

WECHSLER HARWOOD LLP
Jeffrey M. Norton (JN-4827)
488 Madison Avenue, 8th Floor
New York, New York 10022
Tel. (212) 935-7400
Fax (212) 753-3630

[Additional Counsel on Signature Page]

**UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK**

RAYMOND J. KADAGIAN, On Behalf of
Plaintiff and All Others Similarly Situated,

Plaintiff,

vs.

H&R BLOCK, INC., MARK A. ERNST,
JAMES W. YABUKI, AND WILLIAM L.
TRUBECK,

Defendants.

Civil Action No. 06-CV-2306

**CLASS ACTION COMPLAINT
FOR VIOLATIONS OF THE
FEDERAL SECURITIES LAWS**

JURY TRIAL DEMANDED

Plaintiff, individually and on behalf of all other persons similarly situated, by plaintiff's undersigned attorneys, for plaintiff's complaint against defendants, alleges the following based upon personal knowledge as to plaintiff and plaintiff's own acts, and upon information and belief as to all other matters, based on, inter alia, the investigation conducted by and through plaintiff's attorneys, which included, amongst other things, a review of the defendants' press releases, Securities and Exchange Commission ("SEC") filings by H&R Block, Inc. ("H&R Block" or the "Company") and media reports about the Company. Plaintiff believes that substantial evidentiary support will exist for the allegations set forth herein after a reasonable opportunity for discovery.

NATURE OF THE CASE

1. This is a securities class action on behalf of plaintiff and all other persons or entities, except for defendants, who purchased or otherwise acquired H&R Block securities (“the “Class”) during the period February 24, 2004 and through March 14, 2006, inclusive (the “Class Period”), seeking to pursue remedies under the Securities Exchange Act of 1934 (the “Exchange Act”).

2. H&R Block provides various financial services to the general public, principally in the United States, as well as in Canada, Australia, and the United Kingdom. Its tax operations include tax return preparation, filing, and other services and products related to income tax return preparation in the United States. The company’s investment products and services include traditional brokerage products, as well as retirement accounts, annuities, insurance, fee-based accounts, online account access, equity research and focus lists, model portfolios, asset allocation strategies, and other investment tools and information. The company’s mortgage operations originate mortgage loans, service nonprime loans, as well as sell and securitize mortgage loans and residual interests. The company also offers accounting, tax, and consulting services to middle-market companies. These services include wealth management, retirement resources, payroll services, corporate finance, and financial process outsourcing.

3. During the Class Period, defendants caused H&R Block’s shares to trade at artificially inflated levels through the issuance of false and misleading financial statements. As a result of this inflation, H&R Block was able to (i) offer for sale and sell \$400 million 10-year senior unsecured notes, in reliance on defendants’ false and misleading financial reports; (ii) declare higher quarterly stock dividends than might otherwise be possible absent the sale of its debt securities; and (iii) award defendants cash and stock-based compensation based in part on the inflated value of the Company’s stock.

4. Defendants concealed the false and misleading nature of the Company’s financial statements and continued in their concealment of their false and misleading financial statements throughout the Class Period. Defendants continued in their concealment, even though the

Company had assured investors in July of 2004 that, except for minor non-material issues with its accounting internal controls, the Company's accounting controls were effective.

5. At the same time, defendants also concealed the Company's potential exposure to lawsuits stemming from the fraudulent nature and operation of their investment products. Unbeknownst to investors, defendants induced their customers to open investment accounts, using a marketing strategy that consistently misrepresented the benefits and concealed the deficiencies of those accounts. On the basis of confidential communications dating from prior to the beginning of the Class Period, there can be no doubt that defendants were well of the deceitful nature of this marketing strategy and scheme. In fact, the Company's CEO noted that, "...the product is designed to nickel and dime clients to the point where our field people don't feel as good about the product as they should."¹

6. On June 8, 2005, H&R Block revealed that its financial reports for its 2003 and 2004 fiscal years and the first three quarters of its 2005 fiscal year contained numerous accounting errors in the tens of millions of dollars and would be restated. On July 8, 2005, defendants revealed that the Company's restatement of its financial reports for 2003 and 2004 and its annual report for 2005 would be further delayed. As the Company delivered its news of the restatement and filing delays, the price of H&R staged a significant decline, losing as much as 18% of their value over a two month period, until achieving a low of \$23.89 on September 26, 2005.

7. Then, on February 23, 2006, after the close of the markets, defendants shocked investors with the news that the Company's management and its Audit Committee, in consultation with the Company's independent auditors, KPMG LLP, would undertake a

¹ See the Complaint of the NYS Attorney General Eliot Spitzer, against H&R Block, Inc., and H&R Block Financial Advisors, Inc. of March 15, 2006, at <http://www.oag.state.ny.us/press/2006/mar/H%20&%20R%20BLOCK%20COMPLAINT.pdf> and document bates no. 0090229 at [http://www.oag.state.ny.us/press/2006/mar/HR%20Block%20Exhibits%20\(Final\).pdf](http://www.oag.state.ny.us/press/2006/mar/HR%20Block%20Exhibits%20(Final).pdf), last accessed on March 15, 2006.

restatement of the Company's previously issued consolidated financial statements, including fiscal year 2006 quarterly financial statements and financial statements for the fiscal years ended April 30, 2005 and 2004. Following the Company's shocking announcement, the price of the Company's shares plummeted from its previous close on February 23, 2006 of \$25.19, for a loss of \$2.23, losing another 8.85% percent of their value, trading at a midday low of \$22.96 on February 24, 2006, on midday volume of over 5.9 million shares, *nearly four times normal daily volume*.

8. Finally, on March 15, 2006, investors learned of a \$250 million lawsuit by the NY Attorney General, addressing fraudulent marketing practices involving the Company's IRA products. The suit deflated the expectations of the investment community, in reliance on promised results from the Company's Financial Advisory segment.

9. The lawsuit, in combination with the Company's prior corrective disclosures, pointed the investment community to a pervasive pattern of erroneous, false, misleading and deceitful communications regarding the Company's products, financial statements and prospects. As a result, the price of H&R Block shares tumbled again, from the previous close of \$22.00 on March 14, 2006, to close \$20.63 on March 15, 2006, for a loss of \$1.37 or another 6.2% percent, on volume of over 14 million shares, nearly seven times normal daily volume.

10. During the Class Period, defendants knew and concealed that:

- (a) a series of internal control weaknesses existed in the Company's corporate tax accounting function;
- (b) uncorrected accounting errors were significant and remained uncorrected for more than a year after control weaknesses were discovered;
- (c) the Company *offered for sale and sold \$400 million 10-year senior unsecured notes*, despite significant uncorrected errors in the Company's financial statements;
- (d) accounting for acquisitions (primarily the acquisition of Olde Financial Corporation in fiscal year 2000) had resulted in an understatement of deferred tax liabilities and goodwill *of approximately \$129 million*, impacting fiscal years 2000 through 2004;

(e) the Company had overstated its provision for income taxes in connection with acquisitions **by approximately \$11 million** for each of the fiscal years ended April 30, 2004 and 2003;

(f) accounting for a gain on sale of previously securitized residuals in fiscal year 2003 resulted in a net overstatement in revenues for that year **of approximately \$36 million**;

(g) Company accounting for leases resulted in a cumulative overstatement of retained earnings **of approximately \$7 million** as of April 30, 2004;

(h) accounting errors pertaining to the Company's provision for income taxes resulted in a cumulative overstatement **of approximately \$10 million to \$14 million in retained earnings** as of April 30, 2004;

(i) a calculation error pertaining to an incentive compensation accrual at the Company's Mortgage Services segment resulted in an understatement of pre-tax expense in fiscal year 2004 **of \$12.4 million**;

(j) overstatement of capitalized branch office costs at the Company's Investment Services segment and a corresponding understatement of operating expenses resulted in an understatement of pre-tax expense **of approximately \$4 million in fiscal year 2004 and \$2 million in fiscal 2003**;

(k) errors pertaining to the Company's state effective income tax rate for the fiscal quarters ended October 31, 2005 and July 31, 2005, fiscal years ended April 30, 2005 and 2004 and the fiscal quarters for fiscal years 2005 and 2004 resulted in a cumulative understatement of state income tax liability, net of federal income tax benefit, of approximately \$32 million as of April 30, 2005; and

(l) the Company had adopted fraudulent marketing practices for its IRA investment products, at the risk of lawsuits and government action, within the Company's troubled Financial Advisory segment.

JURISDICTION AND VENUE

11. Jurisdiction is conferred by §27 of the 1934 Act. The claims asserted herein arise under §§10(b) and 20(a) of the 1934 Act and Rule 10b-5.

12. Venue is proper in this District pursuant to §27 of the 1934 Act. The corporate headquarters of H&R Block are located in the District.

13. In connection with the acts and conduct alleged herein, defendants, directly and indirectly, used the means and instrumentalities of interstate commerce, including the United States mails and the facilities of the national securities exchanges.

PARTIES

14. Plaintiff purchased shares of H&R Block stock at artificially inflated prices during the Class Period as described in the attached certification and was damaged thereby, as set forth in the accompanying certification, incorporated by reference herein.

15. Defendant provides various financial services to the general public, principally in the United States, as well as in Canada, Australia, and the United Kingdom. Its tax operations include tax return preparation, filing, and other services and products related to income tax return preparation in the United States. The company's investment products and services include traditional brokerage products, as well as annuities, insurance, fee-based accounts, online account access, equity research and focus lists, model portfolios, asset allocation strategies, and other investment tools and information. The company's mortgage operations originate mortgage loans, service nonprime loans, as well as sell and securitize mortgage loans and residual interests. The company also offers accounting, tax, and consulting services to middle-market companies. These services include wealth management, retirement resources, payroll services, corporate finance, and financial process outsourcing. H&R Block was organized in 1955 and maintains its corporate and administrative offices, where the Company's day-to-day business activities are conducted, at 4400 Main Street, Kansas City, Missouri.

16. Defendant Mark A. Ernst (“Ernst”) was Chairman and CEO for the Company. Ernst was hired Company executives with expertise needed to offer clients financial services and was responsible for improvements to the Company’s planning processes. Ernst was a Certified Public Accountant, whose experience included previous positions with PricewaterhouseCoopers (Coopers & Lybrand) and U.S. Treasury Department’s Comptroller of the Currency. On June 9, 2005, defendant Ernst received a \$398,640 cash bonus, 150,000 stock options and 15,000 restricted shares as incentive compensation for fiscal year 2004.²

17. Defendant Jeffrey W. Yabuki (“Yabuki”) was Executive Vice President and COO of the Company during the Class Period. Yabuki’s experience includes his previous position as president and chief executive officer of American Express Tax & Business Services, managing all aspects of the company's tax, accounting and consulting businesses. Yabuki holds CPA certificates in California and Minnesota, a NASD Series 7 license, and is a past member of the Minnesota Board of Accountancy. On June 9, 2005, defendant Yabuki received a \$145,174 cash bonus, 80,000 stock options and 8,000 restricted shares as incentive compensation for fiscal year 2004.³ On November 18, 2005, defendant Yabuki sold 674,118 shares of his H&R Block stock, for proceeds of \$16,398,392.

