FleetCor – Citron believes FTC Lawsuit is Imminent

"Let me be clear. My bet would be that FleetCor is subject to an FTC order either through consent or litigation where FleetCor must pay a significant amount of money and be subject to a consent decree that alters the company's billing and marketing practices."

– Former Director of the FTC's Bureau of Consumer Protection

FleetCor (FLT), the nation's largest operator of fleet cards, has over the course of 10 years skillfully built a business based on deceiving small and medium sized business into paying excessive and erroneous fees. This cannot be disputed. What can be disputed is the legality of the business.

The FleetCor business was best described in a recent Bloomberg article:

"Consumer advocates and some former FleetCor executives say the firm is an embodiment of bare-knuckles, winner-takes-all capitalism, and takes advantage of smaller fish who have little recourse but to complain to regulators or undertake costly litigation."
https://www.bloomberg.com/news/articles/2019-01-31/ceo-made-357-million-from-small-businesses-3-50-at-a-time

All that is about to change as Citron has good reason to believe that the FTC is about to file a formal lawsuit against FleetCor for multiple violations and force the company to change its advertising/marketing and billing practices.

After extensive due diligence and many conversations with former senior FTC officials including a Director of the FTC's Bureau of Consumer Protection, an Executive Director at the FTC who spent more than 25 years with the agency, and an Attorney in the Division of Enforcement at the FTC's Bureau of Consumer Protection, Citron believes we could see a formal lawsuit from the FTC against FleetCor as early as the first week of January.

Background

In 2017, Citron wrote a series of reports on FleetCor, which detailed FleetCor's programmatic ways to charge fees that were hidden and unavoidable to the most vulnerable – the small business.

https://citronresearch.com/wp-content/uploads/2017/04/FLT-final-f.pdf
https://citronresearch.com/wp-content/uploads/2017/04/FLT-followup-final-d.pdf

While Citron knew the FTC would eventually regulate and sanction FleetCor, Wall Street sell-side aggressively defended the company, consistently spewing nonsense like:

"Complaints about FLT's pricing and late fee practices to its smallest customers has prompted some concerns from investors – is there FTC Investigation risk – very little risk in our view" – Morgan Stanley Analyst Danyal Hussain (April 2017)

"We think the bar for intervention is set somewhat higher for B2B vs. B2C matters, as a business owner is presumed to be more commercially sophisticated than a consumer." – Jefferies Analyst Ramsey El-Assal (April 2017)

After the initial Citron reports, Wall Street was so confident that the FTC would not investigate that Deutsche Bank went as far as to call Citron's request for an FTC investigation *"Fake News"* while Morgan Stanley boldly stated the obvious:

"We expect the stock to be down if a CID is disclosed." – Morgan Stanley Analyst Danyal Hussain (April 2017)"

Where is Your Update NOW?

A Civil Investigative Demand (CID) from the FTC was just disclosed in FleetCor's most recent 10-Q. As analysts were saying no way the FTC would investigate FleetCor… only six months later, the company received a CID for information regarding its marketing and billing practices in 2017 yet not disclosed until a month ago.

After further due diligence, Citron believes that any settlement discussions between the FTC and FleetCor have broken down and we will likely see a lawsuit filed in the near future that will forever change the business model affectionately referred to as "FleeceCorp".

FTC Investigation Disclosed

Fast forward two years after the initial Citron report, while FleetCor's valuation and multiple is at an all-time high -- implying that regulatory risk is at an all-time low -- the company just disclosed last month it received a CID from the FTC **two years ago**. The only likely reason for the new disclosure is that the company has now learned through settlement talks that the FTC is seeking a material fine and business model change, which presents a major risk factor to investors. Furthermore, we have reason to believe that FleetCor is not being honest with investors around the scope of the investigation into its billing practices.

