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ADP - Q1 2017 Automatic Data Processing Inc Earnings Call

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OVERVIEW:

Co. reported 1Q17 revenues of $2.9b and adjusted diluted EPS of $0.86. Expects FY17 revenues to grow 7-8% and constant-dollar adjusted diluted EPS to grow 11-13%.

CORPORATE PARTICIPANTS

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PRESENTATION

Operator

My name is Stephanie. I'll be your conference operator. At this time, I'd like to welcome everyone to ADP's first-quarter FY17 earnings call.

I would like to inform you that this conference is being record.

(Operator Instructions)

Thank you. I will now turn the conference over to Christian Greyenbuhl, Vice President Investor Relations. Please, go ahead.

Christian Greyenbuhl - *Automatic Data Processing Inc - VP of IR*

Thank you, Stephanie. Good morning, everyone. This is Christian Greyenbuhl, ADP's Vice President Investor Relations. I'm here today with, Carlos Rodriguez, ADP's President and Chief Executive Officer and Jan Siegmund, ADP's Chief Financial Officer. Thank you for joining us for our first-quarter FY17 earnings call and webcast.

During our call today, we will reference certain non-GAAP financial measures, which we believe to be useful to investors. A reconciliation of these non-GAAP financial measures to their comparable GAAP measures is included in our earnings release and in the supplemental slides on our Investor Relations website. I also want to highlight for you that the quarterly history of revenue and pre-tax earnings for our reportable segments is also available on the Investor Relations section of our website.

These schedules have been updated to include the first quarter of FY17 and have been adjusted to align with recent changes in our segment reporting to align our financial reporting with how management now views the business. Most notably, effective this quarter, we are now allocating stock based compensation to the segments and have made some changes to the allocation methodology for certain corporate level allocations. Accordingly, prior periods presented have been restated. Our segment guidance reflects the impact of these changes.

Before Carlos begins, I'd like to remind everyone that today's call will contain forward-looking statements that refer to future events and as such involve some risk. We encourage you to review our filings with the SEC for additional information on risk factors that could cause actual results to differ materially from our current expectations. Now, let me turn the call over to Carlos.

Carlos Rodriguez - *Automatic Data Processing Inc - President & CEO*

Thank you, Christian. Thank you all for joining our call this morning, we appreciate your interest in ADP. This morning, we reported our first-quarter FY17 results, with revenue up 7% to $2.9 billion, despite 1 percentage point of combined pressure from foreign currency translation and the impact of the sale of the AdvancedMD business at the end of our FY16 first quarter. We are pleased with this revenue growth, which was in line with our expectations. We continue to see the benefits from our recent new business bookings helping to drive growth in the quarter. In addition to this solid revenue growth, adjusted diluted earnings per share grew 26% to $0.86 per share.

Overall, our earnings growth exceeded our expectations this quarter and we are very pleased with our results. There were a number of contributing factors to our strong earnings performance. Jan will walk through these shortly. On the new business bookings front, during the quarter, we were flat compared to the first quarter of 2016, which was in line with our expectations. We continue to forecast 4% to 6% bookings growth for the year.

I want to remind you of the tailwinds we experienced in FY16 from the sale of additional modules related to the Affordable Care Act. Our anticipated FY17 performance, if achieved, would lead to a three-year compounded annual growth rate of 9%, which remains in line with our long-term new business bookings guidance of 8% to 10%. Overall, our revenue growth was solid this quarter. While we do not expect all of the margin expansion we saw this quarter to continue through the remainder of the year, we are pleased with our overall results.

Before I continue, I wanted to share a little more insight regarding retention. During the quarter, we experienced a decline in retention of 100 basis points, which was due to the loss of a contract pertaining to our CHSA business, which we announced today has been sold to WageWorks. Excluding the impact of this single client loss, retention would have been flat in the quarter. We continue to see the benefits of our efforts to upgrade clients to the most appropriate strategic cloud based platforms. These upgrade efforts remain on track and progressed nicely during the quarter.

As I just mentioned, today we announced that WageWorks was acquiring two non-strategic ADP businesses, namely our CHSA and COBRA businesses for $235 million. In selling to a top tier provider in these markets, we believe this agreement will truly unlock the potential of these businesses, while allowing us to sharpen our focus on ADP's core benefits administration offering. In conjunction with these dispositions, ADP entered into a partnership with WageWorks that will allow us to continue offering their COBRA and CHSA solutions to ADP clients in an integrated fashion. This is a great example of ADP continuing to build an eco system of complementary services that allow clients to extend the value of their core ADP human capital management solutions.

Last quarter, we shared details of our service alignment initiative, which is part of our strategy to simplify the service organization by aligning ADP's service operations to our strategic platforms. In addition to improving the client service experience, this initiative is expected to enhance ADP's service capabilities and contribute to operating efficiencies over the long term. We are pleased with the progress we are making at our new strategic locations in Maitland, Florida and Norfolk, Virginia. Efforts to staff and operate from these locations have commenced and are proceeding according to plan.

We will soon announce the location of our third new site in the Western part of the US, which we anticipate being operational toward the latter part of this fiscal year. Our results this quarter reflect the strength of our business model and give us momentum as we stay focused on delivering an outstanding client experience through great service and innovative solutions, many of which are receiving a wealth of external recognition.

Recently, we shared that ADP was named a leader in payroll business process outsourcing by Gartner for the fifth consecutive year. Gartner's study analyzed vendors across all regions, employer sizes and service delivery models, evaluating both their ability to execute and completeness of vision. In naming ADP a leader, Gartner recognized us for combining a clear view of the market's direction and a deep understanding of client needs, with the capabilities and expertise to deliver against them. Payroll outsourcing is core to who we are and is part of delivering outstanding HCM solutions. We are extremely proud of the sustained recognition for our leadership in this area.