18. Defendant William L. Trubeck (“Trubeck”) was Executive Vice President and CFO of the Company during the Class Period. Trubeck’s experience includes his previous position as Chief Financial Officer and Chief Administrative Officer of Waste Management, Inc., where he was responsible for oversight of the corporation's financial affairs, established an internal audit department and developed “Accounting Rules of the Road.”

19. The individuals named as defendants in ¶¶16 -18 are referred to herein as the “Individual Defendants.” The Individual Defendants, because of their positions with the Company and its business segments, possessed the power and authority to control the contents of

² See SEC Form 8-K, filed by defendants on June 9, 2004.

³ Id.

H&R Block quarterly reports, press releases and presentations to securities analysts, money and portfolio managers and institutional investors, *i.e.*, the market. Each defendant was provided with copies of the Company's reports and press releases alleged herein to be misleading prior to or shortly after their issuance and had the ability and opportunity to prevent their issuance or cause them to be corrected. Because of their positions and access to material non-public information available to them but not to the public, each of these defendants knew that the adverse facts specified herein had not been disclosed to and were being concealed from the public and that the positive representations which were being made were then materially false and misleading. The Individual Defendants are liable for the false statements pleaded herein, as those statements were each "group-published" information, the result of the collective actions of the Individual Defendants.

SCIENTER

20. In addition to the above-described involvement, each Individual Defendant had knowledge of H&R Block's problems. Each defendant was motivated to conceal such problems, consistent with their efforts to represent the business as a reputable financial services Company. Defendant Trubeck, as CFO, provided for financial reporting and communications with the market. Communications with the market, including conference calls, as well as internal reports showing H&R Block's forecasted and actual growth were prepared under their direction. Defendant Ernst, having served as CEO also provided for communications with the market, including conference calls, as well as reports on Company operations, financing and press releases issued by the Company. Each Individual Defendant sought to demonstrate that he could lead the Company successfully and generate the growth expected by the market. Each individual defendant also owed a duty to the Company and its shareholders not to trade on inside information.

FRAUDULENT SCHEME AND COURSE OF BUSINESS

21. Each defendant is liable for (a) making false statements, *or* (b) failing to disclose adverse facts known to him about H&R Block. Defendants' fraudulent scheme and course of business that operated as a fraud or deceit on purchasers of H&R Block publicly traded securities was a success, as it (a) deceived the investing public regarding H&R Block's prospects and business; (b) artificially inflated the prices of H&R Block's publicly traded securities; (c) allowed Company insiders, including defendants, to sell millions of dollars of Company stock at artificially inflated prices; and (c) caused plaintiff and other members of the Class to purchase H&R Block's publicly traded securities at inflated prices.

DEFENDANTS' FALSE AND MISLEADING STATEMENTS

MADE DURING THE CLASS PERIOD

22. On February 24, 2004, defendants issued a press release entitled, "H&R Block Reports 59 Cents Per Share Third Quarter Profit - Early Tax Season Results Consistent with Full Year Guidance". The press release stated in part:

KANSAS CITY, Mo. – H&R Block Inc. (NYSE:HRB) today reported net income of \$106.7 million, or 59 cents per diluted share, and record revenues of \$977.2 million for the third quarter ended Jan. 31.

Third quarter revenues increased 2 percent from \$958.4 million last year. Third quarter net income declined \$25.6 million or 19.3 percent compared with last year when the company reported third quarter earnings of \$132.3 million, or 73 cents per diluted share. Third quarter 2004 results include a \$17 million gain on sale of certain mortgage assets. Third quarter 2003 results include a \$130.9 million gain on a similar transaction. Excluding the effect of these gains, third quarter net income increased \$42.9 million or 80.2 percent over the prior year.

The profitable third quarter marks the first time in the company's history that it has reported a profit in each of the first three quarters of its fiscal year. H&R Block typically reports losses in its first and second quarters, and often in its third quarter as well, due to the seasonal nature of its tax and business services units.

"All of our business segments executed effectively and delivered improved performance. We saw double-digit revenue growth in each of our businesses, excluding the mortgage asset sales that we've noted," said Chairman and Chief Executive Officer Mark A. Ernst.

“Performance in the tax filing season thus far is consistent with our overall expectations for a good, but not great, tax season,” Ernst said. “After a slow start, growth in retail tax filing has accelerated in the month of February and our digital tax services are growing very well.”

The quarter results included \$6.8 million in stock-based compensation expense, an expense that was not included in the comparable quarter last year. H&R Block began to expense the costs of stock-based compensation at the beginning of the current fiscal year.

For the nine-month period ending Jan. 31, the company reported net income of \$122.3 million, a 43.1 percent increase compared with last year. Earnings per diluted share increased 45.7 percent to 67 cents. Revenues for the nine month period increased 10.8 percent to \$2.1 billion.

On a consolidated basis, the company continues to expect fiscal 2004 GAAP earnings-per-share in the range of \$3.65 to \$3.85 and revenue growth at the high end of its target range of 10 to 15 percent. Included in these expectations is about \$24 million or 8-cents per share, of non-cash stock-based compensation expenses.

U.S. Tax Operations

U.S. Tax operations reported pretax earnings of \$68.2 million, compared with \$34.1 million last year, an improvement of \$34.1 million. U.S. tax operations reported a 14.9 percent increase in revenues for the quarter to \$463.6 million, compared with \$403.6 million last year.

Compared with last year, the improved performance is due to an increase in the number of clients served, increased revenue per client and better expense management. These improvements were partially off-set by expenses related to adding 873 tax locations to the company’s retail network, including 459 company-owned offices in former franchise territories. Company-owned offices in former major franchise territories contributed \$24.3 million to the increase in revenues.

For the nine-month period, revenues increased 19.8 percent to \$551.4 million, up \$91.1 million from \$460.3 million last year. The segment reported a \$155.9 million pretax loss for the nine-month period, an improvement of \$56.3 million or 26.5 percent compared with the \$212.2 million pretax loss last year.

From Jan. 1 through Jan. 31, tax preparation and related fees from retail tax offices increased 8.6 percent to \$500.3 million. The average fee per client served rose 8.9 percent to \$134.99. Total clients served, including office and digital tax solutions clients, increased 4.6 percent to 5 million. Retail tax offices served 3.7 million clients, a 0.2 percent decline from last year. Clients served by H&R Block’s digital tax solutions increased 21.7 percent.

For the tax season through Feb. 15, tax preparation and related fees from retail tax offices increased 3.9 percent to \$1.1 billion. In the period ending Feb. 15, the average fee per client increased 8 percent to \$135.48. Total clients served, including office and digital tax solutions clients, increased 0.1 percent to 9.9 million. Retail tax offices served 7.9 million clients, a decline of 3.9 percent from last year. Clients served by H&R Block’s digital tax solutions increased 19.6 percent. However, year-over-year comparisons must be viewed cautiously due to

the intra-week variability of tax filings and the difference in the days of the week included in the comparative periods.

“While we saw a slow start to the tax filing season in our retail offices, the growth that we are seeing in February and the mix of clients that are coming to H&R Block indicate that we are likely to be at the lower end of our expected range for retail client growth and at the higher end of our expected range for revenue per client,” Ernst said. “Combined with superior performance in our digital businesses, we believe that we are on track to meet our overall targets for the year.”

Mortgage Operations

Mortgage operations, which include Option One Mortgage Corp. and H&R Block Mortgage Corp., reported pretax earnings of \$154.5 million for the quarter, a \$108 million decrease compared with pretax earnings of \$262.5 million last year. For the nine-month period, pretax earnings decreased 10.8 percent to \$502.3 million, compared with \$563.1 million last year.

Third quarter revenues from mortgage operations decreased 16.4 percent to \$331.9 million, compared with \$397 million last year. For the nine-month period, revenues increased 7 percent to \$986 million, compared with \$921.9 million last year.

Third quarter 2004 results include a \$17 million gain on sale of certain mortgage assets. Third quarter 2003 results include a \$130.9 million gain on a similar transaction. Excluding the effect of these gains, third quarter pretax income from mortgage operations increased 4.5 percent.

“We’re pleased with the mortgage segment results, which continue to meet our expectations. These results support our long-held view that the interest rate environment would not have a significant effect on our mortgage performance. Overall origination activity continued to be strong in the quarter, while margins declined somewhat as we had expected.” Ernst said.

For the third quarter, the company originated \$5.4 billion in mortgage loans, an 18.1 percent increase over last year’s \$4.5 billion. The number of loan originations in the third quarter was 35,795, a 15.8 percent increase compared with last year.

Mortgage servicing revenues for the quarter were \$55.1 million, an increase of \$11.7 million, or 27 percent, compared with \$43.4 million last year. On Jan. 31, 2004, the servicing portfolio was \$42.2 billion, an increase of \$13.3 billion, or 46 percent, compared with Jan. 31, 2003, and up 5.2 percent over the previous quarter.

Third quarter pretax income from H&R Block Mortgage increased 25.9 percent. Nearly 40 percent of the company’s retail loans were to clients of other H&R Block businesses.

The segment’s residual interests continued to perform better than expected, primarily due to better than modeled loss and interest rates. Consequently, the company realized a net write-up in residual balances of \$36 million, which was

recorded in other comprehensive income on the balance sheet, net of deferred taxes.

Business Services

RSM McGladrey Business Services Inc. reported third quarter revenues of \$112.3 million, an 11.5 percent increase compared with \$100.7 million last year. The segment reported pretax earnings of \$2 million, a \$6.2 million improvement, compared with a loss of \$4.2 million in the third quarter last year.

For the nine-month period, revenues increased 8.8 percent to \$319.8 million. The segment reported a pretax loss of \$7.5 million compared with a pretax loss of \$12.3 million last year.

“Our capital markets business enjoyed another strong quarter compared with last year. Higher fees in our core accounting and tax services also contributed to improved performance,” Ernst said.

Investment Services

H&R Block Financial Advisors Inc. reported third quarter revenues of \$57.8 million, an increase of 20.2 percent compared with the same quarter last year. The segment reported a pretax loss of \$12.8 million, a 59.7 percent improvement compared with last year’s pretax loss of \$31.8 million.

“We saw strong improvement in all of the key drivers of the business this quarter,” Ernst said. “Overall, results of our Financial Advisors business reflect sustained changes that should allow us to have continuing performance improvement.”

For the nine-month period, revenues increased 6.8 percent to \$167.4 million, compared with \$156.7 million last year. The segment reported a pretax loss of \$41.9 million compared with \$92.5 million in the first nine months of last year, which included \$24 million in goodwill impairment charges.

International Tax Operations

In the third quarter, revenues from international tax operations increased 23.6 percent to \$10.8 million, compared with \$8.8 million last year. The segment reported a pretax loss of \$6.4 million, compared with a pretax loss of \$5.7 million last year.

