

H&R BLOCK INC  
Form 10-Q  
December 07, 2017  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-Q  
(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934  
For the quarterly period ended October 31, 2017

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 1-06089

H&R Block, Inc.

(Exact name of registrant as specified in its charter)

MISSOURI 44-0607856

(State or other jurisdiction of (I.R.S. Employer  
incorporation or organization) Identification No.)

One H&R Block Way, Kansas City, Missouri 64105

(Address of principal executive offices, including zip code)

(816) 854-3000

(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 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).

Yes  No

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

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company   
Emerging growth company

(Do not check if a smaller reporting company)

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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 November 30, 2017: 209,068,915 shares.



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Form 10-Q for the Period Ended October 31, 2017

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## PART I FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

CONSOLIDATED STATEMENTS OF OPERATIONS  
AND COMPREHENSIVE LOSS

|  | Three months ended |                    | (unaudited,<br>in 000s, except<br>per share amounts) |                    |
|--|--------------------|--------------------|--|--------------------|
|  | October 31,        |                    | Six months ended                                     |                    |
|  | 2017               | 2016               | 2017   | 2016               |
| <b>REVENUES:</b>   |                    |                    |  |                    |
| Service revenues   | \$127,923          | \$118,940          | \$252,618  | \$231,324          |
| Royalty, product and other revenues  | 12,931             | 12,392             | 26,038   | 25,193             |
|  | 140,854            | 131,332            | 278,656  | 256,517            |
| <b>OPERATING EXPENSES:</b>   |                    |                    |  |                    |
| Cost of revenues:  |                    |                    |  |                    |
| Compensation and benefits  | 65,884             | 57,728             | 121,476  | 110,083            |
| Occupancy and equipment  | 105,304            | 99,067             | 203,771  | 193,492            |
| Provision for bad debt   | 1,779              | (131)              | 4,238  | 1,286              |
| Depreciation and amortization  | 29,729             | 29,911             | 58,345   | 57,378             |
| Other  | 37,323             | 39,127             | 79,904   | 74,549             |
|  | 240,019            | 225,702            | 467,734  | 436,788            |
| Selling, general and administrative:   |                    |                    |  |                    |
| Marketing and advertising  | 11,562             | 12,001             | 18,666   | 19,562             |
| Compensation and benefits  | 62,138             | 58,293             | 118,511  | 115,815            |
| Depreciation and amortization  | 15,063             | 15,839             | 30,045   | 29,654             |
| Other selling, general and administrative  | 28,083             | 27,519             | 44,873   | 47,444             |
|  | 116,846            | 113,652            | 212,095  | 212,475            |
| Total operating expenses   | 356,865            | 339,354            | 679,829  | 649,263            |
| Other income (expense), net  | 1,011              | 2,173              | 2,231  | 4,814              |
| Interest expense on borrowings   | (21,265)           | (22,620)           | (42,542)   | (44,086)           |
| Loss from continuing operations before income tax benefit  | (236,265)          | (228,469)          | (441,484)  | (432,018)          |
| Income tax benefit   | (87,953)           | (85,054)           | (165,354)  | (167,577)          |
| Net loss from continuing operations  | (148,312)          | (143,415)          | (276,130)  | (264,441)          |
| Net loss from discontinued operations, net of tax benefits of \$3,067 and \$1,644, \$4,672 and \$3,201 | (5,254)            | (2,805)            | (8,003)  | (5,452)            |
| <b>NET LOSS</b>  | <b>\$(153,566)</b> | <b>\$(146,220)</b> | <b>\$(284,133)</b>                                   | <b>\$(269,893)</b> |
| <b>BASIC AND DILUTED LOSS PER SHARE:</b>   |                    |                    |  |                    |
| Continuing operations  | \$(0.71)           | \$(0.67)           | \$(1.33)   | \$(1.21)           |
| Discontinued operations  | (0.03)             | (0.01)             | (0.03)   | (0.03)             |
| Consolidated   | \$(0.74)           | \$(0.68)           | \$(1.36)   | \$(1.24)           |
| <b>DIVIDENDS DECLARED PER SHARE</b>  | <b>\$0.24</b>      | <b>\$0.22</b>      | <b>\$0.48</b>  | <b>\$0.44</b>      |
| <b>COMPREHENSIVE LOSS:</b>   |                    |                    |  |                    |
| Net loss   | \$(153,566)        | \$(146,220)        | \$(284,133)  | \$(269,893)        |
| Unrealized gains (losses) on securities, net of taxes  | (1)                | —                  | 1  | (11)               |

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Unrealized holding gains (losses) arising during  
the period, net of tax benefits of \$ - , \$ - , \$ - and \$6

Change in foreign currency translation adjustments

(1,384 ) (2,318 ) 1,076 (5,878 )

Other comprehensive income (loss)

(1,385 ) (2,318 ) 1,077 (5,889 )

Comprehensive loss

\$(154,951) \$(148,538) \$(283,056) \$(275,782)

See accompanying notes to consolidated financial statements.

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| CONSOLIDATED BALANCE SHEETS  | (unaudited, in 000s, except share and per share amounts) |                  |                  |
|--|--|------------------|------------------|
|  | As of  | October 31, 2017 | October 31, 2016 |
| <b>ASSETS</b>  |  |                  |                  |
| Cash and cash equivalents  | \$ 180,997   | \$ 232,510       | \$ 1,011,331     |
| Cash and cash equivalents - restricted   | 100,665  | 109,538          | 106,208          |
| Receivables, less allowance for doubtful accounts of \$55,265, \$56,062 and \$55,296   | 77,750   | 104,764          | 162,775          |
| Prepaid expenses and other current assets  | 85,204   | 73,555           | 65,725           |
| Mortgage loans held for sale, net of allowance for loan losses of \$5,484  | —  | 183,107          | —                |
| Total current assets   | 444,616  | 703,474          | 1,346,039        |
| Property and equipment, at cost, less accumulated depreciation and amortization of \$728,811, \$647,689 and \$678,161                        | 262,226  | 293,060          | 263,827          |
| Intangible assets, net   | 406,440  | 433,135          | 409,364          |
| Goodwill   | 493,059  | 477,360          | 491,207          |
| Deferred tax assets and income taxes receivable  | 9,205  | 81,755           | 83,728           |
| Other noncurrent assets  | 101,015  | 93,394           | 99,943           |
| Total assets   | \$ 1,716,561   | \$ 2,082,178     | \$ 2,694,108     |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>  |  |                  |                  |
| <b>LIABILITIES:</b>  |  |                  |                  |
| Accounts payable and accrued expenses  | \$ 114,875   | \$ 139,808       | \$ 217,028       |
| Accrued salaries, wages and payroll taxes  | 42,897   | 40,754           | 183,856          |
| Accrued income taxes and reserves for uncertain tax positions  | 43,879   | 68,832           | 348,199          |
| Current portion of long-term debt  | 1,004  | 903              | 981              |
| Deferred revenue and other current liabilities   | 190,522  | 184,560          | 189,216          |
| Total current liabilities  | 393,177  | 434,857          | 939,280          |
| Long-term debt and line of credit borrowings   | 1,493,828  | 1,967,206        | 1,493,017        |
| Reserves for uncertain tax positions   | 138,024  | 117,553          | 159,085          |
| Deferred revenue and other noncurrent liabilities  | 104,305  | 120,033          | 163,609          |
| Total liabilities  | 2,129,334  | 2,639,649        | 2,754,991        |
| <b>COMMITMENTS AND CONTINGENCIES</b>   |  |                  |                  |
| <b>STOCKHOLDERS' EQUITY:</b>   |  |                  |                  |
| Common stock, no par, stated value \$.01 per share, 800,000,000 shares authorized, shares issued of 246,198,878, 250,578,382 and 246,198,878 | 2,462  | 2,506            | 2,462            |
| Additional paid-in capital   | 753,423  | 751,229          | 754,912          |
| Accumulated other comprehensive loss   | (14,222 )  | (17,122 )        | (15,299 )        |
| Retained deficit   | (433,556 )   | (538,242 )       | (48,206 )        |
| Less treasury shares, at cost, of 37,130,454, 39,085,220 and 39,027,573  | (720,880 )   | (755,842 )       | (754,752 )       |
| Total stockholders' equity (deficiency)  | (412,773 )   | (557,471 )       | (60,883 )        |
| Total liabilities and stockholders' equity   | \$ 1,716,561   | \$ 2,082,178     | \$ 2,694,108     |

See accompanying notes to consolidated financial statements.

