JTH Holding, Inc.
Form 10-Q
December 13, 2013

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

ý Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended October 31, 2013

OR

o 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 001-35588

JTH Holding, Inc.
(Exact name of registrant as specified in its charter)

Delaware (State of incorporation)	27-3561876 (IRS employer identification no.)

1716 Corporate Landing Parkway
Virginia Beach, Virginia 23454
(Address of principal executive offices)
(757) 493-8855
(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 ý No o

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
Yes ý No o

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

Large accelerated filer o	Accelerated filer o
Non-accelerated filer o	Smaller reporting company x

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No ý

The number of shares outstanding of the registrant’s Common Stock, $0.01 par value, at the close of business on December 9, 2013 was 12,082,357 shares.

JTH HOLDING, INC.

Form 10-Q for the Period Ended October 31, 2013

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PART I

ITEM 1
FINANCIAL STATEMENTS

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JTH HOLDING, INC. AND SUBSIDIARIES
Condensed Consolidated Balance Sheets
October 31, 2013 (unaudited) and April 30, 2013
(In thousands, except share data)

	(unaudited) October 31, 2013	April 30, 2013
Assets		
Current assets:		
Cash and cash equivalents	$2,607	$19,013
Receivables (note 2):		
Trade accounts	20,749	41,856
Notes	52,074	34,156
Interest, net	3,180	877
Allowance for doubtful accounts	(4,948)	(5,583)
Total receivables, net	71,055	71,306
Available-for-sale securities (note 3)	4,606	3,619
Income tax receivable	11,759	3
Deferred income taxes (note 7)	2,875	4,232
Other current assets	2,926	4,960
Total current assets	95,828	103,133
Property, equipment, and software, net of accumulated depreciation of $20,355 and $19,006 as of October 31, 2013 and April 30, 2013, respectively	36,470	33,037
Notes receivable, excluding current portion, net of allowance for uncollectible amounts of $1,100 and $1,101 as of October 31, 2013 and April 30, 2013, respectively (note 2)	16,793	14,352
Goodwill (note 4)	7,194	5,685
Other intangible assets, net of accumulated amortization of $5,327 and $3,998 as of October 31, 2013 and April 30, 2013, respectively (note 4)	16,316	10,921
Other assets, net	2,160	2,402
Total assets	$174,761	$169,530
Liabilities and Stockholders' Equity		
Current liabilities:		
Current installments of long-term debt (note 6)	$6,485	$3,400
Accounts payable and accrued expenses	7,851	11,954
Due to area developers (note 2)	8,315	18,248
Income taxes payable (note 7)	—	5,897
Deferred revenue - short-term portion	6,693	7,555
Total current liabilities	29,344	47,054
Long-term debt, excluding current installments (note 6)	22,987	24,283
Revolving credit facility (note 6)	38,459	—
Deferred revenue - long-term portion	8,092	10,381
Liability classified stock-based compensation awards (note 9)	—	5,111
Deferred income taxes (note 7)	2,106	865
Total liabilities	100,988	87,694
Commitments and contingencies (note 12)		
Stockholders' equity (notes 8 and 9):		
Class A preferred stock, $0.01 par value per share, 190,000 shares authorized, 0 shares issued and outstanding	—	—
	—	—

Special voting preferred stock, $0.01 par value per share, 10 shares authorized, issued and outstanding		
Class A common stock, $0.01 par value per share, 21,200,000 shares authorized, 12,037,721 and 11,975,128 shares issued and outstanding at October 31, 2013 and April 30, 2013, respectively	120	120
Class B common stock, $0.01 par value per share, 1,000,000 shares authorized, 900,000 shares issued and outstanding	9	9
Exchangeable shares, $0.01 par value, 100,000 shares issued and outstanding	1	1
Additional paid-in capital	7,818	1,920
Accumulated other comprehensive income, net of taxes	1,639	1,194
Retained earnings	64,186	78,592
Total stockholders' equity	73,773	81,836
Total liabilities and stockholders' equity	$174,761	$169,530

See accompanying notes to condensed consolidated financial statements.