For the nine-month period, revenues increased 24.7 percent to \$35.4 million. The segment reported a \$12.3 million pretax loss, compared with last year’s pretax loss of \$12.4 million.

“We enjoyed a successful conclusion to the tax season in Australia. However, unfavorable exchanges rates in Canada resulted in a higher loss for the quarter,” Ernst said.

Dividend declared

H&R Block's board of directors declared a quarterly cash dividend of 20 cents per share, payable April 1, 2004, to shareholders of record March 11, 2004. This payment will be the company's 166th consecutive quarterly dividend.

Share repurchases

During the third quarter, the company repurchased 3.7 million shares of its common stock at an aggregate cost of \$192.3 million, or an average price of \$52.61 per share. Year to date, the company has repurchased 7.8 million shares at an aggregate cost of \$370 million, or an average price of \$47.51 per share.

23. On June 9, 2004, the Company issued a press release entitled, "H&R Block Reports Record Annual Revenues And Earnings - Company Announces Dividend and Share Repurchase Authorization Increases". The press release stated in part:

H&R Block Inc. (NYSE: HRB) today reported record revenues and net income for both its fourth quarter and fiscal year ended April 30.

Fourth quarter revenues totaled \$2.2 billion, a 14.8 percent increase over the fourth quarter last year. Consolidated net income for the quarter increased 16.4 percent to \$575.6 million. Fourth quarter earnings per diluted share increased 19.2 percent to \$3.23.

Fiscal year revenues increased 12.3 percent to \$4.2 billion. Consolidated net income for the fiscal year increased 20.3 percent to \$697.9 million. Earnings per diluted share increased 23.8 percent to \$3.90, excluding a change in accounting principle. After the change in accounting principle, earnings per share increased 22.5 percent to \$3.86. The company adopted Emerging Issues Task Force No. 00-21 (EITF 00-21) in its second quarter.

"Fourth quarter results completed a year that saw record revenues, record earnings and balanced growth from our mix of businesses," said H&R Block Chairman and Chief Executive Officer Mark A. Ernst. "We experienced improved results across all business lines in our fourth quarter.

"H&R Block's combined annual growth rate for earnings per share has increased 29 percent in the past five years. Our mix of businesses has generated solid results, even in challenging business environments," Ernst said.

H&R Block began to expense the costs of all stock-based compensation at the beginning of fiscal year 2004. The fiscal year results include \$25.7 million, or 9 cents per diluted share, in stock-based compensation expense, compared with \$2.1 million last year.

Fiscal 2005 Outlook

"Next year, we expect earnings per share in the range of \$4.00 to \$4.25 per share. We expect solid growth in our mix of businesses. We continue to believe that,

over the long-term, the company's mix of businesses can generate earnings consistent with our long-term guidance of earnings per share growth in the range of 13 to 18 percent per year," Ernst said.

"A changing interest rate environment will likely result in a flattening or slight decline in mortgage earnings, which will partially offset solid earnings growth in our other businesses," he said.

Board Actions

Reflecting the company's strong financial condition and continuing performance, H&R Block's board of directors approved an increase of the quarterly cash dividend from 20 cents to 22 cents per share, a ten percent increase, effective with the quarterly dividend payment on Oct. 1, 2004 to shareholders of record on Sept. 10, 2004. This payment will be the company's 168th consecutive quarterly dividend.

Also, the board authorized the company to repurchase up to 15 million of its shares, in addition to the 11.3 million shares remaining at year end on its previous repurchase authorization from June 11, 2003.

"In the past year, the company has returned significant value to shareholders by repurchasing \$518.5 million, or 10.6 million, of its shares," Ernst said. "The new repurchase authorization reflects the confidence that the board of directors has in H&R Block's future. Given our strong cash position, share repurchase continues to be a great way for us to enhance shareholder value."

During the fourth quarter, the company repurchased 2.8 million shares at an average cost of \$52.77 per share.

U.S Tax Operations

For the fiscal year, U.S. tax operations reported pretax income of \$627.6 million, an increase of 14.7 percent from pretax income of \$547.1 million in fiscal 2003.

U.S. tax operations reported a 3.2 percent increase in fourth quarter pretax income, which totaled \$783.5 million, up from \$759.3 million in the fourth quarter of fiscal 2003.

The segment's revenues for the year increased 12.5 percent to \$2.1 billion. The increase was driven by an 8 percent increase in the average fee per client served, the acquisition of former major franchise territories during fiscal year 2004, and a change from last year's contractual agreement with Household Taxmasters Inc. that resulted in increased revenues from refund anticipation loan (RAL) participation.

The segment reported \$1.5 billion in revenues for the fourth quarter, an increase of 10.1 percent compared with last year's fourth quarter.

"We improved client satisfaction with our combination of financial information and tax services, which is a unique value of the H&R Block brand. And we made solid progress with our multi-channel strategy. The number of software and online clients increased 12.2 percent to 3.2 million, with the fastest growth in tax

solutions that blend the services of a tax professional with software and online products,” Ernst said.

“While we’re disappointed in the 0.8 percent decline in clients served, we understand the factors behind the decline and are taking steps to strengthen our market position. We will open 500 to 600 new offices in underserved areas where we could not provide the convenience clients wanted. And we are reviewing our marketing plans to identify the best mix of messages, products and services to drive client growth in the early part of tax season.”

Mortgage Operations

Mortgage operations, which includes Option One Mortgage Corp. and H&R Block Mortgage Corp., reported fourth quarter pretax income of \$175.9 million, a 34.4 percent increase, compared with \$130.9 million in the fourth quarter last year.

For fiscal 2004, the mortgage segment reported pretax income of \$678.3 million, a 2.3 percent decrease compared with \$694.0 million in pretax income in fiscal 2003.

Fourth quarter revenues grew 28.4 percent to \$344.3 million, up from \$268.3 million the prior year. Fiscal 2004 revenues increased 10 percent to \$1.3 billion, up from \$1.2 billion in fiscal 2003.

For fiscal 2004, gains on sales of mortgage loans increased 8 percent to \$716.7 million, compared with \$663.6 million in fiscal 2003. In fiscal year 2003, the company reported a \$130.9 million gain on the sale of previously securitized residual interests, compared to \$40.7 million in the current year. Net of \$30.7 million in impairments of older residuals, compared with \$54.1 million in 2003, the mortgage segment’s total gains on sales were \$726.7 million for fiscal 2004, compared to \$740.3 million in the prior year.

Loan production increased to \$23.3 billion in fiscal 2004, a 40.3 percent increase over the previous year. An increase in the number of loan specialists, improvements in the company’s closing ratio, and a 4.9 percent increase in the average loan size all contributed to this growth.

Included within these results, H&R Block Mortgage Corp., H&R Block's retail mortgage subsidiary, originated 6.4 percent more loans, 48.9 percent of which were made to retail clients of other H&R Block businesses.

"The mortgage business performed as we expected it would. We saw continued growth in mortgage originations and lower margins due to the anticipated increase in interest rates," Ernst said.

“Originations have been strong across all of our origination channels, and loan performance has exceeded modeled expectations. We continue to manage our mortgage business to optimize cash earnings, and we remain confident that mortgage operations will continue to perform well,” he said.

Option One’s mortgage servicing business increased the number of loans serviced 31.6 percent to 324,364. The servicing portfolio at year-end increased 44.7 percent to \$45.3 billion, compared with last year’s portfolio.

The segment's residual interests continued to perform better than expected, primarily due to better than modeled credit losses and interest rates. Consequently, the company realized a net write-up to residual balances of \$167.1 million during fiscal year 2004, including \$67.1 million in the fourth quarter, which was recorded in other comprehensive income on the balance sheet, net of deferred taxes.

Business Services

RSM McGladrey Business Services, Inc. reported fourth quarter pretax earnings of \$26.8 million, compared with a net loss of \$1.9 million in the same quarter last year. For fiscal 2004, the segment reported pretax earnings of \$19.3 million, compared with a net loss of \$14.1 million in 2003.

In the fourth quarter, the business services segment reported revenues of \$179.4 million, an increase of 28 percent. For the fiscal year, revenues increased 15 percent to \$499.2 million.

"We are beginning to realize the potential that exists in this business segment. Our capital markets business enjoyed a strong year, and an improving economic environment for our middle market clients resulted in higher revenues in our core accounting and tax services," Ernst said.

Fiscal year 2003 includes a goodwill impairment charge of \$11.8 million related to the segment's payroll and benefits processing company. The segment wrote off \$576,000 in intangible assets in the fourth quarter of 2004.

Investment Services

Investment services reported a fourth quarter pretax loss of \$22.5 million, an improvement of \$13.3 million from a fourth quarter loss last year of \$35.8 million. For the fiscal year, investment services recorded a pretax loss of \$64.4 million, an improvement of \$63.8 million compared with a loss of \$128.3 million in fiscal 2003. Fiscal year 2003 results include \$24 million of goodwill impairment charges.

Investment services reported fourth quarter revenues of \$62 million, a 40.8 percent increase from the same quarter last year. Revenues for the fiscal year increased 14.3 percent to \$229.5 million.

"We see continued improvement in H&R Block Financial Advisors' results. We believe that this business has been restructured in a way that allows us to compete effectively as the investment climate improves," Ernst said.

"The retention and recruitment of experienced advisors continues to be a key initiative in the upcoming year, along with building stronger links between financial advisors and tax professionals in our U.S. tax operations."

24. On July 23, 2004, defendants filed SEC Form 10-K. The filing stated in part: I T E M 9 A . CONTROLS AND PROCEDURES

Disclosures controls are procedures that are designed with the objective of ensuring that information required to be disclosed in reports filed or under the

Securities Exchange Act of 1934, such as this Form 10-K, is recorded, processed, summarized and reported in accordance with the SEC's rule. Disclosure controls are also designed with the objective of ensuring that such information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer or persons performing similar functions, as appropriate, to allow timely decisions regarding disclosure.

Our Disclosure Controls were designed to provide reasonable assurance that the controls and procedures would meet their objectives. Our management, including the CEO and Principal Accounting Officer, does not expect that our Disclosure Controls will prevent all error and all fraud. A control system, no matter how well designed and operated, can provide only reasonable assurance of achieving the designed control objectives and management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simply error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusions of two or more people, or by management override of the control.

Because of the inherent limitations in a cost-effective, maturing control system, submitted misstatements due to error or fraud may occur and not be detected. As of the end of the period covered by this Form 10-K, we evaluated the effectiveness of the design and operation of our Disclosure Controls. The controls evaluation was done under the supervision and with the participation of the management, including our CEO and Principal Accounting Officer.

