PRESSURE BIOSCIENCES INC
Form 10-Q
August 15, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

[X] Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended June 30, 2016

or

[ ] Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from _____________ to _____________

Commission File Number 000-21615

PRESSURE BIOSCIENCES, INC.

(Exact name of registrant as specified in its charter)

Massachusetts	**04-2652826**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
14 Norfolk Avenue South Easton, Massachusetts	**02375**
(Address of principal executive offices)	(Zip Code)

(508) 230-1828

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

[X] Yes [ ] No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

[X] Yes [ ] No

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

Large accelerated filer [ ]	Accelerated filer [ ]
Non-accelerated filer [ ]	Smaller reporting company [X]

Indicate by check mark whether the registrant is a shell company (as defined in Exchange Act Rule 12b-2 of the Exchange Act.

[ ] Yes [X] No

The number of shares outstanding of the Issuer’s common stock as of August 12, 2016 was 29,031,845.

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

PRESSURE BIOSCIENCES, INC. AND SUBSIDIARY

CONDENSED CONSOLIDATED BALANCE SHEETS

(UNAUDITED)

	June 30, 2016	December 31, 2015
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$71,632	$116,783
Accounts receivable	511,108	113,256
Inventories, net of $50,000 reserve at June 30, 2016 and December 31, 2015	1,002,382	1,038,371
Prepaid income taxes	7,381	7,381
Prepaid expenses and other current assets	144,960	213,926
Total current assets	1,737,463	1,489,717
Investment in available-for-sale equity securities	81,783	294,522
Property and equipment, net	8,069	20,149
TOTAL ASSETS	$1,827,315	$1,804,388
LIABILITIES AND STOCKHOLDERS' DEFICIT		
CURRENT LIABILITIES		
Accounts payable	$889,863	$941,389
Accrued employee compensation	196,780	176,009
Accrued professional fees and other	638,920	821,088
Deferred revenue	307,244	140,878
Convertible debt, net of unamortized debt discounts of $29,373 at June 30, 2016 and $0 at December 31, 2015	192,627	100,000
Other debt, net of unamortized discounts of $15,084 and $3,041, respectively	454,369	151,628
Warrant derivative liability	4,552,995	3,295,976
Conversion option derivative liability	5,023,449	3,940,791
Total current liabilities	12,256,247	9,567,759
LONG TERM LIABILITIES		
Related party convertible debt, net of unamortized debt discounts of $233,261 and $0, respectively	57,743	-
Convertible debt, net of unamortized debt discounts of $4,760,592 and $5,223,658, respectively	1,910,908	177,342
Deferred revenue	36,935	36,935

TOTAL LIABILITIES	14,261,833	9,782,036
COMMITMENTS AND CONTINGENCIES (Note 5)		
STOCKHOLDERS' DEFICIT		
Series D Convertible Preferred Stock, $.01 par value; 850 shares authorized; 300 shares issued and outstanding on June 30, 2016 and December 31, 2015, respectively (Liquidation value of $300,000)	3	3
Series G Convertible Preferred Stock, $.01 par value; 240,000 shares authorized; 86,570 shares issued and outstanding on June 30, 2016 and December 31, 2015, respectively	866	866
Series H Convertible Preferred Stock, $.01 par value; 10,000 shares authorized; 10,000 shares issued and outstanding on June 30, 2016 and December 31, 2015, respectively	100	100
Series H2 Convertible Preferred Stock, $.01 par value; 21 shares authorized; 21 shares issued and outstanding on June 30, 2016 and December 31, 2015, respectively	-	-
Series J Convertible Preferred Stock, $.01 par value; 6,250 shares authorized; 3,546 shares issued and outstanding on June 30, 2016 and December 31, 2015, respectively	36	36
Series K Convertible Preferred Stock, $.01 par value; 15,000 shares authorized; 6,816 and 11,416 shares issued and outstanding on June 30, 2016 and December 31, 2015, respectively	68	114
Common stock, $.01 par value; 100,000,000 shares authorized; 29,031,845 and 23,004,898 shares issued and outstanding on June 30, 2016 and December 31, 2015, respectively	290,319	230,050
Warrants to acquire common stock	5,445,336	5,416,681
Additional paid-in capital	26,692,285	26,036,733
Accumulated other comprehensive income	(317,764)	(105,025)
Accumulated deficit	(44,545,767)	(39,557,206)
Total stockholders' deficit	(12,434,518)	(7,977,648)
TOTAL LIABILITIES AND STOCKHOLDERS' DEFICIT	$1,827,315	$1,804,388

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements

PRESSURE BIOSCIENCES, INC. AND SUBSIDIARY

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(UNAUDITED)

	For the Three Months Ended		For the Six Months Ended	
	June 30,		June 30,	
	2016	2015	2016	**2015**
Revenue:				
Products, services, other	$474,187	$333,575	$928,538	$692,939
Grant revenue	36,776	79,529	92,904	160,299
Total revenue	510,963	413,104	1,021,442	853,238
Costs and expenses:				
Cost of products and services	243,105	175,193	464,804	365,976
Research and development	321,428	291,402	656,698	523,325
Selling and marketing	193,885	200,178	385,121	366,401
General and administrative	813,242	810,220	1,621,460	1,536,244
Total operating costs and expenses	1,571,660	1,476,993	3,128,083	2,791,946
Operating loss	(1,060,697)	(1,063,889)	(2,106,641)	(1,938,708)
Other (expense) income:				
Interest expense, net	(1,010,236)	(640,691)	(1,845,380)	(1,246,276)
Other expense	-	(168,111)	(912)	(513,352)
Gain on extinguishment of embedded derivative liabilities	-	186,609	-	848,073
Change in fair value of derivative liabilities	3,032,762	299,841	(1,035,628)	78,031
Total other (expense) income	2,022,526	(322,352)	(2,881,920)	(833,524)
Net income (loss)	961,829	(1,386,241)	(4,988,561)	(2,772,232)
Accrued dividends on convertible preferred stock	-	(6,811)	-	(23,479)
Net income (loss) applicable to common shareholders	$961,829	(1,393,052)	$(4,988,561)	$(2,795,711)
Net income (loss) per share attributable to common stockholders - basic	$0.04	$(0.07)	$(0.20)	$(0.14)
Net income (loss) per share attributable to common stockholders - diluted	$(0.00)	$(0.07)	$(0.20)	$(0.14)
Weighted average common stock shares outstanding used in the basic net income (loss)per share calculation	25,953,828	19,682,632	24,481,039	19,247,895
Weighted average common stock shares outstanding used in the diluted net income (loss) per share calculation	70,762,909	19,682,632	24,481,039	19,247,895

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements

PRESSURE BIOSCIENCES, INC. AND SUBSIDIARY

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(UNAUDITED)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2016	2015	2016	2015
Comprehensive Income (Loss)				
Net income (loss)	$961,829	$(1,386,241)	$(4,988,561)	$(2,772,232)
Other comprehensive loss				
Unrealized loss on marketable securities	(73,041)	-	(212,739)	-
Comprehensive income (loss)	$888,788	$(1,386,241)	$(5,201,300)	$(2,772,232)

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements

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PRESSURE BIOSCIENCES, INC. AND SUBSIDIARY

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

	For the Six Months Ended June 30,	
	2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$(4,988,561)	$(2,772,232)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	12,325	12,187
Accretion of interest and amortization of debt discount	1,831,289	1,047,864
Gain on settlement of debt	(5,044)	-
Stock-based compensation expense	192,311	110,506
Amortization of third party fees paid in common stock and warrants	312,200	167,936
Gain on extinguishment of embedded derivative liabilities	-	(848,073)
Change in fair value of derivative liabilities	1,035,628	(398,411)
Changes in operating assets and liabilities:		
Accounts receivable	(397,852)	(77,936)
Inventories	35,989	66,661
Prepaid expenses and other assets	68,966	16,723
Accounts payable	(51,526)	(56,302)
Accrued employee compensation	20,771	(4,078)
Deferred revenue and other accrued expenses	65,448	87,548
Net cash used in operating activities	(1,868,056)	(1,850,785)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property plant and equipment	(245)	(6,662)
Net cash used in investing activities	(245)	(6,662)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net proceeds from related party convertible debt	96,667	6,300
Payments on related party debt	-	(12,300)
Net proceeds from convertible debt	1,417,382	1,609,437
Payments on convertible debt	-	(667,450)
Net proceeds from non-convertible debt	623,311	992,128
Payments on non-convertible debt	(314,210)	(333,641)
Payment of prepayment penalty	-	(172,800)
Net cash provided by financing activities	1,823,150	1,421,674
NET DECREASE IN CASH	(45,151)	(435,773)
CASH AT BEGINNING OF YEAR	116,783	473,948
CASH AT END OF PERIOD	$71,632	$38,175

SUPPLEMENTAL INFORMATION		
Interest paid in cash	$1,154	$203,311
Income taxes paid in cash	-	-
NON CASH TRANSACTIONS:		
Convertible debt exchanged for common stock	117,837	248,000
Cashless exercise of warrants	11,100	-
Discount due to beneficial conversion feature	7,962	-
Discount due to warrants issued with debt	39,755	-
Common stock issued with debt	10,952	-
Extension fees added to principal	-	54,000
Conversion of preferred stock into common stock	63,459	-
Accrued dividends on preferred stock	-	23,479
Unrealized loss from available-for-sale equity securities	212,739	-
Debt discount from derivative liability	1,304,049	1,555,739
Prepayment penalty and accrued interest enrolled into debt principal	-	48,950

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements

PRESSURE BIOSCIENCES, INC. AND SUBSIDIARY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2016

(UNAUDITED)

1) Business Overview, Liquidity and Management Plans

Pressure BioSciences, Inc. ("we", "our", "the Company") is focused on solving the challenging problems inherent in biological sample preparation, a crucial laboratory step performed by scientists worldwide working in biological life sciences research. Sample preparation is a term that refers to a wide range of activities that precede most forms of scientific analysis. Sample preparation is often complex, time-consuming and, in our belief, one of the most error-prone steps of scientific research. It is a widely-used laboratory undertaking – the requirements of which drive what we believe is a large and growing worldwide market. We have developed and patented a novel, enabling technology platform that can control the sample preparation process. It is based on harnessing the unique properties of high hydrostatic pressure. This process, called pressure cycling technology, or PCT, uses alternating cycles of hydrostatic pressure between ambient and ultra-high levels i.e., 35,000 pounds per square inch ("*psi*") or greater to safely, conveniently and reproducibly control the actions of molecules in biological samples, such as cells and tissues from human, animal, plant and microbial sources.

Our pressure cycling technology uses internally developed instrumentation that is capable of cycling pressure between ambient and ultra-high levels at controlled temperatures and specific time intervals, to rapidly and repeatedly control the interactions of bio-molecules, such as deoxyribonucleic acid ("*DNA*"), ribonucleic acid ("*RNA*"), proteins, lipids and small molecules. Our laboratory instrument, the Barocycler®, and our internally developed consumables product line, which include our Pressure Used to Lyse Samples for Extraction ("*PULSE*") tubes, and other processing tubes, and application specific kits such as consumable products and reagents, together make up our PCT Sample Preparation System ("*PCT SPS*").

In 2015, together with an investment bank, we formed a subsidiary called Pressure BioSciences Europe ("PBI Europe") in Poland. We have 49% ownership interest with the investment bank retaining 51%. As of now, PBI Europe does not have any operating activities but is expected to commence operations in 2016. Therefore, we don't have control of the subsidiary and did not consolidate in our financial statements.

2) Going Concern

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern, which contemplates the realization of assets and the liquidation of liabilities in the normal course of business. However, we have experienced negative cash flows from operations with respect to our pressure cycling technology business since our inception. As of June 30, 2016, we do not have adequate working capital resources to satisfy our current liabilities and as a result, there is substantial doubt regarding our ability to continue as a going concern. We have been successful in raising cash through debt and equity offerings in the past and as described in Note 6, we completed an over-subscribed $5.0 million debt financing on March 31, 2016 with a total amount raised of $6.3 million. We have financing efforts in place to continue to raise cash through debt and equity offerings.

Management has developed a plan to continue operations. This plan includes obtaining equity or debt financing. During the six months ended June 30, 2016 we received $2,137,360 net proceeds, in additional convertible and non-convertible debt. Although we have successfully completed financings and reduced expenses in the past, we cannot assure you that our plans to address these matters in the future will be successful.

We need substantial additional capital to fund normal operations in future periods. In the event that we are unable to obtain financing on acceptable terms, or at all, we will likely be required to cease our operations, pursue a plan to sell our operating assets, or otherwise modify our business strategy, which could materially harm our future business prospects. These financial statements do not include any adjustments that might result from this uncertainty.

3) **Interim Financial Reporting**

The accompanying unaudited condensed consolidated balance sheet as of December 31, 2015, which was derived from audited financial statements, and the unaudited interim condensed consolidated financial statements of Pressure BioSciences, Inc. have been prepared in accordance with accounting principles generally accepted in the United States of America ("generally accepted accounting principles" or "GAAP") for interim financial information. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all material adjustments (consisting of only normal recurring adjustments) considered necessary for a fair presentation have been included. Operating results for the three months and six months ended June 30, 2016 are not necessarily indicative of the results that may be expected for the year ending December 31, 2016. For further information, refer to the audited consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K (the "Form 10-K") for the fiscal year ended December 31, 2015 as filed with the Securities and Exchange Commission on April 5, 2016.

4) **Summary of Significant Accounting Policies**

Principles of Consolidation

The condensed consolidated financial statements include the accounts of Pressure BioSciences, Inc., and its wholly-owned subsidiary PBI BioSeq, Inc. All intercompany accounts and transactions have been eliminated in consolidation.

Use of Estimates

To prepare our condensed consolidated financial statements in conformity with accounting principles generally accepted in the United States of America, we are required to make significant estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. In addition, significant estimates were made in projecting future cash flows to quantify deferred tax assets, the costs associated with fulfilling our warranty obligations for the instruments that we sell, and the estimates employed in our calculation of fair value of stock options awarded and warrant derivative liability. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results could differ from the estimates and assumptions used.

Concentrations

Credit Risk

Our financial instruments that potentially subject us to concentrations of credit risk consist primarily of cash, cash equivalents, and trade receivables. We have cash investment policies which, among other things, limit investments to investment-grade securities. We perform ongoing credit evaluations of our customers, and the risk with respect to trade receivables is further mitigated by the fact that many of our customers are government institutions, large pharmaceutical and biotechnology companies, and academic laboratories.

The following table illustrates the level of concentration as a percentage of total revenues during the three months and six months ended June 30, 2016 and 2015.

	For the Three Months Ended June 30,	
	2016	2015
Top Five Customers	68%	65 %
Federal Agencies	8 %	27 %

	For the Six Months Ended June 30,	
	2016	2015
Top Five Customers	40%	49 %
Federal Agencies	10%	22 %

The following table illustrates the level of concentration as a percentage of net accounts receivable balance as of June 30, 2016 and December 31, 2015:

	June 30, 2016	December, 31, 2015
Top Five Customers	73 %	93 %
Federal Agencies	0 %	1 %

Product Supply

BIT Group, Inc. of California has been our sole contract manufacturer for our PCT NEP3229 and NEP2320 instrumentation. However, the Company has reached agreement for a Massachusetts-based contract manufacturer to assemble its future instrumentation builds starting with the new NEP2320 Extreme Barocycler instrument, effective in May 2016.

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Investment in Available-For-Sale Equity Securities

As of June 30, 2016, we held 601,500 shares of common stock of Everest Investments Holdings S.A. ("Everest"), a Polish publicly traded company listed on the Warsaw Stock Exchange. We account for this investment in accordance with ASC 320 *"Investments — Debt and Equity Securities"* as securities available for sale. On June 30, 2016, our consolidated balance sheet reflected the fair value of our investment in Everest to be $81,783, based on the closing price of Everest shares of $0.14 per share on that day. The carrying value of our investment in Everest common stock held will change from period to period based on the closing price of the common stock of Everest as of the balance sheet date. This change in market value will be recorded by us on a quarterly basis as an unrealized gain or loss in Comprehensive Income or Loss.