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| CONSOLIDATED STATEMENTS OF CASH FLOWS                                       | (unaudited, in 000s) |             |
|---|----------------------|-------------|
| Six months ended October 31,  | 2017                 | 2016        |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>                                |                      |             |
| Net loss  | \$(284,133)          | \$(269,893) |
| Adjustments to reconcile net loss to net cash used in operating activities: |                      |             |
| Depreciation and amortization   | 88,390               | 87,032      |
| Provision for bad debt  | 4,238                | 1,286       |
| Deferred taxes  | 58,634               | 6,489       |
| Stock-based compensation  | 11,627               | 12,472      |
| Changes in assets and liabilities, net of acquisitions:                     |                      |             |
| Receivables   | 77,958               | 48,653      |
| Prepaid expenses and other current assets                                   | (19,283 )            | (7,386 )    |
| Other noncurrent assets   | 8,984                | 7,713       |
| Accounts payable and accrued expenses                                       | (85,846 )            | (99,378 )   |
| Accrued salaries, wages and payroll taxes                                   | (141,491 )           | (120,672 )  |
| Deferred revenue and other current liabilities                              | 3,775                | (46,531 )   |
| Deferred revenue and other noncurrent liabilities                           | (60,857 )            | (52,548 )   |
| Income tax receivables, accrued income taxes and income tax reserves        | (296,023 )           | (282,234 )  |
| Other, net  | (14,430 )            | (5,379 )    |
| Net cash used in operating activities                                       | (648,457 )           | (720,376 )  |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>                                |                      |             |
| Principal payments and sales of mortgage loans and real estate owned, net   | —                    | 19,009      |
| Capital expenditures  | (56,750 )            | (44,918 )   |
| Payments made for business acquisitions, net of cash acquired               | (27,522 )            | (36,151 )   |
| Franchise loans funded  | (10,939 )            | (10,171 )   |
| Payments received on franchise loans  | 10,322               | 14,263      |
| Other, net  | 5,474                | 2,177       |
| Net cash used in investing activities                                       | (79,415 )            | (55,791 )   |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>                                |                      |             |
| Repayments of line of credit borrowings                                     | —                    | (50,000 )   |
| Proceeds from line of credit borrowings                                     | —                    | 525,000     |
| Dividends paid  | (100,082 )           | (95,971 )   |
| Repurchase of common stock, including shares surrendered                    | (7,581 )             | (215,511 )  |
| Proceeds from exercise of stock options                                     | 27,522               | 1,630       |
| Other, net  | (26,717 )            | (43,734 )   |
| Net cash provided by (used in) financing activities                         | (106,858 )           | 121,414     |
| Effects of exchange rate changes on cash                                    | (1,147 )             | (4,110 )    |
| Net decrease in cash, cash equivalents and restricted cash                  | (835,877 )           | (658,863 )  |
| Cash, cash equivalents and restricted cash, beginning of period             | 1,117,539            | 1,000,911   |
| Cash, cash equivalents and restricted cash, end of period                   | \$281,662            | \$342,048   |
| <b>SUPPLEMENTARY CASH FLOW DATA:</b>  |                      |             |
| Income taxes paid, net of refunds received                                  | \$76,451             | \$112,339   |
| Interest paid on borrowings   | 39,902               | 40,670      |
| Accrued additions to property and equipment                                 | 3,874                | 12,920      |

|                                  |   |       |
|----------------------------------|---|-------|
| Accrued purchase of common stock | — | 7,143 |
|----------------------------------|---|-------|

See accompanying notes to consolidated financial statements.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**BASIS OF PRESENTATION** – The consolidated balance sheets as of October 31, 2017 and 2016, the consolidated statements of operations and comprehensive loss for the three and six months ended October 31, 2017 and 2016, and the consolidated statements of cash flows for the six months ended October 31, 2017 and 2016 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 as of October 31, 2017 and 2016 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 information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States (GAAP) have been condensed or omitted. These consolidated financial statements should be read in conjunction with the financial statements and notes thereto included in our April 30, 2017 Annual Report to Shareholders on Form 10-K. All amounts presented herein as of April 30, 2017 or for the year then ended are derived from our April 30, 2017 Annual Report to Shareholders on Form 10-K.

**MANAGEMENT ESTIMATES** – The preparation of financial statements in conformity with GAAP requires management to make 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 periods. Significant estimates, assumptions and judgments are applied in the evaluation of contingent losses arising from our discontinued mortgage business, contingent losses associated with pending claims and litigation, reserves for uncertain tax positions and related matters. Estimates have been prepared based on the best information available as of each balance sheet date. As such, actual results could differ materially from those estimates.

**SEASONALITY OF BUSINESS** – Our operating revenues are seasonal in nature with peak revenues typically occurring in the months of February through April. Therefore, results for interim periods are not indicative of results to be expected for the full year.

**DISCONTINUED OPERATIONS** – Our discontinued operations include the results of operations of Sand Canyon Corporation, previously known as Option One Mortgage Corporation (including its subsidiaries, collectively, SCC), which exited its mortgage business in fiscal year 2008. See notes 9 and 10 for additional information on litigation, claims, and other loss contingencies related to our discontinued operations.

**NEW ACCOUNTING PRONOUNCEMENTS** –

**Restricted Cash in Statement of Cash Flows.** In November 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. 2016-18, "Restricted Cash (a consensus of the FASB Emerging Issues Task Force)," (ASU 2016-18). This guidance requires that restricted cash be included with cash and cash equivalents when reconciling the beginning and end-of-period total amounts shown on the statement of cash flows. This guidance must be applied retrospectively to all periods presented. We adopted ASU 2016-18 effective May 1, 2017. All prior periods have been adjusted to conform to the current period presentation, which resulted in a decrease in cash used in operations of \$5.4 million for the six months ended October 31, 2016.

**Stock-Based Compensation.** In March 2016, the FASB issued Accounting Standards Update No. 2016-09, "Improvements to Employee Share-Based Payment Accounting," (ASU 2016-09). This guidance requires that, among other things: (1) all excess tax benefits and tax deficiencies would be recognized as income tax expense or benefit in the income statement; and (2) excess tax benefits would not be separated from other income tax cash flows and, thus, would be classified along with other cash flows as an operating activity. The transition requirements for this guidance varies by component, but the changes applicable to us were applied prospectively. We adopted ASU 2016-09 effective May 1, 2017. We recorded a discrete tax benefit of \$5.2 million related to stock-based compensation during the six months ended October 31, 2017.

**Revenue Recognition.** In May 2014, the FASB issued Accounting Standards Update No. 2014-09, "Revenue from Contracts with Customers," (ASU 2014-09) which is a comprehensive new revenue recognition model that requires

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an entity to recognize the amount of revenue which reflects the consideration it expects to receive in exchange for the transfer of the promised goods or services to customers. This ASU also requires additional disclosure about the nature, amount, timing, and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract, and clarifies guidance for multiple-element arrangements. This guidance will replace most existing revenue recognition guidance in GAAP when it becomes effective. The new standard is effective for us on May 1, 2018. The standard permits the use of either the full retrospective or modified retrospective transition method.

We have substantially completed our evaluation of the impact of ASU 2014-09 on our United States (U.S.) assisted tax preparation fees, U.S. royalties, the online portion of U.S. DIY tax preparation fees, and revenues from Peace of Mind® Extended Service Plan (POM), and based on the preliminary results of our evaluation, we do not expect the application of this guidance to have a material impact on the recognition of revenue related to these services. Changes to our client agreements or service design before adoption of the new standard could change our preliminary conclusions. We are still evaluating the impact of this guidance as it relates to other revenue streams, as well as certain associated expenses. Depending on the results of our review, there could be changes to the classification and timing of recognition of revenues and expenses related to other revenue streams. We currently expect to adopt using the full retrospective transition method, under which we will recast prior periods to comply with this new guidance. We are continuing our assessment, including evaluating the standard's impact on our internal controls.

**NOTE 2: LOSS PER SHARE AND STOCKHOLDERS' EQUITY**

**LOSS PER SHARE** – Basic and diluted loss per share is computed using the two-class method. The two-class method is an earnings allocation formula that determines net income per share for each class of common stock and participating security according to dividends declared and participation rights in undistributed earnings. Per share amounts are computed by dividing net income or loss from continuing operations attributable to common shareholders by the weighted average shares outstanding during each period. The dilutive effect of potential common shares is included in diluted earnings per share except in those periods with a loss from continuing operations. 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 3.4 million shares for the three and six months ended October 31, 2017, and 4.6 million shares for the three and six months ended October 31, 2016, as the effect would be antidilutive due to the net loss from continuing operations during those periods.

The computations of basic and diluted loss per share from continuing operations are as follows:

(in 000s, except per share amounts)

|  | Three months ended<br>October 31, |             | Six months ended<br>October 31, |             |
|--|-----------------------------------|-------------|---------------------------------|-------------|
|  | 2017                              | 2016        | 2017                            | 2016        |
| Net loss from continuing operations attributable to shareholders               | \$(148,312)                       | \$(143,415) | \$(276,130)                     | \$(264,441) |
| Amounts allocated to participating securities                                  | (161)                             | (143)       | (321)                           | (267)       |
| Net loss from continuing operations attributable to common shareholders        | \$(148,473)                       | \$(143,558) | \$(276,451)                     | \$(264,708) |
| Basic weighted average common shares   | 209,065                           | 215,535     | 208,500                         | 218,009     |
| Potential dilutive shares  | —                                 | —           | —                               | —           |
| Dilutive weighted average common shares  | 209,065                           | 215,535     | 208,500                         | 218,009     |
| Loss per share from continuing operations attributable to common shareholders: |                                   |             |                                 |             |
| Basic  | \$(0.71)                          | \$(0.67)    | \$(1.33)                        | \$(1.21)    |
| Diluted  | (0.71)                            | (0.67)      | (1.33)                          | (1.21)      |

The weighted average shares outstanding for the three and six months ended October 31, 2017 decreased to 209.1 million and 208.5 million, respectively, from 215.5 million and 218.0 million, respectively, for the three and six months ended October 31, 2016, primarily due to share repurchases completed in the prior year. We did not

repurchase any shares during the six months ended October 31, 2017 for retirement. During the six months ended October 31, 2016,

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we purchased and immediately retired 9.6 million shares at an aggregate cost of \$217.0 million (average price of \$22.51 per share).

**STOCK-BASED COMPENSATION** – During the six months ended October 31, 2017, we acquired 0.2 million shares of our common stock at an aggregate cost of \$7.6 million. These shares represent shares swapped or surrendered to us in connection with the vesting or exercise of stock-based awards. During the six months ended October 31, 2016, we acquired 0.2 million shares at an aggregate cost of \$5.6 million for similar purposes.

During the six months ended October 31, 2017 and 2016, we issued 2.1 million and 0.9 million shares of common stock, respectively, due to the vesting or exercise of stock-based awards.

During the six months ended October 31, 2017, we granted equity awards equivalent to 1.2 million shares under our stock-based compensation plans, consisting primarily of nonvested units. Stock-based compensation expense of our continuing operations totaled \$6.8 million and \$11.6 million for the three and six months ended October 31, 2017, and \$6.9 million and \$12.5 million for the three and six months ended October 31, 2016. As of October 31, 2017, unrecognized compensation cost for stock options totaled \$1.3 million, and for nonvested shares and units totaled \$42.3 million.