The evaluation of our Disclosure Controls included a review of the controls' objectives and design, our implementation of the controls and the effect of the controls on the information generated for the use in this Form 10-K. In the course of the controls evaluation, we identified a series of control weaknesses related to our corporate tax accounting function. These weaknesses relate specifically to the reconciliation and level of detailed support of both current and deferred income tax accounts. We also determined an acceleration of taxable income was warranted in one of our segments, however, there was no change to our total income tax provision. Upon identification of these control weaknesses, immediate corrective action was undertaken. Our efforts to strengthen financial and internal controls continue. We expect these efforts to be completed by the end of fiscal year 2005.

Based on this evaluation, other than the item described above, our CEO and Principal Accounting Officer have concluded these controls are effective. There have been no significant changes in internal controls, or in other factors, which would significantly affect these controls subsequent to the date of evaluation.

25. On August 24, 2004, the Company issued a press release entitled, "H&R Block Reports First Quarter Financial Results - The company reported a loss of 26 cents per diluted share, compared to 3 cents of earnings last year". The press release stated in part:

KANSAS CITY, Mo. -- H&R Block Inc. (NYSE: HRB) today reported a \$44.1 million net loss for its first quarter, compared with earnings of \$5.2 million last year. Revenues totaled \$482.7 million, a 2.6 percent decline from last year. The company reported a loss of 26 cents per diluted share, compared to 3 cents of earnings last year.

The decline in earnings was primarily due to decreased mortgage segment income and additional off-season costs associated with expanding the company's tax business.

"The first quarter loss is in line with our internal expectations, and consistent with our annual earnings guidance range of \$4 to \$4.25 per share," said H&R Block Chairman and Chief Executive Officer Mark A. Ernst. "This quarter we also repurchased 7.5 million shares in accordance with our objective to return excess capital to shareholders.

"In our mortgage unit, loan production increased more than 28 percent for the quarter, while margins declined because of the increase in market interest rates. We expected margin compression in the first two quarters of our fiscal year, with improved earnings performance in the second half of the year after adjusting to the higher rate environment. Our mortgage business is on track to meet our expectations for the year," Ernst said.

In its first quarter, H&R Block acquired 7.5 million shares of its common stock at an aggregate cost of \$347.4 million, or an average price of \$46.56 per share. Over the past year, the number of H&R Block shares outstanding has declined 6.8 percent to 166.2 million shares outstanding.

The first quarter results include \$4.6 million in stock-based compensation expense, compared with \$1 million last year. H&R Block began to expense the costs of all stock-based compensation at the beginning of fiscal year 2004.

The prior year results include a change in accounting principle related to the adoption of Emerging Issues Task Force No. 00-21 (EITF 00-21) as of May 1, 2003. This change reduced last year's first quarter net income by \$6.4 million, or 3 cents per diluted share.

Tax Services

Beginning with the first quarter of fiscal year 2005, the company has aggregated its U.S and International tax services into one segment.

Tax services revenues increased 9.7 percent to \$50.4 million. The segment reported a pretax loss of \$113 million, which was 13.5 percent higher than the pretax loss of \$99.6 million in the first quarter of fiscal 2004. Results were negatively affected by an additional \$9 million in off-season losses related to

former major franchise territories acquired during the second quarter of fiscal year 2004.

“We’re on pace to open 500 to 600 new offices in under-penetrated areas where we see growth opportunities. We also expect to add 400 more Wal-Mart locations,” Ernst said. “We are confident in the value that clients receive from H&R Block and are working to make our services even more accessible.”

Mortgage Services

Mortgage services, which include Option One Mortgage Corp. and H&R Block Mortgage Corp., reported first quarter pretax income of \$93.5 million, a 42.9 percent decrease, compared with \$163.8 million in the first quarter last year.

First quarter revenues declined 8.4 percent to \$268.1 million, from \$292.6 million the prior year.

The mortgage segment’s total gains on sales were \$137.5 million for the first quarter, a 24.6 percent decline compared with \$182.3 million in the prior year’s first quarter.

Loan production increased to a record \$6.8 billion for the quarter, a 28.4 percent increase over the previous year’s quarter. An increase in the number of loan applications, improvements in the company’s closing ratio, and an increase in the average loan size all contributed to this growth.

Included within these results, H&R Block Mortgage Corp., H&R Block's retail mortgage subsidiary, reported a 7.8 percent decline in originations. About 48 percent of H&R Block Mortgage’s loans were made to retail clients of other H&R Block businesses.

“I’m confident in the actions we have taken to position the business for success in this changing rate environment. We are increasing our distribution capability and improving our ability to serve clients and sustain our competitive position as a service leader. We believe these investments, along with reduced interest rate volatility, will result in another year of strong mortgage financial results,” Ernst said.

The segment’s residual interests continued to perform better than expected, primarily due to better than modeled credit losses. Consequently, the company realized a net write-up to residual balances of \$53.5 million during the first quarter of fiscal year 2005, which was recorded as other comprehensive income, net of deferred taxes. The company did not realize any gains from the sale of residual assets in the quarter.

Business Services

Business services reported a first quarter pretax loss of \$10.1 million, compared with a pretax loss of \$6.7 million in the same quarter last year. The segment reported revenues of \$109.1 million, an increase of 10.8 percent.

A significant backlog in the capital markets business at the end of fiscal year 2003 increased first quarter revenue and earnings last year, which affected the year to year comparison with the first quarter of 2005.

“Our core accounting and tax services enjoyed a strong off-season quarter. It’s encouraging that most of our increased revenue is the result of our strategic growth initiatives, including the development and implementation of a marketing and sales infrastructure. We’re well-positioned to capitalize on the opportunity this market offers,” Ernst said.

Investment Services

Investment services reported a first quarter pretax loss of \$18.3 million, an increased loss of \$4.5 million compared with last year’s \$13.8 million loss.

Investment services reported first quarter revenues of \$53.6 million, a 6 percent decrease from the same quarter last year.

“We’re disappointed with investment services’ first quarter results, which are consistent with the weak investment climate affecting the entire industry. However, I’m confident that our business has been positioned in a way that will allow us to grow in support of the investment needs of our clients,” Ernst said.

26. On October 22, 2004, the Company issued a press release entitled, “H&R Block to Issue \$400 Million in 10-Year Notes”⁴. The press release stated in part:

Block Financial Corp., a subsidiary of H&R Block Inc. (NYSE: HRB), today announced that it has priced and will issue \$400 million in 10-year senior unsecured notes to be unconditionally guaranteed by H&R Block. The notes will bear an interest rate of 5 1/8 percent per year and will mature in 2014.

The company expects to use the proceeds from the offering for general corporate purposes, including the repayment of \$250 million 6 3/4 percent senior notes when they come due in November 2004.

A registration statement relating to these securities has been filed with the Securities and Exchange Commission and has become effective. This press release shall not constitute an offer to sell or the solicitation of an offer to buy nor shall there be any sale of these securities in any state in which such offer, solicitation or sale would be unlawful under the securities laws of any such state.

JPMorgan Securities, Inc. and Merrill Lynch & Co. serve as co-lead underwriters and joint bookrunners for the transaction. Citigroup Global Markets Inc., Goldman Sachs & Co. and H&R Block Financial Advisors Inc. are serving as co-managers.

⁴ The documents underlying and incorporated by this press release include defendants’ SEC Form S-3 filed on August 6, 2004, SEC Form 424B3 filed on October 22, 2004, SEC Form 424B5 filed on October 26, 2004 and SEC Form 8-K filed on October 21, 2004.

27. On November 23, 2004, the Company issued a press release entitled, “H&R Block Reports Second Quarter Financial Results - Lower full-year earnings guidance on Mortgage outlook”. The press release stated in part:

H&R Block Inc. (NYSE: HRB) today reported a \$52.2 million net loss for the second quarter of its 2005 fiscal year, compared with earnings of \$10.4 million in the second quarter last year. Revenues totaled \$539.3 million, a 5.2 percent decline from last year. The company reported a loss of 32 cents per diluted share, compared with 6 cents of earnings last year.

The decline in earnings was due primarily to decreased income in the mortgage segment. An asset write-down in investment services and corporate development spending associated with new business initiatives also contributed to the earnings decline. Historically, H&R Block has reported second quarter losses because of the seasonal nature of its tax and accounting businesses, although the company reported a profit in the second quarter of fiscal 2004.

“The competitive environment in the mortgage industry limited our pricing flexibility in the face of rising interest rates in the secondary market,” said Chairman and Chief Executive Officer Mark A. Ernst. “In view of industry-wide trends, we were satisfied with our levels of loan originations, which grew 2.7 percent compared with the second quarter last year, although operating margins did not improve as much as we had anticipated.

“We will begin deploying a series of technology enabled service enhancements to our mortgage broker clients during the fourth quarter. We believe that these will improve productivity and position our mortgage business for success as we transition to a higher rate environment. Primarily due to the current mortgage pricing environment and investments in support of these technology enhancements, we are lowering our current fiscal year earnings guidance to the range of \$3.50 to \$4.00 per share,” Ernst said.

In the second quarter, H&R Block acquired 3.8 million shares of its common stock at an aggregate cost of \$182.2 million, or an average price of \$47.81 per share. Over the past year, the number of H&R Block shares outstanding has decreased 8 percent to 163.5 million shares outstanding.

The second quarter results include \$7.9 million in stock-based compensation expense, compared with \$3.1 million last year. H&R Block began to expense the costs of all stock-based compensation at the beginning of fiscal year 2004.

For the six months ended Oct. 31, H&R Block reported a net loss of \$96.3 million, or 58 cents per diluted share, compared with earnings of \$15.5 million last year, or 9 cents per diluted share. Revenues for the six-month period decreased 4 percent to \$1 billion, from \$1.1 billion last year.

The prior year results include a change in accounting principle related to the adoption of Emerging Issues Task Force No. 00-21 (EITF 00-21) as of May 1, 2003. This change reduced last year’s first quarter net income by \$6.4 million, or 3 cents per diluted share.

Tax Services

Tax services revenues increased 11.8 percent to \$74.1 million. The segment reported a pretax loss of \$134 million, which was 2.8 percent higher than the pretax loss of \$130.4 million in the second quarter of fiscal 2004.

For the six-month period, revenues were \$124.6 million, up \$12.3 million from \$112.3 million last year, a 10.9 percent increase. The pretax loss for the six-month period was \$247 million, \$17 million, or 7.4 percent, higher than last year.

“We continue on pace to open more than 600 new offices and 400 additional Wal-Mart locations. This investment in expanding our office network will make our tax services more accessible and convenient to a greater number of tax filers, which we expect will drive client growth this tax season. Our off-season costs remain in line with our expectations,” Ernst said.

Investment Services

Investment services reported a second quarter pretax loss of \$24.6 million, an increase of \$9.2 million compared with last year's \$15.3 million loss. The second quarter loss included a \$6 million write-down of a branch office facility. Investment services reported second quarter revenues of \$53.8 million, a 2 percent increase from the same quarter last year.

The pretax loss for the second quarter increased 34.5 percent, or \$6.3 million compared with the first quarter of fiscal year 2005. Revenues improved slightly, up .3 percent compared with first quarter revenues of \$53.6 million.