Today, ADP is delivering HCM solutions to more than 650,000 clients and 39 million employees worldwide. These data points are important for a number of reasons. They clearly demonstrate our unique reach and marketplace success over a sustained period of time. But they also represent a unique differentiator for ADP. The scale and the data that this client base represents allows us to deliver a suite of new capabilities that we believe hold the potential to transform the strategic value of the HR function. Because we pay one in six workers in the US, we are in the unique position to deliver advanced analytics capabilities that can help clients address workforce productivity, talent development and retention.

Leveraging this data, we introduced the ADP DataCloud to allow business leaders and HR professionals to generate actionable insights from the workforce data embedded in their ADP HCM solutions. Today, more than 3,200 clients are using our analytics platform. About a year ago, we introduced benchmarking to this platform. The benchmarking capability provides users with a unique competitive advantage by delivering insight from actual live data to help clients evaluate their workforce against other companies in their market space.

Our benchmarking capability puts key industry workforce metrics at our clients' fingertips, avoiding the inherent time lag or inaccuracy associated with salary and other types of survey based data. A few weeks ago, at the HR technology conference in Chicago, we received two distinctive recognitions for our DataCloud benchmarking capability. At the show, HR Executive Magazine named this one of its top products for 2016 and recognized it as one of the year's awesome new technologies for HR.

I should note, this is the second year in a row that we've received these distinguished awards. We received them both last year for the ADP marketplace, the first and largest HCM app ecosystem in the market. I've said before that innovation is a job that's never done. But we are proud of the progress to date and the external recognition we are receiving. We believe that innovations like these and the investments we are making to simplify our portfolio are essential to our long-term success. With that, I'll turn the call over to Jan for further review of our first-quarter results.

Jan Siegmund - *Automatic Data Processing Inc - CFO*

Thank you very much, Carlos. Good morning, everyone. During the quarter, we recorded a restructuring charge of about $40 million related to our service alignment initiative. Certain non-GAAP measures in my commentary to follow exclude the impact of this charge, as well as certain other one-time items recognized in the prior fiscal year. A reconciliation of these non-GAAP measures can be found in this morning's press release and in the supplemental slides on our Investor Relations website.

Before I begin reviewing this quarter's results, I wanted to highlight some additional detail regarding the disposition of our COBRA and CHSA businesses. We currently expect the sale to be completed during the second quarter of FY17 for a pre-tax gain of approximately $200 million, subject to normal and customary closing conditions. The results of operations of these two businesses are currently included in the employer services segment and will not be reflected as a discontinued operation.

Accordingly, we have factored the operational impacts from these dispositions into our updated FY17 outlook. As Carlos mentioned, ADP revenues grew 7% in the quarter to $2.9 billion or 8% on a constant dollar basis. On a reported basis, net earnings grew 10% or 9% on a constant dollar basis. Adjusted earnings before interest and taxes or adjusted EBIT grew 21% or 20% on a constant dollar basis. Adjusted EBIT margin increased about 230 basis points compared to the 17.6% in the last year's first quarter. This increase was driven by operational efficiencies and a slower growth in our selling expenses.

Adjusted diluted earnings per share grew 26% to $0.86 and 26% on a constant dollar basis and benefited from a lower effective tax rate and fewer shares outstanding compared with a year ago. Our adjusted effective tax rate was positively impacted following the adoption of our new stock compensation related accounting pronouncement in our first quarter, which helped drive a decrease of our adjusted effective tax rate of approximately 290 basis points to 30.8% or 3% on an EPS -- $0.03, I apologize, $0.03 on an EPS basis for the quarter.

As you read this morning's press release, new business bookings growth was flat for the quarter but in line with our own expectations, following two years of successive double-digit growth, with meaningful contributions from human capital management modules that assist clients in complying with the Affordable Care Act. Overall, our results in the quarter were very good, yielding solid revenue growth with a better than expected margin growth. Although we still have a lot of work ahead of us, I'm also pleased with the progress to date on our service alignment initiative.

Now, our employer services segment. Revenues grew 6% for the quarter and 6% on a constant dollar basis. Our same-store pays per control metric in the US grew 2.7% in the first quarter. Average client fund balances grew 4% compared to a year ago and 4% on a constant dollar basis. This growth was driven by additions of net new business and increased wage levels compared to the prior year's first quarter. Outside the US, we continue to see solid revenue growth and margin growth, driven largely by the success of our multi-national solutions, which continue to perform well. Employer services margin increased about 230 basis points in the quarter.

This increase was driven by operational efficiencies and a slower growth in our selling expenses, following on from the difficult selling compare in the first quarter of FY16. The PEO continues to perform well, growing revenues by 13% in the quarter, with average worksite employees growing 13% to 439,000 employees. A portion of the 13% revenue growth was impacted by slower growth in our benefit pass-through cost, resulting from lower healthcare renewal premiums, which outweighed growth from higher benefit plan participation from our worksite employees during the quarter. Along with this revenue growth, the PEO delivered approximately 90 basis points of margin expansion this quarter through increased operating efficiencies.

Both of our segments performed well in the quarter and as Carlos mentioned, we are off to a good start. But we also see a mix of factors that impact our FY17 outlook. I will now take a moment to walk you through our revised outlook with you. First, as I mentioned, our new business bookings growth in the quarter was in line with our plans coming off a difficult compare in the first -- prior-year first quarter. Accordingly, we are reaffirming our full-year guidance of 4% to 6% growth on the $1.75 billion sold in FY16.