**NOTE 3: RECEIVABLES**

Receivables consist of the following:

(in 000s)

| As of   | October 31, 2017 |           | October 31, 2016 |           | April 30, 2017 |           |
|---|------------------|-----------|------------------|-----------|----------------|-----------|
|   | Short-term       | Long-term | Short-term       | Long-term | Short-term     | Long-term |
| Loans to franchisees  | \$37,953         | \$ 42,443 | \$48,772         | \$ 46,998 | \$39,911       | \$ 36,614 |
| Receivables for U.S assisted tax preparation and related fees | 36,926           | 6,316     | 37,303           | 5,528     | 54,506         | 6,316     |
| Instant Cash Back® receivables                                | 2,256            | —         | 2,630            | —         | 37,150         | —         |
| H&R Block Emerald Advance® lines of credit                    | 21,218           | 9,209     | 23,495           | —         | 26,325         | 5,069     |
| Software receivables from retailers                           | 484              | —         | 5,596            | —         | 16,715         | —         |
| Royalties and other receivables from franchisees              | 10,198           | 790       | 15,348           | —         | 13,275         | 1,585     |
| Other   | 23,980           | 3,791     | 27,682           | 3,712     | 30,189         | 3,314     |
|   | 133,015          | 62,549    | 160,826          | 56,238    | 218,071        | 52,898    |
| Allowance for doubtful accounts                               | (55,265 )        | —         | (56,062 )        | —         | (55,296 )      | —         |
|   | \$77,750         | \$ 62,549 | \$104,764        | \$ 56,238 | \$162,775      | \$ 52,898 |

Balances presented above as short-term are included in receivables, while the long-term portions are included in other noncurrent assets in the consolidated balance sheets.

**LOANS TO FRANCHISEES** – Franchisee loan balances as of October 31, 2017 and 2016 and April 30, 2017, consisted of \$25.3 million, \$31.4 million and \$27.0 million, respectively, in revolving lines of credit primarily for the purpose of funding off-season working capital needs and \$55.1 million, \$64.4 million and \$49.5 million, respectively, in term loans made primarily to finance the purchase of franchises.

As of October 31, 2017 and 2016 and April 30, 2017, loans with a principal balance of \$2.3 million, \$1.4 million and \$0.1 million, respectively, were more than 90 days past due. We had no loans to franchisees on non-accrual status.

**INSTANT CASH BACK® PROGRAM** – Refunds advanced under the Instant Cash Back® program in Canada are not subject to credit approval, therefore the primary indicator of credit quality is the age of the receivable amount. Instant Cash Back® amounts are generally received within 60 days of filing the client's return. As of October 31, 2017 and 2016 and April 30, 2017, \$39 thousand, \$29 thousand and \$1.5 million of Instant Cash Back® balances were more than 60 days old, respectively.

**H&R BLOCK EMERALD ADVANCE® LINES OF CREDIT (EAs)** – We review the credit quality of our purchased participation interests in EA receivables based on pools, which are segregated by the year of origination, with older

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years being deemed more unlikely to be repaid. These amounts as of October 31, 2017, by year of origination, are as follows:

(in 000s)

Credit Quality Indicator – Year of origination:

|                 |          |
|-----------------|----------|
| 2017            | \$8,641  |
| 2016 and prior  | 6,717    |
| Revolving loans | 15,069   |
|                 | \$30,427 |

As of October 31, 2017 and 2016 and April 30, 2017, \$27.9 million, \$20.8 million and \$28.0 million of EAs were on non-accrual status and classified as impaired, or more than 60 days past due, respectively.

ALLOWANCE FOR DOUBTFUL ACCOUNTS – Activity in the allowance for doubtful accounts for our EA and all other short-term receivables for the six months ended October 31, 2017 and 2016 is as follows:

(in 000s)

|                                 | EAs      | All<br>Other | Total    |
|---------------------------------|----------|--------------|----------|
| Balances as of April 30, 2017   | \$10,123 | \$45,173     | \$55,296 |
| Provision                       | —        | 4,238        | 4,238    |
| Charge-offs, net of recoveries  | —        | (4,269 )     | (4,269 ) |
| Balances as of October 31, 2017 | \$10,123 | \$45,142     | \$55,265 |
| Balances as of April 30, 2016   | \$9,007  | \$48,004     | \$57,011 |
| Provision                       | 451      | 835          | 1,286    |
| Charge-offs, net of recoveries  | —        | (2,235 )     | (2,235 ) |
| Balances as of October 31, 2016 | \$9,458  | \$46,604     | \$56,062 |

## NOTE 4: GOODWILL AND INTANGIBLE ASSETS

Changes in the carrying amount of goodwill for the six months ended October 31, 2017 and 2016 are as follows:

(in 000s)

|   | Goodwill  | Accumulated<br>Impairment<br>Losses | Net       |
|---|-----------|-------------------------------------|-----------|
| Balances as of April 30, 2017               | \$523,504 | \$ (32,297 )                        | \$491,207 |
| Acquisitions                                | 961       | —                                   | 961       |
| Disposals and foreign currency changes, net | 891       | —                                   | 891       |
| Impairments                                 | —         | —                                   | —         |
| Balances as of October 31, 2017             | \$525,356 | \$ (32,297 )                        | \$493,059 |
| 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 |

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<br>Carrying<br>Amount | Accumulated<br>Amortization | Net       |
|---|-----------------------------|-----------------------------|-----------|
| As of October 31, 2017:                                 |                             |                             |           |
| Reacquired franchise rights                             | \$331,290                   | \$ (101,987 )               | \$229,303 |
| Customer relationships                                  | 234,909                     | (147,881 )                  | 87,028    |
| Internally-developed software                           | 146,985                     | (117,162 )                  | 29,823    |
| Noncompete agreements                                   | 32,471                      | (28,644 )                   | 3,827     |
| Franchise agreements                                    | 19,201                      | (11,414 )                   | 7,787     |
| Purchased technology                                    | 54,700                      | (34,889 )                   | 19,811    |
| Acquired assets pending final allocation <sup>(1)</sup> | 28,861                      | —                           | 28,861    |
|   | \$848,417                   | \$ (441,977 )               | \$406,440 |
| 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 <sup>(1)</sup> | 22,694                      | —                           | 22,694    |
|   | \$799,775                   | \$ (366,640 )               | \$433,135 |
| As of April 30, 2017:                                   |                             |                             |           |
| Reacquired franchise rights                             | \$331,150                   | \$ (90,877 )                | \$240,273 |
| Customer relationships                                  | 234,603                     | (133,207 )                  | 101,396   |
| Internally-developed software                           | 139,709                     | (108,379 )                  | 31,330    |
| Noncompete agreements                                   | 32,408                      | (27,559 )                   | 4,849     |
| Franchise agreements                                    | 19,201                      | (10,774 )                   | 8,427     |
| Purchased technology                                    | 54,700                      | (31,973 )                   | 22,727    |
| Acquired assets pending final allocation <sup>(1)</sup> | 362                         | —                           | 362       |
|   | \$812,133                   | \$ (402,769 )               | \$409,364 |

<sup>(1)</sup> Represents business acquisitions for which final purchase price allocations have not yet been determined.

During the six months ended October 31, 2017 and 2016, we made payments to acquire franchisee and competitor businesses totaling \$27.5 million and \$36.2 million, respectively.

Amortization of intangible assets for the three and six months ended October 31, 2017 was \$19.4 million and \$38.7 million, respectively. Amortization for the three and six months ended October 31, 2016 was \$20.1 million and \$38.0 million, respectively. Estimated amortization of intangible assets for fiscal years 2018, 2019, 2020, 2021 and 2022 is \$76.0 million, \$61.1 million, \$44.8 million, \$30.5 million and \$20.2 million, respectively.

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## NOTE 5: LONG-TERM DEBT

The components of long-term debt are as follows:

|   | (in 000s)           |                     |                   |
|---|---------------------|---------------------|-------------------|
| As of                                   | October 31,<br>2017 | October 31,<br>2016 | April 30,<br>2017 |
| 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                | 6,125               | 7,024               | 6,610             |
| Debt issuance costs and discounts       | (11,293 )           | (13,915 )           | (12,612 )         |
|   | 1,494,832           | 1,968,109           | 1,493,998         |
| Less: Current portion                   | (1,004 )            | (903 )              | (981 )            |
|   | \$1,493,828         | \$1,967,206         | \$1,493,017       |

On September 22, 2017, we entered into a Second Amended and Restated Credit and Guarantee Agreement (2017 CLOC), which further amended our First Amended and Restated Credit and Guarantee Agreement (2016 CLOC), extending the scheduled maturity date from September 22, 2021 to September 22, 2022. Other material terms remain unchanged from the 2016 CLOC. The 2017 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 and meeting certain other conditions. The 2017 CLOC will mature on September 22, 2022, unless extended pursuant to the terms of the 2017 CLOC, at which time all outstanding amounts thereunder will be due and payable. The 2017 CLOC includes an annual facility fee, which will vary depending on our then current credit ratings.

The 2017 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 ratio (EBITDA-to-interest expense) 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 2017 CLOC includes provisions for an equity cure which could potentially allow us to independently cure certain defaults. Proceeds under the 2017 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, 2017.

We had no outstanding balance under the 2017 CLOC as of October 31, 2017, and amounts available to borrow were limited by the debt-to-EBITDA covenant to approximately \$1.5 billion as of October 31, 2017. We began borrowing on our 2017 CLOC in November for seasonal working capital needs.