For the six-month period, revenues decreased 2.1 percent to \$107.3 million from \$109.7 million last year. The pretax loss increased \$13.7 million, or 47.2 percent compared with a loss of \$29.1 million for the first six months of fiscal year 2004.

“The general market climate for investment services remained very weak during the early months of the quarter, though we began to see improvement in October and into November,” Ernst said.

Dividend declared

H&R Block's board of directors declared a quarterly cash dividend of 22 cents per share, payable Jan. 3, 2005, to shareholders of record Dec. 13, 2004. This payment will be the company's 169th consecutive quarterly dividend.

28. On February 24, 2005, the Company issued press release entitled, “H&R Block Reports 55 Cents Per Share Third Quarter Profit - Increases in Tax Clients and Mortgage Originations Highlight Strong Quarter”. The press release stated in part:

H&R Block Inc. (NYSE:HRB) today reported net income of \$91.7 million, or 55 cents per diluted share, for the third quarter ended Jan. 31, 2005. Revenues in the third quarter were a record \$1.03 billion, a 7.2 percent increase over the prior year's quarter.

"A strong start to the tax season combined with solid performances from our mortgage and business services segments were highlights of a good quarter," said Mark A. Ernst, chairman and chief executive officer. "I'm particularly pleased that the strategic actions taken in our tax and mortgage businesses are generating success in their respective markets."

Early tax season results through Feb. 15 included a 10.6 percent increase in total tax preparation and related fees over the comparable period last year, paced by 4 percent retail client growth and a 6.3 percent increase in average fees per retail client.

"The performance thus far is consistent with our expectations for a good tax filing season, supported by strong, new client acquisition, solid retention and increased client satisfaction with our services," Ernst said.

Mortgage results included a 56.8 percent increase in loan originations to \$8.4 billion over the comparable quarter last year, and a 28.9 percent increase from the previous quarter's origination levels. Continued aggressive pricing in the mortgage market limited gain-on-sale margins. At the same time, progress was made in the company's effort to lower overall cost of origination, offsetting a significant share of the gain-on-sale margin reduction.

"We're very pleased with the performance of our mortgage business, where our strategy to expand service capacity is leading to strong origination volume growth despite the slowing industry," Ernst said. "In addition, we made considerable progress in lowering the cost of origination, reducing it by 37 basis points in the third quarter alone. This is consistent with our objective to realize a sustained 50 to 75 basis point reduction over the next 12 to 18 months."

Third quarter results include \$12.5 million, or 5 cents per share, in stock-based compensation expense. The expense was \$6.8 million in the previous year. In addition, the results reflect a \$16.7 million litigation payment made to H&R Block.

For the nine months ended Jan. 31, H&R Block reported a net loss of \$4.6 million, or 3 cents per diluted share, compared with net income of \$122.3 million, or 67 cents per diluted share, in the prior year. The reduction was due primarily to declining income from the mortgage segment as competitive pricing has reduced margins across the industry.

Tax Services

A 3.7 percent increase in retail tax clients, combined with higher average fees per client, helped drive revenue and income increases in the tax segment for the third quarter. Tax services revenues climbed 11.9 percent to \$531.1 million compared with last year, while pretax income improved 4.1 percent to \$64.3 million.

Early tax season results from Jan. 1 through Feb. 15 show that tax preparation and related fees from retail tax offices increased 10.6 percent to \$1.2 billion. The average fee per client rose 6.3 percent to \$143.90. Retail tax offices served 8.3 million clients through Feb. 15, while total clients served, including digital tax clients, increased 1.4 percent.

“More than any other factor, the success we’re experiencing can be attributed to the quality of service our tax professionals are providing to our clients,” Ernst said. “Expansion of our office network, operational improvements and successful marketing mean that more consumers are benefiting from that service.”

H&R Block’s digital tax business, including its award-winning TaxCut® software and online tax services, reported a 9.1 percent decrease in paid clients served through Feb. 15. Modest growth in online clients was offset by a decline in software units sold.

“Both consumer and competitive changes in the digital tax market have restricted the client growth that we expected this season. However, we will continue to follow a disciplined approach to pricing and marketing our digital services, although it may limit our ability to achieve this year’s client growth objectives,” Ernst said.

For the nine-month period, tax services revenues rose 11.7 percent to \$655.6 million, while the pretax loss of \$182.6 million was 8.6 percent higher than a year ago.

Reasons For Falsity

29. Defendant H&R Block offers accounting, tax, and consulting services to middle-market companies. Nevertheless, the financial statements issued this tax and accounting services business during the Class Period were false and misleading, as such financial information was not prepared in conformity with generally accepted accounting practices (“GAAP”), nor was the financial information a fair presentation of the Company’s operations due to the Company’s improper accounting, in violation of GAAP and SEC rules.

30. Moreover, during the Class Period, defendants were aware or in conscious and reckless disregard of the fraudulent marketing practices they had adopted for the offering of retirement products within the Company’s troubled Financial Advisory segment. Quarter after quarter, defendants noted heavy losses within their investment services business. Defendants knew that their efforts to offer IRA investment products to their tax clients was being met with resistance by investment professionals, since the fees associated with the accounts typically

outstripped earnings, *resulting in a guaranteed money-losing proposition for nearly 85% of the Company's clients.*

THE TRUTH UNFOLDS

31. On June 8, 2005, the Company issued the first in a string of corrective disclosures regarding its intentions to restate its financial statements for multiple quarters and years, in a press release entitled, "H&R Block Reports 13 Percent Increase in Fourth Quarter EPS - Upcoming Fiscal Year Guidance Set at \$4.25 to \$4.65 Per Share - Company Announces Two-for-One Stock Split, Dividend Increase". The press release stated in part:

H&R Block Inc. (NYSE: HRB - News) today reported record fourth quarter results, driven by revenue growth in each of its lines of business. Fourth quarter revenues increased 7.2 percent over the prior year's quarter to \$2.4 billion. Revenues for the fiscal year were \$4.4 billion, a 4.1 percent increase over the prior year.

Consolidated net income for the fourth quarter increased 6.9 percent to \$616.5 million. Consolidated net income for the fiscal year declined 10.5 percent to \$635 million. Earnings per diluted share for the fourth quarter increased 13 percent to \$3.66. For the fiscal year, earnings per diluted share decreased 4.1 percent to \$3.76.

"We finished our fiscal year on a very high note," said Mark A. Ernst, H&R Block's chairman and chief executive officer. "We successfully completed an important transition year in our tax business, saw our mortgage business returning to more normalized levels of profitability, finished a stellar year at RSM McGladrey, and achieved important changes in our investment services organization during the quarter.

"For our U.S. tax operations, opening more than 1,200 new retail locations this year was an important first step in positioning us for future client growth as these new locations mature.

"Increasing our mortgage sales staff resulted in a 33 percent increase to loan origination volume for the year. At the same time, we are lowering our cost of origination to succeed in a more competitive environment," Ernst said.

Fiscal 2006 Outlook

For fiscal year 2006, the company said it expects earnings per share in the range of \$4.25 to \$4.65.

"Our focus on building our business for the long term is expected to deliver strong financial results in the coming year," Ernst said.

Restated Results

The company said that it will restate its results for fiscal years 2004 and 2003, as well as previously reported quarterly results for fiscal 2005, making several changes that it believes collectively will result in an estimated 6-cent increase in earnings per share in fiscal 2004, and an estimated 8-cent decrease in earnings per share in fiscal 2003. The restatement had the effect of adding 14 cents per share to fiscal 2005 results reported prior to the fourth quarter. The decision to restate was based on the cumulative impact of the items.

The company has not completed its analysis of the restatement adjustments, and accordingly, the effects of the restatement are preliminary and subject to change. These adjustments are being reviewed with the company's current and former auditors, and additional detail will be provided later in the company's Form 8-K and 10-K filings.

Tax Services

Tax services' fourth quarter revenues increased 6.1 percent to \$1.7 billion. Fiscal year revenues rose 7.6 percent to \$2.4 billion.

Pretax income for tax services' fourth quarter increased 4.9 percent to \$845.7 million. For the fiscal year, pretax income was up 4 percent to \$663 million.

Clients served in retail offices declined 0.1 percent for the tax season, compared with a 3.2 percent decline the prior year. Digital tax solutions clients decreased 6.3 percent.

"This year's retail location expansion is part of a multi-year plan to more aggressively compete and reclaim market share," Ernst said. "The expansion contributed to a significant increase in early season clients, reversing a two-year trend of declining client traffic. In addition, the expansion combined with client service improvements made H&R Block more convenient for clients, reduced their wait time, and generated significant increases across all measures of client satisfaction, a strong indication that the changes we're making are working. We plan to continue our expansion program, adding approximately 500 to 700 new offices to our company-owned and franchised network in fiscal 2006.

"While we're disappointed in our digital tax solutions results, we are encouraged by increasing consumer use of our services that blend digital technology with tax professional assistance," Ernst said. "We recognize that digital services are an important and growing client channel, and work has already begun to compete more aggressively and capture a larger market share in the coming tax season."

32. On June 9, 2005, defendants issued SEC Form 8-K. The filing stated in pertinent part:

Item 4.02 Non-Reliance on Previously Issued Financial Statements or a Related Audit Report or Completed Interim Review.

(a) On June 7, 2005, the Company's management and the Audit Committee of the Board of Directors, in consultation with the Company's independent auditors, KPMG LLP, concluded to restate previously issued consolidated financial statements, including 2005 quarterly financial statements and financial statements for the fiscal years ended April 30, 2004 and 2003. The Company arrived at this conclusion during the course of its closing process for the fiscal year ended April 30, 2005. The restatement pertains to the following issues:

- *An error pertaining to its accounting for acquisitions (primarily the acquisition of Olde Financial Corporation in fiscal year 2000) that resulted in an understatement of deferred tax liabilities and goodwill of approximately \$129 million. This error subsequently resulted in an overstatement of the provision for income taxes for each fiscal year subsequent to the acquisition, including an overstatement of approximately \$11 million for each of the fiscal years ended April 30, 2004 and 2003.*
- *An error in calculating a gain on sale of previously securitized residuals in fiscal year 2003, resulting in a net overstatement in revenues for that year of approximately \$36 million. This error will be corrected by deferring the gain as of the transaction date in fiscal year 2003 and recognizing revenue from the sale as revenue from accretion in subsequent fiscal years, including revenue of approximately \$18 million in fiscal year 2004.*
- *An error pertaining to its accounting for leases. This error will be corrected by restating lease expense to record the effect of rent holidays and mandatory rent escalation on a straight-line basis over the lease term. The cumulative overstatement of retained earnings arising from this error was approximately \$7 million as of April 30, 2004.*
- *Calculation errors pertaining to its provision for income taxes arising from a series of control weaknesses related to the Company's corporate tax accounting function that was disclosed in its Form 10-K for the fiscal year ended April 30, 2004. These errors resulted in a cumulative overstatement of approximately \$10 million to \$14 million in retained earnings as of April 30, 2004.*
- *A calculation error pertaining to an incentive compensation accrual at the Company's Mortgage Services segment as of April 30, 2004. This error resulted in an understatement of pre-tax expense in fiscal year 2004 of \$12.4 million.*
- *An error that resulted in the overstatement of capitalized branch office costs at the Company's Investment Services segment and a corresponding understatement of operating expenses. This error resulted in an understatement of pre-tax expense of approximately \$4 million in fiscal year 2004 and \$2 million in fiscal 2003.*

The Company has determined that the cumulative effect of the errors could be material to the financial statements for the year ended April 30, 2005 if prior period financial statements were not restated. Accordingly, the Company determined that the errors were most appropriately corrected through restatement of previously issued financial statements. The Company has not completed its preparation of restated consolidated financial statements, including its valuation

analysis of additional goodwill arising from the restatement, and such restated financial statements have not been audited. Accordingly, the effects of the items noted above on such consolidated financial statements are preliminary and subject to change. The Company will file restated consolidated financial statements as part of its Annual Report on Form 10-K for the fiscal year ended April 30, 2005, or by amending previous SEC filings.