Inventories

Inventories are valued at the lower of cost (average cost) or market (sales price). The cost of Barocyclers consists of the cost charged by the contract manufacturer. The cost of manufactured goods includes material, freight-in, direct labor, and applicable overhead. The composition of inventory is as follows:

	June 30, 2016	December 31, 2015
Raw materials	$407,949	$310,367
Finished goods	644,433	778,004
Inventory Reserve	(50,000)	(50,000)
Total	$1,002,382	$1,038,371

Debt Issuance Costs

In April 2015, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2015-03, "Simplifying the Presentation of Debt Issuance Costs" ("ASU 2015-03"). ASU 2015-03 requires that debt issuance costs be presented as a direct deduction from the carrying amount of the related debt liability, consistent with the presentation of debt discounts. Prior to the issuance of ASU 2015-03, debt issuance costs were required to be presented as deferred charge assets, separate from the related debt liability. ASU 2015-03 does not change the recognition and measurement requirements for debt issuance costs. The Company early-adopted ASU 2015-03 as of the end of its Fiscal 2015, and applied its provisions retrospectively.

Computation of Loss per Share

Basic loss per share is computed by dividing loss available to common shareholders by the weighted average number of common shares outstanding. Diluted loss per share is computed by dividing loss available to common shareholders by the weighted average number of common shares outstanding plus additional common shares that would have been outstanding if dilutive potential common shares had been issued. For purposes of this calculation, convertible preferred stock, common stock dividends, and warrants and options to acquire common stock, are all considered common stock equivalents in periods in which they have a dilutive effect and are excluded from this calculation in periods in which these are anti-dilutive to our net loss.

The following table illustrates our computation of loss per share for the three months and six months ended June 30, 2016 and 2015:

	For the Three Months Ended		For the Six Months Ended	
	June 30,		June 30,	
	2016	2015	2016	2015
Numerator:				
Net loss	$961,829	$(1,386,241)	$(4,988,561)	$(2,772,232)
Accretion of interest and amortization of debt discount	991,286	-	-	-
Change in fair value of derivative liabilities	(2,016,593)	-	-	-
Preferred dividends accrued	-	(6,811)	-	(23,479)
Net loss applicable to common shareholders	$(763,478)	$(1,393,052)	$(4,988,561)	$(2,795,711)
Denominator for basic and diluted loss per share:				
Weighted average common stock shares outstanding	25,953,828	19,682,632	24,481,039	19,247,895
Net effect of dilutive common stock equivalents	44,808,781	-	-	-
Weighted average shares outstanding - diluted	70,762,609	19,682,632	24,481,039	19,247,895
Income (loss) per common share - basic	$0.04	$(0.07)	$(0.20)	$(0.14)
Income (loss) per common share - diluted	$(0.00)	$(0.07)	$(0.20)	$(0.14)

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The following table presents securities that could potentially dilute basic loss per share in the future. For all periods presented except for the three months ended June 30, 2016, the potentially dilutive securities were not included in the computation of diluted loss per share because these securities would have been anti-dilutive to our net loss. The Series D Convertible Preferred Stock, Series G Convertible Preferred Stock, Series H Convertible Preferred Stock, Series J Convertible Preferred Stock and Series K Convertible Preferred Stock are presented below as if they were converted into common shares according to the conversion terms.

	As of June 30,	
	2016	2015
Stock options	5,385,250	3,251,250
Convertible debt	25,343,864	14,420,144
Common stock warrants	26,403,340	19,182,201
Convertible preferred stock:		
Series D Convertible Preferred Stock	750,000	750,000
Series G Convertible Preferred Stock	865,700	865,700
Series H Convertible Preferred Stock	1,000,000	1,000,000
Series H2 Convertible Preferred Stock	2,100,000	2,100,000
Series J Convertible Preferred Stock	3,546,000	3,546,000
Series K Convertible Preferred Stock	6,816,000	11,416,000
	72,210,153	56,531,295

Accounting for Stock-Based Compensation Expense

We maintain equity compensation plans under which incentive stock options and non-qualified stock options are granted to employees, independent members of our Board of Directors and outside consultants. We recognize stock-based compensation expense over the requisite service period using the Black-Scholes formula to estimate the fair value of the stock options on the date of grant.

Determining Fair Value of Stock Option Grants

Valuation and Amortization Method - The fair value of each option award is estimated on the date of grant using the Black-Scholes pricing model based on certain assumptions. The estimated fair value of employee stock options is amortized to expense using the straight-line method over the vesting period.

Expected Term - The Company uses the simplified calculation of expected life, as the Company does not currently have sufficient historical exercise data on which to base an estimate of expected term. Using this method, the expected term is determined using the average of the vesting period and the contractual life of the stock options granted.

Expected Volatility - Expected volatility is based on the Company’s historical stock volatility data over the expected term of the award.

Risk-Free Interest Rate - The Company bases the risk-free interest rate used in the Black-Scholes valuation method on the implied yield currently available on U.S. Treasury zero-coupon issues with an equivalent remaining term.

Forfeitures - The Company records stock-based compensation expense only for those awards that are expected to vest. The Company estimated a forfeiture rate of 5% for awards granted based on historical experience and future expectations of options vesting. The Company used this historical rate as our assumption in calculating future stock-based compensation expense.

The Company recognized stock-based compensation expense of $90,849 and $55,616 for the three months ended June 30, 2016 and 2015, respectively. The following table summarizes the effect of this stock-based compensation expense within each of the line items of our costs and expenses within our Condensed Consolidated Statements of Operations:

	For the Three Months Ended June 30,	
	2016	2015
Research and development	15,650	11,523
Selling and marketing	9,803	7,099
General and administrative	65,396	36,994
Total stock-based compensation expense	90,849	55,616

The Company recognized stock-based compensation expense of $192,311 and $110,506 for the six months ended June 30, 2016 and 2015, respectively. The following table summarizes the effect of this stock-based compensation expense within each of the line items of our costs and expenses within our Condensed Consolidated Statements of Operations:

	For the Six Months Ended June 30	
	2016	2015
Research and development	36,031	22,865
Selling and marketing	22,493	14,075
General and administrative	133,787	73,566
Total stock-based compensation expense	192,311	110,506

Fair Value of Financial Instruments

Due to their short maturities, the carrying amounts for cash and cash equivalents, accounts receivable, accounts payable, and accrued expenses approximate their fair value. Long-term liabilities are primarily related to convertible debentures and deferred revenue with carrying values that approximate fair value.

Fair Value Measurements

The Company follows the guidance of FASB ASC Topic 820, "*Fair Value Measurements and Disclosures*" ("ASC 820") as it related to all financial assets and financial liabilities that are recognized or disclosed at fair value in the financial statements on a recurring basis.

The Company generally defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (exit price). The Company uses a three-tier fair value hierarchy, which classifies the inputs used in measuring fair values. These tiers include: Level 1, defined as observable inputs such as quoted prices for identical instruments in active markets; Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and Level 3, defined as unobservable inputs in which little or no market data exists, therefore requiring the Company to develop its own assumptions.

Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. The Company has determined that its financial assets are classified within Level 1 and its financial liabilities are currently classified within Level 3 in the fair value hierarchy. The development of the unobservable inputs for Level 3 fair value measurements and fair value calculations are the responsibility of the Company's management.

The following tables set forth the Company's financial assets and liabilities that were accounted for at fair value on a recurring basis as of June 30, 2016:

		Fair value measurements at June 30, 2016 using:		
	June 30, 2016	Quoted prices in active markets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Available-For-Sale Equity Securities	81,783	81,783	0	0
Total Financial Assets	$ 81,783	$ 81,783	$ -	$ 0

	June 30, 2016	Quoted prices in active markets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Series D Preferred Stock Purchase Warrants	$ 167,702	-	-	$ 167,702
Warrants Issued with Convertible Debt	4,385,293	-	-	4,385,293
Conversion Option Derivative Liabilities	5,023,449	-	-	5,023,449
Total Derivatives	$ 9,576,444	$ -	$ -	$ 9,576,444

The following table provides a summary of the changes in fair value, including net transfers in and/or out, of the derivative financial instruments, measured at fair value on a recurring basis using significant unobservable inputs for the six months ended June 30, 2016:

	December 31, 2015	Issuance fair value	Change in fair value	Gain on extinguishment of derivative liabilities	June 30, 2016
Available-For-Sale Equity Securities	$ 294,522		$ (212,739)	$ -	$ 81,783

Total Financial Assets	$ 294,522	$ -	$(212,739)	$ -	$ 81,783

	December 31, 2015	Issuance fair value	Change in fair value	June 30, 2016
Series D Preferred Stock Purchase Warrants	$ 173,526	$-	$(5,824)	$167,702
Convertible Debt Warrants	3,122,450	1,094,432	168,411	4,385,293
Conversion Option Liabilities	3,940,791	1,547,127	(464,469)	5,023,449
Total Derivatives	$ 7,236,767	$2,641,559	$(301,882)	$9,576,444

The amounts above valued at issuance includes $1,337,510 that was charged directly to “change in fair value of derivative liabilities” at issuance.

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The following tables set forth the Company's financial assets and liabilities that were accounted for at fair value on a recurring basis as of December 31, 2015:

		Fair value measurements at December 31, 2015 using:		
	December 31, 2015	Quoted prices in active markets (Level 1)	**Significant other observable inputs (Level 2)**	**Significant unobservable inputs (Level 3)**
Available-For-Sale Equity Securities	294,522	294,522	-	-
Total Financial Assets	$294,522	$294,522	$ -	$ -

	December 31, 2015	Quoted prices in active markets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Series D Preferred Stock Purchase Warrants	$173,526	-	-	$ 173,526
Warrants Issued with Convertible Debt	3,122,450	-	-	3,122,450
Conversion Option Derivative Liabilities	3,940,791	-	-	3,940,791
Total Derivatives	$7,236,767	$ -	$ -	$ 7,236,767

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The assumptions for the binomial pricing model are represented in the table below for the warrants issued in the Series D private placement reflected on a per share common stock equivalent basis.

Assumptions	November 10, 2011	Warrants revalued at December 31, 2015	Warrants revalued at June 30, 2016
Expected life (in months)	60.0	11.0	4.0
Expected volatility	104.5 %	104.9 %	96.2 %
Risk-free interest rate	0.875 %	0.65 %	0.26 %
Exercise price	$ 0.81	$ 0.25	$ 0.25
Fair value per warrant	$ 0.54	$ 0.16	$ 0.16

The assumptions for the binomial pricing model are represented in the table below for the warrants issued with the Convertible Debt throughout the period reflected on a per share common stock equivalent basis.

Assumptions	At Issuance Fair value	Warrants revalued at December 31, 2015	Warrants revalued at June 30, 2016
Expected life (in months)	36.0-60.0	55.0-60.0	48.0-60.0
Expected volatility	114.3 - 138.3 %	136.3-141.6 %	137.9 -142.2 %
Risk-free interest rate	0.86-1.69 %	1.29-1.76 %	1.01-1.21 %
Exercise price	$0.40-0.42	0.40	$0.40
Fair value per warrant	$0.19-$.40	0.30	$0.32-$0.40

The assumptions for the binomial pricing model are represented in the table below for the conversion options reflected on a per share common stock equivalent basis.

Assumptions	At Issuance fair value	Conversion options revalued at December 31, 2015	Conversion options revalued at June 30, 2016
Expected life (in months)	3-24	18-24	6-24
Expected volatility	97.6-153.8 %	112.2-114.7 %	94.8-113.67 %
Risk-free interest rate	0.37-0.99 %	1.06 %	0.36-0.73 %
Exercise price	$0.24-$0.45	$0.28	$0.28-$0.45
Fair value per conversion option	$0.07-$0.30	$0.14-$0.33	$0.08-$0.30

5) Commitments and Contingencies

Operating Leases

Our corporate offices are currently located at 14 Norfolk Avenue, South Easton, Massachusetts 02375. We are currently paying $4,800 per month, on a lease extension, signed on December 29, 2015, that expires December 31, 2016, for our corporate office.

On November 1, 2014 we signed a lease for lab space in Medford, MA. We subsequently expanded our space in Medford. The lease expires December 30, 2017 and requires monthly payments of $5,385 subject to annual cost of living increases.

Rental costs are expensed as incurred. During the six months ended June 30, 2016 and 2015 we incurred $70,567 and $50,406 in rent expense, respectively for the use of our corporate office and research and development facilities.

Government Grants

We have received a $1.05 million NIH SBIR Phase II Grant. Under the grant, the NIH has committed to pay the Company to develop a high-throughput, high pressure-based DNA Shearing System for Next Generation Sequencing and other genomic applications.

6) Convertible Debt and Other Debt

Senior Secured Convertible Debentures and Warrants

We entered into Subscription Agreements (the "Subscription Agreement") with various individuals (each, a "Purchaser") between July 23, 2015 and March 31, 2016, pursuant to which the Company sold Senior Secured Convertible Debentures (the "Debentures") and warrants to purchase shares of common stock equal to 50% of the number of shares issuable pursuant to the subscription amount (the "Warrants") for an aggregate purchase price of $6,329,549 (the "Purchase Price").

The Company issued a principal aggregate amount of $6,962,504 in Debentures which includes a 10% original issue discount on the Purchase Price. The Debenture does not accrue any additional interest during the first year it is outstanding but accrues interest at a rate equal to 10% per annum for the second year it is outstanding. The Debenture has a maturity date of two years from issuance. The Debenture is convertible any time after its issuance date. The Purchaser has the right to convert the Debenture into shares of the Company’s common stock at a fixed conversion price equal to $0.28 per share, subject to applicable adjustments. In the second year that the Debenture is outstanding, any interest accrued shall be payable quarterly in either cash or common stock, at the Company’s discretion.

At any time after the Issuance Date, the Company has the option, subject to certain conditions, to redeem some or all of the then outstanding principal amount of the Debenture for cash in an amount equal to the sum of (i) 120% of the then outstanding principal amount of the Debenture, (ii) accrued but unpaid interest and (iii) any liquidated damages and other amounts due in respect of the Debenture.

The Company issued warrants exercisable into a total of 11,302,766 shares of our common stock. The Warrants issued in this transaction are immediately exercisable at an exercise price of $0.40 per share, subject to applicable adjustments including full ratchet anti-dilution in the event that we issue any securities at a price lower than the exercise price then in effect. The Warrants have an expiration period of five years from the original issue date. The Warrants are subject to adjustment for stock splits, stock dividends or recapitalizations and also include anti-dilution price protection for subsequent equity sales below the exercise price.

Subject to the terms and conditions of the Warrants, at any time commencing six months from the Final Closing, the Company has the right to call the Warrants for cancellation if the volume weighted average price of its Common Stock on the OTC QB Market (or other primary trading market or exchange on which the Common Stock is then traded) equals or exceeds three times the per share exercise price of the Warrants for 15 out of 20 consecutive trading days.

In connection with the Subscription Agreement and Debenture, the Company entered into Security Agreements with the Purchasers whereby the Company agreed to grant to Purchasers an unconditional and continuing, first priority security interest in all of the assets and property of the Company to secure the prompt payment, performance and discharge in full of all of Company’s obligations under the Debentures, Warrants and the other Transaction Documents.

The Company determined that the conversion feature of the Debentures met the definition of a liability in accordance with ASC 815-40 and therefore bifurcated the conversion feature on each debt agreement and accounted for it as a derivative liability. The fair value of the conversion feature was accounted for as a note discount and are amortized to interest expense over the life of the loan. The fair value of the conversion feature was reflected in the conversion option liability line in the condensed consolidated balance sheets.