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## NOTE 6: 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, 2017 |                      | October 31, 2016 |                      | April 30, 2017  |                      |
|--|------------------|----------------------|------------------|----------------------|-----------------|----------------------|
|  | Carrying Amount  | Estimated Fair Value | Carrying Amount  | Estimated Fair Value | Carrying Amount | Estimated Fair Value |
| <b>Assets:</b>                                 |                  |                      |                  |                      |                 |                      |
| Cash and cash equivalents                      | \$ 180,997       | \$ 180,997           | \$ 232,510       | \$ 232,510           | \$ 1,011,331    | \$ 1,011,331         |
| Cash and cash equivalents - restricted         | 100,665          | 100,665              | 109,538          | 109,538              | 106,208         | 106,208              |
| Receivables, net - short-term                  | 77,750           | 77,750               | 104,764          | 104,764              | 162,775         | 162,775              |
| Receivables, net - long-term                   | 62,549           | 62,549               | 56,238           | 56,238               | 52,898          | 52,898               |
| <b>Liabilities:</b>                            |                  |                      |                  |                      |                 |                      |
| Long-term debt (excluding debt issuance costs) | 1,502,654        | 1,606,583            | 1,968,109        | 2,067,234            | 1,502,735       | 1,569,033            |
| Contingent consideration                       | 10,145           | 10,145               | 7,817            | 7,817                | 10,428          | 10,428               |

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).

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 and tax preparation 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 financial institutions (Level 2).

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

## NOTE 7: INCOME TAXES

We file a consolidated federal income tax return in the U.S. with the Internal Revenue Service (IRS) and file tax returns in various state and foreign jurisdictions. Tax returns are typically examined and either settled upon completion of the examination or through the appeals process. The Company's U.S. federal income tax return for 2014 is currently under examination. Our U.S. federal returns for 2015 and 2016 have not been audited and remain open to examination. Our U.S. federal returns for 2013 and all prior periods are closed. With respect to state and local jurisdictions and countries outside of the United States, we are typically subject to examination for three to six years after the income tax returns have been filed. Although the outcome of the tax audits is always uncertain, we believe that adequate amounts of tax, interest and penalties have been provided for in the accompanying consolidated financial statements for any adjustments that might be incurred due to federal, state, local or foreign audits.

We had gross unrecognized tax benefits of \$132.9 million, \$105.7 million and \$149.9 million as of October 31, 2017 and 2016 and April 30, 2017, respectively. The gross unrecognized tax benefits decreased \$17.0 million and \$5.8 million during the six months ended October 31, 2017 and 2016, respectively. The decrease in unrecognized tax benefits during the six months ending October 31, 2017 is related to favorable audit settlements in various states and foreign jurisdictions as well as state and federal statute of limitations periods ending in the current quarter. We believe it is reasonably possible that the balance of unrecognized tax benefits could decrease by approximately \$7.5 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. For such matters where a change in the balance of unrecognized



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tax benefits is not yet deemed reasonably possible, no estimate has been included. The portion of unrecognized benefits expected to be cash settled within the next twelve months amounts to \$6.2 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.

Deferred tax assets and income taxes receivable decreased by \$74.5 million from April 30, 2017 primarily due to a change in tax accounting method related to our deferred POM revenue and intercompany transfers of intangible assets. Consistent with prior years, our pretax loss for the six months ended October 31, 2017 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, management has 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 \$9.6 million was recorded in the six months ended October 31, 2017, compared to a discrete tax benefit of \$10.8 million in the same period of the prior year. The discrete tax benefit recorded in the current period resulted from exercises of employee stock options, audit settlements in various states and foreign jurisdictions and the expiration of statute of limitation periods. The excess tax benefit recorded in the income statement due to the adoption of ASU 2016-09 as of May 1, 2017 is discussed in note 1. The discrete tax benefit recorded in the prior year resulted primarily from favorable settlements of state audits.

Our effective tax rate for continuing operations, including the effects of discrete tax items, was 37.5% and 38.8% for the six months ended October 31, 2017 and 2016, respectively. Discrete items increased the effective tax rate for the six months ended October 31, 2017 and 2016 by 2.2% and 2.5%, 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.

**NOTE 8: OTHER INCOME AND OTHER EXPENSES**

The following table shows the components of other income (expense), net:  
(in 000s)

|   | Three months<br>ended October<br>31,<br>2017 |         | Six months<br>ended October<br>31,<br>2016 |         |
|---|--|---------|--|---------|
| Mortgage loans and real estate owned, net | \$—  | \$1,508 | \$—  | \$3,045 |
| Interest income                           | 1,311  | 693     | 2,755                                      | 1,790   |
| Foreign currency gains (losses), net      | (117 )                                       | (6 )    | 14   | (27 )   |
| Other, net                                | (183 )                                       | (22 )   | (538 )                                     | 6       |
|   | \$1,011                                      | \$2,173 | \$2,231                                    | \$4,814 |

**NOTE 9: COMMITMENTS AND CONTINGENCIES**

Changes in deferred revenue balances related to our 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,                           | 2017      | 2016      |
|--|-----------|-----------|
| Balance, beginning of the period                       | \$211,223 | \$204,342 |
| Amounts deferred for new extended service plans issued | 2,913     | 2,561     |
| Revenue recognized on previous deferrals               | (63,332 ) | (58,921 ) |
| Balance, end of the period                             | \$150,804 | \$147,982 |

Our liability related to estimated losses under the standard guarantee was \$3.6 million, \$5.0 million and \$6.8 million as of October 31, 2017 and 2016 and April 30, 2017, respectively, and is included as part of our assisted tax

preparation

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services. The short-term and long-term portions of this liability are included in deferred revenue and other liabilities in the consolidated balance sheets.

Our liability related to acquisitions for estimated contingent consideration was \$10.1 million, \$7.8 million and \$10.4 million as of October 31, 2017 and 2016 and April 30, 2017, respectively, 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 \$42.7 million at October 31, 2017, and net of amounts drawn and outstanding, our remaining commitment to fund totaled \$17.6 million.

**LOSS CONTINGENCIES PERTAINING TO 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."

SCC accrues a liability for losses related to representation and warranty claims when those losses are believed to be both probable and reasonably estimable. SCC's loss estimate as of October 31, 2017, is based on the best information currently available, management judgment, developments in relevant case law, and the terms of bulk settlements. 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,     | 2017    | 2016      |
| Balance, beginning of the period | \$4,500 | \$65,265  |
| Loss provisions                  | —       | 235       |
| Payments                         | —       | (40,000 ) |
| Balance, end of the period       | \$4,500 | \$25,500  |

See note 10, which addresses contingent losses that may be incurred with respect to various indemnification or contribution claims by underwriters, depositors, and securitization trustees in securitization transactions in which SCC participated.

**NOTE 10: LITIGATION AND OTHER 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.



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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, including indemnification and contribution claims, and other related 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, 2017. 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, 2017 and 2016 and April 30, 2017, our total accrued liabilities were \$2.5 million, \$2.3 million and \$2.3 million, respectively, for matters addressed in this note.

Our aggregate range of reasonably possible losses includes (1) matters where a liability has been accrued and there is a reasonably possible loss in excess of the amount accrued for that liability, and (2) matters where a loss is believed to be reasonably possible, but a liability has not been accrued. This aggregate range only represents those losses as to which we are currently able to estimate a reasonably possible loss or range of loss. It does not represent our maximum loss exposure. The 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. As of October 31, 2017, 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 precise information about the amount of damages or other remedies being asserted, the defenses to the claims being asserted, discovery from other parties and investigation of factual allegations, rulings by courts on motions or appeals, analysis by experts, or the status or terms 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 AND CONTRIBUTION 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 or contribution, 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,



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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 or contribution, breach of contract, violations of securities laws, and violations of 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. It is difficult to predict either the likelihood of new matters being initiated or the outcome of existing matters. In many of these matters 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.

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 RMBSs. In connection with the sale of loans and/or RMBSs, SCC made certain representations and warranties. The statute of limitations for a contractual claim to enforce a representation and warranty obligation is generally six years or such shorter limitations period that may apply under the law of a state where the economic injury occurred. 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 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 2016 ruling by a New York intermediate appellate court, followed by the federal district court in the second Homeward case described below, 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. Additionally, plaintiffs in litigation to which SCC is not party have alleged breaches of an independent contractual duty to provide notice of material breaches of representations and warranties and pursued separate claims to which, they argue, the statute of limitations ruling in the ACE case does not apply. 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 relating back to timely filed litigation.

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 filed a motion to intervene to add H&R Block, Inc. to the lawsuit and assert claims against H&R Block, Inc. based on alter ego, corporate veil-piercing, and agency law. SCC is opposing the motion to intervene, which remains pending. We believe H&R Block, Inc. has 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.

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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

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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 the 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, which was denied, and also filed a motion for leave to appeal the ruling, which remains pending. On October 6, 2016, the plaintiff filed its second amended complaint. In response to a motion filed by SCC, the court dismissed the plaintiff's claim for breach of one of the representations. The case is proceeding on the remaining claims. Representatives of a holder of certificates in the trust filed a motion to intervene to add H&R Block, Inc. to the lawsuit and assert claims against H&R Block, Inc. based on alter ego, corporate veil-piercing, and agency law. SCC is opposing the motion to intervene, which remains pending. We believe H&R Block, Inc. has meritorious defenses to the extent the court allows any such claims to be asserted. The accrual for representation and warranty claims, as discussed in note 9, is related to some of the 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 21 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 \$3.5 billion). Additional lawsuits against the underwriters or depositors may be filed in the future, and SCC may receive additional notices of claims for indemnification or contribution 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 to assert claims for contribution, which are referred to herein as "contribution claims." Contribution claims 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 or contribution claims is probable, nor have we accrued a liability related to any of these claims.

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 has received notices from securitization trustees of potential indemnification obligations, and may receive additional notices 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 of these indemnification claims is probable, nor have we accrued a liability related to any of these claims.

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, 2017, total approximately \$313 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.



Table of Contents**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 others who may be 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 substantial and could have a material adverse impact on our business and our consolidated financial position, results of operations, and cash flows.