On June 7, 2005, the Company's Audit Committee discussed the matters disclosed in this Item 4.02(a) with management and KPMG, who audited the Company's financial statements for the fiscal year ended April 30, 2004. On June 7, 2005, the Company provided information regarding the matters disclosed in this Item 4.02(a) to PricewaterhouseCoopers LLP ("PwC"), who audited the Company's consolidated financial statements for the fiscal year ended April 30, 2003. The Company has discussed the matters with PwC, which has stated that they have not had the opportunity to fully consider the matters.

33. In the Company's press release of June 8, 2005, defendant Ernst signaled to the investment community his expectations for aggressive efforts to reclaim marketshare. However, on June 29, 2005, a Morgan Stanley Analyst report overturned the assumptions behind Ernst's assertions, recommending that investors take profits in the stock:

Quick Comment: Following management's comments at our conference, there is no change to our thesis and we are maintaining an Underweight rating on HRB.

What's New: CEO Mark Ernst suggested that in spite of a 13% increase in the office count, the actual capacity increased by only 3%. Mr. Ernst believes that the company will not increase its marketing spending going forward. However, he did not provide, in our view, a good explanation for the weak end to F2005. By contrast, the Mortgage business is doing well and the Business Services segment may surprise on the upside.

Implications: We continue to expect flat to down Tax volumes and margins going forward. We have mixed thoughts on the bank charter opportunity. We recommend taking profits at these levels.

34. On July 6, 2005, the Company issued press release entitled, "H&R Block Announces Organization Change". The press release stated in part:

H&R Block Inc. (NYSE: HRB - News) today announced that Melanie K. Coleman, vice president and corporate controller, has decided to leave the company. Coleman has been designated as the controller for the new local telecommunications company expected to be spun off following the proposed merger of Sprint Corp. and Nextel Communications.

Coleman, who joined H&R Block in 2002, will remain with the company through the end of July to ensure a smooth transition of Block's restatement of earnings and filing of the Form 10-K. The company plans to immediately begin a search for her replacement.

35. Then, on July 8, 2005, the Company issued press release entitled, "H&R Block Reschedules Filing of Annual Report on Form 10-K". The press release stated in part:

H&R Block Inc. (NYSE:HRB - News) today disclosed that it will not file its Annual Report on Form 10-K with the Securities and Exchange Commission (SEC) by the prescribed due date of July 14, 2005. The company plans to file a notification of late filing with the SEC to extend the filing due date to July 29, 2005, and anticipates filing the 2005 Annual Report on Form 10-K by the extended filing due date.

The delayed filing is due to additional time required for the company to finalize its restatement of results for fiscal years 2004 and 2003, as previously reported in its fiscal year-end press release on June 8, 2005.

Due to the delay in the Annual Report and Form 10-K filing, the company will also reschedule reporting its first quarter results from the previously announced date of Aug. 18, 2005. The company expects to report first quarter results on Sept. 1, 2005.

36. In light of defendants' disclosures regarding their plans to restate the Company's financial results and uncertainties regarding the Company's financial performance in general, the price of H&R Block stock staged a significant decline, from as high as \$29.20⁵ on July 6, 2005, to a low of \$23.89 on September 26, 2005.

37. In his efforts to drum up interest in the stock, on September 27, 2005 defendant Ernst explained during a presentation at the 2005 Thomas Weisel Partners Consumer Conference his "impatience" with the Company's inability in and the importance of achieving greater client referrals, from those ***having an existing H&R Block tax relationship, to a Financial Advisory relationship, stating in part:***

⁵ As adjusted for a 2:1 split that occurred on August 23, 2005.

Moderator

I guess one last question because we are running out of time here, but the Financial Advisory segment has been under a lot of pressure the last few years. Jeff Yabuki working on it has obviously improved some of the dynamics this past quarter. How do you look at the opportunity to align that with your tax business, the potential of what you had announced last year of maybe a little separate CPA-focused operation, which would be a little bit higher-end than your core customer base? How does that play out?

Mark Ernst - H&R Block - Chairman, CEO

You know, strategically, part of the reason we've been very patient with that business, maybe too patient, but is that strategically that business does for us what we believed it could do for us. In that sense, if a client is referred from a H&R Block tax relationship to also a Financial Advisory relationship, we see a 10 or 11 percentage point increase in client loyalty. So instead of seeing retained at 70%, we will see people retain in the low 80s if they've just added that additional relationship. So from that perspective, strategically it has this loyalty effect in the tax business that gives us additional economic benefit from having done this.

We also believe that, strategically, having access to the Block client base as a referral source gives us a recruiting and a retention advantage with Financial Advisors that we can build off of when it comes to building out this business.

So for those two reasons and a lot of others, we believe that we are strongly positioned to bring these two businesses together.

The key question obviously is that's great but you don't do that unless you can make it profitable and economically attractive at the same time. I think the change we made in the management team about nine months ago now is clearly starting to show up in results. ***This past quarter, for the first time in a long time, we had an operating profit before amortization of intangibles, which is the real measure that I look at. I think we are solidly on a path to get much better performance out of this business. But, it's on a short leash, so --.***

Moderator

That's about all the time we have. Thank you so much, Mark.

38. As the markets waited for tangible signs of brighter business prospects, defendants shocked investors, ***with news of additional accounting errors***, resulting in a cumulative understatement of the Company's tax liability of approximately \$32 million. On February 23, 2006, after the close of the markets, defendants shocked investors with their news

of their intention to make a historical restatement, in their press release entitled, "H&R Block Reports Third Quarter Financial Results". The press release stated in part:

KANSAS CITY, Mo.--(BUSINESS WIRE)--Feb. 23, 2006--H&R Block Inc. (NYSE: HRB - News)

Revenues Up; Earnings Impacted by Lower Mortgage Results and Litigation Settlement Cost

Corporate Tax Remediation to Result in Prior-Period Restatement

Full-Year Earnings Guidance Changed to \$1.65 to \$1.85 per Share

H&R Block Inc. (NYSE: HRB - News) today reported that revenues rose 12 percent in its fiscal third quarter to \$1.2 billion from \$1.0 billion in the prior-year period. Slightly lower revenues in Mortgage Services were offset by higher revenues in all other segments of the company's operations.

Net earnings were \$28.8 million, or 9 cents per diluted share, for the third quarter of fiscal 2006. The quarterly results include an after-tax charge of \$31.7 million, or 10 cents per share, for a previously announced proposed litigation settlement and associated legal costs. For the third quarter of 2005, net earnings were \$92.3 million, or 28 cents per share, which included the benefit of a \$10.1 million after-tax legal recovery representing 3 cents per share.

"As we head into our busiest quarter of the year, we've seen an industry-wide slower start to the tax filing season than in previous years," said Mark A. Ernst, chairman and chief executive officer. "Early season operating challenges experienced in our tax business further hurt our January comparative results. Results since January have begun to reverse the effects of this later start.

"Within our Mortgage business, pricing changes we implemented over the past five months have begun to have the effect that we expected in terms of improving gains on sale," said Ernst. "Loan origination levels have been at the lower end of our expectations as competitive pressures in the industry continue. We continue to take those actions that we believe will optimize the profitability of our business going forward."

Tax Services pretax earnings improved 3 percent over last year's quarter, excluding the effect of the litigation charge, driven by higher pricing. Mortgage Services earnings increased 46 percent over the previous quarter but were down 42 percent over year-ago results. Results for both Investment Services and Business Services matched the company's expectations.

As part of its ongoing work to remediate control weaknesses in its corporate tax function, the company said that it will restate its results for fiscal years 2005 and 2004, as well as previously reported quarterly results for fiscal 2006. *The restatement pertains principally to errors in determining the company's state effective income tax rate, resulting in a cumulative understatement of its state income tax liability of approximately \$32 million as of April 30, 2005. The company estimates that the restatement will result in a 7-*

cent decrease in earnings per share in fiscal 2005 and a 2-cent decrease in earnings per share in fiscal 2004. The company has not completed its analysis of the restatement adjustments, and, accordingly, the effects of the restatement on all prior periods are preliminary and subject to change. These adjustments are also being reviewed with the company's registered public accounting firm. The company will report in amended filings with the Securities and Exchange Commission the further restatement of results for fiscal years 2005 and 2004, and restatements for the first two quarters of fiscal 2006 for the income tax adjustments.

The company has updated its fiscal 2006 earnings guidance to a range of \$1.65 to \$1.85 per share, down from its previous range of \$1.90 to \$2.15 per share. The new range reflects results to date for fiscal 2006 and excludes the litigation and any special charges.

Commenting on the outlook for the company's results, Ernst said, "Given the continued aggressive pricing in the mortgage industry and our slow start to the tax season, we believe that it is prudent to take a cautious view of the fourth quarter."

For the nine months ended Jan. 31, 2006, H&R Block reported a net loss of \$81.4 million, or 25 cents per share, compared with earnings of \$8.8 million, or 3 cents per share, for the same period of fiscal 2005. Nine-month revenues rose 15 percent to \$2.4 billion in fiscal 2006 from \$2.1 billion last year.

39. On February 24, 2006, following the Company's shocking announcement, the price of the Company's shares plummeted from its previous close on February 23, 2006 of \$25.19, for a loss of \$2.23, losing 8.85% percent of their value, trading at a midday low of \$22.96 on February 24, 2006, on midday volume of over 5.9 million shares, *nearly four times normal daily volume.*

40. On March 15, 2006, investors finally learned that defendants' expectation of results from their Financial Advisory segment relied in part on the offering of fraudulent marketing practices. On March 15, 2006, the Attorney General of the State of NY Eliot Spitzer issued a press release entitled, "H&R BLOCK SUED FOR FRAUDULENT MARKETING OF IRAS - Tax Prep Service Failed to Properly Disclose Fees". The press release stated in part:

Attorney General Eliot Spitzer today sued the nation's largest tax preparation company for fraudulent marketing of individual retirement accounts (IRAs).

