COMPANY: Shift4 Payments Inc. | NYSE: FOUR
INDUSTRY: Financial Technology

PRICE (AS OF CLOSE 4/18/2023)
USD 68.54

MARKET CAP
USD 5.8 BN

Shift4 Payments, Inc. ("Shift4" or "the Company") pitches itself as a fast-growing, profitable fintech company at the forefront of new technology in payment processing.

We think this is a façade. We see Shift4 as, in reality, a roll-up of low-tech POS systems and payment processors **which is substantially less profitable, generates far less cash, and is materially more levered than investors are led to believe**.

As Shift4's stock tumbled through 2022, we believe that its CEO faced the threat of a margin call from an unusually large series of stock pledges, creating an existential threat that he would be forced to liquidate up to 10 million shares (12% of diluted shares outstanding).

With the specter of a margin call hanging over the stock, we think that Shift4 engaged in a string of highly questionable and hyper-aggressive accounting maneuvers seemingly designed to keep the stock afloat, from cash flow manipulation to inexplicable distributor acquisitions that enabled it to capitalize a major component of COGS. At the height of its financial gimmickry, Shift4 more than doubled its Q4 2022 operating cash flow simply by recalling a collateral deposit just before fiscal year end, recognizing the inflows as cash from operations, only to re-deposit funds as collateral with the same counterparty right after the quarter ended.

A concerning string of governance issues arose just as this was playing out. Shift4's CFO abruptly left the Company the day before its Q2 2022 earnings call, amidst a lengthy string of correspondence with the SEC over its accounting. Its auditor warned of a material weakness over internal financial controls the very next quarter, just as it spent $256.4 million in a string of M&A that enabled it to capitalize a material share of COGS.

At the same time, Shift4's CEO engaged in stock promotion, saying he was prepared to take the Company private because the stock was "way too cheap." At this time, he claimed to be "a buyer" even though:

- He hadn't made any open-market purchases for months
- Insider ownership filings reveal that he was a net seller over the course of 2022
- He was due to offload up to 2 million shares not long into the future with the settlement of a variable prepaid forward (VPF) contract

We believe that Shift4's accounting gimmicks are enabled by a dismal corporate governance structure, including a board of directors and executive team replete with members of the CEO's family, including his father and brother, as well as a number of his childhood friends. We question whether this lack of independent checks explains why Company coffers are used to pay the CEO's private charter jet company, millions of dollars' worth of commission payouts to his family members, nebulous "consulting fees" to himself, and expenses tied to the promotion of his private space flight.

We estimate that, in total, Shift4's aggressive accounting games and M&A activity inflated 2022 gross profit by 13%, Adj. EBITDA by 34%, and operating income by close to 3x, while its buyout of 50% of its independent distributors and Q4 2022 cash account withdrawal together inflated operating cash flow by 61%. We believe that, as a result, Shift4's true leverage stands at 5.3x Net Debt / Adj. EBITDA, far higher than reported by the Company. **Ultimately, we believe that Shift4's aggressive financial maneuvers mask a company that is far less profitable and less cash generative, and far more levered, than investors are led to believe.**

1. **Threat of Margin Call Coincides with String of Aggressive Financial Maneuvers:** In our opinion, evidence suggests that Shift4's CEO, Jared Isaacman, faced the threat of a margin call amidst the 2022 equity meltdown – one that could have resulted in him being forced to sell 10 million shares (~12% of diluted shares outstanding), and that **did in fact force him to repay some of the loan *and* increase his collateral by more than 50%. The closing of another of his variable prepaid forward (VPF) contracts resulted in him offloading up to 2 million shares just last month (March 2023), which we believe went largely unnoticed by most investors.** The recapitalization and looming threat of possible repeated margin calls, as other tech CEOs faced during the 2022 bear market, coincided with a string of aggressive financial maneuvers, accounting gimmickry, and stock promotion.

2. **Inflating EBITDA through Inexplicable Distributor Acquisitions:** In Q3 FY 2022, when we believe that the margin loans were at their most precarious, Shift4 took the unusual step of rolling up half of its independent distributors. By buying out its distributors, Shift4 effectively moves expenses from cost of goods sold into cash flow from investing, flattering gross profit and EBITDA by paying acquired resellers a sum of cash up front equal to their outstanding commission balances. In our opinion, this is a backhanded way of capitalizing COGS, giving the appearance of stronger gross profit and EBITDA without improving the underlying economics or earnings power of the business whatsoever.

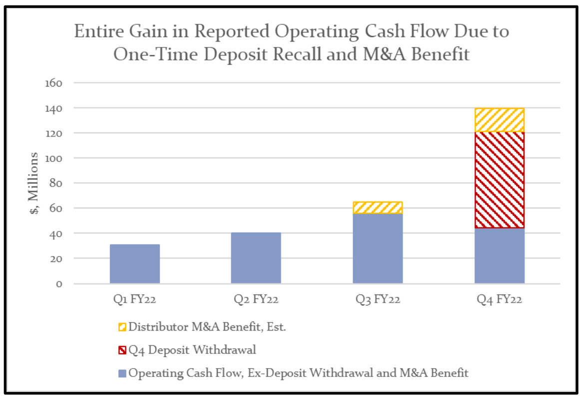
   A. **Distributor M&A Inflates Earnings by Financial Engineering:** Shift4's acquisition of 50% of its third-party resellers for ~$260 million allows it to capitalize residual commissions, which would otherwise run through the income statement via COGS. Management consistently plays coy when asked about the financial impact of this move, and demurs when asked to quantify the impact to COGS. But correspondence between Shift4 and the SEC, in which the SEC challenged its capitalization of bought-out residual commissions, reveals that this expense represents one of Shift4's largest COGS line items, and we calculate that capitalizing 50% of residual commissions would have inflated gross profit and Adj. EBITDA by as much as 22% and 34%, respectively, between 2019 and 2021. We estimate that these acquisitions, which took full effect in Q4 2022, allowed the Company to shift $18.3 million of COGS into cash flow from investing in Q4, inflating gross profit by 15% and Adj. EBITDA by 24%. **On the accounting benefit of these deals alone, Shift4, we estimate, was able to turn what would have been a $5.8 million Adj. EBITDA miss into a $12.5 million Adj. EBITDA beat.**