The proceeds from these convertible debts were allocated between the host debt instrument and the convertible option based on the residual method. The estimated fair value of the convertible option was determined using a binomial formula, resulting in allocations to the convertible option and accounted for as a liability in the Company’s condensed consolidated balance sheet. In accordance with the provisions of ASC 815-40, the gross proceeds are offset by debt discounts, which are amortized to interest expense over the expected life of the debt.

ASC 470-20 states that the proceeds from the issuance of debt with detachable stock warrants should be allocated between the debt and warrants on the basis of their relative fair market values. The debt discount will be amortized to interest expense over the two year term of these loans. We amortized $1,831,289 of the debt discount to interest expense in 2016. The warrants issued in connection with the convertible debentures are classified as warrant derivative liabilities because the warrants are entitled to certain rights in subsequent financings and the warrants contain “down-round protection” and therefore, do not meet the scope exception for treatment as a derivative under ASC 815, Derivatives and Hedging, (“ASC 815”). Since “down-round protection” is not an input into the calculation of the fair value of the warrants, the warrants cannot be considered indexed to the Company's own stock which is a requirement for the scope exception as outlined under ASC 815. The estimated fair value of the warrants was determined using the binomial model, resulting in an allocation of $2,847,624 to the total warrants out of the gross proceeds of $6,329,549. The fair value will be affected by changes in inputs to that model including our stock price, expected stock price volatility, the contractual term, and the risk-free interest rate. We will continue to classify the fair value of the warrants as a liability until the warrants are exercised, expire or are amended in a way that would no longer require these warrants to be classified as a liability, whichever comes first.

Other convertible notes

On May 24 and June 14, 2016, we sold additional convertible notes for $222,000 with warrants to purchase 50,000 shares of common stock at an exercise price of $0.55 per share. The Purchaser has the right to convert the notes into shares of the Company’s common stock at a fixed conversion price equal to $0.45 per share, subject to applicable adjustments. The estimated fair value of the warrants was determined using the binomial model, resulting in an allocation of $12,406 to the total warrants and the recognition of a beneficial conversion feature of $7,962, both of which were recorded as a discount to the note. We issued 30,667 shares in connection with the debt on June 14, 2016 to compensate the lender. We valued the 30,667 shares using the stock prices at the respective dates the note proceeds were received and recorded the relative fair value of the shares amounting to $10,952 as a debt discount to be amortized over the term of the loan. We evaluated these convertible notes and warrants for derivative liability treatment and determined that these instruments do not include certain rights such as price protection like our previous debt financings. Accordingly, we concluded that these financing arrangements did not qualify for derivative accounting treatment.

The specific terms of the convertible debts and outstanding balances as of June 30, 2016 are listed in the table below.

Fixed Rate Convertible Notes

Inception Date	Term	Loan Amount	Outstanding Balance	Original Issue Discount	Interest Rate	Deferred Finance Fees	Discount related to fair value of conversion feature and warrants
July 22, 2015	24 months	$2,180,000	$2,180,000	$218,000 [1]	10 %[2]	$388,532	$2,163,074
September 25, 2015	24 months	1,100,000	1,100,000	110,000 [1]	10 %[2]	185,956	1,022,052
October 2, 2015	24 months	150,000	150,000	15,000 [1]	10 %[2]	26,345	140,832
October 6, 2015	24 months	30,000	30,000	3,000 [1]	10 %[2]	5,168	26,721
October 14, 2015	24 months	50,000	50,000	5,000 [1]	10 %[2]	8,954	49,377
November 2, 2015	24 months	250,000	250,000	25,000 [1]	10 %[2]	43,079	222,723
November 10, 2015	24 months	50,000	50,000	5,000 [1]	10 %[2]	8,790	46,984
November 12, 2015	24 months	215,000	215,000	21,500 [1]	10 %[2]	38,518	212,399
November 20, 2015	24 months	200,000	200,000	20,000 [1]	10 %[2]	37,185	200,000
December 4, 2015	24 months	170,000	170,000	17,000 [1]	10 %[2]	37,352	170,000
December 11, 2015	24 months	360,000	360,000	36,000 [1]	10 %[2]	75,449	360,000
December 18, 2015	24 months	55,000	55,000	5,500 [1]			

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ALLOWANCE FOR DOUBTFUL ACCOUNTS – Activity in the allowance for doubtful accounts for our receivables for the six months ended October 31, 2016 and 2015 is as follows:
(in 000s)

	EAs	All Other	Total
Balances as of May 1, 2016	$9,007	$48,004	$57,011
Provision	451	835	1,286
Charge-offs	—	(2,235)	(2,235)
Balances as of October 31, 2016	$9,458	$46,604	$56,062
Balances as of May 1, 2015	$7,353	$47,174	$54,527
Provision	877	349	1,226
Charge-offs	—	(2,413)	(2,413)
Balances as of October 31, 2015	$8,230	$45,110	$53,340

NOTE 4: MORTGAGE LOANS HELD FOR SALE OR INVESTMENT

In September 2016, our Board of Directors approved a plan to sell our portfolio of mortgage loans and we expect to complete the sale of these assets in our third fiscal quarter. As a result, these loans are presented as held for sale as of October 31, 2016, while they are presented as held for investment as of October 31, 2015 and April 30, 2016.

The composition of our mortgage loan portfolio is as follows:
(dollars in 000s)

As of	October 31, 2016		October 31, 2015		April 30, 2016	
	Amount	% of Total	Amount	% of Total	Amount	% of Total
Adjustable-rate loans	$97,358	52 %	$118,612	52 %	$108,251	52 %
Fixed-rate loans	89,699	48 %	107,612	48 %	97,957	48 %
	187,057	100 %	226,224	100 %	206,208	100 %
Unamortized deferred fees and costs	1,534		1,859		1,695	
Less: Allowance for loan losses	(5,484)		(7,412)		(5,518)	
	$183,107		$220,671		$202,385	

Our loan loss allowance as a percent of mortgage loans was 2.9% as of October 31, 2016, compared to 3.3% as of October 31, 2015 and 2.7% as of April 30, 2016.

Activity in the allowance for loan losses for the six months ended October 31, 2016 and 2015 is as follows:
(in 000s)

Six months ended October 31,	2016	2015
Balance at beginning of the period	$5,518	$7,886
Provision	—	(28)
Recoveries	742	1,050
Charge-offs	(776)	(1,496)
Balance at end of the period	$5,484	$7,412

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Detail of the aging of the mortgage loans in our portfolio as of October 31, 2016 is as follows:
(in 000s)

	Less than 60 Days Past Due	60 – 89 Days Past Due	90+ Days Past Due[1]	Total Past Due	Current	Total
Purchased from SCC	$ 6,350	$ 1,714	$ 38,057	$ 46,121	$ 65,412	$ 111,533
All other	1,471	428	4,620	6,519	69,005	75,524
	$ 7,821	$ 2,142	$ 42,677	$ 52,640	$ 134,417	$ 187,057

[1] We do not accrue interest on loans past due 90 days or more.

NOTE 5: GOODWILL AND INTANGIBLE ASSETS

Changes in the carrying amount of goodwill for the six months ended October 31, 2016 and 2015 are as follows:
(in 000s)

	Goodwill	Accumulated Impairment Losses	Net
Balances as of April 30, 2016	$ 503,054	$ (32,297)	$ 470,757
Acquisitions	7,435	—	7,435
Disposals and foreign currency changes, net	(832)	—	(832)
Impairments	—	—	—
Balances as of October 31, 2016	$ 509,657	$ (32,297)	$ 477,360
Balances as of April 30, 2015	$ 474,128	$ (32,297)	$ 441,831
Acquisitions	1,852	—	1,852
Disposals and foreign currency changes, net	(1,615)	—	(1,615)
Impairments	—	—	—
Balances as of October 31, 2015	$ 474,365	$ (32,297)	$ 442,068

We test goodwill for impairment annually or more frequently if events occur or circumstances change which would, more likely than not, reduce the fair value of a reporting unit below its carrying value.

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Components of intangible assets are as follows:
(in 000s)

	Gross Carrying Amount	Accumulated Amortization	Net
As of October 31, 2016:			
Reacquired franchise rights	$322,916	$ (79,484)	$243,432
Customer relationships	211,106	(117,539)	93,567
Internally-developed software	137,533	(104,022)	33,511
Noncompete agreements	31,625	(26,520)	5,105
Franchise agreements	19,201	(10,134)	9,067
Purchased technology	54,700	(28,941)	25,759
Acquired assets pending final allocation (1)	22,694	—	22,694
	$799,775	$ (366,640)	$433,135
As of October 31, 2015:			
Reacquired franchise rights	$316,142	$ (56,731)	$259,411
Customer relationships	182,137	(89,340)	92,797
Internally-developed software	123,263	(88,091)	35,172
Noncompete agreements	32,428	(24,632)	7,796
Franchise agreements	19,201	(8,854)	10,347
Purchased technology	54,700	(22,877)	31,823
Acquired assets pending final allocation (1)	28,878	—	28,878
	$756,749	$ (290,525)	$466,224
As of April 30, 2016:			
Reacquired franchise rights	$319,354	$ (68,284)	$251,070
Customer relationships	206,607	(104,072)	102,535
Internally-developed software	131,161	(95,768)	35,393
Noncompete agreements	31,499	(25,572)	5,927
Franchise agreements	19,201	(9,494)	9,707
Purchased technology	54,700	(25,909)	28,791
Acquired assets pending final allocation (1)	462	—	462
	$762,984	$ (329,099)	$433,885

(1) Represents business acquisitions for which final purchase price allocations have not yet been determined.
Amortization of intangible assets for the three and six months ended October 31, 2016 was $20.1 million and $38.0 million, respectively. Amortization of intangible assets for the three and six months ended October 31, 2015 was $17.9 million and $34.5 million, respectively. Estimated amortization of intangible assets for fiscal years 2017, 2018, 2019, 2020 and 2021 is $69.8 million, $65.9 million, $51.5 million, $36.6 million and $24.7 million, respectively.

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NOTE 6: LONG-TERM DEBT

The components of long-term debt are as follows:

			(in 000s)
As of	October 31, 2016	October 31, 2015	April 30, 2016
Senior Notes, 4.125%, due October 2020	$650,000	$650,000	$650,000
Senior Notes, 5.500%, due November 2022	500,000	500,000	500,000
Senior Notes, 5.250%, due October 2025	350,000	350,000	350,000
Committed line of credit borrowings	475,000	—	—
Capital lease obligation	7,024	7,835	7,435
Debt issuance costs and discounts	(13,915)	(16,513)	(15,234)
	1,968,109	1,491,322	1,492,201
Less: Current portion	(903)	(808)	(826)
	$1,967,206	$1,490,514	$1,491,375

Effective May 1, 2016, we adopted the provisions of ASU 2015-3 on a retrospective basis. Accordingly, debt issuance costs related to our Senior Notes are included in long-term debt in the consolidated balance sheets. Amounts for prior periods have been retrospectively adjusted to conform to the current period presentation. See note 1 for additional information.

On September 22, 2016, we entered into a First Amended and Restated Credit and Guarantee Agreement (2016 CLOC), which amended our Credit and Guarantee Agreement (2015 CLOC), extending the scheduled maturity date from September 21, 2020 to September 22, 2021 and decreasing the sublimit for standby letters of credit. Other material terms remain unchanged from our 2015 CLOC. The 2016 CLOC provides for an unsecured senior revolving credit facility in the aggregate principal amount of $2.0 billion, which includes a $200.0 million sublimit for swingline loans and a $50.0 million sublimit for standby letters of credit. We may request increases in the aggregate principal amount of the revolving credit facility of up to $500.0 million, subject to obtaining commitments from lenders therefor and meeting certain other conditions. The 2016 CLOC will mature on September 22, 2021, unless extended pursuant to the terms of the 2016 CLOC, at which time all outstanding amounts thereunder will be due and payable. The 2016 CLOC includes an annual facility fee, which will vary depending our then current credit ratings.

The 2016 CLOC is subject to various conditions, triggers, events or occurrences that could result in earlier termination and contains customary representations, warranties, covenants and events of default, including, without limitation: (1) a covenant requiring the Company to maintain a debt-to-EBITDA ratio calculated on a consolidated basis of no greater than (a) 3.50 to 1.00 as of the last day of each fiscal quarter ending on April 30, July 31, and October 31 of each year and (b) 4.50 to 1.00 as of the last day of each fiscal quarter ending on January 31 of each year; (2) a covenant requiring us to maintain an interest coverage (EBITDA-to-interest expense) ratio calculated on a consolidated basis of not less than 2.50 to 1.00 as of the last date of any fiscal quarter; and (3) covenants restricting our ability to incur certain additional debt, incur liens, merge or consolidate with other companies, sell or dispose of assets (including equity interests), liquidate or dissolve, engage in certain transactions with affiliates or enter into certain restrictive agreements. The 2016 CLOC includes provisions for an equity cure which could potentially allow us to independently cure certain defaults. Proceeds under the 2016 CLOC may be used for working capital needs or for other general corporate purposes. We were in compliance with these requirements as of October 31, 2016.

We had an outstanding balance of $475.0 million under the 2016 CLOC as of October 31, 2016. Incremental amounts available to borrow under the 2016 CLOC were limited to approximately $948 million as of October 31, 2016, in accordance with the covenant requiring a minimum debt-to-EBITDA ratio of 3.50 to 1.00.

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NOTE 7: FAIR VALUE

ESTIMATED FAIR VALUE OF FINANCIAL INSTRUMENTS – The carrying amounts and estimated fair values of our financial instruments are as follows:

(in 000s)

As of	October 31, 2016		October 31, 2015		April 30, 2016	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Assets:						
Cash and cash equivalents	$232,510	$232,510	$360,681	$360,681	$896,801	$896,801
Cash and cash equivalents - restricted	109,538	109,538	42,781	42,781	104,110	104,110
Receivables, net - short-term	104,764	104,764	94,760	94,760	153,116	153,116
Mortgage loans held for sale	183,107	195,432	—	—	—	—
Mortgage loans held for investment, net	—	—	220,671	180,437	202,385	190,503
Receivables, net - long-term	56,238	56,238	75,275	75,275	60,407	60,407
Liabilities:						
Long-term debt and line of credit borrowings	1,968,109	2,067,234	1,491,322	1,553,633	1,492,201	1,566,098
Contingent consideration	7,817	7,817	11,932	11,932	8,657	8,657

Fair value estimates, methods and assumptions are set forth below. Fair value was not estimated for assets and liabilities that are not considered financial instruments.

Cash and cash equivalents, including restricted - Fair value approximates the carrying amount (Level 1).

Receivables, net - short-term - For short-term balances the carrying values reported in the balance sheet approximate fair market value due to the relative short-term nature of the respective instruments (Level 1).

Mortgage loans held for sale - The fair value is based on indicative bids received from prospective buyers and is based on estimated valuations of unpaid principal balances (Level 2). These loans were previously reported as held for investment with the related fair value determined as outlined below (Level 3). In accordance with plans approved by our Board of Directors, these loans are now presented as held for sale.

Mortgage loans held for investment, net - The fair value of mortgage loans held for investment is estimated using a third-party pricing service. The fair value is determined using the present value of expected future cash flows at the asset level, assuming future prepayments and using discount factors determined by prices obtained for residential loans with similar characteristics in the secondary market, as discounted for illiquid assets. Quarterly, we perform analytics to assess the reasonableness of the fair value received from the third-party pricing service based on changes in the portfolio and changes in market conditions. We evaluate whether adjustments to third-party pricing is necessary and historically, we have not made adjustments to prices obtained from our third-party pricing service (Level 3).

Receivables, net - long-term - The carrying values for the long-term portion of loans to franchisees approximate fair market value due to variable interest rates, low historical delinquency rates and franchise territories serving as collateral (Level 1). Long-term EA receivables are carried at net realizable value which approximates fair value (Level 3). Net realizable value is determined based on historical collection rates.