From FleetCor's recent 10-Q:

FTC Investigation

"In October 2017, the Federal Trade Commission ("FTC") issued a Notice of Civil Investigative Demand to the Company for the production of documentation and a request for responses to written interrogatories. After discussions with the Company, the FTC proposed in October 2019 to resolve potential claims relating to the Company's advertising and marketing practices. To date, the FTC has not offered a specific proposal as to the amount of potential redress. The Company believes that the FTC's potential claims, which relate principally to its North American Fuel Card business's practices, are without merit. At this time, the Company believes the possible range of outcomes includes the filing by the Commission of a contested civil complaint, further discussions leading to a settlement, or the closure of these matters without further action."
https://www.sec.gov/ix?doc=/Archives/edgar/data/1175454/000117545419000024/flt10-q09302019.htm

FTC Ready to File Lawsuit Against FleetCor

Last Thursday, Capitol Forum reported that the FTC is ready to sue FleetCor and CEO Ron Clarke as the two parties have yet to reach a settlement. For those not familiar with Capitol Forum, they are an independent research organization based out of Washington, D.C. and while they like many research organizations have been hit or miss with some names, their accuracy with FleetCor is better than any Wall Street analyst.

Before FleetCor disclosed its CID in their most recent 10-Q, it was Capitol Forum that reported in March of 2019 that FleetCor had received a CID as they claim to have a "source familiar with the matter."
https://thecapitolforum.com/wp-content/uploads/2019/05/FleetCor-2019.03.18.pdf

The first sign of an FTC investigation was in FleetCor's 10-K that was filed in March of 2019. The 10-K included subtle changes to the language around the FTC and government investigations.

Below is an excerpt from Capitol Forum showing the additional language in the 10-K highlighted in yellow bolded font and removed language in red strike-through text.

> ***Federal Trade Commission Act***
>
> All persons engaged in commerce, including, but not limited to, us and our bank sponsors and customers are subject to Section 5 of the Federal Trade Commission Act prohibiting unfair or deceptive acts or practices, and certain products are subject to the jurisdiction of the Consumer Financial Protection Bureau ('CFPB') regarding the prohibition of unfair, deceptive, or abusive acts and practices (both, collectively, UDAAP). Various federal and state regulatory enforcement agencies including the Federal Trade Commission ('FTC'), CFPB and the state attorneys general have authority to **investigate and** take action against businesses, merchants and financial institutions that **are alleged to** engage in UDAAP or violate other laws, rules and regulations. If we ~~violate~~ **are accused of violating** such laws, rules and regulations, we may be subject to enforcement actions and as a result, may incur losses and liabilities that may impact our business. A number of state laws and regulations also prohibit unfair and deceptive business practices.
>
> ***Litigation and regulatory actions could subject us to significant fines, penalties or requirements resulting in significantly increased expenses, damage to our reputation and/or material adverse effects on our business.***
>
> We are subject to claims and a number of judicial and administrative proceedings considered normal in the course of our current and past operations, including employment-related disputes, contract disputes, intellectual property disputes, government **inquiries, investigations,** audits and regulatory proceedings, customer disputes and tort claims. Responding to proceedings may be difficult and expensive, and we may not prevail.

Eight months later, FleetCor disclosed the CID and now Capitol Forum reports that the FTC is about to sue FleetCor for unfair and deceptive business practices.

While we encourage interested parties to subscribe, in Capitol Forum's note from last week, they report:

THE CAPITOL FORUM Vol. 7 No. 448 December 12, 2019

FleetCor: FTC Ready to Sue FleetCor for Unfair and Deceptive Business Practices

- *"The Federal Trade Commission has determined that FleetCor (FLT) wrongly charged small businesses hundreds of millions of dollars in hidden costs and late fees and* ***the agency is ready to sue the company if it does not settle in the weeks ahead****."*
- *"**The FTC is also seeking penalties against CEO Ron Clarke** who has taken home hundreds of millions of dollars in payouts since leading the company in 2000 and who holds more than a million shares of company stock."*
- ***"If the FTC demands tough sanctions, FleetCor might have to drop some profitable billing and collection practices or fight the agency in court which could draw fresh attention to Ron Clarke's leadership and company practices."***
- ***"Andrew Smith, the FTC Director of Consumer Protection, and other senior agency officials agree that FleetCor has collected hundreds of millions of dollars using unfair and deceptive practices, said sources."***

What peaked Citron's interest even more was the recent wave of upper level management resignations.