   B. **Low-Quality Reseller M&A Suggests Earnings Management as Primary Motivation:** The resellers acquired by Shift4 are a motley collection of small, unsophisticated businesses with hilariously outdated websites and little discernable IP, including many one or two-man teams with no clear attraction as buyout candidates. Among these are included **a related party belonging to a relative of the CEO who was quietly bought out for millions**. Most of the businesses are not disclosed by the Company, and we had to comb LinkedIn and company registration filings to discover the unimpressive details of some of these acquired businesses. We see these deals as inexplicable and unjustifiable outside of Shift4's apparent desire to shuffle one of its largest cost items out of COGS. We find the Company's stated justifications for these acquisitions hollow, and think the better explanation is likely that Shift4 sought to flatter its financials as its share price was hitting new lows, and its CEO's margin loan was at a precarious point. **We also note that, around this time, Shift4's CFO abruptly left the Company.**

RCS, Inc., one of the larger third-party resellers acquired by Shift4 (Link here. N.B.: Best viewed in Netscape.)

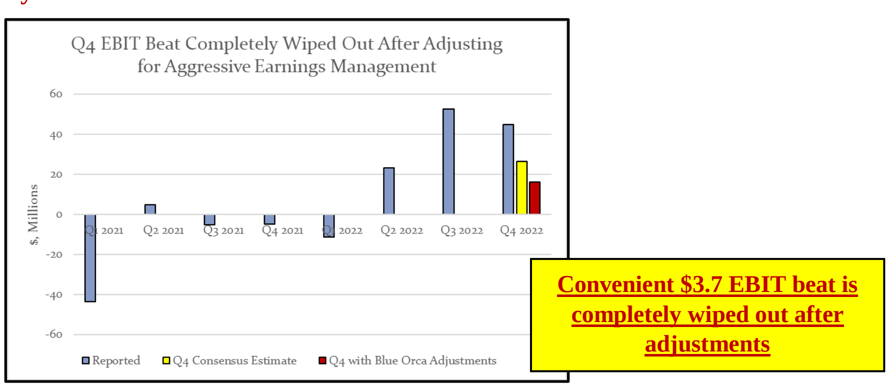
RCS website as of March 2023. Archived at the Wayback Machine.

3. **Cash Flow Manipulation Massively Inflates Operating Cash Flow: Shift4 inflated its operating cash flow in Q4 2022 by more than 2x quarter-over-quarter simply by withdrawing its $76.5 million deposit from its sponsor bank temporarily before quarter end, only to return much of it after fiscal year end.** Shift4 is required to maintain a cash deposit with a sponsor bank to support credit card transactions with certain merchants. Claiming to be in negotiations for a new deal with its sponsor bank, Shift4 withdrew its entire deposit just before the end of Q4, recognizing the reclaimed deposit as operating cash flows. Yet soon after the quarter ended- at some point during the very next month –Shift4 returned a significant portion of the deposit to the bank. In so doing, Shift4 was able to show quarter-over-quarter operating cash flow growth of over 100% merely by temporarily withdrawing cash. Without this subtle and poorly explained, yet, in our opinion, egregious maneuver – in which Shift4 front-loaded its withdrawal before quarter close, and partially undid it only after the December 31 closing date once the gains were conveniently booked – the Company would have instead showed a quarter-over-quarter operating cash flow *contraction*. Excluding the Q4 withdrawal and the benefit of distributor M&A in Q3 and Q4 2022, we estimate that Shift4's 2022 operating cash flow would have been $104.0 million (38%) lower than the Company reported.



Source: Q4 2022 *Shareholder* Letter

4. **Aggressive Accounting Maneuvers Flatter Earnings Significantly:** In our opinion, Shift4 inappropriately capitalizes customer acquisition costs and residual commission buyouts as intangible assets. It maintained these accounting methods since first going public until mid-2022, when it received pushback from the SEC over its treatment of both items, in addition to its exclusion of depreciation of leased equipment from COGS. **We estimate that, taken together, these maneuvers inflated gross profit by as much as 13% and Adj. EBITDA by as much as 36% between 2019 and 2021.** Shift4 only partially caved to the SEC's challenges in mid-2022 by reclassifying gross profit and designating customer acquisition costs as an operating cash item. Even then, it more than made up for these adjustments by extending its depreciation and amortization schedules in Q4 2022 by a weighted-average 29.3%, helping it to turn what would have been a $14.3 million Q4 EBIT miss into a $3.7 million EBIT beat, and, we estimate, to inflate 2023 EBIT by $47.0 million. **We estimate that, between its inappropriately capitalized costs, amended amortization schedules, and removal of residual commissions through its distributor M&A, Shift4 inflated 2022 gross profit by 13.1%, operating income by close to 200%, and Adj. EBITDA by 33.7%.**