JTH HOLDING, INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Operations
Three months and six months ended October 31, 2013 and 2012 (unaudited)
(In thousands, except per share data)

	Three Months Ended October 31,		Six Months Ended October 31,	
	2013	2012	2013	2012
Revenues:				
Franchise fees	$886	$2,138	$1,925	$2,805
Area developer fees	1,880	2,079	3,683	4,001
Royalties and advertising fees	1,180	1,049	2,629	2,373
Financial products	169	169	618	471
Interest income (note 2)	2,200	2,651	4,434	5,199
Tax preparation fees, net of discounts	242	225	628	441
Other revenue	760	1,027	1,465	1,292
Total revenues	7,317	9,338	15,382	16,582
Operating expenses:				
Employee compensation and benefits	8,196	7,615	14,285	14,281
General and administrative expenses	7,744	6,110	14,010	11,926
Area developer expense	705	1,115	1,533	1,832
Advertising expense	2,507	2,539	5,191	5,099
Depreciation, amortization, and impairment charges	1,745	1,432	3,323	3,023
Total operating expenses	20,897	18,811	38,342	36,161
Loss from operations	(13,580)	(9,473)	(22,960)	(19,579)
Other income (expense):				
Foreign currency transaction gains (losses)	(5)	2	(12)	4
Gain on sale of available-for-sale securities	188	—	188	—
Interest expense (note 6)	(357)	(512)	(602)	(804)
Loss before income taxes	(13,754)	(9,983)	(23,386)	(20,379)
Income tax benefit (note 7)	(5,276)	(3,872)	(8,981)	(7,905)
Net loss	$(8,478)	$(6,111)	$(14,405)	$(12,474)
Net loss per share of Class A and Class B common stock:				
Basic and diluted	$(0.66)	$(0.47)	$(1.12)	$(0.99)

See accompanying notes to condensed consolidated financial statements.

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JTH HOLDING, INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Comprehensive Loss
Three months and six months ended October 31, 2013 and 2012 (unaudited)
(In thousands)

	Three Months Ended October 31,		Six Months Ended October 31,	
	2013	2012	2013	2012
Net loss	$(8,478)	$(6,111)	$(14,405)	$(12,474)
Interest rate swap agreements, net of taxes of $-, $67, $-, and $95, respectively	—	110	—	155
Unrealized gain on equity securities available for sale, net of taxes of $397, $93, $540, and $93, respectively (note 3)	645	152	877	152
Reclassified gain on sale of available-for-sale securities included in income, net of taxes of $72, $-, $72, and $-, respectively (note 3)	(116)	—	(116)	—
Foreign currency translation adjustment	(176)	35	(316)	(193)
Comprehensive loss	$(8,125)	$(5,814)	$(13,960)	$(12,360)

See accompanying notes to condensed consolidated financial statements.

JTH HOLDING, INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Cash Flows
Six months ended October 31, 2013 and 2012 (unaudited)
(In thousands)

	2013	2012
Cash flows from operating activities:		
Net loss	$(14,405)	$(12,474)
Adjustments to reconcile net loss to net cash used in operating activities:		
Provision for doubtful accounts	3,430	3,264
Depreciation, amortization and impairment charges	3,323	3,023
Amortization of deferred financing costs	167	139
Stock-based compensation expense related to equity classified awards	741	892
Stock-based compensation expense related to liability classified awards	(872)	—
Gain on bargain purchases and sales of company-owned offices	(518)	(226)
Equity in loss of affiliate	101	69
Deferred tax expense	2,598	3,770
Gain on sale of available-for-sale securities	(188)	—
Changes in assets and liabilities decreasing cash flows from operating activities	(22,258)	(26,098)
Net cash used in operating activities	(27,881)	(27,641)
Cash flows from investing activities:		
Issuance of operating loans to franchisees	(17,420)	(20,855)
Payments received on operating loans to franchisees	1,230	1,227
Purchases of area developer rights and company-owned offices	(4,436)	(2,352)
Proceeds from sale of company-owned offices and area developer rights	205	1,386
Purchase of marketable equity securities	—	(2,980)
Proceeds from sale of available-for-sale securities	456	—
Purchase of property and equipment	(5,463)	(5,673)
Net cash used in investing activities	(25,428)	(29,247)
Cash flows from financing activities:		
Proceeds from the exercise of stock options	2,998	1,592
Repurchase of common stock	(2,495)	(1,413)
Repayment of long-term debt	(2,418)	(1,894)
Borrowings under revolving credit facility	43,104	40,147
Repayments under revolving credit facility	(4,645)	(475)
Payment for debt issue costs	—	(8)
Tax benefit of stock option exercises	416	269
Net cash provided by financing activities	36,960	38,218
Effect of exchange rate changes on cash, net	(57)	(20)
Net decrease in cash and cash equivalents	(16,406)	(18,690)
Cash and cash equivalents at beginning of period	19,013	19,848
Cash and cash equivalents at end of period	$2,607	$1,158

See accompanying notes to condensed consolidated financial statements.