The suit alleges that the H&R Block Company steered hundreds of thousands of its clients, including almost 30,000 New Yorkers, into IRAs that were virtually guaranteed to lose money because of a combination of hidden fees and low interest rates.

"The conduct described in today's complaint is particularly appalling because many of those hardest hit were working families who struggle to save," Spitzer said. "Instead of providing these families with accurate information that would have allowed them to make informed choices, H&R Block steered them into retirement accounts that actually shrank over time."

The Attorney General's office began the investigation in 2005 after receiving information from an H&R Block tax preparer.

Over the past four years, H&R Block opened more than half a million "Express IRA" accounts for its tax preparation clients. Customers were told that the IRA paid "great rates" and was "a better way to save," but 85 percent of the customers who opened the accounts paid the company more in fees than they earned in interest. More than 150,000 H&R Block customers closed their accounts, incurring additional undisclosed fees, as well as nearly \$6 million in tax penalties.

The civil complaint filed today in State Supreme Court in Manhattan cites internal documents showing that H&R Block's senior management knew that many of its customers were losing money on their Express IRAs. For example, in a 2002 email to Mark Ernst, the company CEO, a district manager complained about the impact of these accounts on customers:

"I really don't think maintenance fees should exceed the amount of interest that we are paying on these accounts. Clients won't be happy seeing [their] investments decreasing"

Mr. Ernst forwarded this email to the Express IRA product manager and added his own comments:

"The attached note . . . reflects the general sense that I think exists - that Express IRA is the right thing for our clients, but the product is designed to nickel and dime clients to the point where our field people [don't] feel as good about the product as they should... ."

Some conscientious H&R Block employees (including the person who brought the information to the Attorney General) actually refused to promote the product to clients.

In 2003, an internal H&R Block report prepared by the Express IRA product manager described the growing concerns of tax professionals about the product in the following way:

"Top 4 reasons tax pros are not offering the product:

- 1. \$15 setup fee – 'it's too steep for my clients'***
- 2. \$15 recontribution fee – 'they've already paid once, why charge them again?'***

3. Low interest rate – ‘my client will never make up the fee’

4. \$10 annual maint. fee – ‘my clients have to pay this in addition to the \$15 fee.’”

The company’s management took no action to address these concerns. Instead, H&R Block continued to tout the Express IRA as a good way for lower and moderate income people to save. The complaint alleges that the company pushed the Express IRA in an effort to encourage repeat customers for its tax preparation services and to maximize its fee revenue.

Spitzer’s complaint describes the experience of several New York customers:

– A 32-year-old Albany resident with a taxable income of \$17,847 made a one-time, minimum contribution of \$300 to an Express IRA in 2002. Over the past four years, the investment earned \$10.29 in interest but incurred a total of \$45 in fees. The Albany resident’s investment lost 12 percent of its value and will continue to decline.

– A 68-year-old resident of Brooklyn with a taxable income of \$25,421 made a one-time contribution of \$300 to an Express IRA in 2004. The individual was charged a \$15 account opening fee, a \$10 account maintenance fee, and a \$25 closing fee when the account was closed after 18 months. These fees dwarfed the interest earned on the account (\$5.18) and, as a result, the Brooklyn resident’s investment declined by 15 percent.

Advocates for lower-income consumers praised the lawsuit:

Sarah Ludwig, Director of the Neighborhood Economic Development Advocacy Project in New York, said: "Lower and middle- income New Yorkers encounter a host of abuses at tax prep sites such as H&R Block. The abuse that the Attorney General has uncovered in connection with the Express IRA is particularly troubling. Working families are entitled to know all the facts about a retirement product – both good and bad – before they decide to invest. Our organization strongly encourages people to get their taxes done at free tax prep sites, which will prepare people's taxes professionally, with zero incentive to rip people off."

Spitzer’s lawsuit specifically alleges that H&R Block, based in Kansas City, failed to adequately disclose its fees to its customers, failed to warn that the interest paid would not cover the fees in certain instances, and misleadingly described the interest rates as "great" when they were at times less than one percent annually. This misleading and incomplete disclosure violated New York’s consumer fraud law and was a breach of the company’s fiduciary duty to its clients. Relief sought includes an injunction from further violations of New York law, damages and civil penalties.

The investigation was led by Assistant Attorney General James Park, with Assistant Attorneys General Gary Connor and Matthew Gaul, and Economist Hampton Finer, and was supervised by David D. Brown, IV, Chief of the Investment Protection Bureau.

41. Well aware of the intentions of the State of New York to sue *for almost a month*, defendants declined to disclose the details until after the markets *had fully absorbed the shock of their corrective disclosure of February 23, 2006, regarding the Company's erroneous, false and misleading financial statements*. Following the Attorney General's announcement, defendants immediately issued a response, designed to dissuade investors of any wrongdoing on their part. Defendants' press release entitled, "H&R Block Defends Its Express IRA Product and Delivers Strong Rebuttal to New York AG's Attack; Nearly 600,000 Americans Helped by Block's Retirement Savings Product" stated in part:

KANSAS CITY, Mo.--March 15, 2006-- H&R Block today released a strong rebuttal to the New York State Attorney General's attack on the company's Express IRA product, which has helped more than half a million Americans take a critical and often first step toward saving for their future.

"Make no mistake -- we believe in the Express IRA product and are proud of the opportunities it presents for our clients. At a time when the country's personal savings rate has declined to minus 0.7 percent, we've helped 596,000 of our clients begin saving for their future, and more than 40% of them had never saved before," said H&R Block Chairman and CEO Mark A. Ernst.

"Currently, our Express IRA savers have accumulated more than \$360 million in their accounts plus Saver's Credit tax benefits of over \$50 million. That's a powerful first step toward ensuring a secure financial future," Ernst said.

"If in the unfortunate event this matter does end up in court, H&R Block will fight vigorously to defend the Express IRA product and ensure it remains available to our many clients who rely on it as a helpful savings option."

Last month the company received a Notice of Intent to Sue followed by a settlement demand letter from the Attorney General's office for alleged damages related to the product. In a response, H&R Block Senior Vice President and General Counsel Nick Spaeth, a former Attorney General of North Dakota, challenged the allegations, noting that the product provides a compelling incentive for lower-income Americans to save for the future, with benefits that include:

- A safe, FDIC-insured money market account with no financial market risk;

- Competitive interest rates;

- Low minimum deposit requirements -- either \$300 up front or \$25 a month, which is less than most banks and other financial institutions;

-- Immediate income tax benefits, including access to the Retirement Saver's Credit, for eligible individuals below certain income levels; and

-- Ease and convenience of beginning to save at a time when clients are about to receive a lump sum of cash via their tax refund.

"We have cooperated fully and provided volumes of data and detailed analyses to the Attorney General's office, but it has ignored all of the positives and has chosen to launch this attack," said Spaeth. "Some clients do withdraw their funds early and incur IRS penalties; that's true with any IRA product. However, it should not detract from the enormously positive impact of this program, particularly on first-time savers."

The information shared reflects a case-by-case evaluation of data available for all Express IRA accounts opened between 2001 and 2005. "We will continue to communicate directly with the Attorney General's office to help them understand that this product is an innovative and sound savings choice," Spaeth said.

The company is represented by the New York law firm Stroock & Stroock & Lavan through Robert Abrams, former New York Attorney General.

"H&R Block has been a pioneer in creating a unique product, the Express IRA, which has provided the opportunity for hundreds of thousands of Americans to start a pattern of savings," said Abrams. "Block has worked with scholars, policymakers in the federal government, and leaders in non-profit organizations, such as the Brookings Institution and the Aspen Institute, to provide low- and moderate-income people the chance to open retirement savings accounts and take advantage of tax savings incentives.

"Out of all the Express IRA accounts opened between 2001 and 2005, 78% have experienced positive net tax savings benefits and interest earnings. This is a positive and powerful statement of achievement. Further, this effort has not created windfall profits for H&R Block -- indeed the company has lost money operating this program," Abrams concluded.

Nearly half of the Express IRA clients have been able to save more than \$50 million in taxes because H&R Block helped them claim the Retirement Saver's Credit, a low-income retirement savings incentive enacted by Congress in 2002. Since the debut of the Saver's Credit, H&R Block has helped more than 4 million of its total clients save more than \$715 million via the tax credit, representing approximately 25% of all Saver's Credits claimed.

42. Incredibly, it was defendant Ernst who noted as early as May of 2002 that the Company's Express IRA product was designed to "nickel and dime" the Company's clients. In fact, the Company's fraudulent efforts in doing so were so successful that ***85 percent of its clients actually paid more in fees on the accounts than they earned in interest.***

43. As if the prior revelations regarding defendants' inability, as accounting professionals, to provide accurate financial statements had not sufficiently undermined defendants' credibility, the Company now sought to excuse the "simple logic" of defendants' fraud upon the Company's clients. In combination with the Company's prior corrective disclosures, these latest and shocking revelations, *pointing to a pervasive pattern of erroneous, false, misleading and deceitful communications regarding the Company's products, financial statements and prospects* caused the price of H&R Block shares to tumble again, from the previous close of \$22.00 on March 14, 2006, to close \$20.63 on March 15, 2006, for a loss of \$1.37 or 6.2% percent, on volume of over 14 million shares, nearly seven times normal daily volume.

44. The almost 8.9% decline in H&R Block's stock price on February 24, 2006, and subsequent 6.2% decline on March 15, 2006 at the end of the Class Period, were the direct result of the unraveling of the nature and extent of defendants' fraud finally being revealed to investors and the market. The timing and magnitude of H&R Block's stock price declines negate any inference that the loss suffered by plaintiff and other Class members was caused by changed market conditions, macroeconomic or industry factors or Company-specific facts unrelated to the defendants' fraudulent conduct.

45. On February 24, 2006 in which H&R Block's stock price fell almost 8.9% and again on March 15, 2006, when the stock price fell another 6.2% as a result of defendants' fraud being revealed, the Standard & Poor's 500 securities index was flat. The economic losses, i.e., damages, suffered by plaintiff and other members of the Class on those days were a direct result of defendants' fraudulent scheme to artificially inflate H&R Block's stock price and the subsequent significant decline in the value of H&R Block's stock when defendants' prior misrepresentations and other fraudulent conduct was revealed.