Source: Company Filings, Capital IQ, Blue Orca estimates

5. **Aggressive and Misleading CEO Statements Prop Up the Stock:** At a time when we believe he may have been at risk of a margin call, Shift4's CEO began to engage in highly aggressive stock promotion, proclaiming that FOUR is "way too cheap" and that he is "absolutely" considering taking the Company private. **Shift4's CEO also claimed to be a "buyer" when he was, in fact, a net seller of over 1 million shares in 2022, and just weeks before his planned disposal of up to 2 million shares alongside the closing of his VPF contract. Why is the CEO telling investors that FOUR is a screaming buy when he himself is selling?**

Stock Promotion Even as CEO Sells

Absolutely. It's like, are you kidding me? I mean, **the company is way too cheap right now.** Um, and, you know, um…I mean, yeah, **I'm a buyer.**

- Jared Isaacman – CEO, Shift4 (Dec 7, 2022)

NO YOU'RE NOT!

n-Derivative Securities Acquired, Disposed of, or Beneficially Owned

1. Title of Security (Instr. 3)	2. Transaction Date (Month/Day/Year)	2A. Deemed Execution Date, if any (Month/Day/Year)	3. Transaction Code (Instr. 8)		4. Securities Acquired (A) or Disposed Of (D) (Instr. 3, 4 and 5)			5. Amount of Securities Beneficially Owned Following Reported Transaction(s) (Instr. 3 and 4)	6. Ownership Form: Direct (D) or Indirect (I) (Instr. 4)	7. Nature of Indirect Beneficial Ownership (Instr. 4)
			Code	V	Amount	(A) or (D)	Price			
Class A Common Stock	02/27/2023		C(1)		2,000,000	A	$0.00	2,000,000	I	See footnotes(2)(3)
Class B Common Stock	02/27/2023		J(4)		2,000,000	D	$0.00	23,829,016	I	See footnotes(2)(3)
Class A Common Stock	02/27/2023		J(5)		2,000,000	D	(5)(6)	0	I	See footnotes(2)(3)

Source: Feb 27 Form 4

6. **Suspicious Timing around CFO Departure Raises Major Red Flags:** Former CFO Bradley Herring's separation from the Company was announced on August 3, 2022 – the day before the Q2 earnings call, and amidst the SEC's heavy questioning of Shift4's aggressive accounting. He was immediately replaced by board member Nancy Disman, who was given an immediate cash bonus of $3 million – roughly 2x Herring's annual compensation – for taking on the role. We question whether his abrupt departure and replacement with a board member suggests that Shift4 experienced significant internal strife over its questionable financial maneuvering.

7. **Dismal Corporate Governance:** Shift4's board of directors and executive team are full of members of the CEO's family, including his father and brother, as well as a number of his childhood friends. We do not believe that such a board could provide meaningful independent oversight. We think this governance structure may explain Shift4's unusual related-party transactions – particularly for a company of this size – including **payments to the CEO's private jet company, a multi-million dollar buyout of a family member's "third-party" distribution business, nebulous consulting payments to the CEO, and use of Company funds to promote the CEO's private space flight.**

8. **Incinerating Value with Foolish Crypto Acquisition:** Near the height of the crypto craze, Shift4 acquired a crypto donation processing application for $12.6 million in net cash and $36.4 million in FOUR shares – together worth more than the Company had ever generated in adjusted free cash flow in any single quarter, save for the latest. The acquisition also included a contingent consideration worth up to $246 million, the initial fair value of which was set at $57.8 million but which has since been reduced to just $10.7 million following the 2022 crypto crash. Even then, Shift4 has not written down this seemingly flailing addition: the goodwill associated with the acquisition continues to be assigned a value of $89.4 million. We believe that the demonstrable slowdown in the platform's performance, openly admitted by the Company, more than calls for a write-down of this ill-timed acquisition.

Many of these maneuvers came to a head in Q4 2022, just before the CEO was due to dump up to 2 million shares throughout March 2023 to fulfill his VPF contract. In that quarter, **Shift4 not only turned what would have been a sizable $5.8 million Adj. EBITDA miss into a massive $12.5 million beat via M&A-fueled financial engineering, but, out of thin air, created the appearance of 100% Q-o-Q operating cash flow growth (versus what would have been Q-o-Q contraction) by simply temporarily recalling $76.5 million of deposits from its sponsor bank**, which went reported as a contribution to operating cash flow without adjustment.

Entire Q4 2022 Adj. EBITDA Beat Manufactured via Distributor Acquisitions

$, m	Consensus Estimate (CapIQ)	Reported	Residual Commission Adjustment	Adjusted for Residual Commissions
Adj. EBITDA	81.9	94.4	(18.3)	76.1
Beat/Miss	-	12.5	-	(5.8)
Beat/Miss, %	-	15.3%	-	-7.1%

Source: Q4 2022 Shareholder Letter, Capital IQ, Blue Orca estimates

We think the future for Shift4 is one of continued cash burn and ill-advised M&A to keep the growth story alive and investors satisfied on superficial results. Once it runs up against the limits of its already heavily-levered balance sheet (**5.3x net debt/EBITDA, after our adjustments – far higher than the Street is led to believe**), we think the party ends with stagnant growth or aggressive dilution.