**NOTE 11: CONDENSED CONSOLIDATING FINANCIAL STATEMENTS**

Block Financial LLC (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 2017 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**

| Three months ended October 31, 2017                |                                |                             |                       |              | (in 000s)                    |
|--|--------------------------------|-----------------------------|-----------------------|--------------|------------------------------|
|  | H&R Block, Inc.<br>(Guarantor) | Block Financial<br>(Issuer) | Other<br>Subsidiaries | Eliminations | Consolidated<br>H&R<br>Block |
| Total revenues                                     | \$ —                           | \$ 11,705                   | \$ 132,060            | \$ (2,911 )  | \$ 140,854                   |
| Cost of revenues                                   | —                              | 5,104                       | 234,943               | (28 )        | 240,019                      |
| Selling, general and administrative                | —                              | 3,585                       | 116,144               | (2,883 )     | 116,846                      |
| Total operating expenses                           | —                              | 8,689                       | 351,087               | (2,911 )     | 356,865                      |
| Other income (expense), net                        | (155,999 )                     | 6,992                       | (11,221 )             | 161,239      | 1,011                        |
| Interest expense on external borrowings            | —                              | (21,178 )                   | (87 )                 | —            | (21,265 )                    |
| Loss from continuing operations before tax benefit | (155,999 )                     | (11,170 )                   | (230,335 )            | 161,239      | (236,265 )                   |
| Income tax benefit                                 | (2,433 )                       | (990 )                      | (84,530 )             | —            | (87,953 )                    |
| Net loss from continuing operations                | (153,566 )                     | (10,180 )                   | (145,805 )            | 161,239      | (148,312 )                   |
| Net loss from discontinued operations              | —                              | (5,253 )                    | (1 )                  | —            | (5,254 )                     |
| Net loss   | (153,566 )                     | (15,433 )                   | (145,806 )            | 161,239      | (153,566 )                   |
| Other comprehensive loss                           | (1,385 )                       | —                           | (1,385 )              | 1,385        | (1,385 )                     |
| Comprehensive loss                                 | \$ (154,951 )                  | \$ (15,433 )                | \$ (147,191 )         | \$ 162,624   | \$ (154,951 )                |

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| CONDENSED CONSOLIDATING STATEMENTS OF OPERATIONS   |                                |                             |                       |              | (in 000s)                    |
|--|--------------------------------|-----------------------------|-----------------------|--------------|------------------------------|
| Three months ended October 31, 2016                | H&R Block, Inc.<br>(Guarantor) | Block Financial<br>(Issuer) | Other<br>Subsidiaries | Eliminations | Consolidated<br>H&R<br>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 (expense), net                        | (148,773 )                     | 1,207                       | (13,194 )             | 162,933      | 2,173                        |
| Interest expense on external borrowings            | —                              | (22,248 )                   | (372 )                | —            | (22,620 )                    |
| 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 )                |

| CONDENSED CONSOLIDATING STATEMENTS OF OPERATIONS   |                                |                             |                       |              | (in 000s)                    |
|--|--------------------------------|-----------------------------|-----------------------|--------------|------------------------------|
| Six months ended October 31, 2017                  | H&R Block, Inc.<br>(Guarantor) | Block Financial<br>(Issuer) | Other<br>Subsidiaries | Eliminations | Consolidated<br>H&R<br>Block |
| Total revenues                                     | \$ —                           | \$ 29,261                   | \$ 255,154            | \$ (5,759 )  | \$ 278,656                   |
| Cost of revenues                                   | —                              | 12,964                      | 454,913               | (143 )       | 467,734                      |
| Selling, general and administrative                | —                              | 6,791                       | 210,920               | (5,616 )     | 212,095                      |
| Total operating expenses                           | —                              | 19,755                      | 665,833               | (5,759 )     | 679,829                      |
| Other income (expense), net                        | (288,263 )                     | 13,065                      | (13,639 )             | 291,068      | 2,231                        |
| Interest expense on external borrowings            | —                              | (42,382 )                   | (160 )                | —            | (42,542 )                    |
| Loss from continuing operations before tax benefit | (288,263 )                     | (19,811 )                   | (424,478 )            | 291,068      | (441,484 )                   |
| Income tax benefit                                 | (4,130 )                       | (5,613 )                    | (155,611 )            | —            | (165,354 )                   |
| Net loss from continuing operations                | (284,133 )                     | (14,198 )                   | (268,867 )            | 291,068      | (276,130 )                   |
| Net loss from discontinued operations              | —                              | (8,001 )                    | (2 )                  | —            | (8,003 )                     |
| Net loss   | (284,133 )                     | (22,199 )                   | (268,869 )            | 291,068      | (284,133 )                   |
| Other comprehensive income                         | 1,077                          | —                           | 1,077                 | (1,077 )     | 1,077                        |
| Comprehensive loss                                 | \$ (283,056 )                  | \$ (22,199 )                | \$ (267,792 )         | \$ 289,991   | \$ (283,056 )                |

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| CONDENSED CONSOLIDATING STATEMENTS OF OPERATIONS   |                                |                             |                       |              | (in 000s)                    |
|--|--------------------------------|-----------------------------|-----------------------|--------------|------------------------------|
| Six months ended October 31, 2016                  | H&R Block, Inc.<br>(Guarantor) | Block Financial<br>(Issuer) | Other<br>Subsidiaries | Eliminations | H&R<br>Block<br>Consolidated |
| 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 (expense), net                        | (273,435 )                     | 2,033                       | (22,824 )             | 299,040      | 4,814                        |
| Interest expense on external borrowings            | —                              | (43,562 )                   | (524 )                | —            | (44,086 )                    |
| 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 BALANCE SHEETS

|  |                                |                   |                           |                       | (in 000s)    |                           |
|--|--------------------------------|-------------------|---------------------------|-----------------------|--------------|---------------------------|
| As of October 31, 2017   | H&R Block, Inc.<br>(Guarantor) | Block<br>(Issuer) | Financial<br>Subsidiaries | Other<br>Subsidiaries | Eliminations | Consolidated<br>H&R Block |
| Cash & cash equivalents  | \$ —                           | \$ 4,321          | \$ 176,676                | \$ —                  |              | \$ 180,997                |
| Cash & cash equivalents - restricted                             | —                              | 8,083             | 92,582                    | —                     |              | 100,665                   |
| Receivables, net   | —                              | 54,006            | 23,744                    | —                     |              | 77,750                    |
| Prepaid expenses and other current assets                        | —                              | 4,205             | 80,999                    | —                     |              | 85,204                    |
| Total current assets   | —                              | 70,615            | 374,001                   | —                     |              | 444,616                   |
| Property and equipment, net                                      | —                              | 56                | 262,170                   | —                     |              | 262,226                   |
| Intangible assets, net   | —                              | —                 | 406,440                   | —                     |              | 406,440                   |
| Goodwill   | —                              | —                 | 493,059                   | —                     |              | 493,059                   |
| Deferred tax assets and income taxes<br>receivable               | 7,463                          | 25,453            | —                         | (23,711 )             |              | 9,205                     |
| Investments in subsidiaries                                      | 1,890,500                      | —                 | 91,515                    | (1,982,015 )          |              | —                         |
| Amounts due from affiliates                                      | —                              | 1,467,742         | 2,290,036                 | (3,757,778 )          |              | —                         |
| Other noncurrent assets  | —                              | 62,046            | 38,969                    | —                     |              | 101,015                   |
| Total assets   | \$ 1,897,963                   | \$ 1,625,912      | \$ 3,956,190              | \$(5,763,504)         |              | \$ 1,716,561              |
| Accounts payable and accrued expenses                            | \$ 2,407                       | \$ 9,334          | \$ 103,134                | \$ —                  |              | \$ 114,875                |
| Accrued salaries, wages and payroll taxes                        | —                              | 1,432             | 41,465                    | —                     |              | 42,897                    |
| Accrued income taxes and reserves for<br>uncertain tax positions | —                              | —                 | 43,879                    | —                     |              | 43,879                    |
| Current portion of long-term debt                                | —                              | —                 | 1,004                     | —                     |              | 1,004                     |
| Deferred revenue and other current<br>liabilities                | —                              | 25,977            | 164,545                   | —                     |              | 190,522                   |
| Total current liabilities  | 2,407                          | 36,743            | 354,027                   | —                     |              | 393,177                   |
| Long-term debt   | —                              | 1,488,707         | 5,121                     | —                     |              | 1,493,828                 |
| Reserves for uncertain tax positions                             | 18,293                         | 8,037             | 135,405                   | (23,711 )             |              | 138,024                   |
| Deferred revenue and other noncurrent<br>liabilities             | —                              | 910               | 103,395                   | —                     |              | 104,305                   |
| Amounts due to affiliates  | 2,290,036                      | —                 | 1,467,742                 | (3,757,778 )          |              | —                         |
| Total liabilities  | 2,310,736                      | 1,534,397         | 2,065,690                 | (3,781,489 )          |              | 2,129,334                 |
| Stockholders' equity (deficiency)                                | (412,773 )                     | 91,515            | 1,890,500                 | (1,982,015 )          |              | (412,773 )                |
| Total liabilities and stockholders' equity                       | \$ 1,897,963                   | \$ 1,625,912      | \$ 3,956,190              | \$(5,763,504)         |              | \$ 1,716,561              |