Unexpectedly, two senior FleetCor executives resigned from the company in recent months, including the Group President of the North American Fuel Card business (i.e., the head of the division being investigated by the FTC).

"On September 4, 2019, David J. Krantz informed FleetCor Technologies, Inc. (the "Company") of his intention to resign from his position as Group President of the North American Fuel Card business."
https://www.sec.gov/ix?doc=/Archives/edgar/data/1175454/000162828019011595/a8kseptember102019.htm

"On July 31, 2019, Kurt P. Adams informed FleetCor Technologies, Inc. (the "Company") of his intention to resign from his position as Group President of the Corporate Payments division."
https://www.sec.gov/Archives/edgar/data/1175454/000162828019010149/form8-kaugust62019.htm

Citron believes FleetCor did not originally disclose that it had received a CID as the company thought it was not material at the time. FleetCor's decision to disclose the CID two years later means it has become material… the only question is how material.

The new accusations were damning enough for Citron to hire multiple consultants who, through extensive interviews, gave us this insight about FleetCor and the FTC. It should be noted that these consultants did not have an agenda or incentive to reach any conclusion -- all of the information was given from an unbiased POV.

Citron's Extensive Findings from Former Senior FTC Officials

Citron consulted with former senior FTC officials including a Director of the FTC's Bureau of Consumer Protection, an Executive Director at the FTC who spent more than 25 years with the agency, and an Attorney in the Division of Enforcement at the FTC's Bureau of Consumer Protection. Below are the takeaways from our conversations. For obvious reasons we cannot share their names in a public forum but will present information to any regulator or sell side analyst.

Former Director of the FTC's Bureau of Consumer Protection

- *"FleetCor has squeezed small businesses into paying useless fees and fees for late payments that they couldn't possibly have paid on time. These are abusive practices."*
- *"FleetCor received a CID in October 2017, meaning this investigation is done and the FTC is ready to roll. The recent press indicates that the FTC is gearing up to do something as they think they have a really good case."*
- *"If the FTC spent a year looking into a company and didn't find anything they would have gone home. Over half of these cases, FTC says never mind and walks away but this is clearly not the case. This is a big red flag."*

Former FTC Executive Director

- *"FTC will take an enforcement action against FleetCor for unfair billing practices."*
- *"FleetCor's practices are a classic unfair practice and the exact conduct that the FTC goes after."*
    - https://www.federalreserve.gov/boarddocs/supmanual/cch/ftca.pdf

- *"The fact that the FTC sent a CID to FleetCor means they have all of the company's internal records, complaint records, and internal correspondence."*
- *"FleetCor has no defense as a reasonable person should have been able to know that FleetCor's fees were going to be charged, which were almost impossible to interpret."*
- *"FleetCor is exactly the type of case that Andrew Smith, current Director of the FTC's Bureau of Consumer Protection, would go after as FleetCor's practices are straight out wrong."*
- *"If the FTC finds that FleetCor's unfair billing practices are still ongoing, they can make a referral to the DOJ to investigate the company for criminal charges."*
- *"As cases brought by the FTC have no statute of limitations, FleetCor could end up disgorging all of its ill-gotten profits."*

<u>*Former Attorney in the Division of Enforcement at the FTC's Bureau of Consumer Protection*</u>

- *"If you have an active case after two years it means the FTC found something bad."*
- *"FleetCor disclosing that they're in settlement talks with the FTC means the FTC has found wrongdoing and FleetCor has already received a draft of the FTC lawsuit, which includes a list of the bad acts, evidence supporting the bad acts, and the proposed injunction (e.g., changes to business model). There will definitely be a settlement with business model change or litigation."*
- *"This many lawsuits and private actions against FleetCor backs the FTC into a corner as it's out there. Private lawyers have found substantial evidence of wrongdoing so the FTC can no longer claim they were in the dark as the FTC has also been investigating. It's a bit jarring that FleetCor would characterize this as immaterial as any settlement would be material and require significant change to the business model."*
- *"It is difficult for FleetCor to settle because their profit center would go away."*
- *"FTC almost never includes a CEO as a named defendant unless the business is crazy dirty."*
- *"Democrats and Republicans would want to bring this case as small businesses are being hurt. The FTC got a lot of backlash for just going after*

> *Facebook and not Zuckerberg, which explains why CEO Ron Clarke is reportedly being named as a defendant."*

In summary, these are two direct quotes from our consultant (former Director of the FTC's Bureau of Consumer Protection):

"Let me be clear. My bet would be that FleetCor is subject to an FTC order either through consent or litigation where FleetCor must pay a significant amount of money and be subject to a consent decree that alters the company's billing and marketing practices."