We are reaffirming our ES revenue guidance of 4% to 5% and our remaining -- and maintaining our PEO revenue guidance at 14% to 16%. With the disposition of our CHSA and COBRA businesses, which were included for the full FY16, but expected to be only in our results for about the first half of FY17, we have reduced our revenue expectations for the year by almost 1 percentage point. As a result, we are now forecasting revenue growth of 7% to 8% compared with our prior forecast of 7% to 9%, which is not expected to be significantly impacted by foreign currency translation, based on our current rates.

As a reminder, during the first fiscal year -- first half of FY16, we made certain investments to support our business through the ACA on-boarding process while also continuing to invest in our sales force to leverage the strong tailwinds from the sales of human capital management modules that assist clients in complying with the ACA. We have seen the benefits of these investments help drive our margin expansion this quarter.

I want to caution you, though, against assuming that this momentum will carry through the remainder of our fiscal year, as we begin to lap these easier compares, while continuing to execute on various strategic initiatives, including our client upgrade efforts, investing in innovation and making selective additional service investments. On a segment level, we therefore continue to anticipate margin expansion in ES of about 50 basis points. We are now forecasting about 70 basis -- 75 basis points of margin expansion in the PEO. On a consolidated basis, we have revised our adjusted EBIT margin expansion to about 50 basis points from our previous guidance of 25 to 50 basis points.

Please also note that this margin expansion continues to include about 20 basis points of pressure from dual operation pertaining to our service alignment initiative. We are also now expecting growth in our client fund interest revenue to increase $5 million to $10 million compared with our prior forecasted increase of up to $5 million. The total impact from the client fund extended investment strategy is now expected to be up $5 million compared to the prior forecast of flat growth. The details of this forecast can be found in the supplemental slides on our Investor Relations website.

With the disposition of our CHSA and COBRA businesses, we now expect growth in our adjusted diluted earnings per share of 11% to 13%, compared with the $3.26 in FY16, aided by about 1% from the first-quarter tax benefit related to the stock based compensation accounting change, which is offset by about 1 percentage point of earnings impact from the disposition of our CHSA and COBRA businesses. On a constant dollar basis, our adjusted diluted earnings per share growth is expected to be 11% to 13%.

Our forecast continues to contemplate the return of excess cash to shareholders via share repurchases of $1 billion to $1.4 billion during FY17. This includes any repurchases required to offset any dilution related to employee benefit plans. We believe the adjustments we have made to our FY17 forecast reflect the impact of our planned investment, particularly through the year-end process as we work to grow our strong FY16 sales performance and execute against our strategic initiative.

So with that, I will turn it over to the operator to take your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Rick Eskelsen, Wells Fargo.

Rick Eskelsen - *Wells Fargo Securities - Analyst*

Just the first one, just to confirm the guidance impact on the top line, confirming that the divestitures of the CHSA and the COBRA businesses is responsible for the change in the revenue outlook. Then also confirming that I heard it was a 1% or so earnings impact from that divestiture as well.

Jan Siegmund - *Automatic Data Processing Inc - CFO*

You're correct. That is the case. If you take it digitally, there's actually, with [duct tape] on both ends, the full percentage off our guidance, clearly just on the top end. We clearly had a good revenue performance in the first quarter already.

Rick Eskelsen - *Wells Fargo Securities - Analyst*

That's the only change to the revenue outlook is from that divestiture; correct?

Jan Siegmund - *Automatic Data Processing Inc - CFO*

That is true.

Rick Eskelsen - *Wells Fargo Securities - Analyst*

Okay. Then just following up on the service delivery changes, just wondering, maybe philosophically as you have evolved your business and added a lot more of your technology in the strategic platforms, how has the value of service changed to you or to your clients? Philosophically, how do you approach service now? Thank you.

Carlos Rodriguez - *Automatic Data Processing Inc - President & CEO*

I think as you heard in my comments about the investments we've made in DataCloud and benchmarking, I think there is an evolution of the definition of service to really providing more expertise and more help in terms of analytics and how to run their businesses better. So some of the things that we traditionally have been strong on in service I think still are a key part of our value proposition. So as an example, we have a very effective, very value-added tax business that helps clients with compliance should they gets notices from either federal, state or local agencies regarding tax payments. So those are the types of services I think we remain committed to continuing to provide but also to make better and enhance.

But obviously with the evolution of technology and the evolution of the markets, I think there are opportunities for us to redefine service. I think some of the service alignment initiative I think is intended to go exactly in that direction. So another example I would give is, given the increased penetration of multiple HCM modules when clients purchase our products, particularly in the mid-market or in the up-market, I think the integration of not only our products but of our service experience becomes very important. So you've heard us talk about creating intact teams in some of these new strategic locations that I think is intended to support this evolution of this new service approach or new service model.

Rick Eskelsen - *Wells Fargo Securities - Analyst*

Thank you very much.

Operator

David Ridley-Lane, Bank of America-Merrill Lynch.

David Ridley-Lane - *BofA Merrill Lynch - Analyst*

Within the 20 basis points of the full-year margin headwind related to the dual running cost as you move to your new integrated service delivery centers, how much was in the first quarter? When do you expect the crossover between increased productivity from the new centers to overcome those frictional costs? Is that a second-half event or more likely in FY18?

Carlos Rodriguez - *Automatic Data Processing Inc - President & CEO*

Yes, I would say that it's -- given that we're in the process of ramping up, it's safe to say there was some of that in the first -- some dual operations costs in the first quarter, but it's likely to be more concentrated later in the year in the second half. So that's -- I think you have that right. Probably 40%, I would allocate it just for sake of modeling to 40/60, so 40% maybe first half, 60% second half. But overall, 20 basis points for the year. Again, as Jan pointed out, just because of the way the accounting rules work, that is built into our operating expense versus the restructuring costs are really more intended for things like severance and facilities closure that were directly related to the restructuring and that are non-GAAP.