Capital Structure and Valuation and Debt Metrics

$, m, except share data	
Share Price	$68.54
Shares Outstanding	84.8
Market Cap	5,810.8
Convertible Notes due 2025 (0.49%)	690.0
Convertible Notes due 2027 (0.90%)	632.5
Senior Notes due 2026 (5.13%)	450.0
Total Borrowing	1,772.5
Operating Lease Liabilities	23.4
Total Debt	1,795.9
Non-Controlling Interest	133.3
Less: Cash & Equivalents	776.5
Net Debt	1,152.7
Total Enterprise Value	6,963.5
2022 Adj. EBITDA, per Shift4	289.7
2022 Adj. EBITDA, Adjusted for Aggressive Accounting	216.7
2022 EV / Adj. EBITDA, Shift4	24.0x
EV / Adj. EBITDA, Blue Orca	32.1x
Net Debt / Adj. EBITDA, Shift4	4.0x
Net Debt / Adj. EBITDA, Blue Orca	5.3x

Source: Company Filings, Capital IQ, Blue Orca estimates

We estimate that, in total, Shift4's aggressive accounting games and M&A activity inflated 2022 gross profit by 13%, Adj. EBITDA by 34%, and operating income by close to 3x, and gave the appearance of a much more palatable (though still high) 4.0x Net Debt / Adj. EBITDA against what we believe to be a more realistic and far more worrisome 5.3x. We also believe that its buyout of 50% of its independent distributors and Q4 2022 collateral withdrawal inflated 2022 operating cash flow by 61%.

Total Impact of Aggressive Earnings Management in 2022

$, m	Actual	Adjusted for Earnings Management
Reported Gross Profit (Old Methodology)	470.2	470.2
Less: Depreciation of Equipment Under Lease	(28.4)	(28.4)
Less: Deflated Depreciation due to Dep. Schedule Change	-	*(3.5)*
Gross Profit (New Methodology)	441.8	438.3
Less: Residual Commission Buyouts (Ex-Q3)	-	*(19.1)*
Less: Residual Commissions Removed via M&A (Q3)	-	*(10.4)*
Less: Residual Commissions Removed via M&A (Q4)	-	*(18.3)*
Pro-Forma Gross Profit	441.8	390.5
Less: Pro-Forma Operating Expenses	(347.1)	(347.1)
Less: Capitalized Customer Acquisition Costs	-	*(25.2)*
Less: Deflated D&A due to D&A Schedule Changes	-	*(12.2)*
Plus: Incremental D&A from Capitalized Residual Commissions	-	*26.7*
Pro-Forma Operating Income	94.7	32.7
Plus: D&A (Reported)	149.1	149.1
Plus: D&A Increase from Schedule Changes	-	*15.7*
Less: Incremental D&A from Capitalizeed Residual Commissions	-	*(26.7)*
Plus: Other Items	13.9	13.9
Pro-Forma EBITDA	257.7	184.7
Plus: Adjustments	32.0	32.0
Pro-Forma Adj. EBITDA	289.7	216.7
Gross Profit Inflation, %	***13.1%***	-
Operating Income Inflation, %	***190.0%***	-
Adj. EBITDA Inflation, %	***33.7%***	-
Net Debt / Adj. EBITDA	***4.0x***	***5.3x***

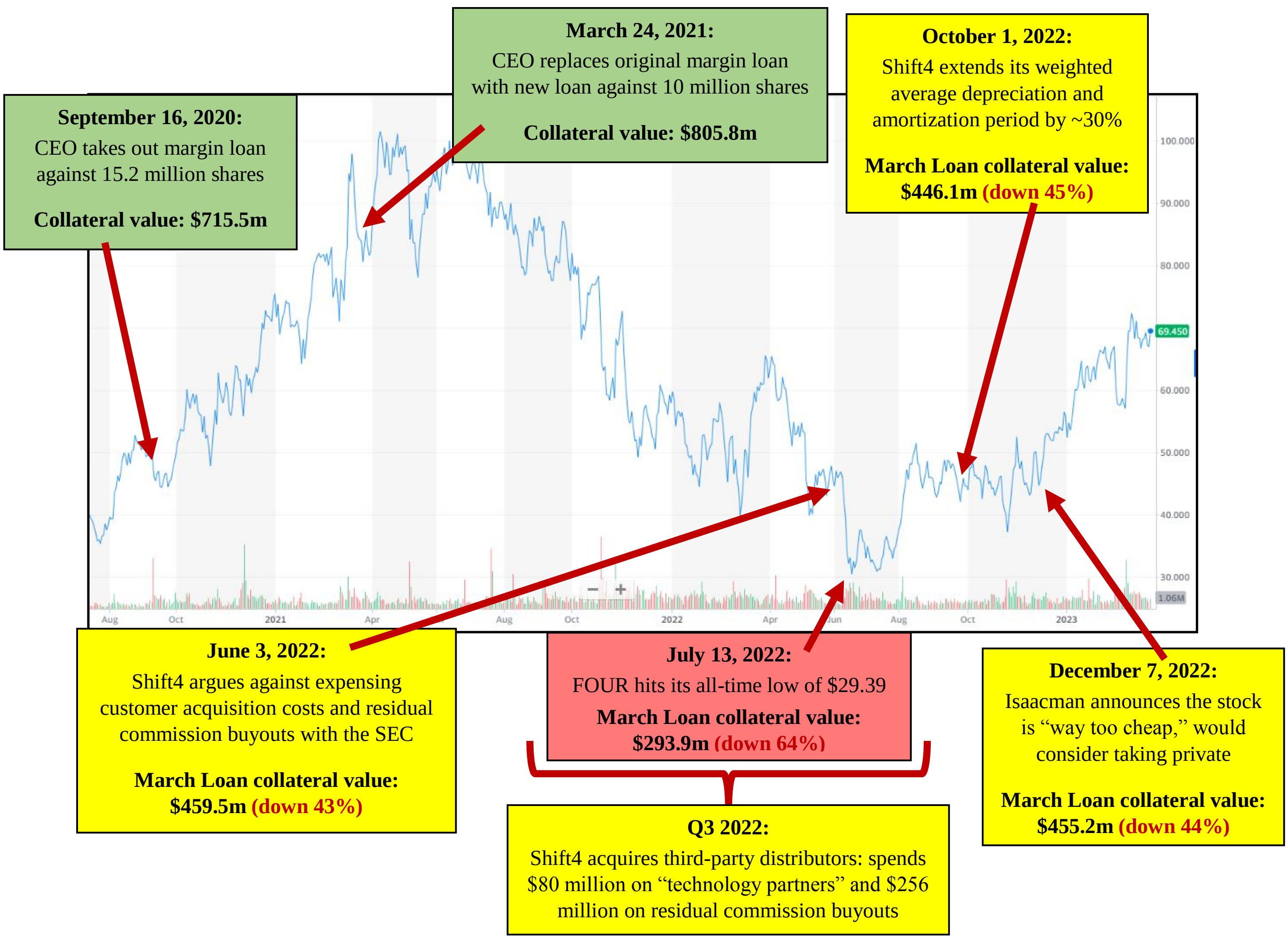
Source: Company Filings, Capital IQ, Blue Orca estimates

