

Top Concerns and Challenges of Midsized Business Leaders in 2013



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Executive Summary

As the still-fragile economy continues to slowly recover, businesses of all sizes in the United States are struggling to build a secure foundation for growth and expansion. However, are midsized businesses – which typically have neither the agility of a small company nor the resources of a large enterprise – more susceptible in an uncertain business climate?

To understand how midsized employers are faring, the ADP Research Institute®, a specialized group within ADP®, conducted an online survey of over 1,000 owners and executives at companies with 50-999 employees in May 2013. As in a similar (2012) survey, respondents answered questions about their concerns, perceptions, challenges, and plans.

Their responses present a picture of uneasiness and mixed perceptions. Although 61% felt that the economy had improved in the past year, only 16% expressed confidence that it will continue to improve over the next 12 months. Compared to the 2012 survey, fewer midsized firms currently plan to increase their head count. Yet, when executives examined their own industry, 52% predicted significant or slight improvement in the coming year.



About half of the respondents reported increases in competition (52%) and growth in revenue/budgets (50%) in the past year. About 46% indicated they are feeling the effects of globalization through new opportunities, as well as increased competition.

Healthcare and other employee benefits are the two most prominent factors influencing labor costs – and hiring. The U.S. Supreme Court's ruling regarding the Affordable Care Act (ACA) has made the ACA and the cost of providing healthcare benefits the top of concerns of midsized business owners and executives. While

70% of midsized company executives expressed confidence that their firms would be in “complete compliance” with the ACA, they still lacked concrete plans to comply. This places a cloud of doubt over their expressions of confidence.

A similar gap between perception and reality exists when it comes to evaluating overall regulatory compliance and physical record keeping. Over 80% of the executives expressed confidence that their firms are compliant with payroll and other regulations. Nonetheless, nearly a third (30%) admit to paying fines or penalties for noncompliance in the past 12 months. In addition, 60% of all respondents' firms store some employee records in paper files, despite the fact that 20% report they have been impacted by a natural disaster that placed these records in harm's way and made them temporarily inaccessible.

While midsized employers are sharing the experience of adverse conditions – from increased compliance requirements to greater competition for talent – many are choosing to transform their challenges into opportunities. Effective human capital management is helping them to stand up, get in the game, and succeed.

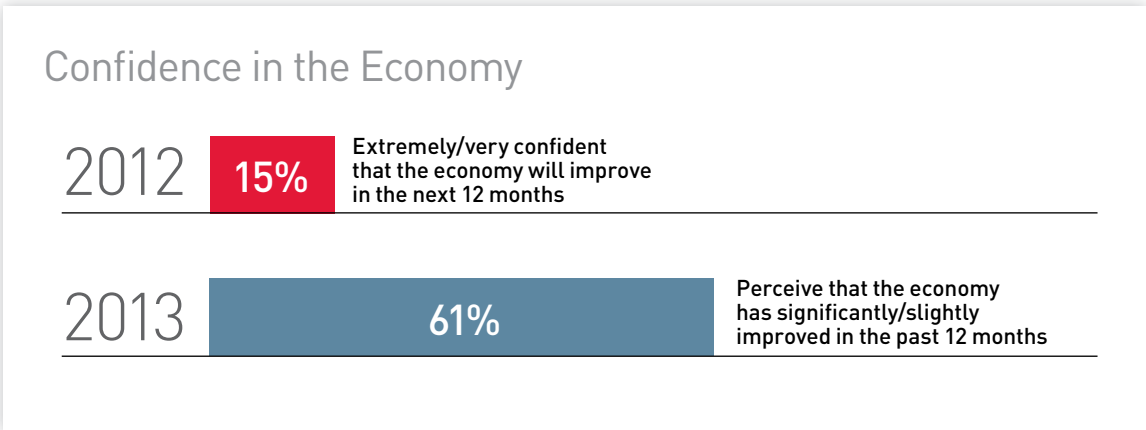
Perceptions of the Economy Don't Match Performance

“ The American economy, responsible for about a fifth of world economic activity, is proceeding in fits and starts and there is no indication that it will not continue in this manner during the rest of 2013.”

Nearly five years of sluggish, on-again off-again recovery from the 2008 financial crisis has created a mood of “defensive pessimism” among business leaders. Just 16% of mid-sized business owners and executives surveyed in 2013 expressed confidence that the economy will improve over the next year.

In the past, however, such pessimism has proven unwarranted.

In 2012, a similar number expressed confidence in the ensuing year's outlook. Yet, when respondents looked back a year, four times that many judged that the economy had improved in the intervening 12 months.



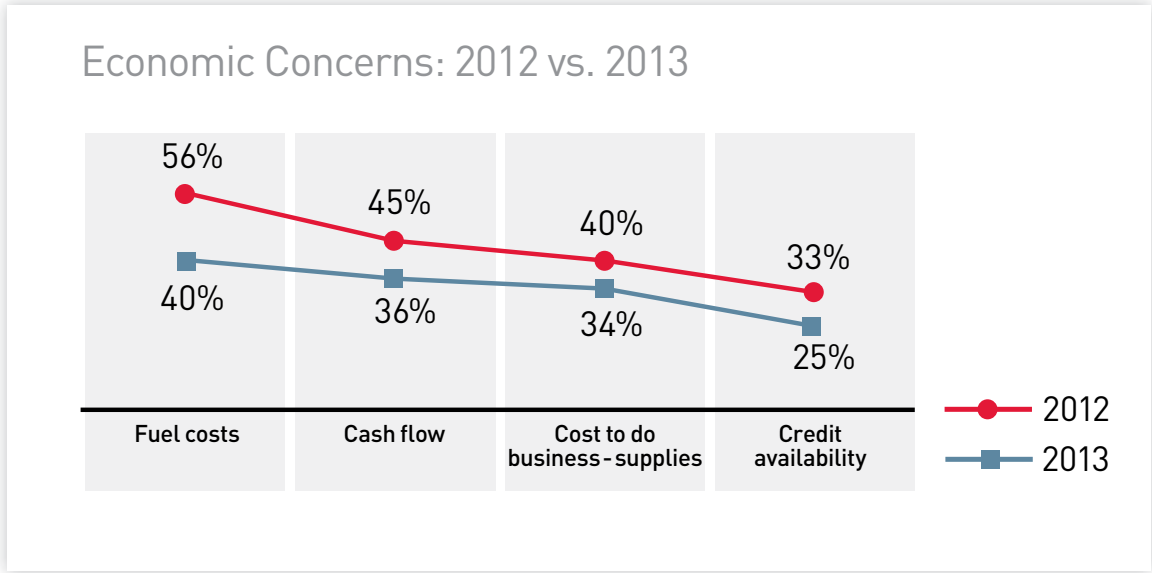
When leaders of mid-sized business turn their attention to the prospects for their own industry, their forecasts are more positive – and far more accurate. In 2012, almost half of survey respondents stated that the economic state of their industry would improve in the coming year. Twelve months later, the very same percentage report they had seen improvements.