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JTH HOLDING, INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Cash Flows
Six months ended October 31, 2013 and 2012 (unaudited)
(In thousands)

	2013	2012
Supplemental disclosures of cash flow information:		
Cash paid for interest, net of capitalized interest	$455	$605
Cash paid for taxes, net of refunds	6,143	6,837
Supplemental disclosures of noncash investing and financing activities:		
During the six months ended October 31, 2013 and 2012, the Company acquired certain assets from franchisees and area developers as follows:		
Fair value of assets purchased	$10,770	$6,474
Receivables applied	(6,076)	(5,242)
Accounts payable canceled	3,187	1,902
Notes and accounts payable issued	(4,716)	(1,508)
Elimination of related deferred revenue	1,271	726
Cash paid to franchisees and area developers	$4,436	$2,352
During the six months ended October 31, 2013 and 2012, the Company sold certain assets to franchisees and area developers as follows:		
Book value of assets sold	$1,872	$2,855
Loss on sale	(39)	(113)
Deferred gain on sale	—	742
Notes received	(1,628)	(2,098)
Cash received from franchisees and area developers	$205	$1,386
Accrued capitalized software costs included in accounts payable	$224	$1,135

See accompanying notes to condensed consolidated financial statements.

JTH HOLDING, INC. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

October 31, 2013 and 2012 (Unaudited)

(1) Organization and Significant Accounting Policies

(a) Organization

JTH Holding, Inc. (the Company), a Delaware corporation, is a holding company engaged through its subsidiaries as a franchisor and operator of a system of income tax preparation offices located in the United States and Canada. The Company's principal operations are conducted through JTH Tax, Inc. (d/b/a Liberty Tax Service) the Company's largest subsidiary. Through this system of income tax preparation offices, the Company also facilitates for its customers' refund-based tax settlement financial products such as instant cash advances, electronic refund checks, and personal income tax refund discounting. The Company also offers online tax preparation services.

Unless specifically noted otherwise, as used throughout these condensed consolidated financial statements, the term "Company" or "Liberty" refers to the consolidated entities of JTH Holding, Inc.

(b) Principles of Consolidation and Unaudited Financial Statements

The condensed consolidated financial statements include the accounts of JTH Holding, Inc. and its wholly owned subsidiaries. Assets and liabilities of the Company's Canadian operations have been translated into U.S. dollars using the exchange rate in effect at the end of the period. Revenues and expenses have been translated using the average exchange rates in effect each month of the period. Transaction gains and losses are recognized when incurred. The Company also consolidates any variable interest entities of which it is the primary beneficiary. When the Company does not have a controlling interest in an entity, but exerts significant influence over the entity, the Company applies the equity method of accounting. All significant intercompany balances and transactions have been eliminated in consolidation.

The unaudited condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (US GAAP) for interim financial information. The condensed consolidated financial statements, including these notes, are unaudited and exclude some of the disclosures only required in annual financial statements. Consolidated balance sheet data as of April 30, 2013 was derived from the Company's April 30, 2013 Annual Report on Form 10-K.

In the opinion of management, all adjustments necessary for a fair presentation of such financial statements in accordance with US GAAP have been recorded. These adjustments consisted only of normal recurring items. The accompanying condensed consolidated financial statements should be read in conjunction with the Company's financial statements and notes thereto included in its April 30, 2013 Annual Report on Form 10-K.

(c) Office Count

The Company operated 4,520 total offices during the 2013 tax season. During the first six months of fiscal 2014 the Company sold 65 franchise territories and purchased 74 territories from franchisees, some of which may be resold and operated by other franchisees during the 2014 tax season or subsequent tax seasons or operated as company-owned stores. Because the Company continues to sell and purchase territories until the start of the 2014 tax season and cannot predict how many offices will operate in each territory, the Company is unable to determine at this time how many offices will be in operation during the 2014 tax season. The Company expects to be able to report this information for the quarter ended January 31, 2014 because all offices should be opened at that time.

(d) Use of Estimates

Management has made a number of estimates and assumptions relating to the reporting of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements, and the reported amounts of revenues and expenses during the reporting period, to prepare these condensed consolidated financial statements and accompanying notes in conformity with US GAAP. Actual results could differ from those estimates.

(e) Foreign Operations

Canadian operations contributed $286,000 and $806,000 in revenues for the three and six months ended October 31, 2013, respectively and $291,000 and $775,000 in revenues for the three and six months ended October 31, 2012, respectively.