David Ridley-Lane - *BofA Merrill Lynch - Analyst*

Got it. Then are you seeing any additional interest in time and attendance offerings, given the Department of Labor's changes to the overtime regulations, which go into place this December?

Carlos Rodriguez - *Automatic Data Processing Inc - President & CEO*

We are -- as we were going through the materials for the earnings call, we get a lot of detail by market segment and also by product. We have seen better sales and more interest in our time and attendance product. I think the challenge for us is scale, given the size of our sales number -- we sold $1.75 billion last year. We're expecting to grow 4% to 6% this year. It just doesn't have the same scale and magnitude of, as an example, ACA. So, for us to really achieve our sales results, we have to have across the board strength in our sales excluding ACA and excluding our time and attendance product.

So I guess the long and short of it is, yes, it helped, but it wasn't material in the grand scheme of things. The deadline is approaching, so it's likely that will continue -- a lot of these changes in regulations and complexity, no different than ACA, we expect it to continue to help with sales and help drive demand for our products, even after the deadline which I believe is in December of this year. But it just doesn't feel like it's having the same magnitude and same kind of scale impact that we had with ACA.

Part of that might be that the ACA rules were really deadline driven and there was a form that needed to be filled out and filed. In this case, these are just changes in rules. So it's a slightly different decision for clients and prospects around -- in some cases, if they go six months without the right tools to be able to manage the new environment, there's really no consequences other than the risk of a potential investigation or fine or whatnot, which is obviously a real risk, but it's just different from a deadline driven event like ACA.

David Ridley-Lane - *BofA Merrill Lynch - Analyst*

Understood. Thank you.

Operator

David Grossman, Stifel Financial.

David Grossman - *Stifel Financial - Analyst*

Carlos, can I ask you just a quick question on mechanics? The bookings comparisons last year are pretty difficult until the fourth quarter. So given that, how should we think of that 4% to 6% bookings target building as this year progresses, given those comparisons?

Carlos Rodriguez - *Automatic Data Processing Inc - President & CEO*

Appreciate that question, I think you may have answered the question yourself. So we expect the comparisons to get easier in the second half and, hence, the mathematically the growth rates should be easier to achieve in getting to our overall 4% to 6% for the year. I think just by way of comparison, we went back and looked historically outside of course times where we had recessions and other economic challenges, but in Q1 of 2014, we had 1% sales growth and that was following on Q1 of 2013, 15% growth. The scenario this quarter was we had flat growth over last year's first quarter of around 14% sales growth.

So I think that when you look at kind of just the size and the scale of these numbers and you look at the way we laid out our forecast for the year, then I think that you can probably deduce that the second half, we expect mathematically to be stronger from a growth rate standpoint than the first half. I also just want to hasten to add that we have the same kind of issue in the second quarter, where we had sequential increase last year's second quarter of 15%. So we had I think it was 13% to 14% growth in the first quarter, then we had 15% in the second quarter. So we will have another difficult compare. I think it would be in line with our expectations to have similar sales results from a growth standpoint for the second quarter.

David Grossman - *Stifel Financial - Analyst*

Okay. It looks like you were 13% in the third quarter, so it sounds like it's pretty back-end loaded to the fourth quarter then?

Carlos Rodriguez - *Automatic Data Processing Inc - President & CEO*

That would be right. But again, we have more information internally around what portion of each of those three quarters was ACA related versus other. I would say that you're generally correct but that we would expect the third quarter to have slightly better -- we try to stay away from -- I don't want to fall in the trap of giving quarterly guidance. You're generally right.

David Grossman - *Stifel Financial - Analyst*

Right. Then maybe I could just ask you a little bit more about -- you made some brief comments about the migration in the mid-market, how that's going and retention. So given that retention was declining all of last year and you said it was flat when you back out the CVB loss of the customer in the quarter. So does that really imply, given that you were losing throughout the year last year, that in fact that business started stabilizing even before this quarter? How just in general are you thinking about retention and the kind of residual base who still has not converted thus far?

Carlos Rodriguez - *Automatic Data Processing Inc - President & CEO*

Sure, I appreciate the question. So the businesses that we had some challenges with last year, which I think we were clear that it was concentrated in the mid-market, have shown improvement for several quarters, including this quarter. But as you know, we have a number of different businesses. We're a global Company. We have down-market, mid-market, up-market, multi-national. Some of our businesses are also lumpy, particularly our up-market businesses and our BPO businesses. So we feel good about the progress we've made where we made the investments to stabilize and the investments were made in service.

As you know, we're making some longer-term investments in terms of some of these new locations. But that's a longer term -- we did a lot of short-term things to stabilize and improve and we've seen results from that. But again, sometimes retention can be uneven just because of the lumpiness and just the way the math works. But we feel pretty good about where we are. We believe that we are on a good trajectory here in terms of continuing to do migrations and upgrades, which allows us to stay on track for what our objectives are without putting additional incremental pressure on retention.

The fact that we've gone back to -- this is now probably the second quarter where we've gone back and started our upgrades at a, what I would call, normal, reasonable pace. We've been able to continue to make improvements in our mid-market retention rates. So that tells me that part of the issue was related to the upgrades themselves, but it was also related to just service challenges, pressure from ACA just because of volumes of work and a couple of other factors. We believe we've done the right things. We feel like we're on the right track. We're also sticking to our plans around our migrations and our upgrades of our clients. Because I think it just strengthens us competitively over the long term.