Ultimately, we believe that Shift4 is far less profitable, generates far less cash, and is dramatically more levered, than investors are led to believe.

1. Threat of Margin Call Coincides with String of Aggressive Financial Maneuvers

Much of the CEO's fortune remains tied up in Shift4, and he has entered into several financial arrangements with the Company to borrow against his ownership and tap into his paper billions. While such arrangements are common among founder-CEOs, we believe that his borrowings have, likely unbeknownst to investors, hung over Shift4 as a unique threat: not only have a meaningful portion of his shares (up to 6.4 million, or 22% of his holdings) been tied to forward sale contracts due to liquidate through 2023-24 – including up to 2 million just in March 2023 – but the decline in FOUR alongside the 2022 tech rout has, we believe, put him at risk of facing a margin call at various points through the past year. **We believe he likely received, in effect, just such a margin call in mid-2022, as he was forced to up his collateral by more than 50% AND to reduce the size of the loan**.

Any serious liquidation of the CEO's margin loan collateral would be devastating for the stock, as the lender would now have the right to dispose of up to 15 million shares upon default, a significant 18% of diluted shares outstanding – in addition to the remaining 4.4 million shares tied to other forward-sale agreements due to be disposed of in 2024. Investors, we think, have, to this point, not been sufficiently privy to this very serious dilution risk. In our opinion, **Shift4's increasingly cavalier accounting maneuvers, cash flow manipulation, and stock promotion must be viewed in the context of the CEO's margin loan – in danger at the time – and continued insider sales**.



2022 Equity Collapse Leads to Effective Margin Call

As of the latest filing, Shift4's CEO owns just under 30 million shares, representing about a third of diluted shares outstanding. Per Company filings, Isaacman, through Rook Holdings, Inc., first entered into a margin loan in September 2020, secured by 15.2 million shares (in the form of 15.2 million LLC units and an equivalent number of B shares, together redeemable by the lender for 15.2 million A shares). This agreement was then replaced on March 24, 2021 by a new loan secured by 10 million shares, at which time shares of FOUR were worth ~$80.

With the loan having been taken out not far from the April 2021 top, we suspect that, as the stock fell to as low as $29.39 in the summer of 2022, and as it remained in the $30s and $40s at highest through much of the rest of the year, the CEO faced the serious threat of margin calls. At the stock's lowest point July 2022, the pledged shares, worth $806 million on March 24, 2021, would have been worth just $294 million.

Though he wasn't liquidated as FOUR reached its deepest lows, **disclosures indicate that the CEO did, in fact, appear to receive an effective margin call on his loan**. Quietly slipped into Shift4's most recent 10-K was an admission that his 10 million share margin loan was "repaid and replaced" with another margin loan "for a lower amount." The stated collateral attached to the margin loan was also quietly **increased** from 10 million shares to 15 million shares, "**in addition to other collateral**."

2021 10-K/A

> Rook entered into a margin loan agreement in September 2020, ("September 2020 Margin Loan"), pursuant to which it pledged LLC Interests and shares of the Company's Class A and Class B common stock (collectively, "Rook Units") to secure a margin loan. The September 2020 Margin Loan was repaid in March 2021.
>
> Rook entered into a margin loan agreement, replacing the September 2020 Margin Loan, in March 2021 ("March 2021 Margin Loan"), pursuant to which it pledged Rook Units to secure a margin loan. If Rook were to default on its obligations under the margin loan and fail to cure such default, the lender would have the right to exchange and sell up to 10,000,000 Rook units for an equal number of the Company's Class A common stock to satisfy Rook's obligation.

Source: 2021 10-K/A

2022 10-K

> Rook has entered into margin loan agreements to repay and replace an existing margin loan for a lower amount, pursuant to which, in addition to other collateral, it has pledged LLC Interests and shares of the Company's Class A and Class B common stock (collectively, "Rook Units") to secure a margin loan. If Rook were to default on its obligations under the margin loan and fail to cure such default, the lender would have the right to exchange and sell up to 15,000,000 Rook units to satisfy Rook's obligation.

Source: 2022 10-K

Based on these disclosers, we think the CEO's loan reached such a precarious state that he was forced to repay some of his loan *and* increase his collateral with the bank by *more* than 50% just to support a margin loan of *smaller* size than the original.

In effect a margin call, this event, in our opinion, provides critical context for the aggressive M&A, financial engineering, stock promotion, and accounting maneuvers undertaken by Shift4 throughout the second half of 2022. Facing the possibility of receiving additional margin calls – as his tech CEO peers such as Peloton's John Foley received "repeatedly" throughout 2022, ultimately at significant personal cost – Shift4 would have been heavily incentivized to keep the Company's financials looking strong and the stock as high as possible.

