

MAY 2011 DEFAULT CASE STUDY

Moody's Analytics Quantitative
Research Group

Authors

Irina Korablev
+1.415.874.6278
irina.korablev@moodys.com

Yu (Lucy) Jiang
+1.415.874.6267
yu.jiang@moodys.com

Editor

Christopher Crossen

Contact Us

Americas
+1-212-553-5160
clientservices@moodys.com

Europe
+44.20.7772.5454
clientservices.emea@moodys.com

Asia (Excluding Japan)
+85 2 2916 1121
clientservices.asia@moodys.com

Japan
+81 3 5408 4100
clientservices.japan@moodys.com

Public Firm Default Report: Jackson Hewitt Tax Service (JHTXQ)

Default Event

On May 24, 2011, **Jackson Hewitt Tax Service**, a provider of tax preparation services for individuals, filed for prepackaged Chapter 11 of US bankruptcy protection in Delaware. As of January 31, 2011, the company had listed asset of \$389 million and debt of \$445 million.

Company Profile

For Jackson Hewitt, there's no season like tax season. The #2 tax preparer in the US behind H&R Block, Jackson Hewitt prepares tax returns for primarily low- and middle-income customers through more than 6,300 offices (primarily franchises), including locations within Wal-Mart Stores and mall kiosks. The aggressively expanding firm prepared more than 2 million tax returns in the fiscal year ended April 2010. The firm's tax preparers use its proprietary ProFiler decision-tree software. Other Jackson Hewitt products and services include electronic filing, refund-anticipation loans, tax school, and a Visa stored-value card. Jackson Hewitt earns some 95% of revenues during the tax season of January through April.

EDF Credit Measure and EDF Drivers

EDF value as of May 24, 2011: 35.00%

Traditional ratings, such as those used by major rating agencies, are currently more commonplace than default probabilities. Therefore, to help facilitate user's understanding, we translate the EDF credit measure into an equivalent Credit Category. Jackson Hewitt Tax Service's Credit Category (not an agency rating) at default was C.

Figure 1. One-year Jackson Hewitt Tax Service's EDF Values.



Figure 1 shows that Jackson Hewitt Tax Service's EDF credit measure has reached 35% since July 2010, ten months prior to default.

Figure 2. Drivers of Jackson Hewitt Tax Service's EDF Values

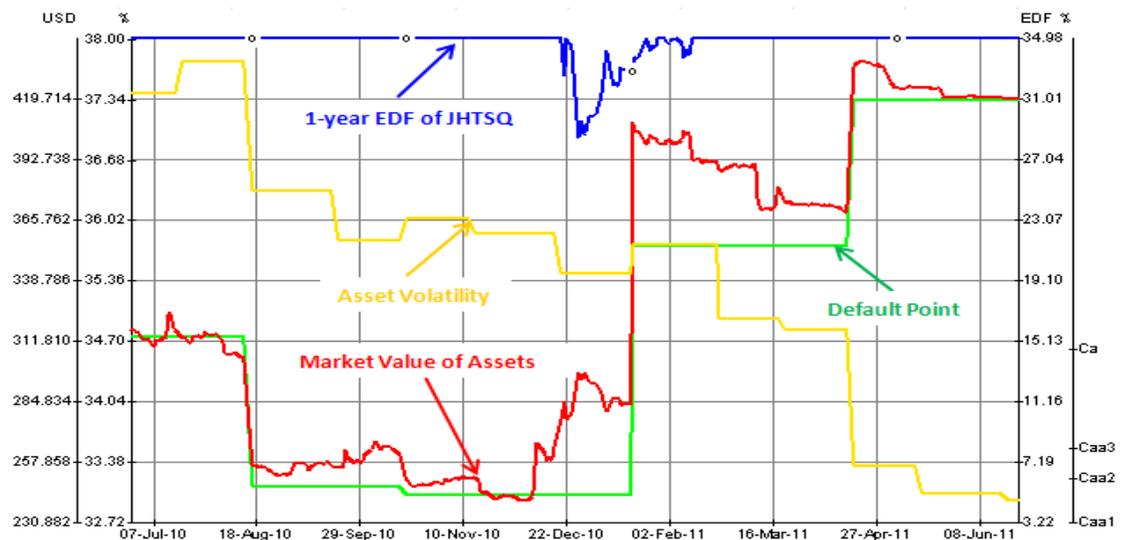


Figure 2 shows the time series of EDF values and EDF drivers, which include market value of assets, asset volatility, default point, and market leverage. Table 1 summarizes the definitions of EDF drivers.

In July 2010, the default point was \$246 million. In recent years, the heavy debt and interest rate company carried limited its financial flexibility especially after US government restricted the loans that tax preparers arrange for customers expecting refunds. As a result, the company's default point soared to \$424 million in May 2011, close to the market value of assets, \$428 million. The company's asset volatility has remained high 35% since July 2010 until default. High financial risk combined with deteriorating business value led the company to default.