David Grossman - *Stifel Financial - Analyst*

Great. Thanks very much for that color.

Operator

Jim Schneider, Goldman Sachs.

Jim Schneider - *Goldman Sachs - Analyst*

Following up on the comments on margins you made earlier, I noted the discussion about lower benefit pass-through costs in the current quarter, but the PEO margins were, I think, a record at 13.5%. Can you maybe talk about whether margins in that segment specifically are sustainable? Whether you saw any kind of -- how much that one-time benefit from the lower pass-through cost had a benefit to optical margin improvement in the quarter?

Jan Siegmund - *Automatic Data Processing Inc - CFO*

Jim, thank you for your question. I will answer it directly to your PEO question, but also put the margin question in a little bit bigger picture because there's a lot going on, on margin. Clearly, we had great margin expansion this first quarter. But we are trying to send a signal that might not be continuing throughout the year. The pass-through actually played a big role in it. So we had -- to answer your first question directly, the operational

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scale that we saw in the PEO was solid with 90 basis points. Clearly that's ahead of our long-term kind of expectations. So we do see and want to make progress in the efficiencies, but it was probably a very good quarter for them.

I would caution you to anticipate that type of level of productivity improvements in the long run. But clearly all our businesses need to deliver scale when we're sticking with our own long-term expectations of driving the margin in the Company of 50 to 75 basis points. Now, relative to the performance in this quarter -- you will be able to dissect this once you go through the Q in a little bit more detail, but the pass-through pressure that we had this year because the PEO is growing actually faster than the overall Company was actually depressing ADP's margin by about 85 basis points.

Now the pass-through pressure is typically actually higher. If you calculate it as between a 150 and 200 basis points of pressure, we call this a portfolio effect, a lower margin business of PEOs growing faster than ES. This quarter, we were helped because that typical -- that higher margin pressure that the pass-throughs give us abated due to that good renewal. That renewal, we're expecting to grow out of it by the second half of the year. So, that is going to be big contributor to slower margin expansion for the second half of the year.

You will also see that -- we mentioned in our call that we had flat sales growth. It's long-standing tradition that if sales are growing slower, our marketing and sales expense is growing slower. So that contributed a chunk of scale that we anticipate clearly per Carlos's discussion, just the prior question, to abate as we accelerate our sales in the second half of the year. Then the scaling of our ACA business plays an important role. Clearly, you're all aware that the revenue stream started really in the second half of the ACA business, while in the first half of last FY16, we made implementation and operational investments to build the business.

So we started to see the revenue contribution kick in. The pressure that the building of the ACA business exuded on the business in the first half of last fiscal year has abated. We are reaping the revenue and the business is profitable. So the scaling of the ACA business also had a meaningful impact on the margin expansion this quarter. Clearly, we expect that actually to abate also in the second half of the year because the business started to generate revenue in the second half of last fiscal year.

Carlos Rodriguez - *Automatic Data Processing Inc - President & CEO*

I think just one other comment on the PEO. I think this is -- I don't remember the last time that our PEO worksite employee growth was the same as our revenue growth. So that obviously -- the very first point that Jan made, I think that helps obviously mathematically, it makes it easier for the PEO to achieve greater margin improvement when they have slower pass-through cost growth.

We generally see that as having been in that business for many years, that slower pass-through growth is related to lower healthcare benefit renewals, which is -- should be a very big positive from a competitive standpoint. So as we're hearing, seeing a lot of headlines about increasing health inflation and the discipline that our business has around selling and renewing clients, I think has, as of this last open enrollment for the PEO, led to very, very competitive renewal rates that are having this impact on the revenue growth but it's a very, very big positive for that business.

Jim Schneider - *Goldman Sachs - Analyst*

That's helpful color. Thank you. Then maybe just a quick clarification. The client loss in the CHSA business that drove the 100 basis point decline in retention was fairly substantial in terms of overall scale. Can you maybe just give us a little bit of color of whether that's a competitive take-away? Then specifically did that -- is that client a customer of ADP in terms of other service offerings? What's the disposition on those other offerings, if any?

Carlos Rodriguez - *Automatic Data Processing Inc - President & CEO*

So fortunately, it's easy to talk about it because WageWorks I think is the company who won that account. They won it -- it was one of the factors in our decision to sell the business to them, because we got to know each other as a result of them winning that contract, which is a government contract from the office of personnel management, OPM, which is a government entity. As you know, we don't have a lot of public sector government business.

We have some and we like that business but we just don't have a lot of it. We certainly don't have a lot of contracts of that size and that scale with or without the government. So the original genesis of that account was, it came through an acquisition of a company called SHPS that we acquired several years back, where we acquired other benefits administrations assets that we were interested in and this account came with it. With it came the risk of when these contracts get put out to bid, you don't always win.

So we took a calculated risk when we made that acquisition, not just with this account but like with all acquisitions. That was one of the items that came along with that acquisition. But it was also an account that -- I can't remember how many months ago it was, but I believe there was a public release by WageWorks regarding the winning of that account. I think some people speculated that it had come from us. We can now confirm that it did come from us.

Jim Schneider - *Goldman Sachs - Analyst*

Thank you.

Operator

(Operator Instructions)

Gary Bisbee, RBC Capital Markets.

Gary Bisbee - *RBC Capital Markets - Analyst*

Carlos, you've been talking about the data analytics opportunity and the value in that data you have I guess really since the Investor Day at the beginning of last year. Can you give us a sense how you've since then progressed in terms of figuring out exactly how you will monetize the asset? Are you charging for this separately at the moment? Are you actively trying to sell that as a standalone offering? Or is it really more focused on an add-in to existing customers to help them see more value in ADP and hopefully improve retention?

