

Tier Technologies, Inc. (TIER)

Activist Investors: Discovery Equity Partners; Parthenon Investors II

4 March 2009

CATALYST SUMMARY

Two activist investors, Discovery Equity Partners and Parthenon Investors II, who together own approximately 19% of Tier Technologies, are seeking to obtain four of nine board seats at the company's **March 11 2009 Annual Meeting**.

According to Discovery's analysis (see link on page 2) Tier is potentially worth \$9.47/share - an 89% premium to its current value.

Due to the activists combined 19% ownership position, Tier's cumulative voting policy, and their two open director seats, it is highly likely the activist investors will win board representation.

If elected, Discovery has publicly stated they plan to (i) improve corporate governance by removing the "poison pill" and reinstating shareholder rights to call a special meeting, (ii) reduce excessive corporate overhead, (iii) evaluate the best use of excess cash, and (iv) evaluate all strategic alternatives to unlock value.

On February 23rd, in an effort to win additional shareholder support for their nominees, Tier raised the threshold on the Poison Pill from 15% to 25% and amended their bylaws to allow shareholders holding more than 10% of the stock to call a special meeting. The company also announced a share repurchase program.

COMPANY PROFILE

Tier Technologies Inc. (www.tier.com) provides electronic payment systems for governments, utilities, educational institutions and others. The company's Electronic Payment Processing (EPP) allows users to collect taxes, fees, and other types of obligations. The IRS accounted for nearly 27% of fiscal 2008 revenue (from continuing operations), but the company's other clients include 25 states, the District of Columbia, and more than 3300 local governments.

ACTIVIST INVESTOR PROFILES

Discovery Equity Partners manages a concentrated investment portfolio of 20 to 30 holdings in small cap public companies. The two Managing Partners at Discovery were previously in senior management positions at Piper Jaffray & Co. and have extensive experience in middle market mergers and acquisitions. Over the past year Discovery has pressed for governance and operating changes at a number of small cap public companies, including Radyne Corp. - which was sold to Comtech Telecommunications Corp in May 2008 for \$11.50/share. Discovery owned 1,743,979 shares of Radyne at an average cost of \$10.01/share.

Parthenon Investors II is a \$750 million private equity fund and part of Parthenon Capital, a private equity fund with a total \$2 billion in assets under management. Parthenon II typically invests \$15 to \$50 million in middle market companies with enterprise values ranging from \$75 million to \$500 million.

COMPANY PROFILE

Previous Close: \$5.01 52 -week Range: \$3.41-\$8.75 Market Cap: \$99 million Enterprise Value: \$53 million \$46 million Cash: Net Cash per Share: \$2.32 EBITDA: -\$5.1M EV/EBITDA: Negative

INVESTOR PROFILE

Principal Activists

Shares Held by Activists:	
Discovery Equity	1,957,563
Parthenon Investors II	1,799,322
Percent Outstanding:	

Discovery Equity

9 9%

Parthenon Investors II

Percent Outstanding: Discovery Equity

Parthenon Investors II	9.1%
Total	19%

Total as a % of float 24%

Cost Basis:

Discovery \$8.30 Parthenon Not Available

CAPITAL STRUCTURE

Common Shares Outstanding 19,734,863
Preferred Shares: 0
Long Term Debt (30 Jan 2009) 0

Although we have done our best to input accurate data certain financial information may be incorrect due to the timing of public filings.

HEDGE FUND SOLUTIONS' VALUE ANALYSIS

Tier's first quarter (Q ending December 31) revenues rose 3% to \$29.74 million versus the same period last year, while the net fell to a loss \$5.15 million, or (\$0.26/share) versus an earlier loss of \$1.431 million (\$.07/share). Included in these results were a \$3.26 million charge from continuing operations versus a gain of \$1.42 million last year, so losses from continued operations improved to \$1.89 million (\$0.10/share) versus \$2.85 million (\$0.14/share). The charges from discontinued operations were related to the company's sale of their Financial Management Systems business (FMS), which was completed in November 2008. Results were also aided by a 2.8% drop in expenses. While cost of goods sold rose less than 1% to \$22.42 million, SG&A fell 11% to \$9.41 million from \$10.52 million.