1 HSBC Global Connections, May 2013.

Looking forward, leaders of mid-sized businesses express even more confidence in the prospects for their industries in 2013, with more than half predicting improvement within the next 12 months. Respondents from smaller firms (50-150 employees) are significantly more optimistic than their colleagues at larger companies (151-999 employees).



More positive views from an industry perspective are reflected in significant declines in the number of respondents who expressed concern about many economic issues, including fuel costs; cash flow; cost of doing business, supplies, and credit availability. To be sure, these issues remain major business impediments, but the reduced levels of concern indicate that mid-sized business leaders are likely adapting to higher fuel costs and other less tangible factors such as “the new normal.”



Increased Competition Drives Opportunity and Growth

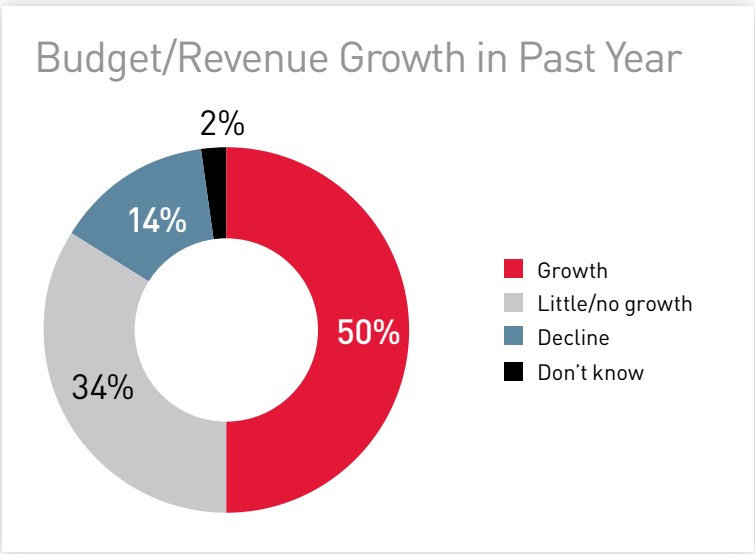
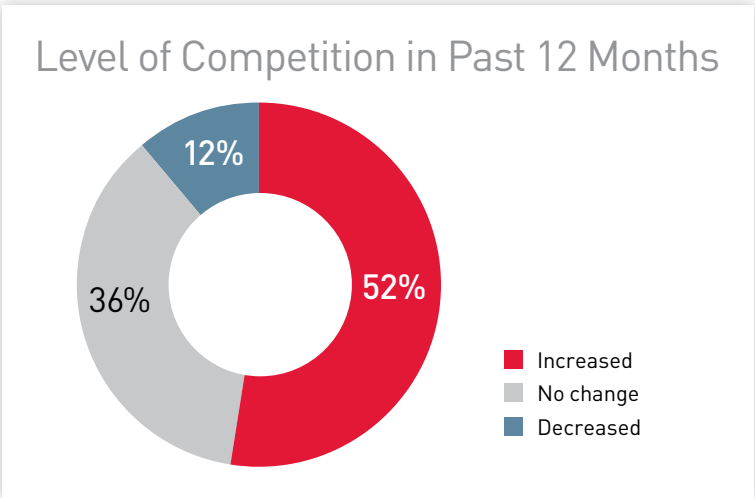
Further indicating that the business climate is (slowly) improving, at least half of mid-sized business owners and executives said their firms had witnessed increases in competition and growth over the past 12 months.

Asked to describe the level of competition in their industry, slightly more than half of the respondents reported an increase. In contrast, only a small minority felt that competition decreased, while just over a third judged it to be about the same as the previous 12-month period.

Company growth (as reflected by revenue and/or budgets) is comparable, with half of all mid-sized firms reporting significant or moderate growth in the past year, while only a minority reported moderate or significant declines.

The similarities of these numbers might suggest that respondents define increased competition as a larger number of available business opportunities rather than purely an increase in the actual number of competing firms.

When asked to cite the reasons for revenue growth, firms of all sizes said the top three were "expanded customer base," "industry growth," and "economic upturn."