Carlos Rodriguez - *Automatic Data Processing Inc - President & CEO*

For now, we are selling it as an add-in. As I mentioned in my comments, we have 3,200 clients right now. That's obviously a very small number of comparison to the total client base that we have. So we think there's still a lot of opportunity. But we do like to leave our options open in terms of the quote, unquote monetization. Because the one thing it clearly does, it's a big differentiator for us. It's a huge way of creating thought leadership for ADP. Most importantly, it's an incredibly important way of driving value for our clients by helping them run their businesses better.

We think there's a number of ways that we could benefit from this, in terms of stronger sales, additional revenue as an add-on module, halo effect in terms of marketing and thought leadership. So I think it's a big winner on a number of fronts, as other analytics and data businesses are for other companies. We're not the only company taking advantage of when you have the scale and you have the data of being able to marshal that to create differentiation and value for clients, I think is a pretty common theme out in the marketplace right now.

Gary Bisbee - *RBC Capital Markets - Analyst*

Is there a product road map as to other analytics and ways to expand the usefulness of this? I guess, one thing that jumps to mind is a potential risk, are there regulatory issues or concerns or hurdles you have to get over in terms of using data about consumers as either part of the benchmarking or however else it's used in this. Thank you.

Carlos Rodriguez - *Automatic Data Processing Inc - President & CEO*

That's a very good question. The answer to the first part of the question is, yes, we do have a road map. We have lots of plans and things that we can do to create more benchmarking solutions and more analytics for our clients. Obviously we're not going to talk about those right now. In terms of the second part, so we do have permission, if you will, to use the data from our clients and most importantly the data is anomamized So this data there is no personally identifiable information. It's not necessary in order to create the benchmarking and the analytics and the information that we deliver back to our clients.

So I think we're very sensitive obviously if there's any Company in the world that understands the value of privacy and sensitivity to security, I think it's ADP. We've been very careful over the last several years to make sure that we have the right kinds of approvals and permissions from our clients and also that we are anonamizing the information so that none of the information has things like Social Security numbers or addresses or anything like that. That's generally not necessary to perform some of the analytics that need to be performed.

Gary Bisbee - *RBC Capital Markets - Analyst*

Great. Then just a quick follow-up. On the accounting -- adoption of the new accounting for stock comp taxes, do you expect in the guidance any impact on the rest of the year? Given the variability of that, do you have confidence in that outlook? Or is this something that could be a positive later in the year but it's just hard for you to predict at this point? Thank you.

Jan Siegmund - *Automatic Data Processing Inc - CFO*

Thank you for the question. Because it is quite a big impact that we experienced as a tax benefit for this year. We have taken the stand not to forecast the impact of -- the tax impact of our equity compensation cost for the future quarters because it is dependent on our share price development. It is also dependent on the employee behavior in executing mostly stock options. So our plan is every quarter to let basically that tax benefit fall through to the bottom line. We will update our guidance for the total EPS growth one-on-one as the tax benefit or the tax hurt is incurred. We have done a historic analysis of our performance under these, so to speak, per forma backwards. Historically, we have experienced benefit out of those accounting rules. But there's no guarantee that would continue in the future. We found it too difficult to forecast. So we take it as falling through. You would get the benefit one-on-one in each quarter.

Operator

Lisa Ellis, Bernstein.

Lisa Ellis - *sanford C. Bernstein & Company - Analyst*

On the service alignment initiative, can you guys just talk a little about how you see the impact of that, both on driving ancillary revenue streams as you I guess move to a team selling model or a team service model, long-term margin improvement and then also any potential disruption in the client relationships as you consolidate people back? What are the puts and takes? How do you see those playing out as you implement the new service alignment model?

Carlos Rodriguez - *Automatic Data Processing Inc - President & CEO*

I think you did a very good job of describing some of the puts and takes and some of the potential upside and some of the risks. As you heard from our comments, we did build in what we're calling dual operations costs to avoid the last part that you mentioned, which is transition challenges, if you will. So, we want to make sure that we have people trained and ready before we move work. But there's obviously always you have to manage through that kind of transition risk as well.

To be clear, this is not -- we're not moving 90% of our associates. We're moving anywhere between 5% and 10% of our associates. So over time, we expect that to have the kind of positive impacts we're talking about in terms of incremental revenue growth, improved service, et cetera. But this is a -- not a one-time overnight dramatic move that is intended to create an enormous amount of risk or frankly, disruption for our associates. Because we have a long history of treating our people right.

We have highly tenured associates that have been very loyal to the Company. So, we're being very, very careful and methodical on how we do this and how we communicate to our associates so that we can move on with our business plans but also treat people the right way. But having said all that, the idea as we've said I think previously is to most importantly deliver better integrated service through intact teams of multiple modules of HCM. So the intention would be that there would be a benefit to retention. We don't have a scientific way of forecasting that or telling you when that will happen. It certainly is not expected to happen this year because we're just in the process of getting these places all ramped up and scaled.

Obviously the effect of having better service, a better reputation and being able to cross-sell more easily should have some impact on our ability to sell and on our revenue growth as well. But again, those are hypotheticals that are very hard to forecast. We're certainly not building anything into our forecast for this year. But we're not doing it just to take risk. We're doing it because we see benefits in terms of operational efficiencies, potential retention and potential growth down the line.

Jan Siegmund - *Automatic Data Processing Inc - CFO*

I might add for our associates it also offers of course a better ability to work in centers that have a defined career path. They are located in areas of the US that we believe give us great access to our associates. So, it will create really also for us as an employer of choice a opportunity to differentiate ourselves in the marketplace.