46. During the Class Period, defendants knew and concealed that:

(a) a series of documented control weaknesses existed in the Company's corporate tax accounting function;

(b) uncorrected accounting errors were significant and remained uncorrected for more than a year after control weaknesses were discovered;

(c) the Company *offered for sale and sold \$400 million 10-year senior unsecured notes*, despite significant uncorrected errors in the Company's financial statements;

(d) accounting for acquisitions (primarily the acquisition of Olde Financial Corporation in fiscal year 2000) had resulted in an understatement of deferred tax liabilities and goodwill *of approximately \$129 million*, impacting fiscal years 2000 through 2004;

(e) the Company had overstated its provision for income taxes in connection with acquisitions *by approximately \$11 million* for each of the fiscal years ended April 30, 2004 and 2003;

(f) accounting for a gain on sale of previously securitized residuals in fiscal year 2003 resulted in a net overstatement in revenues for that year *of approximately \$36 million*;

(g) Company accounting for leases resulted in a cumulative overstatement of retained earnings *of approximately \$7 million* as of April 30, 2004;

(h) accounting errors pertaining to the Company's provision for income taxes resulted in a cumulative overstatement *of approximately \$10 million to \$14 million in retained earnings* as of April 30, 2004;

(i) a calculation error pertaining to an incentive compensation accrual at the Company's Mortgage Services segment resulted in an understatement of pre-tax expense in fiscal year 2004 *of \$12.4 million*;

(j) overstatement of capitalized branch office costs at the Company's Investment Services segment and a corresponding understatement of operating expenses resulted in an understatement of pre-tax expense *of approximately \$4 million in fiscal year 2004 and \$2 million in fiscal 2003*;

(k) errors pertaining to the Company's state effective income tax rate for the fiscal quarters ended October 31, 2005 and July 31, 2005, fiscal years ended April 30, 2005 and 2004 and the fiscal quarters for fiscal years 2005 and 2004 resulted in a cumulative

understatement of state income tax liability, net of federal income tax benefit, of approximately \$32 million as of April 30, 2005; and

(l) the Company had adopted fraudulent marketing practices for its IRA investment products, at the risk of lawsuits and government action, within the Company's troubled Financial Advisory segment.

FALSE FINANCIAL STATEMENTS

47. Defendant H&R Block offers accounting, tax, and consulting services to middle-market companies. Moreover, defendant Trubeck claims considerable accounting expertise in his role as CFO, while defendants Ernst and Yabuki are certified public accountants. In spite of these facts, the financial statements issued by H&R Block during the Class Period and the subsequent statements regarding their restatement were false and misleading, as such financial information was not prepared in conformity with GAAP, nor was the financial information a fair presentation of the Company's operations due to the Company's improper accounting in violation of GAAP and SEC rules.

48. GAAP are those principles recognized by the accounting profession as the conventions, rules and procedures necessary to define accepted accounting practice at a particular time. Regulation S-X (17 C.F.R. §210.4-01(a) (1)) states that financial statements filed with the SEC which are not prepared in compliance with GAAP are presumed to be misleading and inaccurate. Regulation S-X requires that interim financial statements must also comply with GAAP, with the exception that interim financial statements need not include disclosure which would be duplicative of disclosures accompanying annual financial statements. 17 C.F.R. §210.10-01(a).

49. Due to these accounting improprieties, the Company presented its financial results and statements in a manner which violated GAAP, including the following fundamental accounting principles:

(a) The principle that interim financial reporting should be based upon the same accounting principles and practices used to prepare annual financial statements was violated (APB No. 28, ¶10);

(b) The principle that financial reporting should provide information that is useful to present and potential investors and creditors and other users in making rational investment, credit and similar decisions was violated (FASB Statement of Concepts No. 1, ¶34);

(c) The principle that financial reporting should provide information about the economic resources of an enterprise, the claims to those resources, and effects of transactions, events and circumstances that change resources and claims to those resources was violated (FASB Statement of Concepts No. 1, ¶40);

(d) The principle that financial reporting should provide information about how management of an enterprise has discharged its stewardship responsibility to owners (stockholders) for the use of enterprise resources entrusted to it was violated. To the extent that management offers securities of the enterprise to the public, it voluntarily accepts wider responsibilities for accountability to prospective investors and to the public in general (FASB Statement of Concepts No. 1, ¶50);

(e) The principle that financial reporting should provide information about an enterprise's financial performance during a period was violated. Investors and creditors often use information about the past to help in assessing the prospects of an enterprise. Thus, although investment and credit decisions reflect investors' expectations about future enterprise performance, those expectations are commonly based at least partly on evaluations of past enterprise performance (FASB Statement of Concepts No. 1, ¶42);

(f) The principle that financial reporting should be reliable in that it represents what it purports to represent was violated. That information should be reliable as well as relevant is a notion that is central to accounting (FASB Statement of Concepts No. 2, ¶¶58-59);

(g) The principle of completeness, which means that nothing is left out of the information that may be necessary to insure that it validly represents underlying events and conditions was violated (FASB Statement of Concepts No. 2, ¶79); and

(h) The principle that conservatism be used as a prudent reaction to uncertainty to try to ensure that uncertainties and risks inherent in business situations are adequately considered was violated. The best way to avoid injury to investors is to try to ensure that what is reported represents what it purports to represent (FASB Statement of Concepts No. 2, ¶¶95, 97).

50. Further, the undisclosed adverse information concealed by defendants during the Class Period is the type of information which, because of SEC regulations, regulations of the national stock exchanges and customary business practice, is expected by investors and securities analysts to be disclosed and is known by corporate officials and their legal and financial advisors to be the type of information which is expected to be and must be disclosed.

CLASS ACTION ALLEGATIONS

51. Plaintiff brings this action as a class action pursuant to Rule 23 of the Federal Rules of Civil Procedure on behalf of all persons who purchased H&R Block publicly traded securities (the “Class”) on the open market during the Class Period. Excluded from the Class are defendants.

52. The members of the Class are so numerous that joinder of all members is impracticable. The disposition of their claims in a class action will provide substantial benefits to the parties and the Court. H&R Block had more than 327 million shares of stock outstanding, owned by hundreds if not thousands of persons.

53. There is a well-defined community of interest in the questions of law and fact involved in this case. Questions of law and fact common to the members of the Class which predominate over questions which may affect individual Class members include:

- (a) Whether the 1934 Act was violated by defendants;
- (b) Whether defendants omitted and/or misrepresented material facts;
- (c) Whether defendants' statements omitted material facts necessary to make the statements made, in light of the circumstances under which they were made, not misleading;
- (d) Whether defendants knew or deliberately disregarded that their statements were false and misleading;
- (e) Whether the prices of H&R Block's publicly traded securities were artificially inflated; and
- (f) The extent of damage sustained by Class members and the appropriate measure of damages.

54. Plaintiff's claims are typical of those of the Class because plaintiff and the Class sustained damages from defendants' wrongful conduct.

55. Plaintiff will adequately protect the interests of the Class and has retained counsel who are experienced in class action securities litigation. Plaintiff has no interests which conflict with those of the Class.

56. A class action is superior to other available methods for the fair and efficient adjudication of this controversy.

COUNT I

For Violation of §10(b) of the 1934 Act and Rule 10b-5 Against All Defendants

57. Plaintiff incorporates ¶¶1-56 by reference.

58. During the Class Period, defendants disseminated or approved the false statements specified above, which they knew or deliberately disregarded were misleading in that

they contained misrepresentations and failed to disclose material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading.

59. Defendants violated §10(b) of the 1934 Act and Rule 10b-5 in that they:

(a) Employed devices, schemes, and artifices to defraud;

(b) Made untrue statements of material facts or omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or

(c) Engaged in acts, practices, and a course of business that operated as a fraud or deceit upon plaintiff and others similarly situated in connection with their purchases of H&R Block publicly traded securities during the Class Period.

60. Plaintiff and the Class have suffered damages in that, in reliance on the integrity of the market, they paid artificially inflated prices for H&R Block publicly traded securities. Plaintiff and the Class would not have purchased H&R Block publicly traded securities at the prices they paid, or at all, if they had been aware that the market prices had been artificially and falsely inflated by defendants' misleading statements.

61. As a direct and proximate result of these defendants' wrongful conduct, plaintiff and the other members of the Class suffered damages in connection with their purchases of H&R Block publicly traded securities during the Class Period.

COUNT II

For Violation of §20(a) of the 1934 Act Against All Defendants

62. Plaintiff incorporates ¶¶1-61 by reference.

63. The Individual Defendants acted as controlling persons of H&R Block within the meaning of §20(a) of the 1934 Act. By reason of their positions as officers and/or directors of H&R Block, and their ownership of H&R Block stock, the Individual Defendants had the power and authority to cause H&R Block to engage in the wrongful conduct complained of herein. H&R Block controlled each of the Individual Defendants and all of its employees. By reason of

such conduct, the Individual Defendants and H&R Block are liable pursuant to §20(a) of the 1934 Act.

PRAYER FOR RELIEF

WHEREFORE, plaintiff prays for judgment as follows:

- A. Declaring this action to be a proper class action pursuant to FRCP 23;
- B. Awarding plaintiff and the members of the Class damages, interest and costs; and
- C. Awarding such equitable/injunctive or other relief as the Court may deem just and proper.

JURY DEMAND

Plaintiff demands a trial by jury.

DATED: March 23, 2006

Respectfully submitted,

s/ Jeffrey M. Norton

By: _____

Jeffrey M. Norton (JN-4827)
WECHSLER HARWOOD LLP
488 Madison Avenue, 8th Floor
New York, NY 10022
Telephone: (212) 935-7400
Facsimile: (212) 753-3630

David R. Scott (DS-8053)
SCOTT + SCOTT, LLC
108 Norwich Avenue
Colchester, CT 06415
Telephone: (860) 537-3818
Facsimile: (860) 537-4432

-and-

Arthur L. Shingler, III
401 B Street, Suite 307
San Diego, CA 92101
Telephone: (619) 233-4565
Facsimile: (619) 233-0508

Attorneys for Plaintiff

EC/TS

**PLAINTIFF CERTIFICATION
PURSUANT TO FEDERAL SECURITIES LAWS**

Raymond J. Kadagian, ("Plaintiff"), declares, as to the claims asserted under the federal securities laws, that:

1. Plaintiff has reviewed the Complaint and retains Scott + Scott, LLC, and such co-counsel it deems appropriate to associate with, to pursue such action on a contingent fee basis.
2. Plaintiff did not purchase the security that is the subject of this action at the direction of Plaintiff's counsel, or in order to participate in any action.
3. Plaintiff is willing to serve as a representative party on behalf of the class, including providing testimony at deposition and trial, if necessary.
4. Plaintiff's transaction(s) in the H & R Block Inc. security that is the subject of this action during the Class Period is/are as follows:

<u>No of Shares</u>	<u>Buy/Sell</u>	<u>Date</u>	<u>Price Per Share</u>
1300		8/3/04	24.58

5. During the three years prior to the date of this Certification, Plaintiff has not served, or sought to serve as a class representative in a federal securities fraud case, except as follows:

6. Plaintiff will not accept any payment for serving as a representative party on behalf of the class beyond Plaintiff's pro rata share of any recovery, except such reasonable costs and expenses (including lost wages) directly relating to the representation of the class as ordered or approved by the Court.

I declare under penalty of perjury that the foregoing is true and correct. Executed this day of FEB 28, 2006, at LAS VEGAS, NV 89144 (city, state).

Printed Name: RAYMOND J KADAGIAN

Signature: Raymond J. Kadagian

[Faint signature/initials]