For instructive purposes, assuming an initial LTV of 20% for a loan worth ~$160 million, the loan's LTV would have stood at 55% at the stock's all-time low in July 2022, and covering the shortfall in full would have forced him to post an additional 17.4 million shares, or 58% of his holdings. By way of comparison, the margin loan which Elon Musk nearly took out against his Tesla shares in April 2022 to finance his purchase of Twitter – itself a 20% LTV loan – would have experienced a margin call had the LTV reached merely 35% (see here, page A-3).

Typical Margin Loan Falls into Critical Territory During 2022 Bear Market

	March 24, 2021	All-Time Low (July 2022)
Shares Pledged (M)	10.0	10.0
Stock Price	$80.58	$29.39
Value of Pledge (M)	$805.8	$293.9
Delta vs. 3/24/21 (M)	-	$511.9
Delta in Shares (M)	-	17.4
% of Isaacman Holdings	-	58.2%
% of Diluted Shares Outstanding	-	20.6%
Hypothetical LTV on Initial 20% LTV Loan	20.0%	54.8%

Source: Company Filings, Blue Orca estimates (based on hypothetical 20% LTV margin loan)

Using these borrowing terms as benchmarks for an owner-CEO margin loan against a multi-billion dollar company, Shift4's CEO's loan would have easily tripped margin call levels at FOUR's all-time low, to the point that a liquidation of his pledged shares would have netted the lender less than half of the original value of the pledged collateral – and to the point that, **to make up for the 17.4 million share delta in collateral value, the CEO would have had to have pledged nearly the entirety of his remaining total stake of ~30 million FOUR shares to make the lender whole on its initial collateral.** It does not surprise us that he was forced to trim the size of his loan even after he increased his posted collateral by more than 50%, some of which was contributed by assets other than his ownership of FOUR: the value of his initial collateral had fallen so far with the stock that re-upping his collateral to $805.8 million would have meant posting nearly his entire ownership stake – a move with which neither party would likely be comfortable.

Under these circumstances, we would have a hard time believing, even without knowing the precise loan terms, that the CEO did *not* face a margin call. Based on this analysis, we think that the restructuring of the loan described in Shift4's filings was required to avoid what might have been a material liquidation of FOUR shares.

Hence, Shift4's CEO spent much of 2022 facing a similar fate as other CEOs with sizable margin loans who contended with margin calls during the 2022 equity meltdown. With peers like Peloton CEO John Foley undergoing what would be, in his own words, "not a fun personal balance-sheet reset" upon receiving *repeated* margin calls, Shift4's CEO would have faced a tangible risk of experiencing the same outcome as stocks sank in 2022. Accordingly, it concerns us that the looming threat of possible repeated margin calls, as other tech CEOs faced during the 2022 bear market, coincided with what appear to us to be a string of aggressive financial maneuvers, accounting gimmickry, and stock promotion.

CEO Quietly Dumping Shares Tied to VPF Contracts While Telling Investors to Buy

Between March and September 2021, Shift4's CEO also entered into variable prepaid forward contracts ("VPF contracts") covering a total of 6.44 million shares. These contracts allow him to monetize his holdings by committing to deliver shares at a future date without having to formally sell until then, in exchange for taking a haircut on the value of his shares at the date at which the contracts are struck. They enable him to receive the cash up front at a discount on the promise that the shares will be delivered to the counterparty at a future date set out in the contracts.

We note that these contracts effectively represent a complex form of insider selling which, while disclosed in Company filings, are disclosed neither on the typical forms (e.g. Form 4) nor through the channels by which investors typically monitor insider selling at the time that the forward sale actually occurs. **We question whether investors appreciate that the CEO has effectively forward-sold over 20% of his FOUR holdings (and close to 8% of all FOUR diluted shares) through these contracts.**

Critically, the VPF contract struck in March 2021, covering 2 million shares, settled during the month of March 2023, per Company filings: up to 66,667 shares were due to be disposed of each trading day through April 5. As FOUR shares traded below the forward floor price of $73.19 set out in the contract for nearly the duration of the month, investors should expect that close to, if not the full, 2 million shares were sold.

To repeat, for clarity and emphasis: Shift4's CEO quietly dumped up to 2 million shares onto the market just last month. And, due to the nature of the filing through which it was disclosed we think most investors are unaware of this.

Table I - Non-Derivative Securities Acquired, Disposed of, or Beneficially Owned

1. Title of Security (Instr. 3)	2. Transaction Date (Month/Day/Year)	2A. Deemed Execution Date, if any (Month/Day/Year)	3. Transaction Code (Instr. 8)		4. Securities Acquired (A) or Disposed Of (D) (Instr. 3, 4 and 5)			5. Amount of Securities Beneficially Owned Following Reported Transaction(s) (Instr. 3 and 4)	6. Ownership Form: Direct (D) or Indirect (I) (Instr. 4)	7. Nature of Indirect Beneficial Ownership (Instr. 4)
			Code	V	Amount	(A) or (D)	Price			
Class A Common Stock	02/27/2023		C(1)		2,000,000	A	$0.00	2,000,000	I	See footnotes(2)(3)
Class B Common Stock	02/27/2023		J(4)		2,000,000	D	$0.00	23,829,016	I	See footnotes(2)(3)
Class A Common Stock	02/27/2023		J(5)		2,000,000	D	(5)(6)	0	I	See footnotes(2)(3)

