

H&R BLOCK INC
Form 10-Q/A
March 31, 2006

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**SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549**

**FORM 10-Q/A
Amendment No. 1**

(Mark One)

☒ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934**

For the quarterly period ended July 31, 2005

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 1-6089

H&R BLOCK

H&R Block, Inc.

(Exact name of registrant as specified in its charter)

MISSOURI

**(State or other jurisdiction of
incorporation or organization)**

44-0607856

**(I.R.S. Employer
Identification No.)**

4400 Main Street

Kansas City, Missouri 64111

(Address of principal executive offices, including zip code)

(816) 753-6900

(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.

Yes ☒ No ☐

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

Large accelerated filer Yes ☐ Accelerated filer Yes ☐ Non-accelerated filer No ☒

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

Yes ☐ No ☒

The number of shares outstanding of the registrant's Common Stock, without par value, at the close of business on August 31, 2005 was 324,650,475 shares.

H&R BLOCK
Form 10-Q/A for the Period Ended July 31, 2005
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EXPLANATORY NOTE

This Amendment No. 1 on Form 10-Q/A (Form 10-Q/A) to the company's Quarterly Report on Form 10-Q for the quarterly period ended July 31, 2005, initially filed with the Securities and Exchange Commission on September 8, 2005, is being filed to reflect restatements of our consolidated balance sheets at July 31, 2005 and April 30, 2005, consolidated statements of income and comprehensive income for the three months ended July 31, 2005 and 2004, and of cash flows for the three months ended July 31, 2005 and 2004, and the notes related thereto. See detail discussion of the restatements in Item 1, note 2 to the condensed consolidated financial statements.

On February 22, 2006, the Company's management and the Audit Committee of the Board of Directors concluded to restate previously issued consolidated financial statements for the fiscal quarters ended October 31, 2005 and July 31, 2005, the fiscal years ended April 30, 2005 and 2004 and the related fiscal quarters. The Company arrived at this conclusion during the course of its closing process for the quarter ended January 31, 2006.

The restatement pertains primarily to errors in determining the Company's state effective income tax rate, including errors in identifying changes in state apportionment, expiring state net operating losses and related factors.

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CONDENSED CONSOLIDATED BALANCE SHEETS**

	(in 000s, except share amounts)	
	Restated July 31, 2005 (Unaudited)	Restated April 30, 2005
ASSETS		
Cash and cash equivalents	\$ 632,801	\$ 1,100,213
Cash and cash equivalents restricted	416,981	516,909
Marketable securities trading	77,085	11,790
Receivables from customers, brokers, dealers and clearing organizations, net	585,214	590,226
Receivables, less allowance for doubtful accounts of \$46,752 and \$38,879	404,501	418,788
Prepaid expenses and other current assets	473,831	432,708
Total current assets	2,590,413	3,070,634
Residual interests in securitizations available-for-sale	193,207	205,936
Beneficial interest in Trusts trading	185,539	215,367
Mortgage servicing rights	188,708	166,614
Property and equipment, at cost less accumulated depreciation and amortization of \$677,989 and \$658,425	328,684	330,150
Intangible assets, net	232,242	247,092
Goodwill, net	1,018,632	1,015,947
Other assets	278,529	286,316
Total assets	\$ 5,015,954	\$ 5,538,056

LIABILITIES AND STOCKHOLDERS' EQUITY**Liabilities:**

Current portion of long-term debt	\$ 25,854	\$ 25,545
Accounts payable to customers, brokers and dealers	871,715	950,684
Accounts payable, accrued expenses and other current liabilities	497,215	564,749
Accrued salaries, wages and payroll taxes	161,661	318,644
Accrued income taxes	372,114	375,174
Total current liabilities	1,928,559	2,234,796
Long-term debt	923,145	923,073
Other noncurrent liabilities	368,028	430,919
Total liabilities	3,219,732	3,588,788

Stockholders' equity:

