
2004	\$296,258
2005	226,301
2006	139,741
2007	95,010
2008	73,288
Thereafter	99,057
	<b>\$929,655</b>

In addition to fixed rentals, certain leases require payment of maintenance and real estate taxes and contain escalation provisions based on future adjustments in price indices.

As of June 30, 2003, the Company has purchase commitments of approximately \$66 million relating to software and equipment maintenance contracts, of which \$40 million relates to fiscal 2004 and the remaining \$26 million relates to fiscal years 2005 through 2009.

The Company is subject to various claims and litigation in the normal course of business. The Company does not believe that the resolution of these matters will have a material impact on the consolidated financial statements.

It is not our business practice to enter into off-balance sheet arrangements. However, in the normal course of business, the Company does enter into contracts in which it makes representations and warranties that guarantee the performance of the Company's products and services as well as other indemnifications entered into in the normal course of business. Historically, there have been no material losses related to such guarantees and indemnifications.

### **NOTE 12 Accumulated Other Comprehensive Income (Loss)**

Comprehensive income is a measure of income which includes both net income and other comprehensive income (loss). Other comprehensive income (loss) results from items deferred on the balance sheet in shareholders' equity. Other comprehensive income (loss) was \$277 million, \$115 million and (\$4) million in 2003, 2002 and 2001, respectively. The accumulated balances for each component of other comprehensive income (loss) are as follows:

June 30,	2003	2002	2001
Currency translation adjustments	<b>\$(69,535)</b>	\$(243,581)	\$(317,085)
Unrealized gain on available-for-sale securities, net of tax	<b>233,830</b>	125,268	84,121
Minimum pension liability adjustment, net of tax	<b>(5,476)</b>	—	—
Accumulated other comprehensive income (loss)	<b>\$158,819</b>	\$(118,313)	\$(232,964)

### **NOTE 13 Financial Data By Segment**

Employer Services, Brokerage Services and Dealer Services are the Company's largest business units. ADP evaluates performance of its business units based on operating results before interest on corporate funds, foreign currency gains and losses, and income taxes. Certain revenues and expenses are charged to business units at a standard rate for management and motivation reasons. Other costs are recorded based on management responsibility. Prior years' business unit revenues and earnings before income taxes have been adjusted to reflect updated fiscal year 2003 budgeted foreign exchange rates. Business unit assets include funds held for clients but exclude corporate cash, marketable securities and goodwill. "Other" consists primarily of Claims Services, miscellaneous processing services and corporate. Reconciling items for revenues and earnings before income taxes include foreign exchange differences between the actual foreign exchange rates and the fiscal year 2003 budgeted foreign exchange rates and the adjustment for the difference between actual interest income earned on invested funds held for clients and interest credited to Employer Services at a standard rate of 6%. The business unit results also include an internal cost of capital charge related to the funding of acquisitions and other investments. This charge is eliminated in consolidation and as such represents a reconciling item to earnings before income taxes.

## Notes to Consolidated Financial Statements

(In millions)	Employer Services	Brokerage Services	Dealer Services	Other	Reconciling Items	Total
<b>Year ended June 30, 2003</b>						
Revenues	\$ 4,401	\$1,593	\$788	\$ 420	\$ (55)	\$ 7,147
Earnings before income taxes	\$ 1,193	\$ 230	\$132	\$ 143	\$ (53)	\$ 1,645
Assets	\$13,278	\$ 556	\$351	\$5,649	—	\$19,834
Capital expenditures	\$ 66	\$ 24	\$ 26	\$ 18	—	\$ 134
Depreciation and amortization	\$ 193	\$ 95	\$ 50	\$ 46	\$(109)	\$ 275
Year ended June 30, 2002						
Revenues	\$ 4,180	\$1,758	\$706	\$ 425	\$ (65)	\$ 7,004
Earnings before income taxes	\$ 1,110	\$ 354	\$116	\$ 157	\$ 50	\$ 1,787
Assets	\$12,244	\$ 566	\$181	\$5,286	—	\$18,277
Capital expenditures	\$ 71	\$ 33	\$ 21	\$ 21	—	\$ 146
Depreciation and amortization	\$ 208	\$ 108	\$ 40	\$ 45	\$(122)	\$ 279
Year ended June 30, 2001						
Revenues	\$ 3,964	\$1,742	\$683	\$ 412	\$ 53	\$ 6,854
Earnings before income taxes	\$ 937	\$ 332	\$ 99	\$ 60	\$ 97	\$ 1,525
Assets	\$12,320	\$ 523	\$183	\$4,863	—	\$17,889
Capital expenditures	\$ 106	\$ 33	\$ 23	\$ 23	—	\$ 185
Depreciation and amortization	\$ 196	\$ 109	\$ 38	\$ 42	\$ (64)	\$ 321