Long-term debt - The fair value of our Senior Notes is based on quotes from multiple banks (Level 2). For outstanding balances on the 2016 CLOC, fair value approximates the carrying amount (Level 1).

Contingent consideration - Fair value approximates the carrying amount (Level 3).

NOTE 8: INCOME TAXES

We file a consolidated federal income tax return in the United States (U.S.) with the Internal Revenue Service (IRS) and file tax returns in various state and foreign jurisdictions. Tax returns are typically examined and settled upon completion of the examination, with tax controversies settled either at the exam level or through the appeals process.

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The Company currently does not have a U.S. federal income tax return under examination. Our U.S. federal returns for 2012 and all prior periods have been audited by the IRS and are closed. Our U.S. federal returns for 2013 and after have not been audited and remain open to examination. With respect to state and local jurisdictions and countries outside the United States, we and our subsidiaries are typically subject to examination for three to six years after the income tax returns have been filed. Although the outcome of the audits is always uncertain, we believe that adequate amounts of tax, interest and penalties have been provided for in the consolidated financial statements for any adjustments that might be incurred due to state, local or foreign audits.

We had gross unrecognized tax benefits of $105.7 million, $96.6 million and $111.5 million as of October 31, 2016 and 2015 and April 30, 2016, respectively. The gross unrecognized tax benefits decreased $5.8 million and increased $10.3 million during the six months ended October 31, 2016 and 2015, respectively. The decrease in unrecognized tax benefits during the six months ending October 31, 2016 is primarily related to audit settlements in various states. We believe it is reasonably possible that the balance of unrecognized tax benefits could decrease by approximately $11.6 million within the next twelve months. The anticipated decrease is due to the expiration of statutes of limitations and anticipated closure of various state matters currently under exam. The portion of unrecognized benefits expected to be cash settled within the next twelve months amounts to $7.5 million and is included in accrued income taxes on our consolidated balance sheet. The remaining liability for uncertain tax positions is classified as long-term and is included in other noncurrent liabilities in the consolidated balance sheet.

Consistent with prior years, our pretax loss for the six months ended October 31, 2016 is expected to be offset by income in the fourth quarter due to the established pattern of seasonality in our primary business operations. As such, we have determined that it is at least more-likely-than-not that realization of tax benefits recorded in our financial statements will occur within our fiscal year. The amount of tax benefit recorded reflects management’s estimate of the annual effective tax rate applied to the year-to-date loss from continuing operations. Certain discrete tax adjustments are also reflected in income tax expense for the periods presented.

A discrete income tax benefit of $10.8 million was recorded in the six months ended October 31, 2016, compared to a discrete tax benefit of $26.6 million in the same period of the prior year. The discrete tax benefit recorded in the current period resulted primarily from favorable settlements of state audits. The discrete tax benefit recorded in the prior year resulted primarily from a law change enacted in the state of Missouri.

Our effective tax rate for continuing operations, including the effects of discrete income tax items was 38.8% and 43.7% for the six months ended October 31, 2016 and 2015, respectively. Discrete items increased our estimate of the annualized effective tax rate for the six months ended October 31, 2016 and 2015 by 2.5% and 6.3%, respectively. Due to the loss in both periods, a discrete tax benefit in either period increases the tax rate while an item of discrete tax expense decreases the tax rate. The impact of discrete tax items combined with the seasonal nature of our business can cause the effective tax rate through our second quarter to be significantly different than the rate for our full fiscal year.

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NOTE 9: OTHER INCOME AND OTHER EXPENSES

The following table shows the components of other income and other expenses:

(in 000s)

	Three months ended October 31,		Six months ended October 31,	
	2016	2015	2016	2015
Other income, net:				
Mortgage loans and real estate owned, net	$1,508	$34	$3,045	$34
Interest and gains on AFS securities	52	8,768	83	8,768
Other	620	1,703	2,020	2,136
	$2,180	$10,505	$5,148	$10,938
Other expenses, net:				
Foreign currency losses	$(6)	$(23)	$(27)	$(4,622)
Other	(1)	(187)	(307)	(573)
	$(7)	$(210)	$(334)	$(5,195)

In connection with our deregistration as a savings and loan holding company (SLHC), we no longer present interest income on mortgage loans and various other investments as revenues. Effective September 1, 2015, these amounts are prospectively reported in other income on the consolidated statements of operations and comprehensive loss.

NOTE 10: COMMITMENTS AND CONTINGENCIES

Changes in deferred revenue balances related to our Peace of Mind® Extended Service Plan (POM) for both company-owned and franchise offices, which is included in deferred revenue and other liabilities in the consolidated balance sheets, are as follows:

(in 000s)

Six months ended October 31,	2016	2015
Balance, beginning of the period	$204,342	$189,779
Amounts deferred for new extended service plans issued	2,561	2,608
Revenue recognized on previous deferrals	(58,921)	(54,943)
Balance, end of the period	$147,982	$137,444

We accrued $5.0 million, $6.8 million and $7.0 million as of October 31, 2016 and 2015 and April 30, 2016, respectively, related to estimated losses under the standard guarantee, which is included with assisted tax preparation services. The short-term and long-term portions of this liability are included in deferred revenue and other liabilities in the consolidated balance sheets.

We have accrued estimated contingent consideration totaling $7.8 million, $11.9 million and $8.7 million as of October 31, 2016 and 2015 and April 30, 2016, respectively, related to acquisitions, with amounts recorded in deferred revenue and other liabilities. Estimates of contingent payments are typically based on expected financial performance of the acquired business and economic conditions at the time of acquisition. Should actual results differ from our assumptions, future payments made will differ from the above estimate and any differences will be recorded in results from continuing operations.

We have contractual commitments to fund certain franchises with approved revolving lines of credit. Our total obligation under these lines of credit was $56.4 million at October 31, 2016, and net of amounts drawn and outstanding, our remaining commitment to fund totaled $25.0 million.

On October 25, 2016, we entered into a Refund Advance Program Agreement and certain ancillary agreements with certain third parties, pursuant to which they will originate and fund Refund Advance loans, and provide technology, software, and underwriting support services related to such loans. The Refund Advance loans will be offered to eligible assisted U.S. tax preparation clients, based on client eligibility as determined by the loan originator. We will pay loan origination fees based on volume and customer type. The loan origination fees are intended to cover expected loan

losses and payments to capital providers, among other items. In addition, we have provided limited guarantees up to $73 million in the aggregate, subject to specified thresholds, which would cover certain incremental loan losses. We expect that only an immaterial amount of the guarantees will be called upon under anticipated loss scenarios.

NOTE 11: LITIGATION AND RELATED CONTINGENCIES

We are a defendant in numerous litigation matters, arising both in the ordinary course of business and otherwise, including as described below. The matters described below are not all of the lawsuits to which we are subject. In some of the matters, very large or indeterminate amounts, including punitive damages, are sought. U.S. jurisdictions permit considerable variation in the assertion of monetary damages or other relief. Jurisdictions may permit claimants not to specify the monetary damages sought or may permit claimants to state only that the amount sought is sufficient to invoke the jurisdiction of the court. In addition, jurisdictions may permit plaintiffs to allege monetary damages in amounts well exceeding reasonably possible verdicts in the jurisdiction for similar matters. We believe that the monetary relief which may be specified in a lawsuit or a claim bears little relevance to its merits or disposition value due to this variability in pleadings and our experience in litigating or resolving through settlement of numerous claims over an extended period of time.

The outcome of a litigation matter and the amount or range of potential loss at particular points in time may be difficult to ascertain. Among other things, uncertainties can include how fact finders will evaluate documentary evidence and the credibility and effectiveness of witness testimony, and how trial and appellate courts will apply the law. Disposition valuations are also subject to the uncertainty of how opposing parties and their counsel will themselves view the relevant evidence and applicable law.

In addition to litigation matters, we are also subject to claims and other loss contingencies arising out of our business activities, including as described below.

We accrue liabilities for litigation, claims, and other loss contingencies, and any related settlements (each referred to, individually, as a "matter" and, collectively, as "matters") when it is probable that a loss has been incurred and the amount of the loss can be reasonably estimated. Liabilities have been accrued for certain of the matters noted below. If a range of loss is estimated, and some amount within that range appears to be a better estimate than any other amount within that range, then that amount is accrued. If no amount within the range can be identified as a better estimate than any other amount, we accrue the minimum amount in the range.

For such matters where a loss is believed to be reasonably possible, but not probable, or the loss cannot be reasonably estimated, no accrual has been made. It is possible that such matters could require us to pay damages or make other expenditures or accrue liabilities in amounts that could not be reasonably estimated as of October 31, 2016. While the potential future liabilities could be material in the particular quarterly or annual periods in which they are recorded, based on information currently known, we do not believe any such liabilities are likely to have a material adverse effect on our business and our consolidated financial position, results of operations and cash flows. As of October 31, 2016 and 2015 and April 30, 2016, our total accrued liabilities were $2.3 million, $6.2 million and $2.3 million, respectively, for matters addressed in this note.

For some matters where a liability has not been accrued, we are able to estimate a reasonably possible loss or range of loss. This estimated range of reasonably possible loss is based upon currently available information and is subject to significant judgment and a variety of assumptions, as well as known and unknown uncertainties. The matters underlying the estimated range will change from time to time, and actual results may vary significantly from the current estimate. Those matters for which an estimate is not reasonably possible are not included within this estimated range. Therefore, this estimated range of reasonably possible loss represents what we believe to be an estimate of reasonably possible loss only for certain matters meeting these criteria. It does not represent our maximum loss exposure. For those matters, and for matters where a liability has been accrued, as of October 31, 2016, we believe the aggregate range of reasonably possible losses in excess of amounts accrued is not material.

For other matters, we are not currently able to estimate the reasonably possible loss or range of loss. We are often unable to estimate the possible loss or range of loss until developments in such matters have provided sufficient information to support an assessment of the reasonably possible loss or range of loss, such as quantification of a damage demand from plaintiffs, discovery from other parties and investigation of factual allegations, rulings by courts on motions or appeals, analysis by experts, or the status of any settlement negotiations.

On a quarterly and annual basis, we review relevant information with respect to litigation and other loss contingencies and update our accruals, disclosures and estimates of reasonably possible loss or range of loss based on such reviews. Costs incurred with defending matters are expensed as incurred. Any receivable for insurance recoveries is recorded separately from the corresponding liability, and only if recovery is determined to be probable and reasonably estimable.

We believe we have meritorious defenses to the claims asserted in the various matters described in this note, and we intend to defend them vigorously, but there can be no assurances as to their outcomes. In the event of unfavorable outcomes, it could require modifications to our operations; in addition, the amounts that may be required to be paid to discharge or settle the matters could be substantial and could have a material adverse impact on our business and our consolidated financial position, results of operations, and cash flows.

LITIGATION, CLAIMS, INCLUDING INDEMNIFICATION CLAIMS, OR OTHER LOSS CONTINGENCIES PERTAINING TO DISCONTINUED MORTGAGE OPERATIONS – Although SCC ceased its mortgage loan origination activities in December 2007 and sold its loan servicing business in April 2008, SCC or the Company has been, remains, and may in the future be subject to litigation, claims, including indemnification and contribution claims, and other loss contingencies pertaining to SCC's mortgage business activities that occurred prior to such termination and sale. These contingencies, claims, and lawsuits include actions by regulators, third parties seeking indemnification, including depositors, underwriters, and securitization trustees, individual plaintiffs, and cases in which plaintiffs seek to represent a class of others alleged to be similarly situated. Among other things, these contingencies, claims, and lawsuits allege or may allege discriminatory or unfair and deceptive loan origination and servicing (including debt collection, foreclosure, and eviction) practices, other common law torts, rights to indemnification and contribution, breach of contract, violations of securities laws, and a variety of federal statutes, including the Truth in Lending Act (TILA), Equal Credit Opportunity Act, Fair Housing Act, Real Estate Settlement Procedures Act (RESPA), Home Ownership & Equity Protection Act (HOEPA), as well as similar state statutes. Given the impact of the financial crisis on the non-prime mortgage environment, the aggregate volume of these matters is substantial although it is difficult to predict either the likelihood of new matters being initiated or the outcome of existing matters. In many of these matters, including certain of the lawsuits and claims described below, it is not possible to estimate a reasonably possible loss or range of loss due to, among other things, the inherent uncertainties involved in these matters, some of which are beyond the Company's control, and the indeterminate damages sought in some of these matters.

On May 31, 2012, a lawsuit was filed by Homeward Residential, Inc. (Homeward) in the Supreme Court of the State of New York, County of New York, against SCC styled Homeward Residential, Inc. v. Sand Canyon Corporation (Index No. 651885/2012). SCC removed the case to the United States District Court for the Southern District of New York on June 28, 2012 (Case No. 12-cv-5067). The plaintiff, in its capacity as the master servicer for Option One Mortgage Loan Trust 2006-2 and for the benefit of the trustee and the certificate holders of such trust, asserts claims for breach of contract, anticipatory breach, indemnity, and declaratory judgment in connection with alleged losses incurred as a result of the breach of representations and warranties relating to SCC and to loans sold to the trust. The plaintiff seeks specific performance of alleged repurchase obligations or damages to compensate the trust and its certificate holders for alleged actual and anticipated losses, as well as a repurchase of all loans due to alleged misrepresentations by SCC as to itself and as to the loans' compliance with its underwriting standards and the value of underlying real estate. In response to a motion filed by SCC, the court dismissed the plaintiff's claims for breach of the duty to cure or repurchase, anticipatory breach, indemnity, and declaratory judgment. The case is proceeding on the remaining claims. Representatives of a holder of certificates in the trust have requested a pre-motion conference for a proposed motion to intervene to add H&R Block, Inc. to the lawsuit to assert claims against H&R Block, Inc. based on alter ego, corporate veil-piercing and agency law. We believe we have meritorious defenses to the extent the court allows any such claims to be asserted. We have not concluded that a loss related to this matter is probable, nor have we accrued a liability related to this matter.

On September 28, 2012, a second lawsuit was filed by Homeward in the United States District Court for the Southern District of New York against SCC styled Homeward Residential, Inc. v. Sand Canyon Corporation (Case No. 12-cv-7319). The plaintiff, in its capacity as the master servicer for Option One Mortgage Loan Trust 2006-3 and for the benefit of the trustee and the certificate holders of such trust, asserts claims for breach of contract and indemnity in connection with losses allegedly incurred as a result of the breach of representations and warranties relating to 96 loans sold to the trust. The plaintiff seeks specific performance of alleged repurchase obligations or damages to compensate the trust and its certificate holders for alleged actual and anticipated losses. In response to a motion filed by SCC, the court dismissed the plaintiff's claims for breach of the duty to cure or repurchase and for indemnification of its costs associated with the litigation. On September 30, 2016, the court granted a motion allowing plaintiff to file a second amended complaint to include breach of contract claims with respect to 649 additional loans in the trust and to allow such claims with respect to other loans in the trust proven to be in material breach of SCC's representations and warranties. SCC filed a motion for reconsideration and a motion for leave to appeal the ruling, both of which remain pending. On October 6, 2016, plaintiff filed its second amended complaint. SCC filed a motion to dismiss, which also remains pending. Representatives of a holder of certificates in the trust have requested a pre-motion conference for a proposed motion to intervene to add H&R Block, Inc. to the lawsuit to assert claims against H&R Block, Inc. based on alter ego, corporate veil-piercing and agency law. We believe we have meritorious defenses to the extent the court allows any such claims to be asserted. A portion of the accrual for representation and warranty claims, as discussed in note 12, is related to some of the loans included in the original complaint in this case. We have not concluded that a loss related to this lawsuit is probable, nor have we accrued a liability related to this lawsuit.