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| CONDENSED CONSOLIDATING BALANCE SHEETS                           |                                |                   |                           |                       | (in 000s)    |                           |
|--|--------------------------------|-------------------|---------------------------|-----------------------|--------------|---------------------------|
| As of October 31, 2016   | H&R Block, Inc.<br>(Guarantor) | Block<br>(Issuer) | Financial<br>Subsidiaries | Other<br>Subsidiaries | Eliminations | Consolidated<br>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<br>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<br>uncertain tax positions | —                              | —                 | 68,832                    | —                     | —            | 68,832                    |
| Current portion of long-term debt                                | —                              | —                 | 903                       | —                     | —            | 903                       |
| Deferred revenue and other current<br>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<br>borrowings                  | —                              | 1,961,085         | 6,121                     | —                     | —            | 1,967,206                 |
| Reserves for uncertain tax positions                             | 5,917                          | 10,786            | 100,850                   | —                     | —            | 117,553                   |
| Deferred revenue and other noncurrent<br>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 )   | (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 April 30, 2017   | H&R Block, Inc.<br>(Guarantor) | Block Financial<br>(Issuer) | Other<br>Subsidiaries | Eliminations  | Consolidated<br>H&R Block |
| Cash & cash equivalents  | \$ —                           | \$ 4,486                    | \$ 1,006,845          | \$—           | \$ 1,011,331              |
| Cash & cash equivalents - restricted                             | —                              | 8,060                       | 98,148                | —             | 106,208                   |
| Receivables, net   | —                              | 61,250                      | 101,525               | —             | 162,775                   |
| Prepaid expenses and other current assets                        | —                              | 2,280                       | 63,445                | —             | 65,725                    |
| Total current assets   | —                              | 76,076                      | 1,269,963             | —             | 1,346,039                 |
| Property and equipment, net                                      | —                              | 78                          | 263,749               | —             | 263,827                   |
| Intangible assets, net   | —                              | —                           | 409,364               | —             | 409,364                   |
| Goodwill   | —                              | —                           | 491,207               | —             | 491,207                   |
| Deferred tax assets and income taxes<br>receivable               | 5,587                          | 30,743                      | 47,398                | —             | 83,728                    |
| Investments in subsidiaries                                      | 2,158,234                      | —                           | 113,714               | (2,271,948 )  | —                         |
| Amounts due from affiliates                                      | —                              | 1,493,195                   | 2,194,294             | (3,687,489 )  | —                         |
| Other noncurrent assets  | —                              | 51,829                      | 48,114                | —             | 99,943                    |
| Total assets   | \$ 2,163,821                   | \$ 1,651,921                | \$ 4,837,803          | \$(5,959,437) | \$ 2,694,108              |
| Accounts payable and accrued expenses                            | \$ 2,086                       | \$ 14,218                   | \$ 200,724            | \$—           | \$ 217,028                |
| Accrued salaries, wages and payroll taxes                        | —                              | 851                         | 183,005               | —             | 183,856                   |
| Accrued income taxes and reserves for<br>uncertain tax positions | —                              | —                           | 348,199               | —             | 348,199                   |
| Current portion of long-term debt                                | —                              | —                           | 981                   | —             | 981                       |
| Deferred revenue and other current<br>liabilities                | —                              | 26,759                      | 162,457               | —             | 189,216                   |
| Total current liabilities  | 2,086                          | 41,828                      | 895,366               | —             | 939,280                   |
| Long-term debt   | —                              | 1,487,389                   | 5,628                 | —             | 1,493,017                 |
| Reserves for uncertain tax positions                             | 28,324                         | 8,037                       | 122,724               | —             | 159,085                   |
| Deferred revenue and other noncurrent<br>liabilities             | —                              | 953                         | 162,656               | —             | 163,609                   |
| Amounts due to affiliates  | 2,194,294                      | —                           | 1,493,195             | (3,687,489 )  | —                         |
| Total liabilities  | 2,224,704                      | 1,538,207                   | 2,679,569             | (3,687,489 )  | 2,754,991                 |
| Stockholders' equity (deficiency)                                | (60,883 )                      | 113,714                     | 2,158,234             | (2,271,948 )  | (60,883 )                 |
| Total liabilities and stockholders' equity                       | \$ 2,163,821                   | \$ 1,651,921                | \$ 4,837,803          | \$(5,959,437) | \$ 2,694,108              |

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| Six months ended October 31, 2017                               | CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS |                                 |                       |             | (in 000s)                    |
|---|--|---------------------------------|-----------------------|-------------|------------------------------|
|   | H&R Block,<br>(Guarantor)                        | H&R Block Financial<br>(Issuer) | Other<br>Subsidiaries | Elimination | H&R<br>Block<br>Consolidated |
| Net cash used in operating activities                           | \$ —   | \$ (17,827 )                    | \$ (630,630 )         | \$ —        | \$ (648,457 )                |
| Cash flows from investing:                                      |  |                                 |                       |             |                              |
| Capital expenditures  | —  | (10 )                           | (56,740 )             | —           | (56,750 )                    |
| Payments made for business acquisitions, net of cash acquired   | —  | —                               | (27,522 )             | —           | (27,522 )                    |
| Franchise loans funded  | —  | (10,885 )                       | (54 )                 | —           | (10,939 )                    |
| Payments received on franchise loans                            | —  | 10,077                          | 245                   | —           | 10,322                       |
| Intercompany borrowings (payments)                              | —  | 20,163                          | (80,141 )             | 59,978      | —                            |
| Other, net  | —  | (998 )                          | 6,472                 | —           | 5,474                        |
| Net cash provided by (used in) investing activities             | —  | 18,347                          | (157,740 )            | 59,978      | (79,415 )                    |
| Cash flows from financing:                                      |  |                                 |                       |             |                              |
| Dividends paid  | (100,082 )                                       | —                               | —                     | —           | (100,082 )                   |
| Repurchase of common stock, including shares surrendered        | (7,581 )   | —                               | —                     | —           | (7,581 )                     |
| Proceeds from exercise of stock options                         | 27,522   | —                               | —                     | —           | 27,522                       |
| Intercompany borrowings (payments)                              | 80,141   | —                               | (20,163 )             | (59,978 )   | —                            |
| Other, net  | —  | (662 )                          | (26,055 )             | —           | (26,717 )                    |
| Net cash used in financing activities                           | —  | (662 )                          | (46,218 )             | (59,978 )   | (106,858 )                   |
| Effects of exchange rates on cash                               | —  | —                               | (1,147 )              | —           | (1,147 )                     |
| Net decrease in cash, cash equivalents and restricted cash      | —  | (142 )                          | (835,735 )            | —           | (835,877 )                   |
| Cash, cash equivalents and restricted cash, beginning of period | —  | 12,546                          | 1,104,993             | —           | 1,117,539                    |
| Cash, cash equivalents and restricted cash, end of period       | \$ —   | \$ 12,404                       | \$ 269,258            | \$ —        | \$ 281,662                   |

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| CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS                        |                           |                                 |                       |              |              | (in 000s)     |
|---|---------------------------|---------------------------------|-----------------------|--------------|--------------|---------------|
| Six months ended October 31, 2016                                       | H&R Block,<br>(Guarantor) | H&R Block Financial<br>(Issuer) | Other<br>Subsidiaries | Eliminations | H&R<br>Block | Consolidated  |
| Net cash used in operating activities                                   | \$ —                      | \$ (77,906 )                    | \$ (642,470 )         | \$ —         | \$ —         | \$ (720,376 ) |
| Cash flows from investing:  |                           |                                 |                       |              |              |               |
| Principal payments on mortgage loans and sale of real estate owned, net | —                         | 19,009                          | —                     | —            | —            | 19,009        |
| Capital expenditures  | —                         | (5                              | ) (44,913 )           | —            | —            | (44,918 )     |
| Payments made for business acquisitions, net of cash acquired           | —                         | —                               | (36,151 )             | —            | —            | (36,151 )     |
| Franchise loans funded  | —                         | (10,064 )                       | (107 )                | —            | —            | (10,171 )     |
| Payments received on franchise loans                                    | —                         | 14,052                          | 211                   | —            | —            | 14,263        |
| Intercompany borrowings (payments)                                      | —                         | (426,824 )                      | (309,852 )            | 736,676      | —            | —             |
| Other, net  | —                         | (312 )                          | 2,489 )               | —            | —            | 2,177         |
| 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                                       | —                         | —                               | (4,110 )              | —            | —            | (4,110 )      |
| Net decrease in cash, cash equivalents and restricted cash              | —                         | (7,050 )                        | (651,813 )            | —            | —            | (658,863 )    |
| Cash, cash equivalents and restricted cash, beginning of period         | —                         | 38,029                          | 962,882               | —            | —            | 1,000,911     |
| Cash, cash equivalents and restricted cash, end of period               | \$ —                      | \$ 30,979                       | \$ 311,069            | \$ —         | \$ —         | \$ 342,048    |

Table of ContentsITEM MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF  
2. OPERATIONS

Our subsidiaries provide assisted and do-it-yourself (DIY) tax return preparation solutions through multiple channels (including in-person, online and mobile applications, and desktop software) and distribute H&R Block-branded financial products and services, including those of our financial partners, to the general public primarily in the U.S., Canada, Australia, and their respective territories. 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.