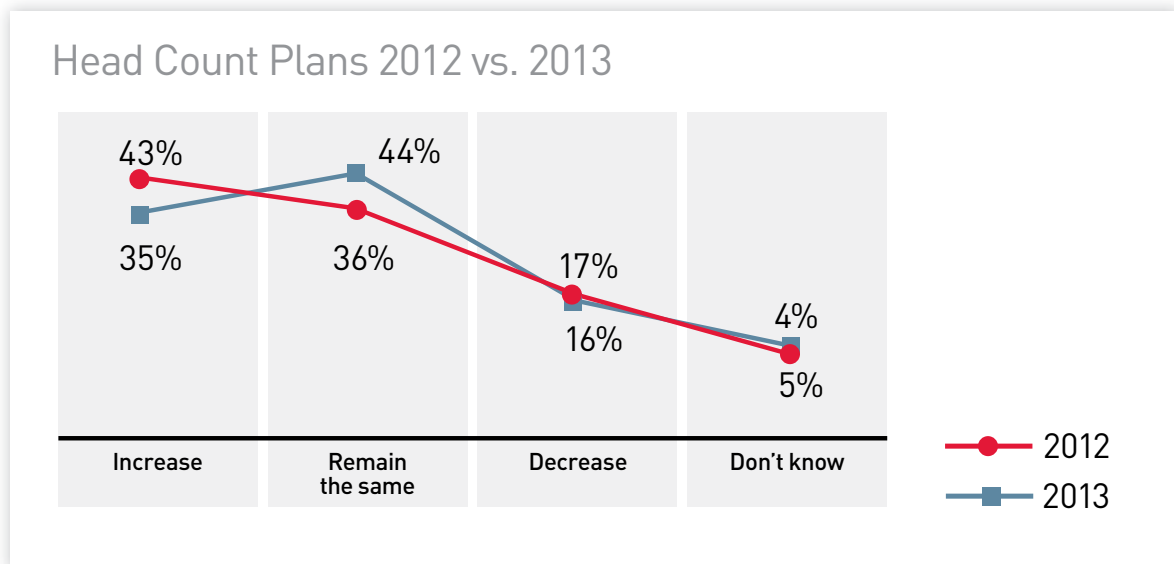
Mixed Messages on Hiring

Hiring plans reflect growth drivers

Hiring plans seem to reflect divergent reasons for growth. For example, smaller firms are substantially more likely to designate increased product demand – which corresponds to their plans to hire – mainly in direct production of a good or service. Larger firms are far more likely to attribute growth to company expansion, focus on strategic initiatives, and innovation. Accordingly, while all companies are primarily hiring in revenue-generating areas such as operations, larger firms are much more likely than their smaller counterparts to be hiring in the areas that support growth initiatives – sales, technology, finance/accounting, and human resources.

“ This remains the slowest-paced rebound since World War II... [and indicates] an economy laboring to produce job-creation potential at a sustained 2.5% rate or higher.”

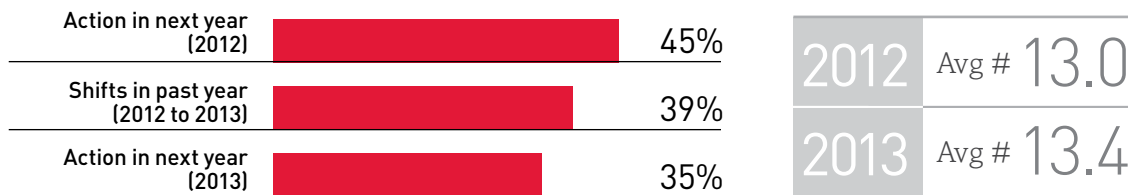
Despite the generally positive outlook on their own industry's prospects, mid-sized business leaders are trimming planned increases in their own businesses' head counts compared to 2012.



On a brighter note, companies that added head count in that past year overwhelmingly plan to continue growing, with nearly two-thirds anticipating increasing their employee count. This indicates pockets of robust business activity, even in the absence of a broad-based economic recovery.

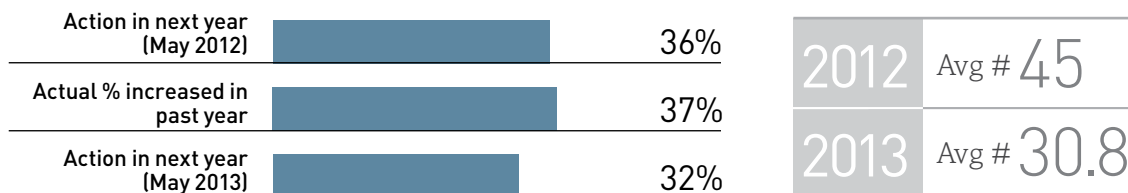
The number of smaller midsized companies planning to increase head count in the coming year has significantly shifted downward in the past year. While this is troubling, those companies that are still planning to hire are anticipating the same hiring level as last year (an average of 13 employees).

Hiring Among Small Midsized Companies (50-150 EEs)



The hiring expectations of larger companies in 2013 appear to almost mirror results from the prior year's study. Thirty-six percent of respondents in the 2012 study anticipated increasing head count in the coming year. When asked in this year's survey, 37% of respondents indicated an increase in employees. However, looking ahead to the next year, owners/executives are somewhat less likely to increase head count. Among those who are planning on increasing head count, there is a significant drop in the number of employees anticipated. All of this seems to reflect fundamental economic concerns.

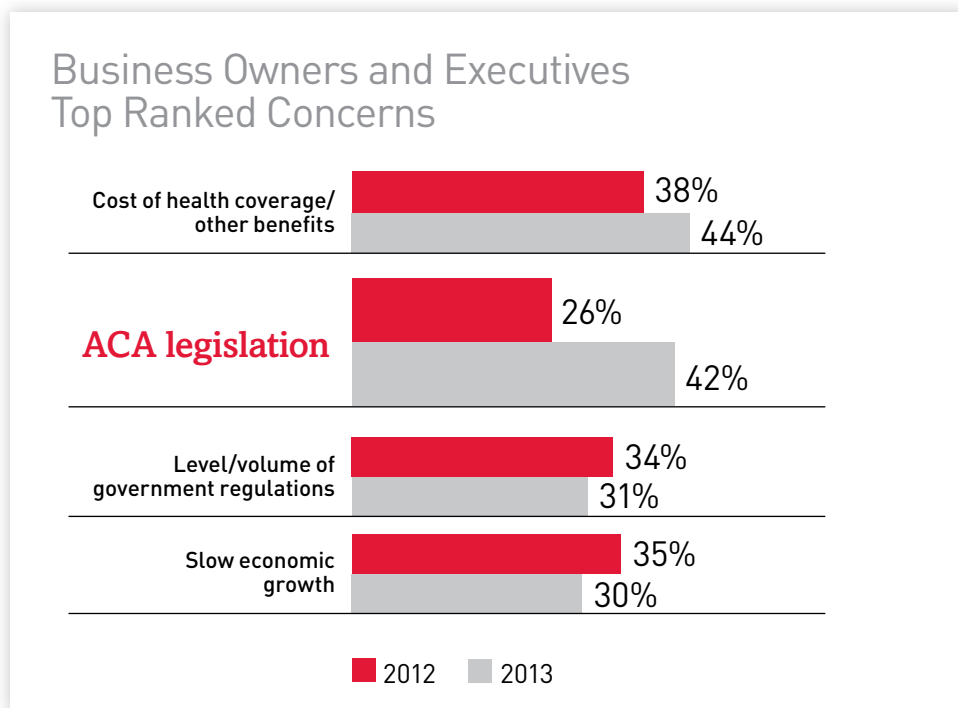
Hiring Among Larger Midsized Companies (151-999 EEs)