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Common stock, no par, stated value \$.01 per share, 800,000,000 shares authorized, 435,890,796 shares issued at July 31, 2005 and April 30, 2005	4,359	4,359
Additional paid-in capital	601,348	598,388
Accumulated other comprehensive income	63,731	68,718
Retained earnings	3,097,151	3,161,682
Less cost of 106,780,588 and 104,649,850 shares of common stock in treasury	(1,970,367)	(1,883,879)
Total stockholders' equity	1,796,222	1,949,268
Total liabilities and stockholders' equity	\$ 5,015,954	\$ 5,538,056

See Notes to Condensed Consolidated Financial Statements

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H&R BLOCK
CONDENSED CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

	(Unaudited, amounts in 000s, except per share amounts)	
Three months ended July 31,	Restated 2005	Restated 2004
Revenues:		
Service revenues	\$ 315,128	\$ 248,588
Other revenues:		
Gains on sales of mortgage assets, net	236,431	183,360
Interest income	49,253	39,720
Product and other revenues	14,181	14,883
	614,993	486,551
Operating expenses:		
Cost of services	343,218	290,975
Cost of other revenues	123,357	78,395
Selling, general and administrative	189,252	160,196
	655,827	529,566
Operating loss	(40,834)	(43,015)
Interest expense	12,435	17,793
Other income, net	7,400	2,008
Loss before taxes	(45,869)	(58,800)
Income tax benefit	(17,875)	(22,846)
Net loss	\$ (27,994)	\$ (35,954)
Basic and diluted loss per share	\$ (0.08)	\$ (0.11)
Basic and diluted shares	330,714	337,270
Dividends per share	\$ 0.11	\$ 0.10
Comprehensive income (loss):		
Net loss	\$ (27,994)	\$ (35,954)
Change in unrealized gain on available-for-sale securities, net	(5,811)	21,470

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Change in foreign currency translation adjustments	824	(330)
Comprehensive income (loss)	\$ (32,981)	\$ (14,814)

See Notes to Condensed Consolidated Financial Statements

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H&R BLOCK
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	(Unaudited, amounts in 000s)	
	Restated 2005	Restated 2004
Three months ended July 31,		
Cash flows from operating activities:		
Net loss	\$ (27,994)	\$ (35,954)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	44,085	38,908
Accretion of residual interests in securitizations	(30,777)	(28,677)
Impairments of residual interests in securitizations	12,415	2,609
Additions to trading securities residual interests in securitizations	(101,002)	
Proceeds from net interest margin transactions, net	40,371	
Additions to mortgage servicing rights	(49,306)	(28,493)
Amortization and impairment of mortgage servicing rights	27,212	18,334
Net change in beneficial interest in Trusts	29,828	(1,433)
Other, net of acquisitions	(255,347)	(480,626)
Net cash used in operating activities	(310,515)	(515,332)
Cash flows from investing activities:		
Cash received from residual interests in securitizations	24,031	38,826
Purchases of property and equipment, net	(30,330)	(22,714)
Payments made for business acquisitions, net of cash acquired	(3,452)	(806)
Other, net	7,935	8,300
Net cash provided by (used in) investing activities	(1,816)	23,606
Cash flows from financing activities:		
Repayments of commercial paper		(314,836)
Proceeds from issuance of commercial paper		419,700
Dividends paid	(36,537)	(33,636)
Acquisition of treasury shares	(131,642)	(347,395)
Proceeds from issuance of common stock	32,318	12,375
Other, net	(19,220)	(127)
Net cash used in financing activities	(155,081)	(263,919)
Net decrease in cash and cash equivalents	(467,412)	(755,645)
Cash and cash equivalents at beginning of the period	1,100,213	1,072,745
Cash and cash equivalents at end of the period	\$ 632,801	\$ 317,100

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

1. Basis of Presentation

The condensed consolidated balance sheet as of July 31, 2005, the condensed consolidated statements of income and comprehensive income for the three months ended July 31, 2005 and 2004, and the condensed consolidated statements of cash flows for the three months ended July 31, 2005 and 2004 have been prepared by the Company, without audit. In the opinion of management, all adjustments (which include only normal recurring adjustments) necessary to present fairly the financial position, results of operations and cash flows at July 31, 2005 and for all periods presented have been made.

H&R Block, the Company, we, our and us are used interchangeably to refer to H&R Block, Inc. or to H&R Block, Inc. and its subsidiaries, as appropriate to the context.