On April 5, 2013, a third lawsuit was filed by Homeward in the United States District Court for the Southern District of New York against SCC. The suit, styled Homeward Residential, Inc. v. Sand Canyon Corporation (Case No. 13-cv-2107), was filed as a related matter to the September 2012 Homeward suit mentioned above. In this April 2013 lawsuit, the plaintiff, in its capacity as the master servicer for Option One Mortgage Loan Trust 2007-4 and for the benefit of the trustee and the certificate holders of such trust, asserts claims for breach of contract and indemnity in connection with losses allegedly incurred as a result of the breach of representations and warranties relating to 159 loans sold to the trust. The plaintiff seeks specific performance of alleged repurchase obligations or damages to compensate the trust and its certificate holders for alleged actual and anticipated losses. In response to a motion filed by SCC, the court dismissed the plaintiff's claims for breach of the duty to cure or repurchase and for indemnification of its costs associated with the litigation. The case is proceeding on the remaining claims. A portion of the accrual for representation and warranty claims, as discussed in note 12, is related to loans in this case. We have not concluded that a loss related to this lawsuit is probable, nor have we accrued a liability related to this lawsuit.

Underwriters and depositors are, or have been, involved in multiple lawsuits related to securitization transactions in which SCC participated. These lawsuits allege or alleged a variety of claims, including violations of federal and state securities laws and common law fraud, based on alleged materially inaccurate or misleading disclosures. SCC has received notices of claims for indemnification relating to lawsuits to which underwriters or depositors are party. Based on information currently available to SCC, it believes that the 22 lawsuits in which notice of a claim has been made involve 39 securitization transactions with original investments of approximately $14 billion (of which the outstanding principal amount is approximately $4 billion). Because SCC has not been a party to these lawsuits (with the exception of Federal Home Loan Bank of Chicago v. Bank of America Funding Corporation, et al., filed in the Circuit Court of Cook County, Illinois (Case No. 10CH45033) and settled as to SCC in August 2015), and has not had control of this litigation or any settlements thereof, SCC does not have precise information about the amount of damages or other remedies being asserted, the defenses to the claims in such lawsuits or the terms of any settlements of such lawsuits. SCC therefore cannot reasonably estimate the amount of potential losses or associated fees and expenses that may be incurred in connection with such lawsuits, which may be material. Additional lawsuits against the underwriters or depositors may be filed in the future, and SCC may receive additional notices of claims for indemnification from underwriters or depositors with respect to existing or new lawsuits or settlements of such lawsuits. Certain of the notices received included, and future notices may include, a reservation of rights, which are referred to as "reserved contribution rights," that encompasses a right of contribution which may become operative if indemnification is unavailable or insufficient to cover all of the losses and expenses involved. We have not concluded that a loss related to any of these indemnification claims or reserved contribution rights is probable, nor have we accrued a liability related to any of these claims or rights.

Securitization trustees also are, or have been, involved in lawsuits related to securitization transactions in which SCC participated. Plaintiffs in these lawsuits allege, among other things, that originators, depositors, servicers or other parties breached their representations and warranties or otherwise failed to fulfill their obligations, including that securitization trustees breached their contractual obligations, breached their fiduciary duties, or violated statutory requirements by failing to properly protect the certificate holders' interests. SCC may receive notices for indemnification with respect to existing or new lawsuits or settlements of such lawsuits in its capacity as originator, depositor, or servicer. We have not concluded that a loss related to any indemnification claims by securitization trustees is probable, nor have we accrued a liability for such claims.

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LITIGATION, CLAIMS OR OTHER LOSS CONTINGENCIES PERTAINING TO CONTINUING OPERATIONS – Compliance Fee Litigation. On April 16, 2012, a putative class action lawsuit was filed against us in the Circuit Court of Jackson County, Missouri styled Manuel H. Lopez III v. H&R Block, Inc., et al. (Case # 1216CV12290) concerning a compliance fee charged to retail tax clients in the 2011 and 2012 tax seasons. The plaintiff seeks to represent all Missouri citizens who were charged the compliance fee, and asserts claims of violation of the Missouri Merchandising Practices Act, money had and received, and unjust enrichment. We filed a motion to compel arbitration of the 2011 claims. The court denied the motion. We filed an appeal. On May 6, 2014, the Missouri Court of Appeals, Western District, reversed the ruling of the trial court and remanded the case for further consideration of the motion. On March 12, 2015, the trial court denied the motion on remand. We filed an additional appeal. On March 8, 2016, the appellate court affirmed the decision of the trial court. We filed an application for transfer of the appeal in the Supreme Court of Missouri, which was denied. We subsequently filed a petition for writ of certiorari with the United States Supreme Court, which remains pending. We have not concluded that a loss related to this matter is probable, nor have we accrued a loss contingency related to this matter.

On April 19, 2012, a putative class action lawsuit was filed against us in the United States District Court for the Western District of Missouri styled Ronald Perras v. H&R Block, Inc., et al. (Case No. 4:12-cv-00450-DGK) concerning a compliance fee charged to retail tax clients in the 2011 and 2012 tax seasons. The plaintiff originally sought to represent all persons nationwide (excluding citizens of Missouri) who were charged the compliance fee, and asserted claims of violation of various state consumer laws, money had and received, and unjust enrichment. In November 2013, the court compelled arbitration of the 2011 claims and stayed all proceedings with respect to those claims. In June 2014, the court denied class certification of the remaining 2012 claims. The plaintiff filed an appeal with the Eighth Circuit Court of Appeals, which was denied on June 18, 2015. In January 2016, the plaintiff filed an amended complaint asserting claims of violation of Missouri and California state consumer laws, money had and received, and unjust enrichment, along with a motion to certify a class of all persons (excluding citizens of Missouri) who were charged the compliance fee in the state of California. We subsequently filed a motion for summary judgment on all claims. On April 29, 2016, the court granted our motion for summary judgment on all claims and denied the plaintiff's motion for class certification as moot. The plaintiff filed an appeal with the Eighth Circuit Court of Appeals, which remains pending. We have not concluded that a loss related to this matter is probable, nor have we accrued a loss contingency related to this matter.

LITIGATION, CLAIMS AND OTHER LOSS CONTINGENCIES PERTAINING TO OTHER DISCONTINUED OPERATIONS –

Express IRA Litigation. On January 2, 2008, the Mississippi Attorney General in the Chancery Court of Hinds County, Mississippi First Judicial District (Case No. G 2008 6 S 2) filed a lawsuit regarding our former Express IRA product that is styled Jim Hood, Attorney for the State of Mississippi v. H&R Block, Inc., H&R Block Financial Advisors, Inc., et al. The complaint alleges fraudulent business practices, deceptive acts and practices, common law fraud and breach of fiduciary duty with respect to the sale of the product in Mississippi and seeks equitable relief, disgorgement of profits, damages and restitution, civil penalties and punitive damages. We have not concluded that a loss related to this matter is probable, nor have we accrued a loss contingency related to this matter.

Although we sold H&R Block Financial Advisors, Inc. (HRBFA) effective November 1, 2008, we remain responsible for any liabilities relating to the Express IRA litigation through an indemnification agreement.

OTHER – We are from time to time a party to litigation, claims and other loss contingencies not discussed herein arising out of our business operations. These matters may include actions by state attorneys general, other state regulators, federal regulators, individual plaintiffs, and cases in which plaintiffs seek to represent a class of others similarly situated.

While we cannot provide assurance that we will ultimately prevail in each instance, we believe the amount, if any, we are required to pay to discharge or settle these other matters will not have a material adverse impact on our business and our consolidated financial position, results of operations, and cash flows.

We believe we have meritorious defenses to the claims asserted in the various matters described in this note, and we intend to defend them vigorously. The amounts claimed in the matters are substantial, however, and there can be no assurances as to their outcomes. In the event of unfavorable outcomes, it could require modifications to our operations; in addition, the amounts that may be required to be paid to discharge or settle the matters could be

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substantial and could have a material adverse impact on our business and our consolidated financial position, results of operations, and cash flows.

NOTE 12: LOSS CONTINGENCIES ARISING FROM REPRESENTATIONS AND WARRANTIES OF OUR DISCONTINUED MORTGAGE OPERATIONS

SCC ceased originating mortgage loans in December 2007 and, in April 2008, sold its servicing assets and discontinued its remaining operations.

Mortgage loans originated by SCC were sold either as whole loans to single third-party buyers, who generally securitized such loans, or in the form of residential mortgage-backed securities (RMBSs). In connection with the sale of loans and/or RMBSs, SCC made certain representations and warranties. Claims under these representations and warranties together with any settlement arrangements related to these losses are collectively referred to as "representation and warranty claims." These representations and warranties varied based on the nature of the transaction and the buyer's or insurer's requirements, but generally pertained to the ownership of the loan, the validity of the lien securing the loan, borrower fraud, the loan's compliance with the criteria for inclusion in the transaction, including compliance with SCC's underwriting standards or loan criteria established by the buyer, ability to deliver required documentation, and compliance with applicable laws. Representations and warranties related to borrower fraud in whole loan sale transactions to institutional investors, which were generally securitized by such investors and represented approximately 68% of the disposal of loans originated in calendar years 2005, 2006 and 2007, included a "knowledge qualifier" limiting SCC's liability to those instances where SCC had knowledge of the fraud at the time the loans were sold. Representations and warranties made in other sale transactions effectively did not include a knowledge qualifier as to borrower fraud. SCC believes it would have an obligation to repurchase a loan only if it breached a representation and warranty and such breach materially and adversely affects the value of the mortgage loan or certificate holder's interest in the mortgage loan.

Representation and warranty claims received by SCC have primarily related to alleged breaches of representations and warranties related to a loan's compliance with the underwriting standards established by SCC at origination and borrower fraud for loans originated in calendar years 2006 and 2007. SCC has received claims representing an original principal amount of $2.6 billion since May 1, 2008, of which $1.9 billion were received prior to fiscal year 2013.

SETTLEMENT ACTIONS – SCC has entered into tolling agreements with counterparties that have made a significant portion of previously denied representation and warranty claims. While tolling agreements remain in effect, they toll the running of any applicable statute of limitations related to potential lawsuits regarding representation and warranty claims and other claims against SCC.

SCC has engaged in discussions with counterparties since fiscal year 2013 regarding the bulk settlement of previously denied and potential future representation and warranty and other claims against SCC. Based on settlement discussions with counterparties, SCC believes a bulk settlement approach, rather than the loan-by-loan resolution process, will be needed to resolve all of the claims that are the subject of these discussions. SCC has utilized that approach to resolve certain of these claims. On July 13, 2016, SCC entered into a settlement agreement with an additional counterparty to resolve certain additional claims. The amount paid under this settlement agreement was fully covered by prior accruals. In the event that the ongoing efforts to settle are not successful, SCC believes claim volumes may increase or litigation may result.

SCC will continue to vigorously contest any request for repurchase when it has concluded that a valid basis for repurchase does not exist. SCC's decision whether to engage in bulk settlement discussions is based on factors that vary by counterparty or type of counterparty and include the considerations used by SCC in determining its loss estimate, described below under "Liability for Estimated Contingent Losses."

LIABILITY FOR ESTIMATED CONTINGENT LOSSES – SCC accrues a liability for losses related to representation and warranty claims when those losses are believed to be both probable and reasonably estimable. Development of loss estimates is subject to a high degree of management judgment and estimates may vary significantly period to period. SCC's loss estimate as of October 31, 2016 is based on the best information currently available, significant management judgment, and a number of factors that are subject to change, including developments in case law and the factors mentioned below. These factors include the terms of prior bulk settlements, the terms expected to result from ongoing bulk settlement discussions, and an assessment of, among other things, historical claim results, threatened claims, terms and provisions of related agreements, counterparty willingness to pursue a settlement, legal standing of

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counterparties to provide a comprehensive settlement, bulk settlement methodologies used and publicly disclosed by other market participants, the potential pro-rata realization of the claims as compared to all claims and other relevant facts and circumstances when developing its estimate of probable loss. SCC believes that the most significant of these factors are the terms expected to result from ongoing bulk settlement discussions, which have been primarily influenced by the bulk settlement methodologies used and publicly disclosed by other market participants and the anticipated pro-rata realization of the claims of particular counterparties as compared to the anticipated realization if all claims and litigation were resolved together with payment of SCC's related administration and legal expense. Changes in any one of the factors mentioned above could significantly impact the estimate.

The liability is included in deferred revenue and other current liabilities on the consolidated balance sheets. A rollforward of SCC's accrued liability for these loss contingencies is as follows:

(in 000s)

Six months ended October 31,	2016	2015
Balance, beginning of the period	$65,265	$149,765
Provisions	235	4,000
Payments	(40,000)	—
Balance, end of the period	$25,500	$153,765

On June 11, 2015, the New York Court of Appeals, New York's highest court, held in ACE Securities Corp. v. DB Structured Products, Inc., that the six-year statute of limitations under New York law starts to run at the time the representations and warranties are made, not the date when the repurchase demand was denied. This decision applies to claims and lawsuits brought against SCC where New York law governs. New York law governs many, though not all, of the RMBS transactions into which SCC entered. However this decision would not affect representation and warranty claims and lawsuits SCC has received or may receive, for example, where the statute of limitations has been tolled by agreement or a suit was timely filed. In response to the statute of limitations rulings in the ACE case and similar rulings in other state and federal courts, parties seeking to pursue representation and warranty claims or lawsuits with respect to trusts where the statute of limitations for representation and warranty claims against the originator has run, have sought, and may in the future seek, to distinguish certain aspects of the ACE decision, pursue alternate legal theories of recovery, or assert claims against other contractual parties such as securitization trustees. For example, a recent ruling by a New York intermediate appellate court allowed a counterparty to pursue litigation on additional loans in the same trust even though only some of the loans complied with the condition precedent of timely pre-suit notice and opportunity to cure or repurchase. The trial court in the second Homeward lawsuit against SCC, discussed above in Note 11, followed that ruling and permitted the plaintiff to amend its complaint to include breach of contract claims with respect to 649 additional loans in the trust and to allow such claims with respect to other loans in the trust proven to be in material breach of SCC’s representations and warranties. The trial court held that claims with respect to the additional loans sufficiently relate back to the timely-asserted claims and therefore are not barred by the statute of limitations. SCC is seeking reconsideration of, and leave to appeal, that ruling. The impact on SCC from alternative legal theories seeking to avoid or distinguish the ACE decision, or judicial limitations on the ACE decision, is unclear. SCC has not accrued liabilities for claims not subject to a tolling arrangement or not asserted prior to the expiration of the applicable statute of limitations.

SCC believes it is reasonably possible that future losses related to representation and warranty claims may vary from amounts accrued for these exposures. SCC currently believes the aggregate range of reasonably estimable possible losses in excess of amounts accrued is not material. This estimated range is based on the best information currently available, significant management judgment and a number of factors that are subject to change, including developments in case law and the factors mentioned above. The actual loss that may be incurred could differ materially from our accrual or the estimate of reasonably possible losses.

As described more fully in note 11, losses may also be incurred with respect to various indemnification claims or reserved contribution rights by underwriters, depositors, and securitization trustees in securitization transactions in which SCC participated. These indemnification claims or reserved contribution rights are frequently not subject to a stated term or limit. We have not concluded that a loss related to any of these indemnification claims or reserved contribution rights is probable, have not accrued a liability for these claims or rights, and are not able to estimate a reasonably possible loss or range of loss for these claims or rights. Accordingly, neither the accrued liability described

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above totaling $25.5 million, nor the estimated range of reasonably possible losses in excess of the amount accrued described above, includes any possible losses which may arise from these indemnification claims or reserved contribution rights. There can be no assurances as to the outcome or impact of these indemnification claims or reserved contribution rights. In the event of unfavorable outcomes on these claims or rights, the amount required to discharge or settle them could be substantial and could have a material adverse impact on our business and our consolidated financial position, results of operations, and cash flows.