Health Care Reform Dominates Top Concerns

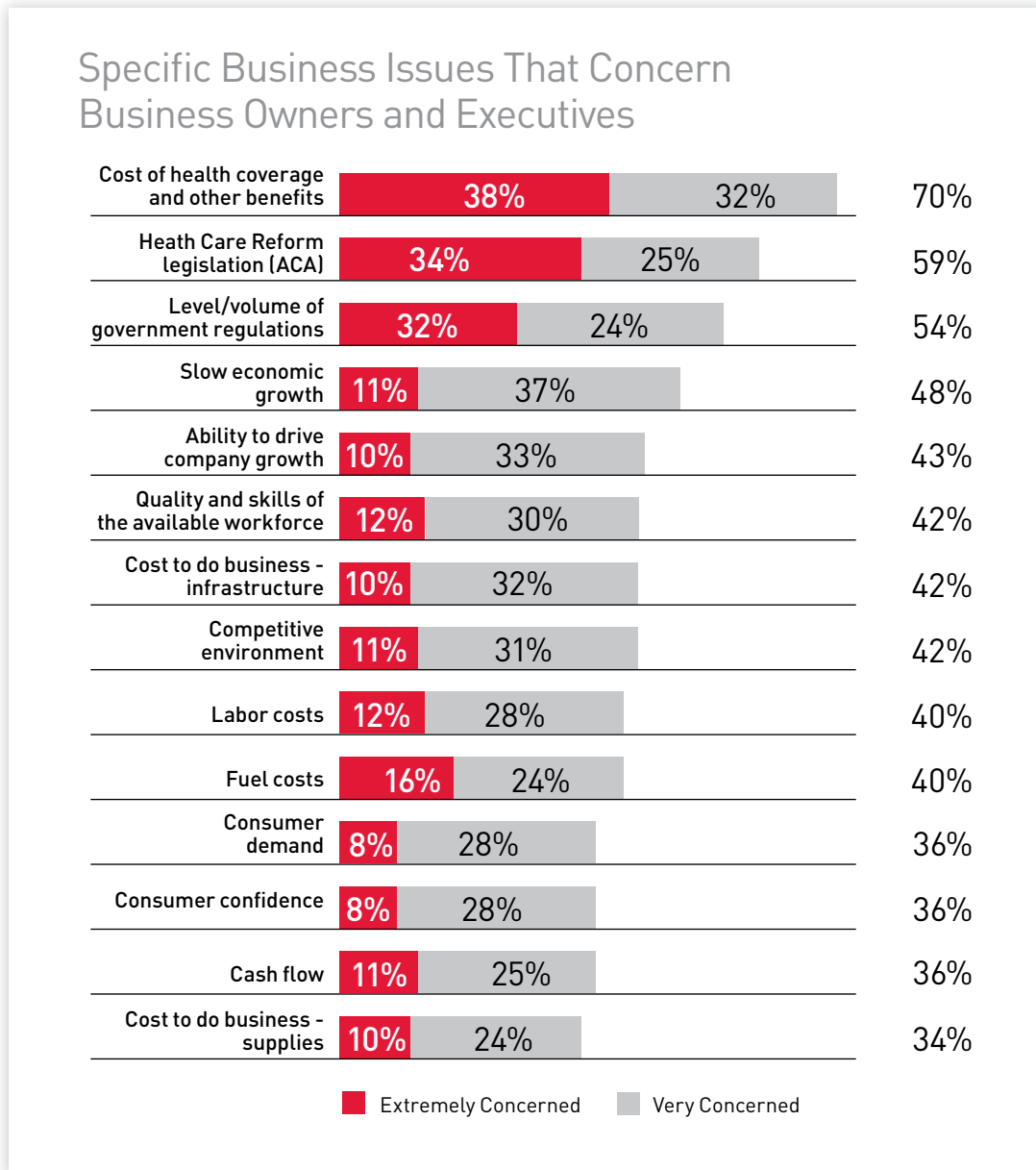
“ In Bank of America Merrill Lynch’s 2013 CFO Outlook, Chief Financial Officers cite growing healthcare costs as the top concern within their own companies.³ ”

The U.S. Supreme Court’s decision regarding the Affordable Care Act (ACA) has vaulted ACA and related issues to the top of the list of **specific business issues** that concern mid-sized businesses. When asked to **rank** their top three business concerns, the cost of health coverage and benefits topped the list. Following a close second, was ACA legislation – a significant increase over 2012 (prior to the Supreme Court decision), and the largest increase of any ranked concern in the 2013 survey. The burdens of employee benefits and government regulations are perennial concerns for business leaders, but they now gain greater specificity and weight in light of the ACA requirements.



³ Bank of America Merrill Lynch, “Top Trends 2013: A review of the major issues that will affect business and shape corporate strategy this year,” February 2013.

These same related issues, again, were the top responses when business leaders were asked to rate their level of concern.



Consistent with 2012 findings, business owners/executives remain concerned with issues that are primarily out of their direct control – healthcare costs, ACA legislation, level/volume of government regulations, and slow economic growth. Complex macroeconomic uncertainties like these are a major contributing factor to the cautious views respondents express specific to the future growth of the overall economy, as well as their own hiring plans.