Carlos Rodriguez - *Automatic Data Processing Inc - President & CEO*

Yes. As Jan was saying, engagement is a very -- associate engagement is an incredibly important part of our success and of any service business' success. I think having large centers with anywhere between 2,000 and 3,000 associates that are able to progress in terms of their careers, move across business units, across different parts of HCM, I think should be a very big positive for us. But again, that's a longer term benefit for the Company.

Lisa Ellis - *sanford C. Bernstein & Company - Analyst*

Got it. Okay. Then just as a quick follow-up, can you give us an idea of -- one thing you don't comment on very frequently is what the retention dynamics are within the PEO. On one hand, I know that the average client size there is smaller, so you're more likely to lose just from companies going out of business. But on the other hand, I don't know why, once you join the PEO, why would you ever leave?

Jan Siegmund - *Automatic Data Processing Inc - CFO*

The PEO average client size is now slightly below 50, actually, so around 40, I believe, I'm looking at Christian, around 40 employees. It has ticked up a little bit. I think this has been partially driven of course by the dynamic over the last few years, where we added slightly larger clients to the PEO because it offers a great answer on compliance and probably partially a little bit aided by the dynamics of the Affordable Care Act. I'm happy to report that the PEO exhibits great retention rates. They have been actually improving over time. I'm looking at Christian -- if I say they did have record retention this quarter, so they're doing well.

Operator

Bryan Keane, Deutsche Bank.

Bryan Keane - *Deutsche Bank - Analyst*

Just noticed, Carlos, in your comments you were talking about the strategic cloud platforms having a positive impact on your business. I'm just curious of what percent you are complete migrating clients to these cloud platforms now?

Carlos Rodriguez - *Automatic Data Processing Inc - President & CEO*

Again, we do look at it by segment because you do have to be careful about units versus revenue, right? Two things are important. So, if you look at it based on units, we're almost 90% migrated. But that's mainly because we moved all of our clients onto our RUN platform in the down-markets. So, from a revenue standpoint, we're a little bit less than half I think of the revenues for the Company. So if you look at it by segment, we're done in the down-market. I think we are -- should be done by the end of this fiscal year.

I think that's consistent with what we've said in the past, that we're on track. We're saying it now -- that we're on track to have our mid-market clients on our WFN current version platform by the end of this fiscal year or within a month or two after that. Then when you move up into the up-market, we have migrated some clients over to Vantage. We have plans underway to continue those migrations. But those are literally one at a time, whereas in the down-market can and then in RUN, there were just large groups of clients that would migrate every week.

In the up-market, it's one at a time, talking to each client individually, creating a schedule and creating a path. But we have done migrations. We will continue to do migrations in the up-market but that will take considerably longer than what we did in our down-market business, which took us probably over the course of two to three years to migrate all of those clients.

So we're very happy with the progress. We believe that when we migrate our clients we create a more defensible, bigger moat against competition. We believe that it creates an opportunity for us to sell additional products and services. We believe it strengthens our relationships with our clients. Most importantly, we think it's the right thing for our clients. So we're still on track and we're continuing to move ahead.

Bryan Keane - *Deutsche Bank - Analyst*

Okay. No, I appreciate the update. Then just as a follow-up, retention was down I think 1 point last year in FY16. If you ex out the divested acquisitions, does it make any difference to that retention number?

Jan Siegmund - *Automatic Data Processing Inc - CFO*

Too small to have an impact. The divestiture really has no impact one way or the other.

Bryan Keane - *Deutsche Bank - Analyst*

So, it was kind of an unusual one-time client loss that caused this (multiple speakers) --

Jan Siegmund - *Automatic Data Processing Inc - CFO*

This was one large client loss. We typically don't have clients of this size. We pointed out, because it is a non-strategic asset and in the public space, so it was really -- this is very unique situation for us.

Carlos Rodriguez - *Automatic Data Processing Inc - President & CEO*

Again, I think we have -- this is disclosed in our 10-K and in our once a year. I don't believe we have another client that represents that size revenue for us.

Bryan Keane - *Deutsche Bank - Analyst*

Okay. Helpful. Thanks so much.

Operator

Jeff Silber, BMO Capital Markets.

Jeff Silber - *BMO Capital Markets - Analyst*

Just a couple of quick questions. I noticed your cash flow from operations was fairly sizable, a nice increase on a year-over-year basis. Were there some timing issues going on either this year or last year? How should we expect the quarters to kind of play out for the rest of the year? Thanks.

Jan Siegmund - *Automatic Data Processing Inc - CFO*

I'm excited that we get a cash flow question, we rarely do get one. You're already also giving the right answer. If you dig a little deeper into our operational cash flows, you'll see a large swing in our accounts receivables on our balance sheet. This is driven mostly due to accounts receivable change in the PEO business and has rectified itself already. If you adjust for a number of one-time items in this, cash flows are expected to really grow in line with our operating results. So it could be these timing issues on accounts receivable here and there, but in the long-run cash flows develop really very nicely in line with our operating performance.

Jeff Silber - *BMO Capital Markets - Analyst*

Okay, great. That's helpful. I know some of the other business services and staffing related companies have been talking about some client uncertainty in terms of making decisions. I'm just curious if you've been seeing any of that?

Carlos Rodriguez - *Automatic Data Processing Inc - President & CEO*

I'm not sure how you measure that. I think we know that for example in FY11, when we had government shutdowns and so forth -- we hesitate to answer the question because we don't have any way of really measuring that. But intuitively, we know that large events do sometimes impact particularly up-market decision making and so forth. So is the election having some kind of impact? You'll have to stay tuned for our next quarter call that we will be able to tell you with the benefit of hindsight, whether or not we experienced some of that. So, very hard to measure. But we have to acknowledge that large events and large uncertainties do sometimes create uncertainties in the market.