The balance sheet ended the quarter very healthy, no doubt a major factor in the activism that is currently playing out. Tier ended Q1 with \$34.39 million in cash, or \$1.74 per share, and \$11.49 million in short term marketable securities, commercial paper in this case, or \$0.58 per share. Since the company has no short or long-term debt, \$2.32 per share in cash and short term investments is fairly compelling, considering Tier's current share price of \$5.01.

However, there are other assets to consider as well, on the long-term side of the balance sheet: \$31.21 million in long-term marketable securities. Here's where valuations can get dicey, as the entire amount is invested in Auction Rate Securities (ARS). Due to difficulties in the auction rate markets relating to the credit crisis, these investments are subject to write downs, as unsuccessful auctions have impaired their value. During fiscal 2008, the company recorded an unrealized loss of \$2.5 million, in order to write these securities down to fair value. However, in November, the company signed an ARS Rights agreement with their investment manager UBS, that allows the company to sell the existing ARS portfolio back to UBS for par value plus accrued but unpaid interest at any time between 6/30/10 and 7/2/12. UBS also has discretion to sell the ARS at par until 7/2/12. Either way, it appears that the ARS portfolio is worth at least its current stated value of \$31.21 million, or \$1.58 per share.

Tier also lists restricted investments of \$7.36 million or \$0.37, but for the sake of conservatism, these will be ignored. All in, considering short and long term investments, purchasing TIER at the current price of \$5.01 is akin to buying \$3.90 in cash, short and long term securities, and getting a call option on the business for \$1.11.

Given the company's renewed focus on the EPP business, shedding of other operations, and stockpile of cash and securities, it's of little wonder that two activists are currently in the mix.

While Tier does not garner a great deal of analyst coverage, "consensus" estimates (a term used lightly because only 2 analysts are in that consensus) are calling for 2010 revenue of \$144 million, and earnings of \$0.14 per share.

[Subsequent event to the end of the quarter disclosure]

Subsequent to the latest quarter end, Tier announced the acquisition of ChoicePay, an ePayments solution provider located in Tulsa, Oklahoma, for \$7.5 million.

RECENT (FEBRUARY 2009) INVESTOR PRESENTATIONS

Discovery Shareholder Presentation (February 18, 2009):

 $\underline{\text{http://www.sec.gov/Archives/edgar/data/1045150/000110465909010265/a09-5828_1ex99d1.htm}}$

Tier Technologies Shareholder Presentation (February 17, 2009):

http://www.sec.gov/Archives/edgar/data/1045150/000095013309000366/w72591a3exv99w1.htm

ANALYSIS PROVIDED BY:

Damien Park is the President and CEO of Hedge Fund Solutions, LLC, a Philadelphia-based firm focused on issues related to shareholder activism.

Mr. Park is widely considered an expert on activist investments. He is a featured commentator on RealMoney.com discussing activist investments and is often quoted in leading business publications, including: *The Wall Street Journal*, *Business Week, CFO Magazine*, *TheStreet.com*, *The Deal, CNN Money, The New York Times, The Nikkei* and *Newsweek Japan*.

Damien frequently speaks at professional conferences and is the Chairman of the Hedge Fund Activism and Shareholder Value Summit, the largest annual gathering of activist hedge funds in the world.

Jonathan Heller, CFA, is a Partner at Hedge Fund Solutions, President of KEJ Financial Advisors - a fee-only financial planning firm, and a featured commentator on RealMoney.com discussing deep value investments.

Previously, Jon spent 17 years at Bloomberg Financial Markets in various roles which included the management of Bloomberg's Equity Fundamental Research Department and Bloomberg's Equity Data Research Department. Jon was also a senior markets editor of Bloomberg's Publishing Group, a writer for Bloomberg Personal Finance Magazine, and an associate editor and contributor for Bloomberg Markets Magazine. In 2005, Jon joined SEI Investments as director of investment communications within SEI's Investment Management Unit.

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IMPORTANT DISCLOSURE INFORMATION

Neither Damien Park nor Jonathan Heller holds long or short positions in TIER as of the date of this research.

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