"Knowing FleetCor's lawyers, the most likely scenario is they grudgingly accept a settlement for significant redress for money going back to consumers and a consent decree that cleans up their advertising/marketing and billing practices. The CEO will be subject to the order. The alternative is all out litigation with the FTC, which will be too much for the company to bear. There will be real restrictions on their marketing/advertising claims and billing practices. They have to clearly disclose their billing practices and they cannot be unfair or deceptive to consumers."

CEO Ron Clarke

Ron Clarke has been consistently touted as one of corporate America's highest paid CEO's. He has made hundreds of millions of dollars since taking over leadership of the company in 2000.

His eye-popping compensation package was bound to draw unwanted scrutiny. As reported by Capitol Forum last week, "the FTC is also seeking penalties against CEO Ron Clarke". This is significant.

When we spoke to our former senior FTC consultants about what that means for Ron Clarke, we learned that this means the FTC has enough evidence through witness testimony, internal correspondence, etc. against Clarke to prove that he knew or should have known about the unfair billing practices at FleetCor. We were told that it is rare for the FTC to go after an individual CEO but when the FTC does it is bad news for the company and CEO.

Conclusion

There is only one response that the company or its analysts can hope for: "FleetCor has settled with the FTC for a reasonable amount and no change to its current practices". Anything short of that should send the stock down to the $200 range which would have it in-line with peer WEX which is actually growing faster than FleetCor.

Citron will no longer write on FleetCor. As we have observed in our 25 years in the market there are two major takeaways:

1. The ability to exploit the "little guy" is a GREAT business
2. It never seems to matter until one day it does

Now that the FTC is involved… our work is done and we believe with the current news flow that risk is skewed heavily to the downside, as FleetCor might finally have to answer for their longstanding business practices.

Cautious Investing to All

These reports have been prepared by either Citron Research ("Citron Research") or Citron Capital, LLC ("Citron Capital"). Citron Research and Citron Capital are referred to collectively as "Citron" and each individually as a "Citron Entity." Each report specifies the publisher and owner of that report. All reports are for informational purposes only and presented "as is" with no warranty of any kind, express or implied. Under no circumstances should any of these reports or any information herein be construed as investment advice, or as an offer to sell or the solicitation of an offer to buy any securities or other financial instruments.

Citron Research produces research reports on publicly traded securities, and Citron Capital is an exempt reporting adviser filed with the California Department of Business Oversight. The reports are the property of the applicable Citron Entity that published that report. The opinions, information and reports set forth herein are solely attributable to the applicable Citron Entity and are not attributable to any Citron Related Person (defined below) (other than the Citron Entity that published the report).

By downloading, accessing, or viewing any research report, you agree to the following Terms of Use. You agree that use of the research presented in any report is at your own risk. You (or any person you are acting as agent for) agree to hold harmless Citron Research, Citron Capital and each of their affiliates and related parties, including, but not limited to any principals, officers, directors, employees, members, clients, investors, consultants and agents (collectively, the "Citron Related Persons") for any direct or indirect losses (including trading losses) attributable to any information in a research report. You further agree to do your own research and due diligence before making any investment decision with respect to securities of the issuers covered herein (each, a "Covered Issuer") or any other financial instruments that reference the Covered Issuer or any securities issued by the Covered Issuer. You represent that you have sufficient investment sophistication to critically assess the information, analysis and opinion presented in any Citron report. You further agree that you will not communicate the contents of reports and other materials made available by Citron to any other person unless that person has agreed to be bound by these Terms of Use. If you access, download or receive the contents of Citron reports or other materials on your own behalf, you agree to and shall be bound by these Terms of Use. If you access, download or receive the contents of Citron reports or other materials as an agent for any other person, you are binding your principal to these same Terms of Use.