## RESULTS OF OPERATIONS

| Consolidated – Financial Results                   | (in 000s, except per share amounts) |             |           |          |   |
|--|-------------------------------------|-------------|-----------|----------|---|
| Three months ended October 31,                     | 2017                                | 2016        | \$ Change | % Change |   |
| Revenues:  |                                     |             |           |          |   |
| U.S. assisted tax preparation fees                 | \$36,665                            | \$35,339    | \$1,326   | 3.8      | % |
| U.S. royalties                                     | 7,008                               | 6,828       | 180       | 2.6      | % |
| U.S. DIY tax preparation fees                      | 4,263                               | 3,089       | 1,174     | 38.0     | % |
| International revenues                             | 47,934                              | 43,539      | 4,395     | 10.1     | % |
| Revenues from Refund Transfers                     | 1,135                               | 757         | 378       | 49.9     | % |
| Revenues from Emerald Card®                        | 9,180                               | 8,644       | 536       | 6.2      | % |
| Revenues from Peace of Mind® Extended Service Plan | 24,585                              | 22,689      | 1,896     | 8.4      | % |
| Interest and fee income on Emerald Advance         | 594                                 | 655         | (61)      | (9.3)    | % |
| Other  | 9,490                               | 9,792       | (302)     | (3.1)    | % |
| Total revenues                                     | 140,854                             | 131,332     | 9,522     | 7.3      | % |
| Compensation and benefits:                         |                                     |             |           |          |   |
| Field wages  | 57,716                              | 50,096      | 7,620     | 15.2     | % |
| Other wages  | 46,723                              | 42,207      | 4,516     | 10.7     | % |
| Benefits and other compensation                    | 23,583                              | 23,718      | (135)     | (0.6)    | % |
|  | 128,022                             | 116,021     | 12,001    | 10.3     | % |
| Occupancy and equipment                            | 105,405                             | 99,037      | 6,368     | 6.4      | % |
| Marketing and advertising                          | 11,562                              | 12,001      | (439)     | (3.7)    | % |
| Depreciation and amortization                      | 44,792                              | 45,750      | (958)     | (2.1)    | % |
| Provision for bad debt                             | 1,779                               | (131)       | 1,910     | **       |   |
| Supplies   | 4,368                               | 4,937       | (569)     | (11.5)   | % |
| Other  | 60,937                              | 61,739      | (802)     | (1.3)    | % |
| Total operating expenses                           | 356,865                             | 339,354     | 17,511    | 5.2      | % |
| Other income (expense), net                        | 1,011                               | 2,173       | (1,162)   | (53.5)   | % |
| Interest expense on borrowings                     | (21,265)                            | (22,620)    | 1,355     | 6.0      | % |
| Pretax loss  | (236,265)                           | (228,469)   | (7,796)   | (3.4)    | % |
| Income tax benefit                                 | (87,953)                            | (85,054)    | 2,899     | 3.4      | % |
| Net loss from continuing operations                | (148,312)                           | (143,415)   | (4,897)   | (3.4)    | % |
| Net loss from discontinued operations              | (5,254)                             | (2,805)     | (2,449)   | (87.3)   | % |
| Net loss   | \$(153,566)                         | \$(146,220) | \$(7,346) | (5.0)    | % |
| Basic and diluted loss per share:                  |                                     |             |           |          |   |
| Continuing operations                              | \$(0.71)                            | \$(0.67)    | \$(0.04)  | (6.0)    | % |
| Discontinued operations                            | (0.03)                              | (0.01)      | (0.02)    | (200.0)  | % |

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|  |  |              |   |              |   |             |   |      |    |
|--|--|--------------|---|--------------|---|-------------|---|------|----|
| Consolidated                                     |  |              |   |              |   |             |   |      |    |
|  |  | \$ (0.74     | ) | \$ (0.68     | ) | \$ (0.06    | ) | (8.8 | )% |
| EBITDA from continuing operations <sup>(1)</sup> |  | \$ (170,208) |   | \$ (160,099) |   | \$ (10,109) |   | (6.3 | )% |

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

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Three months ended October 31, 2017 compared to October 31, 2016

Revenues increased \$9.5 million, or 7.3%, from the prior year. U.S. assisted tax preparation fees and U.S. DIY fees increased primarily due to higher off-season tax return volumes.

International revenues increased \$4.4 million, or 10.1%, primarily due to higher volumes of tax returns and favorable exchange rates in our Australian operations.

Revenues from POM increased \$1.9 million, or 8.4%, due to an increase in units sold in prior years and changes in the timing of forecasted claims.

Total operating expenses increased \$17.5 million, or 5.2%, from the prior year. Field wages increased \$7.6 million, or 15.2%, primarily due to higher office labor in our Australian operations and inflationary increases. Other wages increased \$4.5 million, or 10.7%, due to increased headcount primarily related to information technology resources and inflationary increases in corporate support wages. Occupancy and equipment costs increased \$6.4 million, or 6.4%, primarily due to higher rent rates and an increase in the number of company-owned tax offices due to the acquisition of franchisees.

Other expenses decreased \$0.8 million, or 1.3%, primarily due to the timing of franchise convention costs, which will be incurred in the third quarter this year, partially offset by higher legal fees. The components of other expenses are as follows:

| Three months ended October 31,       | 2017     | 2016     | \$<br>Change | %<br>Change |
|--------------------------------------|----------|----------|--------------|-------------|
| Consulting and outsourced services   | \$19,587 | \$20,775 | \$(1,188)    | (5.7)%      |
| Bank partner fees                    | 1,363    | 1,373    | (10)         | (0.7)%      |
| Client claims and refunds            | 11,200   | 12,692   | (1,492)      | (11.8)%     |
| Employee travel and related expenses | 10,358   | 14,209   | (3,851)      | (27.1)%     |
| Credit card/bank charges             | 2,640    | 2,547    | 93           | 3.7%        |
| Insurance                            | 3,824    | 3,250    | 574          | 17.7%       |
| Legal fees and settlements           | 5,750    | 2,025    | 3,725        | 184.0%      |
| Other                                | 6,215    | 4,868    | 1,347        | 27.7%       |
|                                      | \$60,937 | \$61,739 | \$(802)      | (1.3)%      |

See Item 1, note 7 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, except per share amounts) |            |          |    |
|--|-------------|-------------------------------------|------------|----------|----|
| Six months ended October 31,                       | 2017        | 2016                                | \$ Change  | % Change |    |
| Revenues:  |             |                                     |            |          |    |
| U.S. assisted tax preparation fees                 | \$66,628    | \$60,768                            | \$5,860    | 9.6      | %  |
| U.S. royalties                                     | 13,975      | 13,353                              | 622        | 4.7      | %  |
| U.S. DIY tax preparation fees                      | 7,489       | 6,003                               | 1,486      | 24.8     | %  |
| International revenues                             | 88,351      | 82,414                              | 5,937      | 7.2      | %  |
| Revenues from Refund Transfers                     | 3,951       | 3,991                               | (40)       | (1.0)    | )% |
| Revenues from Emerald Card®                        | 24,167      | 21,709                              | 2,458      | 11.3     | %  |
| Revenues from Peace of Mind® Extended Service Plan | 56,528      | 49,720                              | 6,808      | 13.7     | %  |
| Interest and fee income on Emerald Advance         | 1,258       | 1,459                               | (201)      | (13.8)   | )% |
| Other  | 16,309      | 17,100                              | (791)      | (4.6)    | )% |
| Total revenues                                     | 278,656     | 256,517                             | 22,139     | 8.6      | %  |
| Compensation and benefits:                         |             |                                     |            |          |    |
| Field wages  | 105,839     | 95,139                              | 10,700     | 11.2     | %  |
| Other wages  | 89,920      | 84,307                              | 5,613      | 6.7      | %  |
| Benefits and other compensation                    | 44,228      | 46,452                              | (2,224)    | (4.8)    | )% |
|  | 239,987     | 225,898                             | 14,089     | 6.2      | %  |
| Occupancy and equipment                            | 203,604     | 193,408                             | 10,196     | 5.3      | %  |
| Marketing and advertising                          | 18,666      | 19,562                              | (896)      | (4.6)    | )% |
| Depreciation and amortization                      | 88,390      | 87,032                              | 1,358      | 1.6      | %  |
| Provision for bad debt                             | 4,238       | 1,286                               | 2,952      | 229.5    | %  |
| Supplies   | 7,102       | 7,014                               | 88         | 1.3      | %  |
| Other  | 117,842     | 115,063                             | 2,779      | 2.4      | %  |
| Total operating expenses                           | 679,829     | 649,263                             | 30,566     | 4.7      | %  |
| Other income (expense), net                        | 2,231       | 4,814                               | (2,583)    | (53.7)   | )% |
| Interest expense on borrowings                     | (42,542)    | (44,086)                            | 1,544      | 3.5      | %  |
| Pretax loss  | (441,484)   | (432,018)                           | (9,466)    | (2.2)    | )% |
| Income tax benefit                                 | (165,354)   | (167,577)                           | (2,223)    | (1.3)    | )% |
| Net loss from continuing operations                | (276,130)   | (264,441)                           | (11,689)   | (4.4)    | )% |
| Net loss from discontinued operations              | (8,003)     | (5,452)                             | (2,551)    | (46.8)   | )% |
| Net loss   | \$(284,133) | \$(269,893)                         | \$(14,240) | (5.3)    | )% |
| Basic and diluted loss per share:                  |             |                                     |            |          |    |
| Continuing operations                              | \$(1.33)    | \$(1.21)                            | \$(0.12)   | (9.9)    | )% |
| Discontinued operations                            | (0.03)      | (0.03)                              | —          | —        | %  |
| Consolidated                                       | \$(1.36)    | \$(1.24)                            | \$(0.12)   | (9.7)    | )% |
| EBITDA from continuing operations <sup>(1)</sup>   | \$(310,552) | \$(300,900)                         | \$(9,652)  | (3.2)    | )% |

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

Six months ended October 31, 2017 compared to October 31, 2016

Revenues increased \$22.1 million, or 8.6%, from the prior year. U.S. assisted tax preparation fees increased \$5.9 million, or 9.6%, primarily due to higher off-season tax return volumes, coupled with a favorable change in net average charge and mix.

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International revenues increased \$5.9 million, or 7.2%, primarily due to higher volumes of tax returns and favorable exchange rates in our Australian operations.

Revenues from H&R Block Emerald Card® transactions increased \$2.5 million, or 11.3%, primarily due to fees and interchange income.

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Revenues from POM increased \$6.8 million, or 13.7%, due to an increase in units sold in prior years and changes in the timing of forecasted claims.

Total operating expenses increased \$30.6 million, or 4.7%, from the prior year. Field wages increased \$10.7 million, or 11.2%, primarily due to higher office labor in our Australian operations and inflationary increases. Other wages increased \$5.6 million, or 6.7%, due to increased headcount primarily related to information technology resources and inflationary increases in corporate support wages. Occupancy and equipment costs increased \$10.2 million, or 5.3%, primarily due to higher rent rates and an increase in the number of company-owned tax offices due to the acquisition of franchisees. Bad debt expense increased \$3.0 million primarily due to Instant Cash Back® write-offs in our Canadian operations.