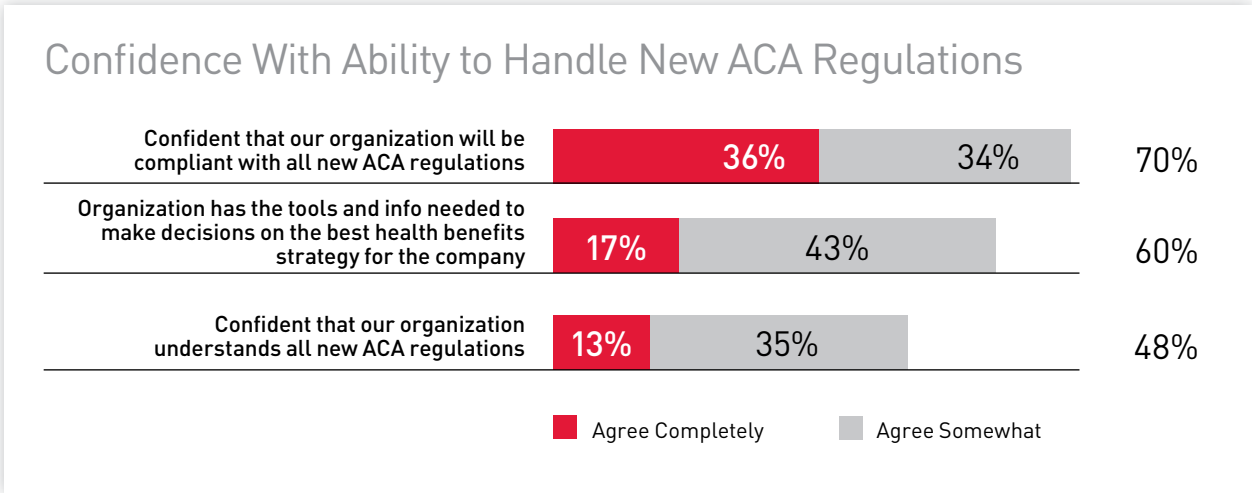
Coping With Healthcare Costs and Complexity

“Mandatory healthcare is the law of the land, yet just exactly what it will demand of businesses, and how it will be enforced, remains unclear.”⁴

Considered together, the high degree of concern about healthcare costs and the reduced plans for hiring in the next 12 months suggest that the Supreme Court’s opinion about the constitutionality of the ACA will dampen the business outlook for midsized businesses, as well as the job outlook for prospective employees.

Indeed, two-thirds of midsized business owners and executives said that the cost of providing employer-sponsored medical health insurance to employees is a barrier to achieving company business goals. Only one in 10 respondents felt that it is not at all an important barrier.

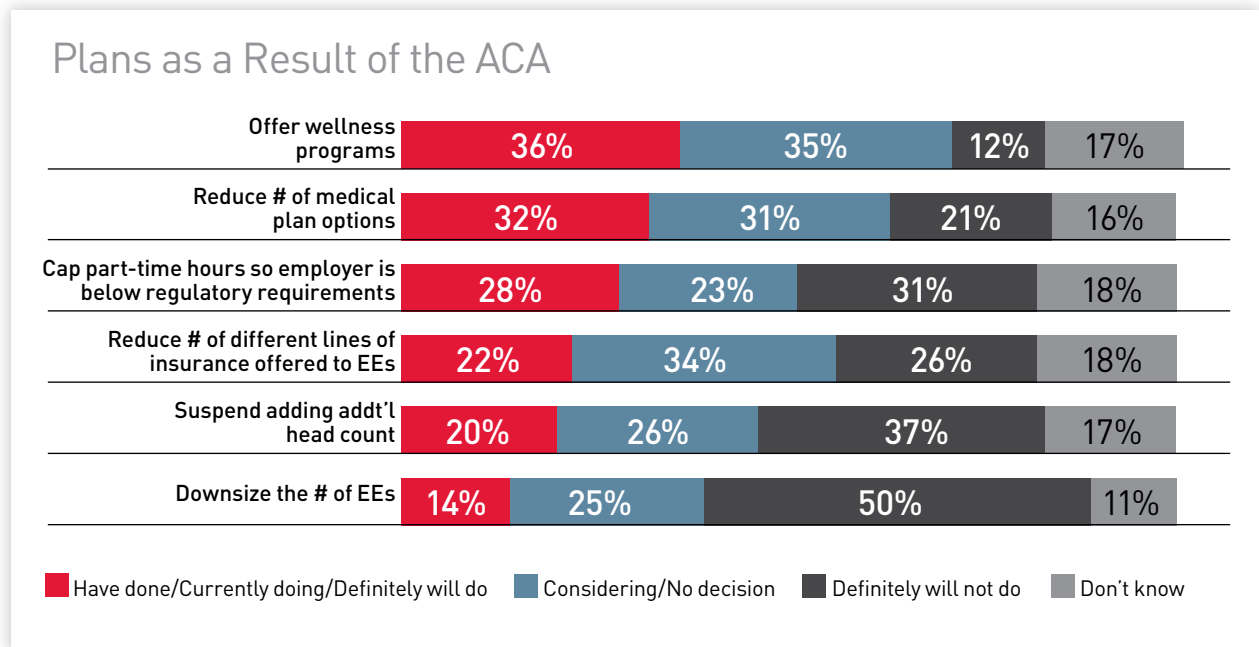
Notwithstanding, less than a year after the Supreme Court’s ruling upholding the constitutionality of the ACA, in the 2013 survey, most midsized business leaders expressed confidence that their companies can fulfill their ACA requirements. The majority are confident that their organizations will be compliant with all new ACA regulations and that their firms have the tools and information needed to make decisions on the best health benefits strategy for the company. However, less than half of respondents expressed confidence that their firm actually **understands** all of the new ACA regulations.



⁴ Bank of America Merrill Lynch, “Top Trends 2013: A review of the major issues that will affect business and shape corporate strategy this year,” February 2013.

The declining levels of confidence – as the questions move from the abstract intention to conform to ACA regulations through the tools and understanding that will enable actual compliance – could express the executives’ faith that their HR staff will “sort out the details.” That faith may be misplaced, however. A separate survey of HR/Benefits decision makers in June 2013 found that only 32% of those respondents were “extremely” or “very confident” in their firm’s understanding of pending healthcare responsibilities.⁵ In addition, over one-quarter of those executives surveyed indicated that their domestic HR/Benefits department is understaffed – an increase from 21% in 2012. (Only 5% of the 2013 respondents felt that HR/Benefits were overstaffed.) Shortages of HR professionals and expertise will complicate efforts to comply with cumbersome and, in some cases, still-developing ACA requirements.

