

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

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

FORM 10-Q

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

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 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 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, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

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(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 No

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	—	—
	—	—

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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.

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.

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