Certain reclassifications have been made to prior year amounts to conform to the current year presentation. These reclassifications had no effect on our results of operations or stockholders' equity as previously reported. Adjustments related to the restatements of previously issued financial statements are detailed in note 2.

On June 8, 2005, our Board of Directors declared a two-for-one stock split of the Company's Common Stock in the form of a 100% stock distribution, effective August 22, 2005, to shareholders of record as of the close of business on August 1, 2005. All share and per share amounts in this document have been adjusted to reflect the retroactive effect of the stock split.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted. These condensed consolidated financial statements should be read in conjunction with the financial statements and notes thereto included in our April 30, 2005 Annual Report to Shareholders on Form 10-K/A.

Operating revenues of the Tax Services and Business Services segments are seasonal in nature with peak revenues occurring in the months of January through April. Therefore, results for interim periods are not indicative of results to be expected for the full year.

We file our federal and state income tax returns on a calendar year basis. The condensed consolidated income statements reflect the effective tax rates expected to be applicable for the respective full fiscal years.

2. Restatements of Previously Issued Financial Statements

(A) On February 22, 2006, management and the Audit Committee of the Board of Directors concluded to restate previously issued consolidated financial statements for the fiscal quarters ended October 31, 2005 and July 31, 2005, the fiscal years ended April 30, 2005 and 2004 and the related fiscal quarters. We arrived at this conclusion during the course of our closing process for the quarter ended January 31, 2006. This restatement pertains primarily to errors in determining the Company's state effective income tax rate, including errors in identifying changes in state apportionment, expiring state net operating losses and related factors. These errors resulted in an understatement of income tax benefit (net of federal income tax benefit) of \$0.3 million and \$0.8 million for the three months ended July 31, 2005 and 2004, respectively, an overstatement of deferred income tax assets of \$1.2 million as of July 31, 2005 and April 30, 2005, and an understatement of accrued income taxes of \$25.5 million and \$25.9 million as of July 31, 2005 and April 30, 2005, respectively. The effect of the above adjustments on the condensed consolidated financial statements is set forth in 2C below.

(B) On June 7, 2005, management and the Audit Committee of the Board of Directors determined that restatement of our previously issued consolidated financial statements, including financial statements for the three months ended July 31, 2004 was appropriate as a result of the errors noted below. All amounts listed are pretax, unless otherwise noted.

§ An error in calculating the gain on sale of residual interests in fiscal year 2003. This error was corrected by deferring a portion of the gain on sale of residual interests as of the transaction date in fiscal year 2003 and recognizing revenue from the sale as interest income from accretion of residual interests in subsequent periods. Interest income from accretion increased \$3.0 million for the three months ended July 31, 2004.

This correction also decreased impairments of residual

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interests \$0.8 million and increased comprehensive income \$2.4 million for the three months ended July 31, 2004.

- § An error in the calculation of an incentive compensation accrual at our Mortgage Services segment as of April 30, 2004. This error resulted in an overstatement of compensation expense for the three months ended July 31, 2004 of \$12.1 million.
- § An error in accounting for leased properties related to rent holidays and mandatory rent escalation in our Tax Services, Mortgage Services and Investment Services segments. Rent expense was understated for the three months ended July 31, 2004 by \$0.2 million.
- § An error from the capitalization of certain branch office costs at our Investment Services segment, which should have been expensed as incurred. This error resulted in an understatement of occupancy expenses and an overstatement of depreciation expense and capital expenditures, resulting in a net understatement of operating expenses of \$0.1 million for the three months ended July 31, 2004.
- § Errors related to accounting for acquisitions at our Business Services and Investment Services segments, the largest of which was the acquisition of OLDE in fiscal year 2000. Amortization of customer relationships was understated by \$1.8 million and the provision for income taxes was overstated by approximately \$3.7 million for the three months ended July 31, 2004.

The effect of the above adjustments on the condensed consolidated financial statements is set forth in 2C below.

(C) Notes 4, 5, 7, 11, and 13 have been restated to reflect the above described adjustments.