If the amount that SCC is ultimately required to pay with respect to claims and litigation related to its past sales and securitizations of mortgage loans, together with payment of SCC's related administration and legal expense, exceeds SCC's net assets, the creditors of SCC, other potential claimants, or a bankruptcy trustee if SCC were to file or be forced into bankruptcy, may attempt to assert claims against us for payment of SCC's obligations. Claimants may also attempt to assert claims against or seek payment directly from the Company even if SCC's assets exceed its liabilities. SCC's principal assets, as of October 31, 2016, total approximately $346 million and consist primarily of an intercompany note receivable. We believe our legal position is strong on any potential corporate veil-piercing arguments; however, if this position is challenged and not upheld, it could have a material adverse effect on our business and our consolidated financial position, results of operations, and cash flows.

NOTE 13: CONDENSED CONSOLIDATING FINANCIAL STATEMENTS

Block Financial is a 100% owned subsidiary of the Company. Block Financial is the Issuer and the Company is the full and unconditional Guarantor of the Senior Notes, our 2016 CLOC and other indebtedness issued from time to time. These condensed consolidating financial statements have been prepared using the equity method of accounting. Earnings of subsidiaries are, therefore, reflected in the Company's investment in subsidiaries account. The elimination entries eliminate investments in subsidiaries, related stockholders' equity and other intercompany balances and transactions.

CONDENSED CONSOLIDATING STATEMENTS OF OPERATIONS (in 000s)

Three months ended October 31, 2016	H&R Block, Inc. (Guarantor)	Block Financial (Issuer)	Other Subsidiaries	Eliminations	Consolidated H&R Block
Total revenues	$ —	$ 10,934	$ 120,423	$ (25)	$ 131,332
Cost of revenues	—	5,666	220,061	(25)	225,702
Selling, general and administrative	—	1,732	111,920	—	113,652
Total operating expenses	—	7,398	331,981	(25)	339,354
Other income, net	—	2,256	1,639	(1,715)	2,180
Interest expense on external borrowings	—	(22,248)	(372)	—	(22,620)
Other expenses, net	(148,773)	(1,049)	(14,833)	164,648	(7)
Loss from continuing operations before tax benefit	(148,773)	(17,505)	(225,124)	162,933	(228,469)
Income tax benefit	(2,553)	(5,962)	(76,539)	—	(85,054)
Net loss from continuing operations	(146,220)	(11,543)	(148,585)	162,933	(143,415)
Net loss from discontinued operations	—	(2,805)	—	—	(2,805)
Net loss	(146,220)	(14,348)	(148,585)	162,933	(146,220)
Other comprehensive loss	(2,318)	—	(2,318)	2,318	(2,318)
Comprehensive loss	$ (148,538)	$ (14,348)	$ (150,903)	$ 165,251	$ (148,538)

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CONDENSED CONSOLIDATING STATEMENTS OF OPERATIONS (in 000s)

Three months ended October 31, 2015	H&R Block, Inc. (Guarantor)	Block Financial (Issuer)	Other Subsidiaries	Eliminations	Consolidated H&R Block
Total revenues	$ —	$ 13,972	$ 114,471	$ (28)	$ 128,415
Cost of revenues	—	9,810	216,618	(27)	226,401
Selling, general and administrative	3,415	13,374	119,059	(1)	135,847
Total operating expenses	3,415	23,184	335,677	(28)	362,248
Other income, net	821	11,040	902	(2,258)	10,505
Interest expense on external borrowings	—	(14,085)	(96)	—	(14,181)
Other expenses, net	(145,429)	(276)	(13,166)	158,661	(210)
Loss from continuing operations before tax benefit	(148,023)	(12,533)	(233,566)	156,403	(237,719)
Income tax benefit	(3,016)	(4,047)	(88,138)	—	(95,201)
Net loss from continuing operations	(145,007)	(8,486)	(145,428)	156,403	(142,518)
Net loss from discontinued operations	—	(2,489)	—	—	(2,489)
Net loss	(145,007)	(10,975)	(145,428)	156,403	(145,007)
Other comprehensive loss	(7,974)	(7,257)	(7,974)	15,231	(7,974)
Comprehensive loss	$ (152,981)	$ (18,232)	$ (153,402)	$ 171,634	$ (152,981)

Six months ended October 31, 2016	H&R Block, Inc. (Guarantor)	Block Financial (Issuer)	Other Subsidiaries	Eliminations	Consolidated H&R Block
Total revenues	$ —	$ 26,438	$ 230,223	$ (144)	$ 256,517
Cost of revenues	—	14,272	422,660	(144)	436,788
Selling, general and administrative	—	4,212	208,263	—	212,475
Total operating expenses	—	18,484	630,923	(144)	649,263
Other income, net	—	5,935	6,323	(7,110)	5,148
Interest expense on external borrowings	—	(43,562)	(524)	—	(44,086)
Other expenses, net	(273,435)	(3,902)	(29,147)	306,150	(334)
Loss from continuing operations before tax benefit	(273,435)	(33,575)	(424,048)	299,040	(432,018)
Income tax benefit	(3,542)	(11,756)	(152,279)	—	(167,577)
Net loss from continuing operations	(269,893)	(21,819)	(271,769)	299,040	(264,441)
Net loss from discontinued operations	—	(5,451)	(1)	—	(5,452)
Net loss	(269,893)	(27,270)	(271,770)	299,040	(269,893)
Other comprehensive loss	(5,889)	—	(5,889)	5,889	(5,889)
Comprehensive loss	$ (275,782)	$ (27,270)	$ (277,659)	$ 304,929	$ (275,782)

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CONDENSED CONSOLIDATING STATEMENTS OF OPERATIONS (in 000s)

Six months ended October 31, 2015	H&R Block, Inc. (Guarantor)	Block Financial (Issuer)	Other Subsidiaries	Eliminations	Consolidated H&R Block
Total revenues	$ —	$ 38,739	$ 227,515	$ (121)	$ 266,133
Cost of revenues	—	21,565	418,464	(120)	439,909
Selling, general and administrative	3,415	17,750	212,875	(1)	234,039
Total operating expenses	3,415	39,315	631,339	(121)	673,948
Other income, net	1,730	11,535	1,456	(3,783)	10,938
Interest expense on external borrowings	—	(22,521)	(235)	—	(22,756)
Other expenses, net	(248,022)	(744)	(25,421)	268,992	(5,195)
Loss from continuing operations before tax benefit	(249,707)	(12,306)	(428,024)	265,209	(424,828)
Income tax benefit	(5,041)	(761)	(180,003)	—	(185,805)
Net loss from continuing operations	(244,666)	(11,545)	(248,021)	265,209	(239,023)
Net loss from discontinued operations	—	(5,643)	—	—	(5,643)
Net loss	(244,666)	(17,188)	(248,021)	265,209	(244,666)
Other comprehensive loss	(17,948)	(8,444)	(17,948)	26,392	(17,948)
Comprehensive loss	$ (262,614)	$ (25,632)	$ (265,969)	$ 291,601	$ (262,614)

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CONDENSED CONSOLIDATING BALANCE SHEETS (in 000s)

As of October 31, 2016	H&R Block, Inc. (Guarantor)	Block Financial (Issuer)	Other Subsidiaries	Eliminations	Consolidated H&R Block
Cash & cash equivalents	$ —	$ 1,965	$ 230,545	$ —	$ 232,510
Cash & cash equivalents - restricted	—	29,014	80,524	—	109,538
Receivables, net	—	73,675	31,089	—	104,764
Prepaid expenses and other current assets	—	8,237	65,318	—	73,555
Mortgage loans held for sale	—	183,107	—	—	183,107
Total current assets	—	295,998	407,476	—	703,474
Property and equipment, net	—	92	292,968	—	293,060
Intangible assets, net	—	—	433,135	—	433,135
Goodwill	—	—	477,360	—	477,360
Deferred tax assets and income taxes receivable	1,947	62,722	17,086	—	81,755
Investments in subsidiaries	1,460,925	—	81,868	(1,542,793)	—
Amounts due from affiliates	—	1,696,151	2,005,485	(3,701,636)	—
Other noncurrent assets	—	58,636	34,758	—	93,394
Total assets	$ 1,462,872	$ 2,113,599	$ 3,750,136	$ (5,244,429)	$ 2,082,178
Accounts payable and accrued expenses	$ 8,941	$ 8,434	$ 122,433	$ —	$ 139,808
Accrued salaries, wages and payroll taxes	—	2,143	38,611	—	40,754
Accrued income taxes and reserves for uncertain tax positions	—	—	68,832	—	68,832
Current portion of long-term debt	—	—	903	—	903
Deferred revenue and other current liabilities	—	48,176	136,384	—	184,560
Total current liabilities	8,941	58,753	367,163	—	434,857
Long-term debt and line of credit borrowings	—	1,961,085	6,121	—	1,967,206
Deferred tax liabilities and reserves for uncertain tax positions	5,917	10,786	100,850	—	117,553
Deferred revenue and other noncurrent liabilities	—	1,107	118,926	—	120,033
Amounts due to affiliates	2,005,485	—	1,696,151	(3,701,636)	—
Total liabilities	2,020,343	2,031,731	2,289,211	(3,701,636)	2,639,649
Stockholders' equity (deficiency)	(557,471)	81,868	1,460,925	(1,542,793)	(557,471)
Total liabilities and stockholders' equity	$ 1,462,872	$ 2,113,599	$ 3,750,136	$ (5,244,429)	$ 2,082,178

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CONDENSED CONSOLIDATING BALANCE SHEETS (in 000s)

As of October 31, 2015	H&R Block, Inc. (Guarantor)	Block Financial (Issuer)	Other Subsidiaries	Eliminations	Consolidated H&R Block
Cash & cash equivalents	$ —	$ 6,864	$ 353,817	$ —	$ 360,681
Cash & cash equivalents - restricted	—	—	42,781	—	42,781
Receivables, net	187	74,835	19,738	—	94,760
Deferred tax assets and income taxes receivable	—	82,862	63,050	—	145,912
Prepaid expenses and other current assets	—	8,236	72,528	—	80,764
Total current assets	187	172,797	551,914	—	724,898
Mortgage loans held for investment, net	—	220,671	—	—	220,671
Property and equipment, net	—	186	298,416	—	298,602
Intangible assets, net	—	—	466,224	—	466,224
Goodwill	—	—	442,068	—	442,068
Deferred tax assets and income taxes receivable	—	41,328	—	(30,064)	11,264
Investments in subsidiaries	1,105,707	—	90,350	(1,196,057)	—
Amounts due from affiliates	—	1,334,559	1,128,832	(2,463,391)	—
Other noncurrent assets	—	78,846	35,900	—	114,746
Total assets	$ 1,105,894	$ 1,848,387	$ 3,013,704	$ (3,689,512)	$ 2,278,473
Accounts payable and accrued expenses	$ 4,305	$ 12,048	$ 124,717	$ —	$ 141,070
Accrued salaries, wages and payroll taxes	—	1,657	35,855	—	37,512
Accrued income taxes and reserves for uncertain tax positions	—	51,385	16,347	—	67,732
Current portion of long-term debt	—	—	808	—	808
Deferred revenue and other current liabilities	—	181,519	137,907	—	319,426
Total current liabilities	4,305	246,609	315,634	—	566,548
Long-term debt and line of credit borrowings	—	1,483,487	7,027	—	1,490,514
Deferred tax liabilities and reserves for uncertain tax positions	—	26,737	143,866	(30,064)	140,539
Deferred revenue and other noncurrent liabilities	—	1,204	106,911	—	108,115
Amounts due to affiliates	1,128,832	—	1,334,559	(2,463,391)	—
Total liabilities	1,133,137	1,758,037	1,907,997	(2,493,455)	2,305,716
Stockholders' equity (deficiency)	(27,243)	90,350	1,105,707	(1,196,057)	(27,243)
Total liabilities and stockholders' equity	$ 1,105,894	$ 1,848,387	$ 3,013,704	$ (3,689,512)	$ 2,278,473

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CONDENSED CONSOLIDATING BALANCE SHEETS					(in 000s)
As of April 30, 2016	H&R Block, Inc. (Guarantor)	Block Financial (Issuer)	Other Subsidiaries	Eliminations	Consolidated H&R Block
Cash & cash equivalents	$ —	$ 9,025	$ 887,776	$ —	$ 896,801
Cash & cash equivalents - restricted	—	29,004	75,106	—	104,110
Receivables, net	—	71,882	81,234	—	153,116
Prepaid expenses and other current assets	—	6,925	59,649	—	66,574
Total current assets	—	116,836	1,103,765	—	1,220,601
Mortgage loans held for investment, net	—	202,385	—	—	202,385
Property and equipment, net	—	136	293,429	—	293,565
Intangible assets, net	—	—	433,885	—	433,885
Goodwill	—	—	470,757	—	470,757
Deferred tax assets and income taxes receivable	5,917	77,270	36,936	—	120,123
Investments in subsidiaries	1,738,643	—	108,995	(1,847,638)	—
Amounts due from affiliates	—	1,307,612	1,714,009	(3,021,621)	—
Other noncurrent assets	—	62,806	43,103	—	105,909
Total assets	$ 1,744,560	$ 1,767,045	$ 4,204,879	$ (4,869,259)	$ 2,847,225
Accounts payable and accrued expenses	$ 1,531	$ 18,596	$ 239,459	$ —	$ 259,586
Accrued salaries, wages and payroll taxes	—	1,766	160,020	—	161,786
Accrued income taxes and reserves for uncertain tax positions	—	52,976	320,778	—	373,754
Current portion of long-term debt	—	—	826	—	826
Deferred revenue and other current liabilities	—	87,982	155,671	—	243,653
Total current liabilities	1,531	161,320	876,754	—	1,039,605
Long-term debt and line of credit borrowings	—	1,484,766	6,609	—	1,491,375
Deferred tax liabilities and reserves for uncertain tax positions	5,917	10,786	116,257	—	132,960
Deferred revenue and other noncurrent liabilities	—	1,178	159,004	—	160,182
Amounts due to affiliates	1,714,009	—	1,307,612	(3,021,621)	—
Total liabilities	1,721,457	1,658,050	2,466,236	(3,021,621)	2,824,122
Stockholders' equity	23,103	108,995	1,738,643	(1,847,638)	23,103
Total liabilities and stockholders' equity	$ 1,744,560	$ 1,767,045	$ 4,204,879	$ (4,869,259)	$ 2,847,225

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CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS (in 000s)

Six months ended October 31, 2016	H&R Block, Inc. (Guarantor)	Block Financial (Issuer)	Other Subsidiaries	Eliminations	Consolidated H&R Block
Net cash used in operating activities:	$ —	$ (77,916)	$ (647,881)	$ —	$ (725,797)
Cash flows from investing:					
Sales, maturities of and payments received on AFS securities	—	144	—	—	144
Principal payments on mortgage loans, net	—	16,706	—	—	16,706
Capital expenditures	—	(5)	(44,913)	—	(44,918)
Payments made for business acquisitions, net of cash acquired	—	—	(36,151)	—	(36,151)
Loans made to franchisees	—	(10,064)	(107)	—	(10,171)
Repayments from franchisees	—	14,052	211	—	14,263
Intercompany borrowings (payments)	—	(426,824)	(309,852)	736,676	—
Other, net	—	1,847	2,489	—	4,336
Net cash used in investing activities	—	(404,144)	(388,323)	736,676	(55,791)
Cash flows from financing:					
Repayments of line of credit borrowings	—	(50,000)	—	—	(50,000)
Proceeds from line of credit borrowings	—	525,000	—	—	525,000
Dividends paid	(95,971)	—	—	—	(95,971)
Repurchase of common stock, including shares surrendered	(215,511)	—	—	—	(215,511)
Proceeds from exercise of stock options	1,630	—	—	—	1,630
Intercompany borrowings (payments)	309,852	—	426,824	(736,676)	—
Other, net	—	—	(43,734)	—	(43,734)
Net cash provided by financing activities	—	475,000	383,090	(736,676)	121,414
Effects of exchange rates on cash	—	—	(4,117)	—	(4,117)
Net decrease in cash and cash equivalents	—	(7,060)	(657,231)	—	(664,291)
Cash and cash equivalents at beginning of the period	—	9,025	887,776	—	896,801
Cash and cash equivalents at end of the period	$ —	$ 1,965	$ 230,545	$ —	$ 232,510