5. From February 27, 2023 to April 7, 2023 (the "Settlement Period"), Rook SPV is scheduled to settle the Transaction with the Counterparty, relating to 2,000,000 shares of Shift4 Payments, Inc.'s Class A common stock (the "Class A Common Stock") in accordance with the following Transaction terms previously agreed upon as of March 16, 2021 and reported on March 18, 2021. The Transaction is divided into 30 individual components (each comprising 66,667 shares (or 66,666 in the case of the first 10 valuation dates) (the "Component Shares") of Class A Common Stock) over the 30 scheduled trading days up to, and including, April 5, 2023 (the "Valuation Period"). The number of Class A Common Stock to be delivered to the Counterparty with respect to each component during each day of the Settlement Period will be based on the volume weighted average price per share of the Class A Common Stock for each trading day during the Valuation Period (the "Settlement Price") as follows:

Source: Feb 27 Form 4

We believe that most investors are likely blind to this massive share dump, as these transactions went undetected by most public insider transaction screeners such as OpenInsider, Finviz, and Benzinga, because there was, by necessity, no fixed value tied to the future share sales, or due to the non-traditional transaction codes associated with them ("C" for "Conversion of derivative security," and "J" for "Other acquisition or disposition," per the SEC). Even on professional screeners such as Capital IQ, the value of the share sales is listed as "$0", again because there was no set price tied to the future sales.

This disposal should be of critical concern to all investors not just because it represents a massive insider sale by Shift4's most important insider, but because, with 85 million diluted shares outstanding (and just 54 million A shares trading), it is large enough to dilute existing shareholders to a material degree. Yet we believe that much of the investing public is likely unaware that Shift4's CEO disposed of up to 2 million shares just last month.

Importantly, it's not just the lack of transparency that we find troubling in this case: we think it's particularly problematic that the CEO sold this massive quantity of shares even as he proclaimed to be "a buyer" (more below).

2. Inflating EBITDA through Inexplicable Distributor Acquisitions

In our opinion, Shift4's acquisition of half of its third-party resellers in Q3 2022 for just under $260 million only amplifies the distortive effect of the Company's aggressive accounting methods on reported earnings, allowing it to capitalize nearly a quarter of its COGS (outside of network fees) simply by taking much of its independent sales force in-house without changing the Company's underlying earnings power whatsoever. We view **such acquisitions as accounting gimmickry which inflated gross profit and EBITDA at a critical moment in time when Shift4's languishing stock price hung under the threat of a margin call.** We also note that Shift4's CFO departed at this critical juncture.

We think these deals superficially inflate gross profit by as much as 22% and Adj. EBITDA by as much as 34% on a run-rate basis.

And, with up to 2 million of the shares associated with the CEO's VPF contracts having been scheduled to be liquidated immediately after Q4 2022 earnings, we think this accounting maneuver produced an artificially strong Q4 print immediately prior to a sustained period of pre-planned insider sales. We estimate that Shift4's conveniently timed $12.5 million Q4 EBITDA beat can be attributed in its entirety to financial engineering via distributor acquisitions. Without the dubious M&A, we estimate that Shift4 would have **missed** on EBITDA by a sizable $5.8 million.

Distributor M&A Inflates Earnings via Financial Engineering

In Q3 FY22, Shift4 took the unusual step of acquiring distributors representing roughly 50% of its independent sales force, after having employed third-party resellers almost exclusively throughout its existence to that point. These distributors are responsible not only for marketing Shift4's products and services, but for managing the relationship between Shift4 and merchants over the life of each deal, for which they receive a "residual commission." As a consequence, costs associated with distribution that might have otherwise been allocated to SG&A are instead run through Shift4's income statement via COGS, as its independent sales force is paid primarily through commissions which are expensed as a cost of goods sold.

By buying out its distributors, Shift4 effectively moves costs from its income statement into cash flow from investing, flattering gross profit and EBITDA by paying acquired resellers a sum of cash up front equal to their outstanding commission balances. In our view, this is a back-handed way of capitalizing COGS, giving the appearance of stronger gross profit and EBITDA without improving the underlying economics or earnings power of the business whatsoever.

Critically, while the sell-side has some awareness of the directional impact of the accounting around these deals on earnings, we believe that both analysts and the investing public are ignorant of the relative magnitude of residual commissions as a share of COGS – and, consequently, of the dramatic effect of Shift4's distributor acquisitions on Company financials. Shift4 has been coy about the weight of these costs, and has not, to our knowledge, openly quantified them when asked about the financial implications of its distributor acquisitions.[1]

However, buried in a letter from Shift4 to the SEC regarding its accounting practices, we observe that residual commissions have accounted for a massive 40-45% of non-network fee COGS each year since FY19 ($115M in FY21). Removing this cost of sales from the income statement in its entirety would have permitted Shift4 to report an Adj. EBITDA by 60-70% between FY19-21.

> *(2) Residual commissions: Subsequent to the upfront payment, Shift4 pays monthly residual commissions to its third-party distribution partners which are based on a percentage of payment-based revenue earned during that respective month by their portfolio of merchants. These payments are expensed in cost of sales (approximately $115 million, $60 million, and $55 million in 2021, 2020, and 2019, respectively) as the related revenue is earned and reported in operating activities in our statement of cash flows. Residual commissions are earned for the life of the end-to-end processing relationship the merchant has with Shift4, incentivizing all stakeholders to maintain the existing relationships, whereas the capitalized acquisition costs are the initial cost incurred by Shift4 to secure the end-to-end processing agreement with the merchant.*

Source: June 30, 2022 correspondence

[1] Shift4's Q3 2022 10-Q and 2022 10-K disclose a *net* change in residual commissions within COGS, of which they describe the residual commission buyouts as a contributing factor, but nowhere is the isolated impact of residual commission buyouts disclosed.