As of the publication date of a Citron report, Citron Related Persons (possibly along with or through its members, partners, affiliates, employees, and/or consultants), Citron Related Persons clients and/or investors and/or their clients and/or investors have a position (long or short) in one or more of the securities of a Covered Issuer (and/or options, swaps, and other derivatives related to one or more of these securities), and therefore may realize significant gains in the event that the prices of a Covered Issuer's securities decline or appreciate. Citron Research, Citron Capital and/or the Citron Related Persons may continue to transact in Covered Issuers' securities for an indefinite period after an initial report on a Covered Issuer, and such position(s) may be long, short, or neutral at any time hereafter regardless of their initial position(s) and views as stated in the Citron research. Neither Citron Research nor Citron Capital will update any report or information to reflect changes in positions that may be held by a Citron Related Person.

This is not an offer to sell or a solicitation of an offer to buy any security. Neither Citron Research nor any Citron Related Person (including Citron Capital) are offering, selling or buying any security to or from any person through any Citron research reports. Citron Research is affiliated with Citron Capital. Citron Capital is an exempt reporting adviser filed with the California Department of Business Oversight and is not registered as investment adviser in any other jurisdiction. Citron Capital does not render investment advice to anyone unless it has an investment adviser-client relationship with that person evidenced in writing. You understand and agree that Citron Capital does not have any investment advisory relationship with you or does not owe fiduciary duties to you. Giving investment advice requires knowledge of your financial situation, investment objectives, and risk tolerance, and Citron Capital has no such knowledge about you.

The research and reports made available by Citron reflect express the opinion of the applicable Citron Entity as of the time of the report only. Reports are based on generally available information, field research, inferences and deductions through the applicable Citron Entity's due diligence and analytical process. To the best of the applicable Citron Entity's ability and belief, all information contained herein is accurate and reliable, is not material non-public information, and has been obtained from public sources that the applicable Citron Entity believe to be accurate and reliable, and who are not insiders or connected persons of the Covered Issuers or who may otherwise owe a fiduciary duty, duty of confidentiality or any other duty to the Covered Issuer (directly or indirectly). However, such information is presented "as is," without warranty of any kind, whether express or implied. With respect to their respective research reports, Citron Research and Citron Capital makes no representation, express or implied, as to the accuracy, timeliness, or completeness of any such information or with regard to the results to be obtained from its use. Further, any research report contains a very large measure of analysis and opinion. All expressions of opinion are subject to change without notice, and Citron does not undertake to update or supplement any reports or any of the information, analysis and opinion contained in them.

In no event shall Citron Research, Citron Capital or any Citron Related Persons be liable for any claims, losses, costs or damages of any kind, including direct, indirect, punitive, exemplary, incidental, special or, consequential damages, arising out of or in any way connected with any information presented in any Citron report. This limitation of liability applies regardless of any negligence or gross negligence of Citron Research, Citron Capital or any Citron Related Persons. You accept all risks in relying on the information presented in any report.

You agree that the information in any Citron research report is copyrighted, and you therefore agree not to distribute this information in any manner without the express prior written consent of the applicable Citron Entity. If you have obtained Citron research reports in any manner other than as provided by Citron, you may not read such research without agreeing to these Terms of Use. You further agree that any dispute between you and Citron and their affiliates arising from or related to this report or viewing the material presented herein shall be governed by the laws of the State of California, without regard to any conflict of law provisions. The failure of Citron Research or Citron Capital to exercise or enforce any right or provision of these Terms of Use shall not constitute a waiver of this right or provision. You agree that each Citron Related Person is a third-party beneficiary to these Terms of Use. If any provision of these Terms of Use is found by a court of competent jurisdiction to be invalid, the parties nevertheless agree that the court should endeavor to give effect to the parties' intentions as reflected in the provision and rule that the other provisions of these Terms of Use remain in full force and effect, in particular as to this governing law and jurisdiction provision. You agree that regardless of any statute or law to the contrary, any claim or cause of action arising out of or related to Citron report or related material must be filed within one (1) *year after the occurrence of the alleged harm that gave rise to such claim or cause of action, or such claim or cause of action be forever barred.*