(f) Seasonality of Business

The Company’s operating revenues are seasonal in nature with peak revenues occurring in the months of January through April. Therefore, results for interim periods are not indicative of results to be expected for the full year.

(2) Notes and Accounts Receivable

The Company provides financing to franchisees for the purchase of franchises, clusters of territories, company-owned offices and/or for working capital and equipment needs. The franchise-related notes generally are payable over five years and the working capital and equipment notes generally are due within one year. All notes bear interest at 12%. Activity related to notes receivable for the six months ended October 31, 2013 and the fiscal year ended April 30, 2013 was as follows:

	October 31, 2013	April 30, 2013
	(In thousands)	
Balance at beginning of period	$89,340	$79,838
Notes received for:		
Sales of franchises and clusters of territories	2,898	6,770
Sales of certain assets to franchisees	1,628	15,130
Franchisee to franchisee note assumptions	3,889	11,259
Working capital and equipment loans to franchisees	17,420	75,642
Refinancing of accounts receivable	7,182	18,527
	33,017	127,328
Repayment of notes	(3,877)	(95,664)
Notes canceled	(10,052)	(21,981)
Foreign currency adjustment	(161)	(181)
Balance at end of period	108,267	89,340
Unrecognized revenue portion of notes receivable	(38,300)	(39,731)
Notes receivable less unrecognized revenue	$69,967	$49,609

Most of the notes receivable are due from the Company's franchisees and area developers (ADs) and are collateralized by the underlying franchise and are guaranteed by the respective franchisee or AD and franchise or AD owner(s). The franchisees' ability to repay the notes is dependent upon both the performance of the tax preparation industry as a whole and the individual franchisees' or ADs' areas.

The refinancing of accounts receivable results from a franchisee electing to deliver to the Company a promissory note for past-due royalties and advertising fees that have been previously recorded as accounts receivable in the condensed consolidated financial statements. Effective October 1, 2013, the Company reduced the interest rate on its past due accounts receivable to 12% and, therefore, has ceased its practice of refinancing accounts receivable into notes receivable. This is not expected to have a material effect on the Company's condensed consolidated financial statements.

Notes canceled are comprised of the cancellation of existing unpaid notes of selling franchisees in franchisee to franchisee sales that include the assumption of debt by the acquiring franchisee, and any unpaid notes receivable from a franchisee or AD related to specific territories or clusters of territories that the Company reacquires. In the latter transactions, the cancellation of notes is part of the consideration paid by the Company, and any excess of the consideration paid over the fair value of assets acquired is written off to the allowance for doubtful accounts. Unrecognized revenue relates to the financed portion of franchise fees and area developer fees and, in the case of sales of company-owned offices, the financed portion of gains related to these sales, in each case where revenue has not yet been recognized. For franchise fees and gains related to the sale of company-owned offices, revenue is recorded as note payments

are received by the Company. Payments on area developer fee notes receivable generate a corresponding increase in deferred revenue, which is amortized into revenue over the life of the area developer contract, generally 10 years. Management believes that the recorded allowance is adequate based upon its consideration of the estimated value of the franchises and ADs supporting the receivables. Any adverse change in the tax preparation industry or the individual franchisees' or ADs' areas could affect the Company's estimate of the allowance.
Notes and accounts receivable include royalties billed that relate to territories operated by franchisees located in AD territories. The Company has recorded amounts payable to area developers for their share of these receivables of $8,315,000 and $18,248,000 at October 31, 2013 and April 30, 2013, respectively.

Activity in the allowance for doubtful accounts for the six months ended October 31, 2013, and 2012 was as follows:

	2013	2012
	(In thousands)	
Beginning balance	$6,684	$5,290
Additions charged to expense	3,430	3,264
Write-offs	(4,028)	(2,680)
Foreign currency adjustment	(38)	(30)
Ending balance	$6,048	$5,844

Management considers accounts and notes receivable to be impaired if the amounts due exceed the fair value of the underlying franchise and estimates an allowance for doubtful accounts based on that excess. Amounts due include contractually obligated accounts and notes receivable less unrecognized revenue, reduced by the allowance for uncollected interest, amounts due ADs, the related deferred revenue and amounts owed to the franchisee by the Company. In establishing the fair value of the underlying franchise, management considers net fees of open offices earned during the most recently completed tax season and the number of unopened offices.