Revenues and assets by geographic area are as follows:

(In millions)	United States	Europe	Canada	Other	Total
<b>Year ended June 30, 2003</b>					
Revenues	\$ 6,016	\$ 775	\$ 292	\$ 64	\$ 7,147
Assets	\$16,841	\$1,476	\$1,391	\$126	\$19,834
Year ended June 30, 2002					
Revenues	\$ 5,978	\$ 673	\$ 270	\$ 83	\$ 7,004
Assets	\$16,055	\$1,214	\$ 843	\$165	\$18,277
Year ended June 30, 2001					
Revenues	\$ 5,827	\$ 641	\$ 279	\$107	\$ 6,854
Assets	\$15,799	\$1,055	\$ 910	\$125	\$17,889

### NOTE 14 Quarterly Financial Results (Unaudited)

Summarized quarterly results of operations for the two years ended June 30, 2003 are as follows:

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
<b>Year ended June 30, 2003</b>				
Revenues	\$1,646,685	\$1,682,995	\$1,905,778	\$1,911,559
Net earnings	\$ 210,400	\$ 261,690	\$ 329,390	\$ 216,670
Basic earnings per share	\$ .35	\$ .44	\$ .55	\$ .36
Diluted earnings per share	\$ .34	\$ .43	\$ .54	\$ .36
Year ended June 30, 2002				
Revenues	\$1,607,883	\$1,681,028	\$1,870,036	\$1,845,316
Net earnings	\$ 196,600	\$ 264,600	\$ 352,260	\$ 287,310
Basic earnings per share	\$ .32	\$ .43	\$ .57	\$ .47
Diluted earnings per share	\$ .31	\$ .42	\$ .56	\$ .46



## Report of Management and Independent Auditors' Report

### Report of Management

Management is responsible for the preparation of the accompanying financial statements. The financial statements, which include amounts based on the application of business judgments, have been prepared in conformity with generally accepted accounting principles. Deloitte & Touche LLP, independent certified public accountants, has audited our consolidated financial statements as described in their report.

The Company maintains financial control systems designed to provide reasonable assurance that assets are safeguarded and that transactions are executed and recorded in accordance with management authorization. The control systems are supported by written policies and the control environment is regularly evaluated by both the Company's internal auditors and Deloitte & Touche LLP.

The Board of Directors has an Audit Committee comprised of four outside directors. The Audit Committee meets with both Deloitte & Touche LLP and the internal auditors with and without management's presence. It monitors and reviews the Company's financial statements and internal controls, and the scope of the internal auditors' and Deloitte & Touche LLP's audits. Deloitte & Touche LLP and the internal auditors have free access to the Audit Committee.



Arthur F. Weinbach  
Chairman and Chief Executive Officer



Karen E. Dykstra  
Chief Financial Officer

Roseland, New Jersey  
July 28, 2003

### Independent Auditors' Report

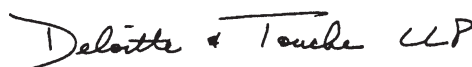
Board of Directors and Shareholders  
Automatic Data Processing, Inc.  
Roseland, New Jersey

We have audited the accompanying consolidated balance sheets of Automatic Data Processing, Inc. and subsidiaries (the "Company") as of June 30, 2003 and 2002, and the related consolidated statements of earnings, shareholders' equity, and cash flows for each of the three years in the period ended June 30, 2003. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Automatic Data Processing, Inc. and subsidiaries as of June 30, 2003 and 2002, and the results of their operations and their cash flows for each of the three years in the period ended June 30, 2003, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1 to the consolidated financial statements, on July 1, 2001, the Company adopted the non-amortization provisions of Statement of Financial Accounting Standards No.142, "Goodwill and Other Intangible Assets."



New York, New York  
July 28, 2003

## Directors and Corporate Officers

### Directors

Gregory D. Brenneman<sup>(1)\*,(2)</sup>  
*President & CEO, Turnworks, Inc.*  
*Chairman, ADP Compensation*  
*Committee*

Leslie A. Brun<sup>(4)</sup>  
*Chairman, Hamilton Lane*

Gary C. Butler  
*President and Chief Operating Officer*

Joseph A. Califano, Jr.<sup>(1)</sup>  
*Chairman of the Board and President,*  
*The National Center on Addiction and*  
*Substance Abuse at Columbia*  
*University (CASA)*