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CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS (in 000s)

Six months ended October 31, 2015	H&R Block, Inc. (Guarantor)	Block Financial (Issuer)	Other Subsidiaries	Eliminations	Consolidated H&R Block
Net cash provided by (used in) operating activities:	$ —	$ 36,078	$ (638,791)	$ —	$ (602,713)
Cash flows from investing:					
Sales, maturities of and payments received on AFS securities	—	430,460	3,801	—	434,261
Principal payments on mortgage loans, net	—	17,006	—	—	17,006
Capital expenditures	—	(20)	(38,759)	—	(38,779)
Payments made for business acquisitions, net of cash acquired	—	—	(61,846)	—	(61,846)
Loans made to franchisees	—	(10,206)	(75)	—	(10,281)
Repayments from franchisees	—	17,301	172	—	17,473
Intercompany borrowings (payments)	—	(1,200,465)	(1,611,564)	2,812,029	—
Other, net	—	4,854	2,392	—	7,246
Net cash provided by (used in) investing activities	—	(741,070)	(1,705,879)	2,812,029	365,080
Cash flows from financing:					
Proceeds from long-term debt	—	996,831	—	—	996,831
Customer banking deposits, net	—	(327,145)	—	440	(326,705)
Transfer of HRB Bank deposits	—	(419,028)	—	—	(419,028)
Dividends paid	(110,338)	—	—	—	(110,338)
Repurchase of common stock, including shares surrendered	(1,517,786)	—	—	—	(1,517,786)
Proceeds from exercise of stock options	16,875	—	—	—	16,875
Intercompany borrowings (payments)	1,611,564	—	1,200,465	(2,812,029)	—
Other, net	(315)	(16,879)	(20,626)	—	(37,820)
Net cash provided by (used in) financing activities	—	233,779	1,179,839	(2,811,589)	(1,397,971)
Effects of exchange rates on cash	—	—	(10,905)	—	(10,905)
Net decrease in cash and cash equivalents	—	(471,213)	(1,175,736)	440	(1,646,509)
Cash and cash equivalents at beginning of the period	—	478,077	1,529,553	(440)	2,007,190
Cash and cash equivalents at end of the period	$ —	$ 6,864	$ 353,817	$ —	$ 360,681

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Our subsidiaries provide assisted and do-it-yourself (DIY) tax return preparation through multiple channels (including in-person, online and mobile applications, and desktop software) and distribute the H&R Block-branded financial products and services of our financial partners. Tax returns are either prepared by H&R Block tax professionals (in company-owned or franchise offices or virtually via the internet) or prepared and filed by our clients through our DIY tax solutions. We operate as a single segment that includes all of our continuing operations, which are designed to enable clients to obtain tax preparation and related services seamlessly.

RECENT DEVELOPMENTS

REFUND ADVANCE LOANS – We will offer interest-free Refund Advance loans during the 2017 tax season. The loans will be made available to eligible assisted U.S. tax preparation clients of the Company and participating franchise locations. On October 25, 2016, subsidiaries of the Company entered into a Refund Advance Program Agreement with MetaBank, a federal savings bank (MetaBank), and Specialty Consumer Services, L.P., a Texas limited partnership (SCS), pursuant to which MetaBank will originate Refund Advance loans and SCS will provide technology, software, and underwriting support services. MetaBank and BofI will provide funding for the loans, with BofI also performing certain disbursement and repayment services. The aggregate funding capacity for the loans being provided by MetaBank and BofI was initially $1.45 billion, but has subsequently been increased to $1.65 billion.

The Refund Advance loans will be offered in amounts of $500, $750 or $1,250, based on client eligibility as determined by the loan originator. We will pay loan origination fees to MetaBank based on volume and customer type and expect to pay approximately $32 to $36 on average for each funded loan. The loan origination fees are intended to cover expected loan losses and payments to capital providers, among other items. In addition, Block Financial has provided MetaBank and BofI with limited guarantees up to $73 million in the aggregate, subject to specified thresholds, which would cover certain incremental loan losses. We expect that only an immaterial amount of the guarantees will be called upon under anticipated loss scenarios.

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RESULTS OF OPERATIONS

A summary of the financial results for our operations is as follows:

Consolidated – Financial Results			(in 000s)	
Three months ended October 31,	2016	2015	$ Change	% Change
Revenues:				
U.S. assisted tax preparation fees	$35,339	$36,403	$(1,064)	(2.9)%
U.S. royalties	6,828	6,680	148	2.2 %
U.S. DIY tax preparation fees	3,089	3,469	(380)	(11.0)%
International revenues	43,539	40,071	3,468	8.7 %
Revenues from Refund Transfers	757	821	(64)	(7.8)%
Revenues from Emerald Card®	8,644	9,808	(1,164)	(11.9)%
Revenues from Peace of Mind® Extended Service Plan	22,689	19,325	3,364	17.4 %
Interest and fee income on Emerald Advance	655	417	238	57.1 %
Other	9,792	11,421	(1,629)	(14.3)%
Total revenues	131,332	128,415	2,917	2.3 %
Compensation and benefits:				
Field wages	50,096	53,525	(3,429)	(6.4)%
Other wages	42,207	46,127	(3,920)	(8.5)%
Benefits and other compensation	23,718	24,635	(917)	(3.7)%
	116,021	124,287	(8,266)	(6.7)%
Occupancy and equipment	99,037	94,997	4,040	4.3 %
Marketing and advertising	12,001	12,965	(964)	(7.4)%
Depreciation and amortization	45,750	42,349	3,401	8.0 %
Bad debt	(131)	1,182	(1,313)	**
Supplies	4,937	4,728	209	4.4 %
Other	61,739	81,740	(20,001)	(24.5)%
Total operating expenses	339,354	362,248	(22,894)	(6.3)%
Other income	2,180	10,505	(8,325)	(79.2)%
Interest expense on borrowings	(22,620)	(14,181)	(8,439)	(59.5)%
Other expenses	(7)	(210)	203	96.7 %
Pretax loss	(228,469)	(237,719)	9,250	3.9 %
Income tax benefit	(85,054)	(95,201)	10,147	10.7 %
Net loss from continuing operations	(143,415)	(142,518)	(897)	(0.6)%
Net loss from discontinued operations	(2,805)	(2,489)	(316)	(12.7)%
Net loss	$(146,220)	$(145,007)	(1,213)	(0.8)%
Basic and diluted loss per share:				
Continuing operations	$(0.67)	$(0.54)	$(0.13)	(24.1)%
Discontinued operations	(0.01)	(0.01)	—	— %
Consolidated	$(0.68)	$(0.55)	$(0.13)	(23.6)%
EBITDA from continuing operations [(1)]	$(160,099)	$(181,145)	$21,046	11.6 %
EBITDA from continuing operations - adjusted [(1)]	(160,676)	(168,760)	$8,084	4.8 %

(1) See "Non-GAAP Financial Information" at the end of this item for a reconciliation of non-GAAP measures.

Three months ended October 31, 2016 compared to October 31, 2015

Revenues increased $2.9 million, or 2.3%, over the prior year. U.S. assisted tax preparation fees declined $1.1 million, or 2.9%, primarily due to lower tax return volumes, which were partially offset by improved rate and mix.

Revenues from our international operations increased $3.5 million, or 8.7%, primarily due to foreign currency exchange rates.
Revenues from fees for POM increased $3.4 million, or 17.4%, due to an increase in units sold and changes in the timing of forecasted claims.
Total operating expenses decreased $22.9 million, or 6.3%, from the prior year. Compensation and benefits decreased $8.3 million, or 6.7%, primarily due to reduced headcount in our offices and corporate operations. Occupancy costs increased $4.0 million, or 4.3%, and depreciation and amortization expense increased $3.4 million, or 8.0%, primarily due to acquisitions of franchisee and competitor businesses. Other expenses decreased $20.0 million, or 24.5%, primarily due to prior year costs related to changes in our capital structure and the divestiture of H&R Block Bank (HRB Bank). We also saw favorable declines in consulting expenses. These reductions were partially offset by higher POM claims.
Interest expense on borrowings increased $8.4 million due to the issuance of $1.0 billion in Senior Notes in September 2015. Other income decreased $8.3 million primarily due to the sale of AFS securities in the prior year of $8.4 million offset by the change in presentation of our mortgage loan portfolio, as discussed in Item 1, note 9 to the consolidated financial statements.
See Item 1, note 8 to the consolidated financial statements for discussion of the impact of income taxes for the period.

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Consolidated – Financial Results			(in 000s)	
Six months ended October 31,	2016	2015	$ Change	% Change
Revenues:				
U.S. assisted tax preparation fees	$60,768	$63,688	$(2,920)	(4.6)%
U.S. royalties	13,353	13,406	(53)	(0.4)%
U.S. DIY tax preparation fees	6,003	6,648	(645)	(9.7)%
International revenues	82,414	80,665	1,749	2.2%
Revenues from Refund Transfers	3,991	2,992	999	33.4%
Revenues from Emerald Card®	21,709	25,497	(3,788)	(14.9)%
Revenues from Peace of Mind® Extended Service Plan	49,720	47,028	2,692	5.7%
Interest and fee income on Emerald Advance	1,459	731	728	99.6%
Other	17,100	25,478	(8,378)	(32.9)%
Total revenues	256,517	266,133	(9,616)	(3.6)%
Compensation and benefits:				
Field wages	95,139	99,463	(4,324)	(4.3)%
Other wages	84,307	87,996	(3,689)	(4.2)%
Benefits and other compensation	46,452	47,286	(834)	(1.8)%
	225,898	234,745	(8,847)	(3.8)%
Occupancy and equipment	193,408	184,796	8,612	4.7%
Marketing and advertising	19,562	21,496	(1,934)	(9.0)%
Depreciation and amortization	87,032	82,443	4,589	5.6%
Bad debt	1,286	3,187	(1,901)	(59.6)%
Supplies	7,014	7,127	(113)	(1.6)%
Other	115,063	140,154	(25,091)	(17.9)%
Total operating expenses	649,263	673,948	(24,685)	(3.7)%
Other income	5,148	10,938	(5,790)	(52.9)%
Interest expense on borrowings	(44,086)	(22,756)	(21,330)	(93.7)%
Other expenses	(334)	(5,195)	4,861	93.6%
Pretax loss	(432,018)	(424,828)	(7,190)	(1.7)%
Income tax benefit	(167,577)	(185,805)	18,228	9.8%
Net loss from continuing operations	(264,441)	(239,023)	(25,418)	(10.6)%
Net loss from discontinued operations	(5,452)	(5,643)	191	3.4%
Net loss	$(269,893)	$(244,666)	$(25,227)	(10.3)%
Basic and diluted loss per share:				
Continuing operations	$(1.21)	$(0.88)	$(0.33)	(37.5)%
Discontinued operations	(0.03)	(0.02)	(0.01)	(50.0)%
Consolidated	$(1.24)	$(0.90)	$(0.34)	(37.8)%
EBITDA from continuing operations [1]	$(300,900)	$(319,449)	$18,549	5.8%
EBITDA from continuing operations - adjusted [1]	(300,665)	(306,106)	$5,441	1.8%

(1) See "Non-GAAP Financial Information" at the end of this item for a reconciliation of non-GAAP measures.

Six months ended October 31, 2016 compared to October 31, 2015

Revenues decreased $9.6 million, or 3.6%, over the prior year. U.S. assisted tax preparation fees declined $2.9 million, or 4.6%, primarily due to lower tax return volumes, which were partially offset by improved rate and mix. Revenues in our international operations were up primarily due to foreign currency exchange rates.

Revenues from H&R Block Emerald Prepaid MasterCard® transactions decreased $3.8 million, or 14.9%, primarily due to our agreement with BofI and lower assisted return volumes.

Revenues from fees for POM increased $2.7 million, or 5.7%, due to an increase in units sold and favorable changes in the timing of forecasted claims.

Other revenues declined $8.4 million, or 32.9%, primarily due to the presentation of income from our mortgage loan portfolio and investments in AFS securities as other income in the current year rather than as revenue in the prior year.

Total operating expenses decreased $24.7 million, or 3.7%, from the prior year. Compensation and benefits decreased $8.8 million, or 3.8%, primarily due to reduced headcount in our offices and corporate operations. Occupancy costs increased $8.6 million, or 4.7%, and depreciation and amortization expense increased $4.6 million, or 5.6%, primarily due to acquisitions of franchisee and competitor businesses. Other expenses decreased $25.1 million, or 17.9%, primarily due to the prior year including fees related to changes in our capital structure and the divestiture of HRB Bank. We also saw favorable declines in consulting and travel expenses. These reductions were partially offset by additional POM claims.

Other income decreased $5.8 million primarily due to the sale of AFS securities in the prior year of $8.4 million offset by the change in presentation of our mortgage loan portfolio. Other expenses declined $4.9 million primarily due to a decrease in foreign currency exchange losses.

Interest expense on borrowings increased $21.3 million, or 93.7%, due to the issuance of $1.0 billion in Senior Notes in September 2015, as discussed in Item 1, note 6 to the consolidated financial statements.

See Item 1, note 8 to the consolidated financial statements for discussion of the impact of income taxes for the period.

DISCONTINUED OPERATIONS

Discontinued operations include our discontinued mortgage operations.

CONTINGENT LOSSES – SCC has accrued a liability as of October 31, 2016, for estimated contingent losses arising from representation and warranty claims of $25.5 million. See Item 1, note 12 to the consolidated financial statements for changes in this accrual. The estimate of accrued loss is based on the best information currently available, significant management judgment, and a number of factors that are subject to change, including developments in case law and other factors. Changes in any one of these factors could significantly impact the estimate.

Losses may also be incurred with respect to various indemnification claims by underwriters, depositors and securitization trustees in securitization transactions in which SCC participated. SCC has not concluded that a loss is probable or reasonably estimable related to these indemnification claims, therefore there is no accrued liability for these contingent losses as of October 31, 2016.

See additional discussion in Item 1A, "Risk Factors" and Item 7, under "Critical Accounting Estimates" in our Annual Report on Form 10-K.

FINANCIAL CONDITION

These comments should be read in conjunction with the consolidated balance sheets and consolidated statements of cash flows included in Part 1, Item 1.

CAPITAL RESOURCES AND LIQUIDITY – OVERVIEW – Our primary sources of capital and liquidity include cash from operations (including changes in working capital), draws on our 2016 CLOC, and issuances of debt. We use our sources of liquidity primarily to fund working capital, service and repay debt, pay dividends, repurchase shares of our common stock, and acquire businesses.

Our operations are highly seasonal and substantially all of our revenues and cash flow are generated during the period from January through April. Therefore, we require the use of cash to fund losses from May through December, and typically rely on available cash balances from the prior tax season and borrowings to meet our off-season liquidity needs.

Given the likely availability of a number of liquidity options discussed herein, we believe that, in the absence of any unexpected developments, our existing sources of capital as of October 31, 2016 are sufficient to meet our operating and financing needs.

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DISCUSSION OF CONSOLIDATED STATEMENTS OF CASH FLOWS – The following table summarizes our statements of cash flows for the six months ended October 31, 2016 and 2015. See Item 1 for the complete consolidated statements of cash flows for these periods.

	(in 000s)	
Six months ended October 31,	2016	2015
Net cash provided by (used in):		
Operating activities	$(725,797)	$(602,713)
Investing activities	(55,791)	365,080
Financing activities	121,414	(1,397,971)
Effects of exchange rates on cash	(4,117)	(10,905)
Net change in cash and cash equivalents	$(664,291)	$(1,646,509)

Operating Activities. Cash used in operations increased, primarily due to higher restricted cash balances and settlement payments related to representation and warranty claims.