The allowance for doubtful accounts at October 31, 2013 and April 30, 2013 was allocated as follows:

	October 31, 2013	April 30, 2013
	(In thousands)	
Impaired:		
Notes receivable, including interest, and less unrecognized revenue	$8,478	$9,399
Accounts receivable	4,588	5,907
Less allowance for uncollected interest, amounts due ADs, related deferred revenue and amounts due franchisees	(2,017)	(2,336)
Net amount due	$11,049	$12,970
Allowance for doubtful accounts for impaired notes and accounts receivable	$5,255	$6,120
Nonimpaired:		
Notes receivable, including interest, and less unrecognized revenue	$66,195	$42,459
Accounts receivable	18,577	37,650
Less allowance for uncollected interest, amounts due ADs, related deferred revenue and amounts due franchisees	(11,574)	(19,992)
Net amount due	$73,198	$60,117
Allowance for doubtful accounts for non-impaired notes and accounts receivable	$793	$564

Total allowance for doubtful accounts	$6,048	$6,684

The aging of accounts and notes receivable at October 31, 2013 was as follows:

	Total Past Due	Allowance for Uncollected Interest	Current	Total Receivables
	(In thousands)			
Accounts receivable	$20,153	$(2,416)	$3,012	$20,749
Notes receivable	8,124	(1,526)	66,549	73,147
Total	$28,277	$(3,942)	$69,561	$93,896

Accounts receivable are considered to be past due if unpaid after 30 days and notes receivable are considered past due if unpaid after 90 days, at which time the notes are put on nonaccrual status.

The Company's average investment in impaired notes receivable during the six months ended October 31, 2013 and 2012 was $8,938,000 and $6,250,000, respectively. Interest income related to impaired notes was $161,000 and $362,000 for the three and six months ended October 31, 2013, respectively, and $107,000 and $245,000 for the three and six months ended October 31, 2012, respectively. The Company's investment in notes receivable on nonaccrual status at October 31, 2013 and April 30, 2013 was $6,598,000 and $8,375,000, respectively.

At October 31, 2013, the Company had unfunded lending commitments for working capital loans to franchisees and area developers of $13,308,000.

(3) Investments

During fiscal 2013, the Company purchased corporate equity securities, as a strategic investment in a business partner, for $2,980,000. At October 31, 2013, the fair value of the unsold portion of the investment was $4,606,000. The Company classifies this investment as available-for-sale and recognizes unrealized gain on the available-for sale-securities, net of tax, in accumulated other comprehensive income in the stockholders' equity section of the consolidated balance sheets. The unrealized gain, net of tax, on the available-for-sale securities at October 31, 2013 was $1,148,000.

Available-for-sale securities with a basis of $268,000 were sold during the three months ended October 13, 2013. A gain on the sale of $188,000 was recognized and reclassified out of accumulated other comprehensive income and recorded as other income.

(4) Goodwill and Intangible Assets

Changes in the carrying amount of goodwill for the six months ended October 31, 2013 are as follows:

	Goodwill	Accumulated impairment loss	Net
	(In thousands)		
Balance at April 30, 2013	$6,457	$(772)	$5,685
Acquisitions of assets from franchisees	2,763	—	2,763
Disposals and foreign currency changes, net	(1,289)	125	(1,164)
Impairments	—	(90)	(90)
Balance at October 31, 2013	$7,931	$(737)	$7,194

Components of intangible assets are as follows:

		As of October 31, 2013			As of April 30, 2013		
	Amortization period	Gross carrying amount	Accumulated amortization	Net carrying amount	Gross carrying amount	Accumulated amortization	Net carrying amount
	(In thousands)						
Amortizable other intangible assets:							
Acquired customer lists	7 years	$1,603	$(427)	$1,176	$1,603	$(171)	$1,432
Assets acquired from franchisees:							
Customer lists	4 years	2,576	(722)	1,854	1,834	(582)	1,252
Reacquired rights	2 years	2,203	(1,280)	923	1,640	(905)	735
Area developer rights	10 years	15,261	(2,898)	12,363	9,842	(2,340)	7,502
		$21,643	$(5,327)	$16,316	$14,919	$(3,998)	$10,921

During the six months ended October 31, 2013, the Company acquired the assets of various franchisees for $5,181,000. These acquisitions were accounted for as business combinations, with all value allocated to the identifiable intangible assets. The acquired businesses are operated as Company-owned offices until a buyer is found and a new franchise agreement is entered into.

The purchase price of assets acquired from franchisees was allocated as follows:

	Six Months Ended October 31,	
	2013	2012
	(In thousands)	
Customer lists and reacquired rights	$2,418	$1,797
Goodwill	2,763	2,353
Total	$5,181	