Leon G. Cooperman<sup>(1)\*,(3),(4)</sup>  
*Chairman and Chief Executive Officer,*  
*Omega Advisors, Inc.*  
*Chairman, ADP Audit Committee*

Ann Dibble Jordan<sup>(1)</sup>  
*Consultant*  
*Member of various boards*

Harvey M. Krueger<sup>(3)</sup>  
*Vice Chairman, Lehman Brothers*  
*Chairman, ADP Executive Committee*

Frederic V. Malek<sup>(2),(3),(4)</sup>  
*Chairman, Thayer Capital Partners*  
*Chairman, ADP Nominating/Corporate*  
*Governance Committee*

Henry Taub<sup>(3)</sup>  
*Honorary Chairman of the Board*

Laurence A. Tisch<sup>(2)</sup>  
*Co-Chairman, Loews*

Arthur F. Weinbach<sup>(3)</sup>  
*Chairman and Chief Executive Officer*

Josh S. Weston<sup>(3)</sup>  
*Honorary Chairman of the Board*

- (1) Audit Committee  
 \* a designated "audit committee  
 financial expert"  
 (2) Compensation Committee  
 (3) Executive Committee  
 (4) Nominating/Corporate Governance  
 Committee

### Corporate Officers

Arthur F. Weinbach  
*Chairman and Chief Executive Officer*

Gary C. Butler  
*President and Chief Operating Officer*

#### Group Presidents

Richard J. Daly  
 Russell P. Fradin  
 John P. Hogan  
 S. Michael Martone

#### Corporate Vice Presidents

Steven J. Anenen  
 John D. Barfitt  
 James B. Benson  
 Richard C. Berke  
 Janice M. Colby  
 Raymond L. Colotti  
 Vincent R. Coppola

J. Russ DeLoach  
 G. Harry Durity  
 Karen E. Dykstra, *Chief Financial Officer*  
 Eugene A. Hall, *Senior VP*  
 Campbell B. Langdon  
 Peter H. Op de Beeck  
 Jay C. Rising  
 Carlos Rodriguez  
 Michael P. Rooney  
 Robert Schifellite  
 Dan Sheldon  
 George I. Stoeckert  
 Dante F. Terzo  
 Thomas J. Tremba

#### Staff Vice Presidents

Gary E. Tarino  
 Daniel A. Zaccardo

# Automatic Data Processing, Inc.

## Corporate Headquarters

Automatic Data Processing, Inc.  
One ADP Boulevard  
Roseland, New Jersey 07068-1728  
973.974.5000

## Transfer Agent

Mellon Investor Services  
Overpeck Centre  
85 Challenger Road  
Ridgefield Park, New Jersey 07660  
888.414.6896

## Corporate Counsel

Paul, Weiss, Rifkind,  
Wharton & Garrison LLP

## Auditors

Deloitte & Touche LLP

## Annual Report, Form 10-K and Other Reports

This 2003 Annual Report is also available online under "Investor Information" on ADP's Web site at [www.adp.com](http://www.adp.com). Our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, proxy statement, statements of change in beneficial ownership and other SEC filings, and amendments to those reports, statements and filings, are available, without charge, on ADP's Web site as soon as reasonably practicable after they are filed electronically with the SEC. Copies also are available, without charge, from ADP Investor Relations at: One ADP Boulevard, Roseland, New Jersey 07068-1728. Phone: 973.974.5858.

## Product Information

For information about ADP's products and services, visit us at [www.adp.com](http://www.adp.com).

## Corporate Governance

Visit ADP's Web site, at [www.adp.com](http://www.adp.com), to see its key corporate governance documents, including its Corporate Philosophy, Code of Business Conduct & Ethics, Code of Ethics for Principal Executive Officer and Senior Financial Officers, Corporate Governance Principles, Audit Committee Charter, Compensation Committee Charter, Nominating/Corporate Governance Committee Charter and Executive Committee Charter.

## Contact ADP's Audit Committee or Board of Directors

For reporting complaints about ADP's accounting, internal accounting controls or auditing matters, or other concerns, to the Audit Committee or the Board of Directors send a detailed note, with relevant documents, to P.O. Box 34, Roseland, New Jersey 07068, leave a message for a return call at 973.974.5770, or send an email to [adp\\_audit\\_committee@adp.com](mailto:adp_audit_committee@adp.com).

## Annual Meeting

This year's stockholders' meeting will be held at Automatic Data Processing, Inc., One ADP Boulevard, Roseland, New Jersey, on November 11, 2003 at 10:00 a.m. A notice of the meeting, proxy statement, and proxy voting card will be mailed to stockholders starting on or about September 22, 2003.

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**Automatic Data Processing, Inc.**  
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