The following is a summary of the impact of the restatement described in 2A above on our condensed consolidated balance sheet as of July 31, 2005:

	(in 000s, except per share amounts)		
	As Previously Reported ⁽¹⁾	Adjustments ⁽²⁾	Restated
Other assets	\$ 279,756	\$ (1,227)	\$ 278,529
Total assets	5,017,181	(1,227)	5,015,954
Accrued income taxes	346,568	25,546	372,114
Total current liabilities	1,903,013	25,546	1,928,559
Total liabilities	3,194,186	25,546	3,219,732
Retained earnings	3,123,924	(26,773)	3,097,151
Total stockholders' equity	1,822,995	(26,773)	1,796,222
Total liabilities and stockholders' equity	5,017,181	(1,227)	5,015,954

- ⁽¹⁾ As reported in our Form 10-Q filed on September 8, 2005 for the three months ended July 31,

2005.

- (2) Adjusted to reflect the restatement described in 2A above.

The following is a summary of the impact of the restatement described in 2A above on our condensed consolidated statement of income and comprehensive income for the three months ended July 31, 2005:

	As Previously Reported (1)	Adjustments (2)	Restated
Income tax benefit	\$ (17,545)	\$ (330)	\$ (17,875)
Net loss	(28,324)	330	(27,994)
Basic and diluted loss per share	\$ (0.09)	\$ 0.01	\$ (0.08)
Comprehensive income (loss)	\$ (33,311)	\$ 330	\$ (32,981)

- (1) As reported in our Form 10-Q filed on September 8, 2005 for the three months ended July 31, 2005.

- (2) Adjusted to reflect the restatement described in 2A above.

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The following is a summary of the impact of the restatements on our condensed consolidated statement of income and comprehensive income for the three months ended July 31, 2004:

	As Previously Reported (1)	Adjustments (2)	As Previously Restated (3)	Adjustments (4)	Restated
Gain on sale of mortgage assets, net	\$ 182,534	\$ 826	\$ 183,360	\$	\$ 183,360
Interest income	36,706	3,014	39,720		39,720
Total revenues	482,711	3,840	486,551		486,551
Total operating expenses	539,490	(9,924)	529,566		529,566
Operating loss	(56,779)	13,764	(43,015)		(43,015)
Loss before taxes	(72,564)	13,764	(58,800)		(58,800)
Income tax benefit	(28,481)	6,423	(22,058)	(788)	(22,846)
Net loss	(44,083)	7,341	(36,742)	788	(35,954)
Basic and diluted loss per share	\$ (.13)	\$ 0.02	\$ (.11)	\$	\$ (.11)
Change in unrealized gain on marketable securities, net	\$ 23,843	\$ (2,373)	\$ 21,470	\$	\$ 21,470
Comprehensive income (loss)	(20,570)	4,968	(15,602)	788	(14,814)

(1) As reported in our Form 10-Q filed on September 8, 2004 for the three months ended July 31, 2004. Amounts have been reclassified to conform to current year presentation. See discussion of reclassifications in note 1.

(2) Adjusted to reflect the restatement described in 2B above, as derived from the Company's Form 10-K/A filed on

August 5, 2005
for the fiscal
year ended
April 30, 2005.

(3) As reported in
our Form 10-Q
filed on
September 8,
2005 for the
three months
ended July 31,
2005.

(4) Adjusted to
reflect the
restatement
described in 2A
above.

The following is a summary of the impact of the restatement described in 2A above on our condensed consolidated statement of cash flows for the three months ended July 31, 2005:

	As Previously Reported ⁽¹⁾	Adjustments ⁽²⁾	Restated
Net loss	\$ (28,324)	\$ 330	\$ (27,994)
Other, net of acquisitions	(255,017)	(330)	(255,347)

(1) As reported in
our Form 10-Q
filed on
September 8,
2005 for the
three months
ended July 31,
2005.

(2) Adjusted to
reflect the
restatement
described in 2A
above.