Investing Activities. Cash used in investing activities totaled $55.8 million for the six months ended October 31, 2016 compared to $365.1 million provided by investing activities in the prior year period. This change resulted from cash received on our AFS securities in the prior year, offset by a decrease of $25.7 million in payments for business acquisitions.

Financing Activities. Cash provided by financing activities totaled $121.4 million for the six months ended October 31, 2016 compared to a use of $1.4 billion in the prior year period. Changes in cash from financing activities resulted primarily from share repurchase activity, prior year changes in customer deposit balances and borrowings.

CASH REQUIREMENTS –

Dividends and Share Repurchases. Returning capital to shareholders in the form of dividends and the repurchase of outstanding shares has historically been a significant component of our capital allocation plan.

We have consistently paid quarterly dividends. Dividends paid totaled $96.0 million and $110.3 million for the six months ended October 31, 2016 and 2015, respectively. The decline from the prior year is due to lower outstanding shares as a result of share repurchase activity. Although we have historically paid dividends and plan to continue to do so, there can be no assurances that circumstances will not change in the future that could affect our ability or decisions to pay dividends.

In September 2015, we announced that our Board of Directors approved a $3.5 billion share repurchase program, effective through June 2019. As a part of the repurchase program, during the six months ended October 31, 2016, we purchased $217.0 million of our common stock at an average price of $22.51 per share. See Item 1, note 2 to the consolidated financial statements for additional information. As of October 31, 2016, payment of $7.1 million related to 0.3 million shares had not yet settled and was accrued as a liability on the consolidated balance sheet. Although we may continue to repurchase shares, there is no assurance that we will purchase up to the full board authorization.

Capital Investment. Our business is not capital intensive. Capital expenditures totaled $44.9 million and $38.8 million for the six months ended October 31, 2016 and 2015, respectively. Our capital expenditures relate primarily to recurring improvements to retail offices, as well as investments in computers, software and related assets. In addition to our capital expenditures, we also made payments to acquire franchisee and competitor businesses totaling $36.2 million and $61.8 million for the six months ended October 31, 2016 and 2015, respectively.

FINANCING RESOURCES – Our 2016 CLOC has capacity up to $2.0 billion, and is scheduled to expire in September 2021. See Item 1, note 6 to the consolidated financial statements for discussion of the Senior Notes and our 2016 CLOC. Proceeds under the 2016 CLOC may be used for working capital needs or for other general corporate purposes. We were in compliance with our 2016 CLOC covenants as of October 31, 2016.

We had an outstanding balance of $475.0 million under the 2016 CLOC as of October 31, 2016. Incremental amounts available to borrow under the 2016 CLOC were limited to approximately $948 million as of October 31, 2016, in accordance with the covenant requiring a minimum debt-to-EBITDA ratio of 3.50 to 1.00.

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The following table provides ratings for debt issued by Block Financial as of October 31, 2016 and April 30, 2016:

As of	October 31, 2016			April 30, 2016		
	Short-term	Long-term	Outlook	Short-term	Long-term	Outlook
Moody's	P-3	Baa3	Stable	P-3	Baa3	Stable
S&P	A-2	BBB	Negative	A-2	BBB	Stable

Other than as described above, there have been no material changes in our borrowings from those reported as of April 30, 2016 in our Annual Report on Form 10-K.

CASH AND OTHER ASSETS – As of October 31, 2016, we held cash and cash equivalents of $232.5 million, including $110.2 million held by our foreign subsidiaries.

In September 2016, our Board of Directors approved a plan to sell our portfolio of mortgage loans. As a result, these loans are presented as held for sale as of October 31, 2016. We expect to close and receive cash proceeds in December 2016 for the value of our mortgage loan portfolio and real estate owned of approximately $190 million, based on indicative bids received from prospective buyers. We anticipate proceeds from the sale of these mortgage loans will be used for general corporate purposes.

Foreign Operations. Seasonal borrowing needs of our Canadian operations are typically funded by our U.S. operations. To mitigate foreign currency exchange rate risk, we sometimes enter into foreign exchange forward contracts. There were no forward contracts outstanding as of October 31, 2016.

We do not currently intend to repatriate any non-borrowed funds held by our foreign subsidiaries.

The impact of changes in foreign exchange rates during the period on our international cash balances resulted in a decrease of $4.1 million during the six months ended October 31, 2016 compared to $10.9 million in the prior year.

CONTRACTUAL OBLIGATIONS AND COMMERCIAL COMMITMENTS – As discussed further in Item 1, note 10 to the consolidated financial statements, we have provided limited guarantees under our Refund Advance Program Agreement of up to $73 million in the aggregate, subject to specified thresholds.

There have been no other material changes in our contractual obligations and commercial commitments from those reported as of April 30, 2016 in our Annual Report on Form 10-K.

REGULATORY ENVIRONMENT – On October 5, 2016, the Consumer Financial Protection Bureau (CFPB) released its final rules regulating prepaid products (Final Rules). The Final Rules take effect on October 1, 2017, with certain provisions phased in over time following that date. The Final Rules make limited changes from the original proposed rules issued in November 2014, which are discussed in Item 1A, “Risk Factors” in our Annual Report on Form 10-K for the fiscal year ended April 30, 2016.

Once effective, the Final Rules will apply to the H&R Block Emerald Prepaid MasterCard®, EAs, and Refund Advance loans. The Final Rules, among other things: (i) establish disclosures required to be made to consumers prior to establishing or purchasing a prepaid account; (ii) require periodic statements or online access to specified account information; (iii) establish certain overdraft protections similar to those required of credit cards; (iv) impose a 30-day waiting period after the time a consumer registers a new prepaid card before the consumer can be offered a separate credit feature; and (v) prohibit the use of funds in a prepaid account to pay an outstanding credit balance, unless the consumer affirmatively opts in to such repayment.

We are in the process of assessing the impact of these changes on the H&R Block Emerald Prepaid MasterCard®, EAs, and Refund Advance loans, and our consolidated financial statements.

There have been no other material changes in our regulatory environment from what was reported as of April 30, 2016 in our Annual Report on Form 10-K.

NON-GAAP FINANCIAL INFORMATION

Non-GAAP financial measures should not be considered as a substitute for, or superior to, measures of financial performance prepared in accordance with GAAP. Because these measures are not measures of financial performance under GAAP and are susceptible to varying calculations, they may not be comparable to similarly titled measures for other companies.

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We consider our non-GAAP financial measures to be performance measures and a useful metric for management and investors to evaluate and compare the ongoing operating performance of our business on a consistent basis across reporting periods, as it eliminates the effect of items that are not indicative of our core operating performance.
The following are descriptions of adjustments we make for our non-GAAP financial measures:
We exclude losses from settlements and estimated contingent losses from litigation and favorable reserve adjustments. This does not include legal defense costs.
We exclude material non-cash charges to adjust the carrying values of goodwill, intangible assets, other long-lived assets and investments to their estimated fair values.
We exclude material severance and other restructuring charges in connection with the termination of personnel, closure of offices and related costs.
We exclude the material gains and losses on business dispositions, including investment banking, legal and accounting fees from both business dispositions and acquisitions.
We exclude the gains and losses on extinguishment of debt.
We may consider whether other significant items that arise in the future should also be excluded from our non-GAAP financial measures.
We measure the performance of our business using a variety of metrics, including earnings before interest, taxes, depreciation and amortization (EBITDA) from continuing operations and adjusted EBITDA from continuing operations, adjusted pretax and net income of continuing operations, and adjusted diluted earnings per share from continuing operations. Adjusted EBITDA from continuing operations, adjusted pretax and net income from continuing operations, and adjusted diluted earnings per share from continuing operations eliminate the impact of items that we do not consider indicative of our core operating performance and, we believe, provide meaningful information to assist in understanding our financial results, analyzing trends in our underlying business, and assessing our prospects for future performance. We also use EBITDA from continuing operations and pretax income of continuing operations, each subject to permitted adjustments, as performance metrics in incentive compensation calculations for our employees.
The following is a reconciliation of EBITDA from continuing operations to net loss:

				(in 000s)
	Three months ended October 31,		Six months ended October 31,	
	2016	2015	2016	2015
Net loss - as reported	$(146,220)	$(145,007)	$(269,893)	$(244,666)
Add back:				
Discontinued operations, net	2,805	2,489	5,452	5,643
Income taxes of continuing operations	(85,054)	(95,201)	(167,577)	(185,805)
Interest expense of continuing operations	22,620	14,225	44,086	22,936
Depreciation and amortization of continuing operations	45,750	42,349	87,032	82,443
	(13,879)	(36,138)	(31,007)	(74,783)
EBITDA from continuing operations	$(160,099)	$(181,145)	$(300,900)	$(319,449)

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The following is a reconciliation of our results from continuing operations to our adjusted results from continuing operations, which are non-GAAP financial measures:

	(in 000s)					
Three months ended October 31,	2016			2015		
	Pretax loss	Net loss	EBITDA	Pretax loss	Net loss	EBITDA
From continuing operations	$(228,469)	$(143,415)	$(160,099)	$(237,719)	$(142,518)	$(181,145)
Adjustments (pretax):						
Loss contingencies - litigation	(577)	(577)	(577)	71	71	71
Costs related to HRB Bank and recapitalization transactions	—	—	—	20,766	20,766	20,766
Gains on AFS securities	—	—	—	(8,426)	(8,426)	(8,426)
Gain on sales of tax offices	—	—	—	(26)	(26)	(26)
Tax effect of adjustments [1]	—	217	—	—	(4,642)	—
	(577)	(360)	(577)	12,385	7,743	12,385
As adjusted - from continuing operations	$(229,046)	$(143,775)	$(160,676)	$(225,334)	$(134,775)	$(168,760)
EPS - as reported		$(0.67)			$(0.54)	
Impact of adjustments		—			0.03	
EPS - adjusted		$(0.67)			$(0.51)	

	(in 000s)					
Six months ended October 31,	2016			2015		
	Pretax loss	Net loss	EBITDA	Pretax loss	Net loss	EBITDA
From continuing operations	$(432,018)	$(264,441)	$(300,900)	$(424,828)	$(239,023)	$(319,449)
Adjustments (pretax):						
Loss contingencies - litigation	235	235	235	689	689	689
Costs related to HRB Bank and recapitalization transactions	—	—	—	20,818	20,818	20,818
Gains on AFS securities	—	—	—	(8,138)	(8,138)	(8,138)
Gain on sales of tax offices	—	—	—	(26)	(26)	(26)
Tax effect of adjustments [1]	—	(85)	—	—	(5,000)	—
	235	150	235	13,343	8,343	13,343
As adjusted - from continuing operations	$(431,783)	$(264,291)	$(300,665)	$(411,485)	$(230,680)	$(306,106)
EPS - as reported		$(1.21)			$(0.88)	
Impact of adjustments		—			0.03	
EPS - adjusted		$(1.21)			$(0.85)	

[1] Tax effect of adjustments is computed as the pretax effect of the adjustments multiplied by our effective tax rate before discrete items.

FORWARD-LOOKING INFORMATION

This report and other documents filed with the Securities and Exchange Commission (SEC) may contain forward-looking statements. In addition, our senior management may make forward-looking statements orally to analysts, investors, the media and others. Forward-looking statements can be identified by the fact that they do not relate strictly to historical or current facts. They often include words or variation of words such as "expects," "anticipates," "intends," "plans," "believes," "seeks," "estimates," "projects," "forecasts," "targets," "would," "will," "should," "could," "may" or other similar expressions. Forward-looking statements provide management's current expectations or predictions of future conditions, events or results. All statements that address operating performance, events or developments that we expect or anticipate will occur in the future are forward-looking statements. They may include estimates of revenues, income, earnings per share, capital expenditures, dividends, stock repurchase, liquidity, capital structure or other financial items, descriptions of management's plans or objectives for future operations, services or products, or descriptions of assumptions underlying any of the above. All forward-looking statements speak only as of the date they are made and reflect the Company's good faith beliefs, assumptions and expectations, but they are not guarantees of future performance or events. Furthermore, the Company disclaims any obligation to publicly update or revise any forward-looking statement to reflect changes in underlying assumptions, factors, or expectations, new information, data or methods, future events or other changes, except as required by law.

By their nature, forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from those suggested by the forward-looking statements. Factors that might cause such differences include, but are not limited to, a variety of economic, competitive, operational and regulatory factors, many of which are beyond the Company's control. Investors should understand that it is not possible to predict or identify all such factors and, consequently, should not consider any such list to be a complete set of all potential risks or uncertainties. Details about risks, uncertainties and assumptions that could affect various aspects of our business are included throughout our Annual Report on Form 10-K for the fiscal year ended April 30, 2016 and are also described from time to time in other filings with the SEC. Investors should carefully consider all of these risks, and should pay particular attention to Item 1A, "Risk Factors," and Item 7 under "Critical Accounting Policies" of our Annual Report on Form 10-K for the fiscal year ended April 30, 2016.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There have been no material changes in our market risks from those reported at April 30, 2016 in our Annual Report on Form 10-K.

ITEM 4. CONTROLS AND PROCEDURES

EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES – As of the end of the period covered by this Form 10-Q, we evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)). The controls evaluation was done under the supervision and with the participation of management, including our Chief Executive Officer and Chief Financial Officer. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were effective as of the end of the period covered by this Quarterly Report on Form 10-Q.

CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING – There were no changes during the last fiscal quarter that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

For a description of our material pending legal proceedings, see discussion in Part I, Item 1, note 11 to the consolidated financial statements.

ITEM 1A. RISK FACTORS

There have been no material changes in our risk factors from those reported at April 30, 2016 in our Annual Report on Form 10-K.

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ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

A summary of our purchases of H&R Block common stock during the second quarter of fiscal year 2017 is as follows:
(in 000s, except per share amounts)

	Total Number of Shares Purchased (1)	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (2)	Maximum Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (2)
August 1 - August 31	—	$ 23.73	—	$ 1,451,435
September 1 - September 30	5,877	$ 21.95	5,876	$ 1,322,548
October 1 - October 31	1,725	$ 22.86	1,725	$ 1,283,125
	7,602	$ 22.16	7,601	

(1) We purchased approximately 1 thousand shares in connection with funding employee income tax withholding obligations arising upon the lapse of restrictions on restricted shares and restricted share units.

(2) In September 2015, we announced that our Board of Directors approved a $3.5 billion share repurchase program, effective through June 2019.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

The following exhibits are numbered in accordance with the Exhibit Table of Item 601 of Regulation S-K:

10.1	First Amended and Restated Credit and Guarantee Agreement dated September 22, 2016, by and among Block Financial LLC, H&R Block, Inc., the lenders party thereto from time to time, and JPMorgan Chase Bank, N.A., as administrative agent, filed as Exhibit 10.1 to the Company's current report on Form 8–K filed September 26, 2016, file number 1–06089, is incorporated herein by reference.
12.1	Computation of Ratio of Earnings to Fixed Charges for H&R Block, Inc.
12.2	Computation of Ratio of Earnings to Fixed Charges for Block Financial LLC.
31.1	Certification by Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification by Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification by Chief Executive Officer pursuant to 18 U.S.C. 1350, as adopted by Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification by Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted by Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema
101.CAL	XBRL Extension Calculation Linkbase
101.LAB	XBRL Taxonomy Extension Label Linkbase
101.PRE	XBRL Taxonomy Extension Presentation Linkbase
101.DEF	XBRL Taxonomy Extension Definition Linkbase

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SIGNATURES

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

H&R BLOCK, INC.

/s/ William C. Cobb
William C. Cobb
President and Chief Executive Officer
December 8, 2016

/s/ Tony G. Bowen
Tony G. Bowen
Chief Financial Officer
December 8, 2016

/s/ Kellie J. Logerwell
Kellie J. Logerwell
Chief Accounting Officer
December 8, 2016