Asked about specific plans in light of the ACA, over one-third of mid-sized business leaders said their firms will offer, or already are offering, wellness programs. A similar number are reducing medical plan options, while more than one-quarter envision restricting the hours of part-time employees to ensure the organization remains below the levels required for providing coverage. Fully half of the respondents said that they “definitely will not” reduce the number of employees in response to the ACA, but one in five said they have or will suspend additional hiring, while another quarter are considering hiring freezes.



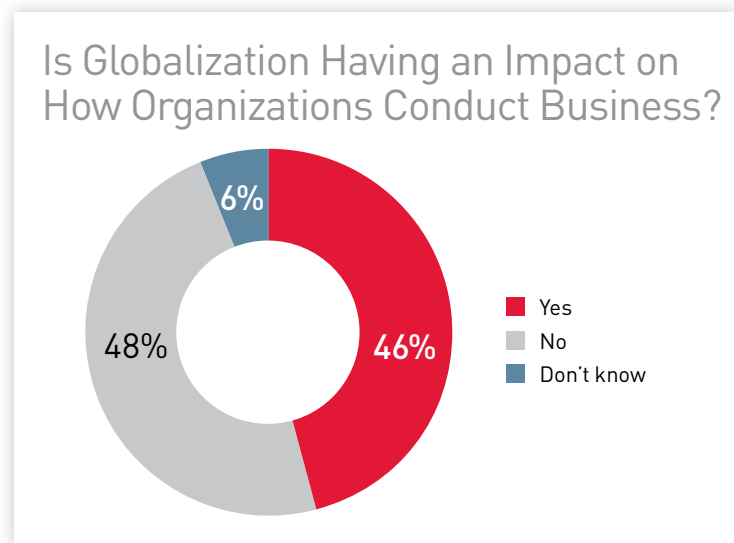
The lack of specificity in these plans – as well as the fact that one-third to one-half of the surveyed business leaders are either still considering or don’t know how their firm will act on each option – illustrates that their response to the ACA’s requirements is still very much in the formative stages.

⁵ Employee Benefits Study, ADP Research Institute, June 2013.

The Impact of Globalization

Thinking globally is becoming an imperative for U.S.-based mid-sized businesses. The Internet makes every public communication accessible worldwide. Consumer demand compels companies to engage emerging markets in such countries as China, India, and South America. And translation technologies, such as Google Translate, allow visitors to convert the language of any website into the language of their choice and interact with companies that have no organized multilingual Web initiatives.

While only a small percentage of mid-sized companies in this survey have offices outside of the United States, nearly half of all survey respondents indicated that globalization impacts their day-to-day operations. And, mid-sized businesses are beginning to play a larger role in the global economy. A recent study indicated that about 26 percent of U.S.-based multinational companies have U.S. parent companies that are classified by the U.S. government as small or medium-sized businesses because they employ fewer than 500 people.⁶



When asked to describe how globalization affects their business activities, respondents expressed issues ranging from the cost of labor to social media distribution to the need for global partnership strategies.

“Asia has put pressure on U.S. workers to get paid less or produce more.”

“We see new non-domestic competitors and less expensive offshore outsourcing.”

“Customers from all countries have access to our social media site 24/7, which requires delicate responses.”

“Lower barriers for global communication have increased [the number of] potential competitors.”

“Companies are combining resources, which makes it harder for individual firms to compete.”

“We need to take into account stakeholders in various countries, market to consumers worldwide, and partner with organizations worldwide.”

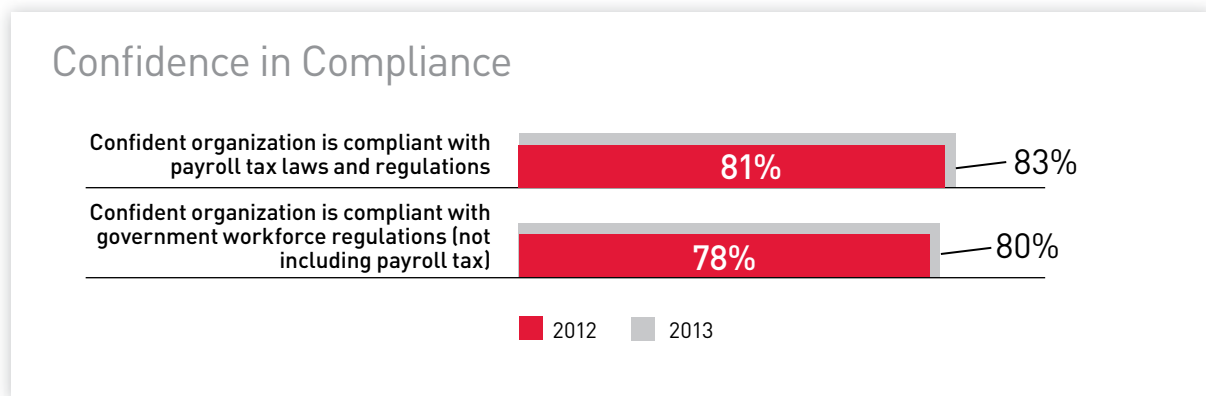
⁶ American Companies and Global Supply Networks Driving U.S. Economic Growth and Jobs by Connecting with the World, Matthew J. Slaughter, January 2013.

Misconceptions About Compliance

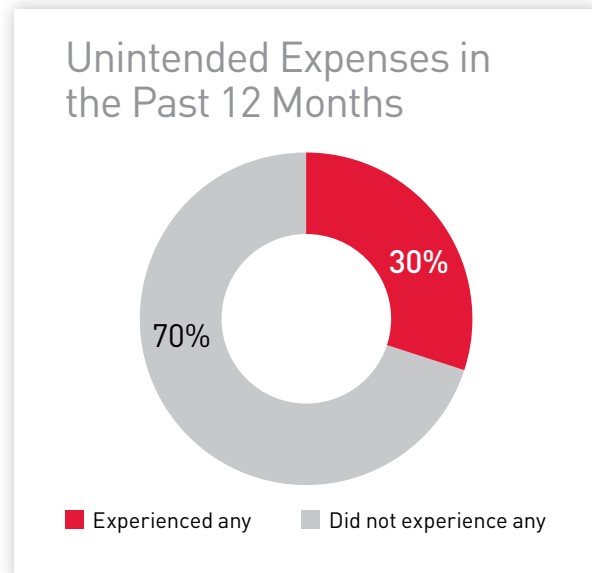
“ Midsized firms tend to bear the heaviest burden of new regulations, since smaller firms are often given some exemptions initially, whereas bigger firms have legions of lawyers to cope with the additional rules.”