Other expenses increased \$2.8 million, or 2.4%, primarily due to higher legal fees. The components of other expenses are as follows:

| Six months ended October 31,         | 2017      | 2016      | \$<br>Change | %<br>Change |
|--------------------------------------|-----------|-----------|--------------|-------------|
| Consulting and outsourced services   | \$38,092  | \$39,289  | \$(1,197)    | (3.0)%      |
| Bank partner fees                    | 2,996     | 3,143     | (147)        | (4.7)%      |
| Client claims and refunds            | 26,365    | 26,378    | (13)         | —%          |
| Employee travel and related expenses | 16,435    | 18,006    | (1,571)      | (8.7)%      |
| Credit card/bank charges             | 7,222     | 4,925     | 2,297        | 46.6%       |
| Insurance                            | 7,113     | 7,689     | (576)        | (7.5)%      |
| Legal fees and settlements           | 7,897     | 4,727     | 3,170        | 67.1%       |
| Other                                | 11,722    | 10,906    | 816          | 7.5%        |
|                                      | \$117,842 | \$115,063 | \$2,779      | 2.4%        |

See Item 1, note 7 to the consolidated financial statements for discussion of the impact of income taxes for the period.

**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 2017 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 February through April. Therefore, we require the use of cash to fund losses from May through January, 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, 2017 are sufficient to meet our operating, investing 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, 2017 and 2016. See Item 1 for the complete consolidated statements of cash flows for these periods.

|  | (in 000s)   |             |
|--|-------------|-------------|
| Six months ended October 31,                             | 2017        | 2016        |
| Net cash provided by (used in):                          |             |             |
| Operating activities                                     | \$(648,457) | \$(720,376) |
| Investing activities                                     | (79,415 )   | (55,791 )   |
| Financing activities                                     | (106,858 )  | 121,414     |
| Effects of exchange rates on cash                        | (1,147 )    | (4,110 )    |
| Net change in cash, cash equivalents and restricted cash | \$(835,877) | \$(658,863) |

Operating Activities. Cash used in operations decreased, primarily due to prior year settlement payments related to representation and warranty claims and collections on receivables.

Investing Activities. Cash used in investing activities totaled \$79.4 million for the six months ended October 31, 2017 compared to \$55.8 million in the prior year period. This change resulted from cash received from our portfolio of mortgage loans in the prior year, which was subsequently sold, and an increase in capital expenditures in the current year.

Financing Activities. Cash used in financing activities totaled \$106.9 million for the six months ended October 31, 2017 compared to cash provided of \$121.4 million in the prior year period. This change resulted primarily from borrowings on our CLOC and share repurchases in the prior year period.

**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 \$100.1 million and \$96.0 million for the six months ended October 31, 2017 and 2016, respectively. 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.

Capital Investment. Capital expenditures totaled \$56.8 million and \$44.9 million for the six months ended October 31, 2017 and 2016, 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 \$27.5 million and \$36.2 million for the six months ended October 31, 2017 and 2016, respectively.

FINANCING RESOURCES – Our 2017 CLOC has capacity up to \$2.0 billion, and is scheduled to expire in September 2022. Proceeds under the 2017 CLOC may be used for working capital needs or for other general corporate purposes. We were in compliance with our 2017 CLOC covenants and had no outstanding balance under the 2017 CLOC as of October 31, 2017. Amounts available to borrow under the 2017 CLOC were limited by the debt-to-EBITDA covenant to approximately \$1.5 billion as of October 31, 2017. See Item 1, note 5 to the consolidated financial statements for discussion of the Senior Notes and our 2017 CLOC. We began borrowing on our 2017 CLOC in November for seasonal working capital needs.

The following table provides ratings for debt issued by Block Financial as of October 31, 2017 and April 30, 2017:

| As of   | October 31, 2017 |           |         | April 30, 2017 |           |          |
|---------|------------------|-----------|---------|----------------|-----------|----------|
|         | 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       | Stable  | A-2            | BBB       | Negative |

There have been no material changes in our borrowings from those reported as of April 30, 2017 in our Annual Report on Form 10-K.



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**CASH AND OTHER ASSETS** – As of October 31, 2017, we held cash and cash equivalents of \$181.0 million, including \$80.2 million held by our foreign subsidiaries.

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 was one forward contract outstanding as of October 31, 2017, which had a recorded amount of \$0.2 million.

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 \$1.1 million during the six months ended October 31, 2017 compared to \$4.1 million in the prior year.

**CONTRACTUAL OBLIGATIONS AND COMMERCIAL COMMITMENTS** – There have been no material changes in our contractual obligations and commercial commitments from those reported as of April 30, 2017 in our Annual Report on Form 10-K.

**REGULATORY ENVIRONMENT** – Tax reform is a current focus of the federal government, with separate tax reform bills having passed both the U.S. House of Representatives and Senate as of the date of this filing. While we continue to assess the impact of the tax legislation proposals on our business and our consolidated financial statements, it is not yet clear what the terms of final tax legislation might be, or what impact any such legislation could have on our business and our consolidated financial position, results of operations, and cash flows.

On July 10, 2017, the Consumer Financial Protection Bureau (CFPB) issued a final rule that, among other things, would prohibit the use of class action waivers in pre-dispute arbitration clauses in connection with a broad range of consumer financial products and services. The rule was scheduled to become effective September 18, 2017, with a compliance deadline of March 19, 2018. However, Congress subsequently passed a joint resolution disapproving of the rule under the Congressional Review Act. Therefore, the rule has no force or effect. In addition, this action prohibits the CFPB from issuing a rule that is substantially the same in the future without congressional action.

On November 17, 2017, the CFPB officially published its final rule changing the regulation of certain consumer credit products, including payday loans, vehicle title loans, and high-cost installment loans. The rule is scheduled to become effective January 16, 2018, with a compliance date for certain provisions of August 19, 2019. We are in the process of analyzing the impact of this rule on the consumer financial products and services we offer and our consolidated financial statements.

There have been no other material changes in our regulatory environment from what was reported as of April 30, 2017 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.

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.

We may consider whether significant items that arise in the future should 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. 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.

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The following is a reconciliation of EBITDA from continuing operations to net loss:

|  | (in 000s)          |             |                  |             |
|--|--------------------|-------------|------------------|-------------|
|  | Three months ended |             | Six months ended |             |
|  | October 31,        |             | October 31,      |             |
|  | 2017               | 2016        | 2017             | 2016        |
| Net loss - as reported                                 | \$(153,566)        | \$(146,220) | \$(284,133)      | \$(269,893) |
| Discontinued operations, net                           | 5,254              | 2,805       | 8,003            | 5,452       |
| Net loss from continuing operations - as reported      | (148,312 )         | (143,415 )  | (276,130 )       | (264,441 )  |
| Add back:  |                    |             |                  |             |
| Income taxes of continuing operations                  | (87,953 )          | (85,054 )   | (165,354 )       | (167,577 )  |
| Interest expense of continuing operations              | 21,265             | 22,620      | 42,542           | 44,086      |
| Depreciation and amortization of continuing operations | 44,792             | 45,750      | 88,390           | 87,032      |
|  | (21,896 )          | (16,684 )   | (34,422 )        | (36,459 )   |
| EBITDA from continuing operations                      | \$(170,208)        | \$(160,099) | \$(310,552)      | \$(300,900) |

**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, client trajectory, income, earnings per share, capital expenditures, dividends, stock repurchase, liquidity, capital structure, market share, industry volumes 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, 2017 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, 2017.

**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, 2017 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, management, under the supervision and with the participation of our Chief Executive Officer and Chief Financial





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Officer, 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)). 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 10 to the consolidated financial statements.

## ITEM 1A. RISK FACTORS

Except as described in Part, I, Item 2, Regulatory Environment, there have been no material changes in our risk factors from those reported at April 30, 2017 in our Annual Report on Form 10-K.

## 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 2018 is as follows: (in 000s, except per share amounts)

|                            | Total Number of<br>Shares Purchased <sup>(1)</sup> | Average<br>Price Paid<br>per Share | Total Number of Shares<br>Purchased as Part of<br>Publicly Announced Plans<br>or Programs <sup>(2)</sup> | Maximum<br>Dollar Value of<br>Shares that May<br>Yet Be<br>Purchased<br>Under the Plans<br>or Programs <sup>(2)</sup> |
|----------------------------|--|------------------------------------|--|---|
| August 1 - August 31       | 2  | \$ 30.61                           | —  | \$ 1,183,190  |
| September 1 - September 30 | —  | \$ —                               | —  | \$ 1,183,190  |
| October 1 - October 31     | —  | \$ —                               | —  | \$ 1,183,190  |
|                            | 2  | \$ 30.51                           | —  |   |

<sup>(1)</sup> We purchased approximately 2 thousand shares in connection with funding employee income tax withholding obligations arising upon the lapse of restrictions on restricted shares and restricted share units.

<sup>(2)</sup> 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.

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ITEM 6. EXHIBITS

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

- 10.1 Form of 2018 Long Term Incentive Plan Award Agreement for Deferred Stock Units, as approved on November 3, 2017.  
Second Amended and Restated Credit and Guarantee Agreement dated September 22, 2017, 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 25, 2017, file number 1-06089, is incorporated herein by reference.
- 10.2 H&R Block, Inc. 2018 Long Term Incentive Plan, filed as Exhibit 10.1 to the Company's current report on Form 8-K filed September 14, 2017, file number 1-06089, is incorporated herein by reference.
- 10.3 Form of 2018 Long Term Incentive Plan Award Agreement for Restricted Share Units, filed as Exhibit 10.2 to the Company's current report on Form 8-K filed September 14, 2017, file number 1-06089, is incorporated herein by reference.
- 10.4 Form of 2018 Long Term Incentive Plan Award Agreement for Non-Qualified Stock Options, filed as Exhibit 10.3 to the Company's current report on Form 8-K filed September 14, 2017, 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/ Jeffrey J. Jones II  
Jeffrey J. Jones II  
President and Chief Executive Officer  
December 7, 2017

/s/ Tony G. Bowen  
Tony G. Bowen  
Chief Financial Officer  
December 7, 2017

/s/ Kellie J. Logerwell  
Kellie J. Logerwell  
Chief Accounting Officer  
December 7, 2017

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