Jeff Silber - *BMO Capital Markets - Analyst*

Yes, I guess what they've been saying is that they've been seeing some delays in terms of new business sign-up. I thought maybe you'd seen some of that impact on your bookings, not necessarily just the tough comparisons versus last year.

Carlos Rodriguez - *Automatic Data Processing Inc - President & CEO*

Through the first quarter, the answer would be, if you exclude -- again, this is also not scientifically easy to do because we sold so much additional modules related to -- not just ACA, but related to ACA, so benefits, administration, et cetera. But if you look at our sales results and take a general swag at if you took out -- if you could somehow back out the ACA sales from last year, we had I would say good sales results for the quarter.

So I would say that through the first quarter the answer would be, we didn't see a lot of that but I think you should be -- you should not hear in my comments any level of confidence that there isn't that happening. Because large events like we saw with the 2011 and -- there were a couple of budget battles and a couple of issues around government shutdown and so forth that it did seem that there were some kind of delays in terms of decision making in the marketplace. But back then and today, we have no you way of measuring that other than anecdotal stories.

Jeff Silber - *BMO Capital Markets - Analyst*

Okay. I know it's a tough question to answer, I appreciate you taking a stab at it. Thanks.

Carlos Rodriguez - *Automatic Data Processing Inc - President & CEO*

Thank you.

Operator

Mark Marcon, Baird.

Mark Marcon - *Robert W. Baird & Company, Inc. - Analyst*

Just with regards to majors, how many more clients do you still have to transition? How would you characterize those clients as they're coming up along the tail end? Are they more likely to go through a smooth transition? Or are they more inclined to be kind of the types that would take a look at other alternatives?

Carlos Rodriguez - *Automatic Data Processing Inc - President & CEO*

It's a great question. I think the -- as usual, the answer is I think it's mixed in terms of -- we have a lot more experience obviously now in migrating clients, in particular, the experience we developed last year, when our volumes of upgrades almost doubled as we were trying to move clients over to the new platform in order to be able to give them the ACA product. That really created an enormous amount of learning opportunity for us in terms of how to do it better and how to do it at scale and what not to do around these upgrades. Because they're intended to be a positive and to create a better experience and a better -- and deliver a better product to the client.

So I think on one side of the scale, you would say huge -- we have an enormous amount of body of knowledge now on how to do this better. On the other side of the scale, human nature is such that no one consciously does this. When you go through these types of events, you realize, it looks like we have some of the toughest ones waiting towards the end. Because there might be clients for example that we approach and ask them to upgrade and they say, well, I don't want to do it now. Call me in quarter. We are getting to the point now where we're going to have to migrate them or upgrade them. So we probably have some of that as well. I don't think there's an enormous amount of that.

It's not like we only have the hard ones left and they ones that didn't want to go. Just being realistic in the sense that -- and also deferent to our associates who have still a lot of hard work ahead of them over the next three quarters or so, because it's not going to be -- it's not going to be easy getting across the finish line. But our volumes now are at a more manageable level where I think we're doing a much higher quality job. So we feel good about our ability to do it but your questions are I think fair and I think the answer is the scales are balanced.

Mark Marcon - *Robert W. Baird & Company, Inc. - Analyst*

Okay, I appreciate the answer. Then with regards to the -- to Vantage, how well positioned is that now for -- like once you get you through this and you're going through the next stage of transitions, do you feel good about that solution as it currently stands? I know you're always innovating, always optimizing. Is it matters or degree or is it -- in terms of getting it to exactly where you want?

Carlos Rodriguez - *Automatic Data Processing Inc - President & CEO*

Well, to put it in perspective, we have about double the number of clients. I think it's up to 270 or 280, somewhere in that range at the end of this quarter versus same period last year. So I think that tells you something.

Mark Marcon - *Robert W. Baird & Company, Inc. - Analyst*

Yes, it's great.

Carlos Rodriguez - *Automatic Data Processing Inc - President & CEO*

We would have liked it to have been higher by now. I think we're still growing well. We had good growth in the quarter in terms of Vantage. I think that in terms of the product itself, we're pretty happy with the progress we've made, particularly over the last two or three releases. We've had -- again, we get a lot of metrics and a lot of data around stability and other factors, defects, et cetera, and we've made a lot of progress. So it feels like the trajectory is in a positive direction for vantage, not just growth wise but I think in terms of the underlying metrics that we measure around quality and stability.

Operator

Thank you. This concludes our Q&A session for today. I am pleased to hand the program over to Carlos Rodriguez for closing remarks.

Carlos Rodriguez - *Automatic Data Processing Inc - President & CEO*

We thank you all for joining our call today. As you can tell, we got off to a really good start. On top of the great results, we're incredibly happy about the positive recognition we're getting in the marketplace. As you heard from some of my comments. It really helps us in terms of our thought leadership in the market. I think the investments we're making and our innovation efforts and also our simplification of our portfolio and aligning them to our service model. I think are going to yield great results for us. I think we have a lot of confidence in our ability to execute against those plans.

The last thing I want to do is just acknowledge our associates. We had a very tough year last year. I know I said it last quarter, but we had a challenging year. We really appreciate all the efforts to continue to deliver great service to our clients. The commitment that our service associates have to our clients is unmatched. It's one of the great strengths of ADP. So I just want to acknowledge them and give them my appreciation. I also want to thank all of you for joining us today. Thank you for your interest in ADP.

Operator

Thank you, ladies and gentlemen. That does conclude today's conference. You may all disconnect. Everyone, have a great day.