While midsized business owners and executives remain highly confident in their firms' ability to comply with laws and regulations, there appears to be a continued misalignment between perception and experiences.

When asked to indicate their level of agreement with a series of statements, the vast majority expressed confidence in their organization's compliance with payroll tax laws and other government regulations.

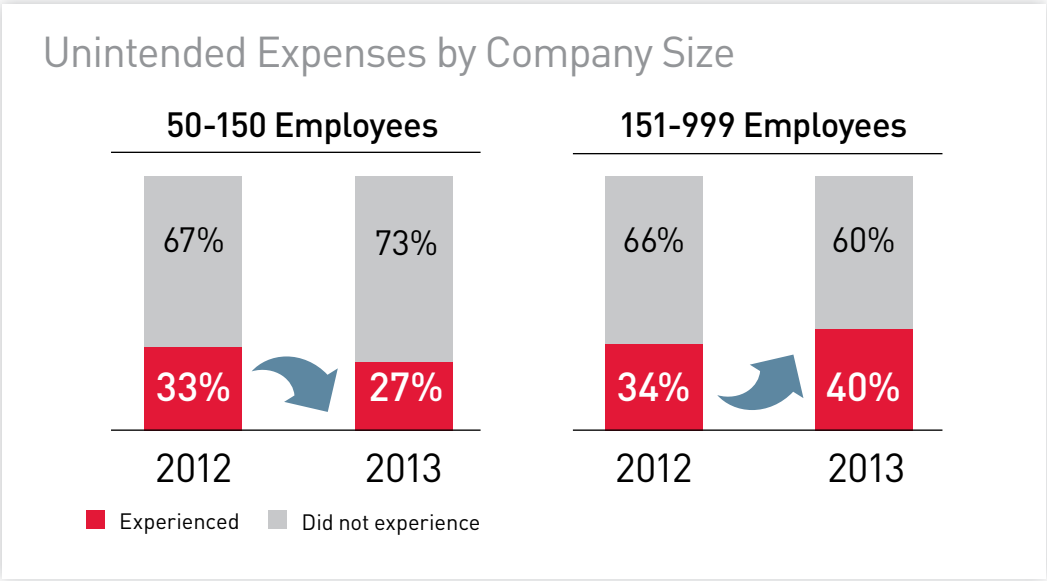


However, for many, their confidence about compliance is not reflected in actual experience. Almost one-third of all respondents reported unintended expenses – such as fines, penalties or lawsuits – as a result of noncompliance with governmental regulations (federal, state, or local) in the past 12 months. Of those that were fined or penalized, midsized firms reported an average of six fines or penalties per year. Organizations processing payroll in-house received almost twice as many fines or penalties as those that outsource payroll processing.



7 The Economist, "The Mighty Middle," October 20, 2012.

While the incidence of such expenses fell for smaller midsized companies compared to 2012, the occurrence among larger firms increased significantly.



The level/volume of government regulations remains a top-three concern of midsized business owners and executives. As such, they need to remain alert in the area of compliance, especially as laws and regulations continue to evolve and multiply.

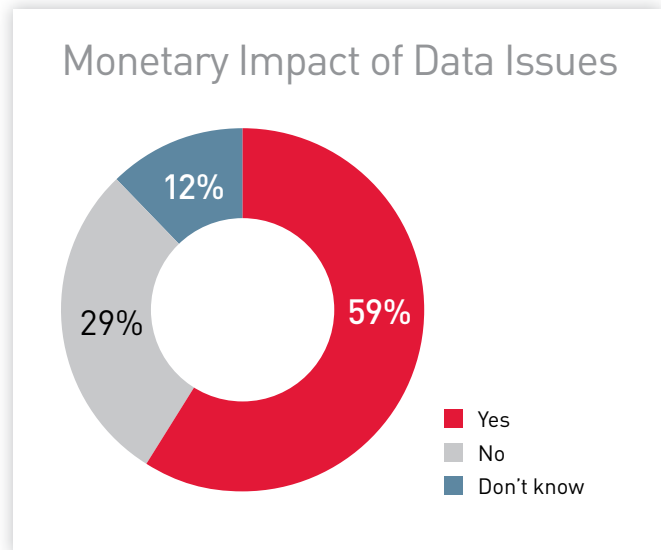
Taking Risks With Records

Despite the ongoing “digitalization” of the workplace and the looming specter of increasingly complex healthcare and other HR regulations, the majority of mid-sized businesses surveyed still rely to some extent on paper files and desktop records systems, such as spreadsheets.

Nearly three out of five firms stated that they keep paper files of employee data that cannot be stored in the company’s payroll or HR system, while almost one-third use Microsoft Excel. Predictably, smaller firms are more likely than larger firms to rely on paper-based storage.

As demonstrated in the aftermath of Hurricane Sandy in 2012, paper and other nonredundant data storage systems are highly susceptible to natural disasters or other major business interruptions, either because they may be destroyed or damaged outright, or because the office or storage facility becomes inaccessible. Twenty percent of mid-sized business owners and executives said their company had been impacted by some kind of disaster (hurricane, fire, blackout, etc.) in the past two years.

In addition to the recovery and backup benefits of distributed data storage, integrated electronic systems for employee records typically offer greater accuracy and security than paper records. Nearly three in five mid-sized businesses reported monetary impacts from inaccurate data, including payments for unearned time off and unnecessary payments to terminated employees, as a result of using systems that were not integrated. Moreover, issues related to workers’ compensation, payroll taxes, and 401(k) plan management are three of the leading sources of unintended fines and penalties, especially for larger mid-sized firms.