The following is a summary of the impact of the restatements on our condensed consolidated statement of cash flows for the three months ended July 31, 2004:

(in 000s)

As
Previously

As
Previously

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Three months ended July 31, 2004	Reported (1)	Adjustments (2)	Restated (3)	Adjustments (4)	Restated
Net loss	\$ (44,083)	\$ 7,341	\$ (36,742)	\$ 788	\$ (35,954)
Depreciation and amortization	37,137	1,771	38,908		38,908
Accretion of residual interests in securitizations	(25,663)	(3,014)	(28,677)		(28,677)
Impairment of residual interests in securitizations	3,435	(826)	2,609		2,609
Other, net of acquisitions	(474,367)	(5,471)	(479,838)	(788)	(480,626)
Net cash provided by operating activities	(515,133)	(199)	(515,332)		(515,332)
Purchases of property and equipment, net	(22,913)	199	(22,714)		(22,714)
Net cash provided by (used in) investing activities	23,407	199	23,606		23,606

(1) As reported in our Form 10-Q filed on September 8, 2004 for the three months ended July 31, 2004. Amounts have been reclassified to conform to current year presentation. See discussion of reclassifications in note 1.

(2) Adjusted to reflect the restatement described in 2B above, as derived from the Company's Form 10-K/A filed on August 5, 2005 for the fiscal year ended April 30, 2005.

(3) As reported in our Form 10-Q filed on

September 8,
2005 for the
three months
ended July 31,
2005.

- (4) Adjusted to
reflect the
restatement
described in 2A
above.

The restatements had no impact on our cash flows from financing activities as previously reported.

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Basic earnings (loss) per share is computed using the weighted average shares outstanding during each period. The dilutive effect of potential common shares is included in diluted earnings (loss) per share except in those periods with a loss. Diluted earnings per share excludes the impact of shares of common stock issuable upon the lapse of certain restrictions or the exercise of options to purchase 33.7 million shares and 37.0 million shares of stock for the three months ended July 31, 2005 and 2004, respectively, as the effect would be antidilutive due to the net loss recorded during the periods.

The weighted average shares outstanding for the three months ended July 31, 2005 decreased to 330.7 million from 337.3 million last year, primarily due to our purchases of treasury shares. The effect of these purchases was partially offset by the issuance of treasury shares related to our stock-based compensation plans.

During the three months ended July 31, 2005 and 2004, we issued 2.5 million shares and 1.2 million shares, respectively, of common stock pursuant to the exercise of stock options, employee stock purchases and awards of restricted shares, in accordance with our stock-based compensation plans.

During the three months ended July 31, 2005, we acquired 4.6 million shares of our common stock, of which 4.4 million shares were purchased from third parties with the remaining shares swapped or surrendered to us, at an aggregate cost of \$131.6 million. During the three months ended July 31, 2004, we acquired 14.9 million shares of our common stock, of which 14.8 million shares were purchased from third parties with the remaining shares swapped or surrendered to us, at an aggregate cost of \$347.4 million.

4. Mortgage Banking Activities

Activity related to available-for-sale residual interests in securitizations consists of the following:

		(in 000s) Restated 2004
Three months ended July 31,	2005	
Balance, beginning of period	\$ 205,936	\$ 210,973
Additions from net interest margin (NIM) transactions	2,109	
Cash received	(24,031)	(38,826)
Accretion	30,777	28,677
Impairments of fair value	(11,875)	(2,609)
Other	(330)	
Changes in unrealized holding gains, net	(9,379)	35,067
Balance, end of period	\$ 193,207	\$ 233,282

We sold \$10.8 billion and \$6.7 billion of mortgage loans in whole loan sales to warehouse trusts (Trusts) or other buyers during the three months ended July 31, 2005 and 2004, respectively, with gains totaling \$222.8 million and \$185.3 million, respectively, recorded on these sales.

Trading residual interests valued at \$101.0 million were recorded in connection with the securitizations of mortgage loans during the three months ended July 31, 2005, with net cash proceeds of \$40.4 million received in connection with NIM transactions. Total net additions to residual interests from net interest margin (NIM) transactions for the three months ended July 31, 2005 were \$2.1 million. We did not complete any securitizations or NIM transactions during the three months ended July 31, 2004.

At July 31, 2005, we had \$58.0 million in residual interests classified as trading securities.