Table 1. Drivers for EDF Values

EDF DRIVERS	DEFINITION
Market Value of Assets	The market's view of the enterprise value of the firm as determined by the firm's equity value, equity volatility, and liability structure
Default Point	The liabilities that matter in case of default. If the market value of assets falls below this value, it is assumed that the firm will be unable to sell assets or raise additional capital to pay its debt. A firm's default point is a value close to its short-term liabilities plus half of its long-term liabilities
Market Leverage	Ratio indicating how much of the market value of assets is financed by debt. It is calculated as the default point/market value of assets
Asset Volatility	Standard deviation of the annual change in the market value of the assets

The two main EDF value drivers are asset volatility and market leverage. **Figure 3** depicts a meter showing the level of risk on each of the two measures. The levels are relative values computed on the United States & Canada Small and Mid-Size Corporates Group.

Figure 3. United States & Canada Small & Mid-Size Corporates Group



Asset Volatility. EDF credit measures for United States & Canada Small and Mid-Size Corporate issuers such as Jackson Hewitt Tax Service reflect an average of asset volatility levels over the past three years. As of the default date, Jackson Hewitt Tax Service's asset volatility was 33.04%, within the 25th percentile relative to the United States & Canada Small and Mid-Size Corporates Group.

Market Leverage. Jackson Hewitt Tax Service's market leverage is 99.52%, which falls within the 99th percentile of the entire United States & Canada Small and Mid-Size Corporates Group.

Relative Analysis

The relative analysis feature allows users to chart EDF, fundamental data, and bond values for a selected company or group relative to other companies and/or groups. Users may manually select their own list of peer companies or groups for comparison or view a Moody's Analytics' predefined peer list, based on an automated algorithm. To determine peers for each company, Moody's Analytics finds all of the companies that share the company's Bloomberg Subgroup. Users can also customize and save their own peer company and peer group choices for future use.

Figure 4. One-year Jackson Hewitt Tax Service vs. US Consumer Services Group

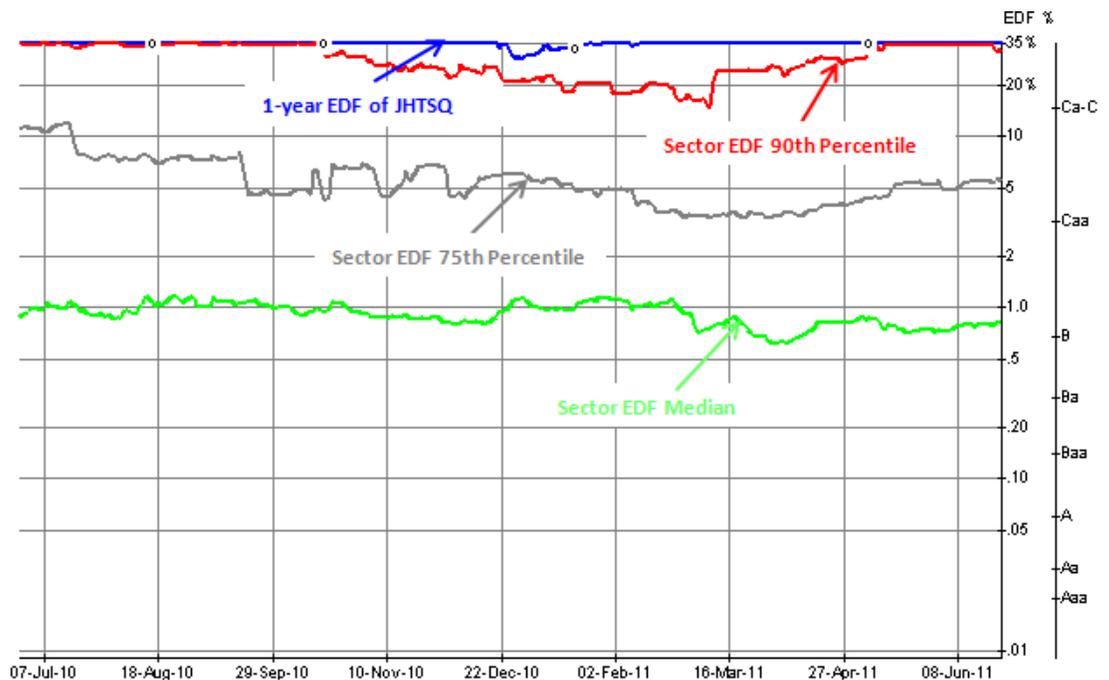


Figure 4 shows Jackson Hewitt Tax Service's EDF value surpassed the 90th percentiles of the US Consumer Services Group beginning in July 2010. The company bankrupted in May 2011.

Conclusion

Jackson Hewitt Tax Service's EDF Credit Measure indicated high default risk before default occurred. Firm EDF values remained above the 90th percentile relative to the peer group of US Consumer Services Group beginning in July 2010. High financial risk combined with deteriorating business value led the company to default.

Copyright © 2011, Moody's Analytics, Inc and/or its licensors and affiliates. All Rights Reserved. All information in this report is provided "as is" without warranty of any kind.