Given the growing complexity, increased government scrutiny, and financial impacts, this is one area where mid-sized business leaders may want to exercise more vigilance. Interestingly, more than half of survey respondents expressed some level of interest in an integrated digital storage solution to organize and integrate their paper files with their automated Payroll or HR Management solution.

In Conclusion

As the economy slowly improves, mid-sized business owners and executives face a brewing “perfect storm” in the form of complex new healthcare regulations and requirements, stiff competition for top talent, and rising expectations from a workforce that increasingly expects HR and other work-related information to be shared conveniently and accessed remotely. Together, these constitute the overriding challenge of Human Capital Management (HCM) in the years ahead.

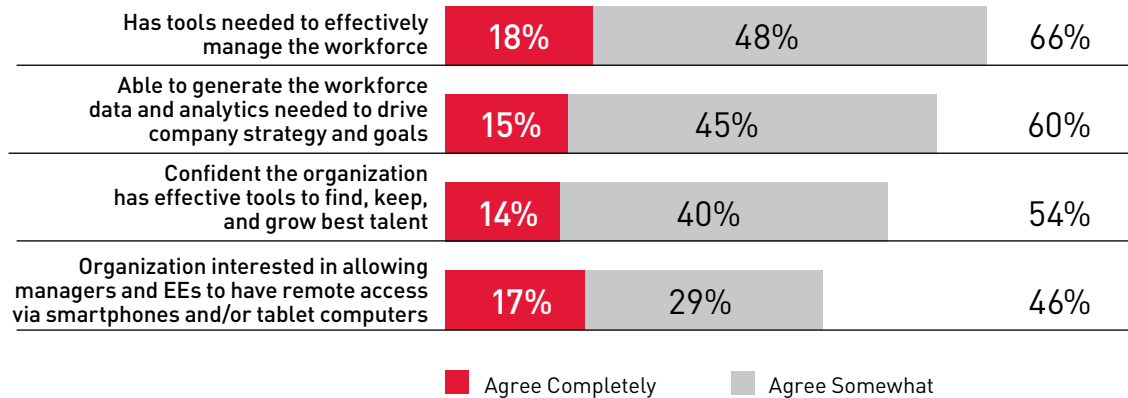
“ In a knowledge-based economy, skilled talent may be what most differentiates great companies from the rest of the pack. Skilled talent can help drive innovation and customer value, creates growth opportunities, and mitigates a growing river of risk. Organizations that do an extraordinary job managing their talent agendas have an opportunity to set themselves apart – in both the talent arena and in the broader marketplace.⁸ ”

The ACA and related governmental regulations potentially pose significant business and financial risks, including compliance issues and penalties resulting from noncompliance. However, ACA is really new clothing on a very old challenge for mid-sized businesses: How to help control the employer’s cost for healthcare benefits while still providing attractive benefits packages for employees. Shaping an ACA response that can satisfy both of these competing demands will help determine a business’s ability to cost effectively attract and retain talent.

Respondents to this year’s survey expressed a fair degree of confidence about many HCM issues. But, the results may be deceiving because about one in five respondents or fewer express “complete agreement” on HCM issues.

Barely half of all respondents express confidence that their organization has the tools to effectively find, keep, and grow the best talent. Moreover, 46% have some interest in allowing remote access to HR data via handheld devices – with larger companies predictably more interested in this prospect than smaller companies. Such policies are responsive to the expectations of a workforce that is increasingly comfortable with both remote work and “always-on” connectivity – and can save costs by diverting calls from HR staff.

Degree of Confidence With HCM Issues



Midsized businesses must constantly review HCM policies and practices in order to help ensure that they do not fall behind in the battle for top talent.

Looking Ahead

Even in the face of adverse conditions, the most ardent competitors find a way to succeed. Midsized businesses that thrive on transforming challenges into opportunities are not waiting on the sidelines for the slow economic recovery to get up to speed. They are in the game now, making major decisions, expanding their customer base, increasing market share and, when necessary, adding to head count to support growth.

These employers are choosing to act, despite facing the “perfect storm” of unprecedented and complex healthcare regulations, increased competitive pressures of globalization, and stiff competition for the best talent. To some degree, each of these strategic challenges involves two universal touch points:

1. the need to address compliance-driven noncore business requirements, and
2. the management of human capital

Many midsized employers – particularly those that are laser-focused on core goals and objectives – are increasingly opting to administer their noncore necessities by outsourcing such tasks to a partner with proven, employment-related compliance and HCM expertise.

Research Methodology

The ADP Research Institute conducted the ADP Business Owner Study in May 2013 among 1012 business owners, C-suite executives, and senior-level executives in U.S. mid-sized organizations.

The study universe included representative samples of all categories of U.S. enterprises with 50-999 employees, except state/federal government and public education.

A statistically projectable sample of 1012 respondents in mid-sized businesses was interviewed, split between two size groups: enterprises with 50-150 and 151-999 total U.S. employees. The resulting data achieved statistical reliability at the 95% confidence level both overall and in each of the size groups.

Respondents had to be business owners [Partner, Principal, Owner], C-suite executives [President, CEO, CFO, COO] or senior level executives [Executive VP, Senior VP, VP, Assistant VP; Controller/Assistant Controller; General Manager; Director/Senior Director/Department Head].

About ADP

With more than \$11 billion in revenues and more than 60 years of experience, ADP® (NASDAQ: ADP) serves approximately 620,000 clients in more than 125 countries. As one of the world's largest providers of business outsourcing and human capital management solutions, ADP offers a wide range of human resource, payroll, talent management, tax and benefits administration solutions from a single source, and helps clients comply with regulatory and legislative changes, such as the Affordable Care Act (ACA). ADP's easy-to-use solutions for employers provide superior value to companies of all types and sizes. ADP is also a leading provider of integrated computing solutions to auto, truck, motorcycle, marine, recreational vehicle, and heavy equipment dealers throughout the world. For more information about ADP or to contact a local ADP sales office, reach us at **1.800.225.5237** or visit the company's website at **www.adp.com**.

About the ADP Research Institute

The ADP Research Institute provides insights to leaders in both the private and public sectors regarding issues in human capital management, employment trends, and workforce strategy.

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