Thus, by bringing ~50% of its independent resellers in-house, we estimate that Shift4 eliminates ~20-25% of its non-network fee COGS, immediately increasing its pro-forma Adj. EBIDTA on paper by 30-35% without, in our view, changing the underlying quality or earnings power of the business in any way.

Pro-Forma Full-Year Impact of Third-Party Distributor In-Sourcing: 50% In-Sourced

$, m	Actual Results			Pro-Forma, 50% of Residual Commissions Removed from COGS		
	2019	2020	2021	2019	2020	2021
Gross Profit	173.4	177.8	278.4	173.4	177.8	278.4
Less: Depreciation of Leased Equipment	(0.2)	(9.8)	(21.8)	(0.2)	(9.8)	(21.8)
Gross Profit (New Methodology)	173.2	168.0	256.6	173.2	168.0	256.6
Plus: Residual Commissions	-	-	-	*27.5*	*30.0*	*57.5*
Pro-Forma Gross Profit	173.2	168.0	256.6	200.7	198.0	314.1
Less: Operating Expenses[2]	(177.6)	(225.6)	(305.8)	(177.6)	(225.6)	(305.8)
Plus: Depreciation & Amortization[2]	62.6	84.2	104.4	62.6	84.2	104.4
Plus: Other Items	1.0	(16.0)	0.1	1.0	(16.0)	0.1
Pro-Forma EBITDA	59.2	10.6	55.3	86.7	40.6	112.8
Total Adjustments	30.6	77.1	111.9	30.6	77.1	111.9
Pro-Forma Adj. EBITDA	89.8	87.7	167.2	117.3	117.7	224.7
Gross Profit Inflation %	-	-	-	***15.9%***	***17.9%***	***22.4%***
Adj. EBITDA Inflation %	-	-	-	***30.6%***	***34.2%***	***34.4%***

Source: Company Filings, Blue Orca estimates

Importantly, we don't think Shift4 takes on significant SG&A with its reseller acquisitions: the vast majority of distributor economics are tired to residual commissions, which the Company has shifted from the income statement to the cash flow statement with its recent M&A. Assumed salaries will pale in comparison, seemingly confirmed by the fact that Shift4's Q4 2022 SG&A margin of 13.7% was its second-lowest of FY 2022 – lower than both Q1 and Q3. Shift4's CFO herself seems to confirm this as well. Responding to a question regarding the positive earnings impact of these deals on the Q3 2022 earnings call, she acknowledged that Shift4 would see some "offset" in adding SG&A even as COGS were reduced. However, she gave no specifics, and responded that "the mechanics as you've just defined them" – that is, that gross profit and EBITDA would improve as a result of the acquisitions – "are appropriate." Even then, she did not quantify the impact on SG&A, gross profit, or EBITDA – likely, we think, because the Company does not want to disclose the massive impact of its accounting maneuvers, hoping instead to take credit for the resulting earnings improvement.

The financial impact of Shift4's actions took full effect in Q4 2022, the first quarter during which the acquired resellers were fully integrated into the Company. Shift4 reported non-network fee COGS of $61.1 million, inclusive of depreciation of equipment under lease, in Q4 2022. We estimate that, by acquiring distributors and wiping out ~23% of COGS (excluding network fees), Shift4 eliminated $18.3 million of residual commissions from its income statement, flattering gross profit (using its new methodology) by 15% and Adj. EBITDA by 24%.

[2] "Depreciation & Amortization" includes depreciation and amortization from both COGS and SG&A. "Depreciation & Amortization" and "Operating Expenses" are unadjusted for incremental amortization from residual commission buyouts, which would simultaneously increase operating expenses and decrease D&A, and have no net impact on EBITDA.

Shift4 Q4 2022 Results Inflated by Distributor M&A

$, m	Actual	Adjusted
Gross Profit (Previous Methodology)	144.1	144.1
Less: Depreciation of Equipment under Lease	(5.8)	(5.8)
Gross Profit	138.3	138.3
Less: Residual Commissions (Est.)	-	*(18.3)*
Pro-Forma Gross Profit	138.3	120.0
Less: Operating Expenses	(108.3)	(108.3)
Plus: Incremental D&A from Capitalized Residual Commissions	-	*16.0*
Pro-Forma Operating Income	30.0	27.7
Plus: Depreciation & Amortization	47.5	47.5
Less: Incremental D&A from Capitalized Residual Commissions	-	*(16.0)*
Plus: Other Items	14.7	14.7
Pro-Forma EBITDA	92.2	73.9
Plus: Adjustments	2.2	2.2
Pro-Forma Adj. EBITDA	94.4	76.1
Gross Profit Inflation %	-	***15.3%***
Adj. EBITDA Inflation %	-	***24.1%***

Source: Company Filings, Blue Orca estimates

Critically, sell-side consensus around Shift4's Q4 Adj. EBITDA was $81.9 million going into earnings. **We estimate that, by removing $18.3 million of COGS from the income statement, Shift4 turned what would have been a $5.8 million Adj. EBITDA miss into a significant $12.5 million Adj. EBITDA beat.** And, given the public's ignorance of the magnitude of residual commissions removed via the distributor acquisitions, we don't think that the impact of these accounting machinations was accounted for by analysts in their pre-earnings estimates.

Entire Q4 2022 Adj. EBITDA Beat Manufactured via Distributor Acquisitions

$, m	Consensus Estimate (CapIQ)	Reported	Residual Commission Adjustment	Adjusted for Residual Commissions
Adj. EBITDA	81.9	94.4	(18.3)	76.1
Beat/Miss	-	12.5	-	(5.8)
Beat/Miss, %	-	15.3%	-	-7.1%

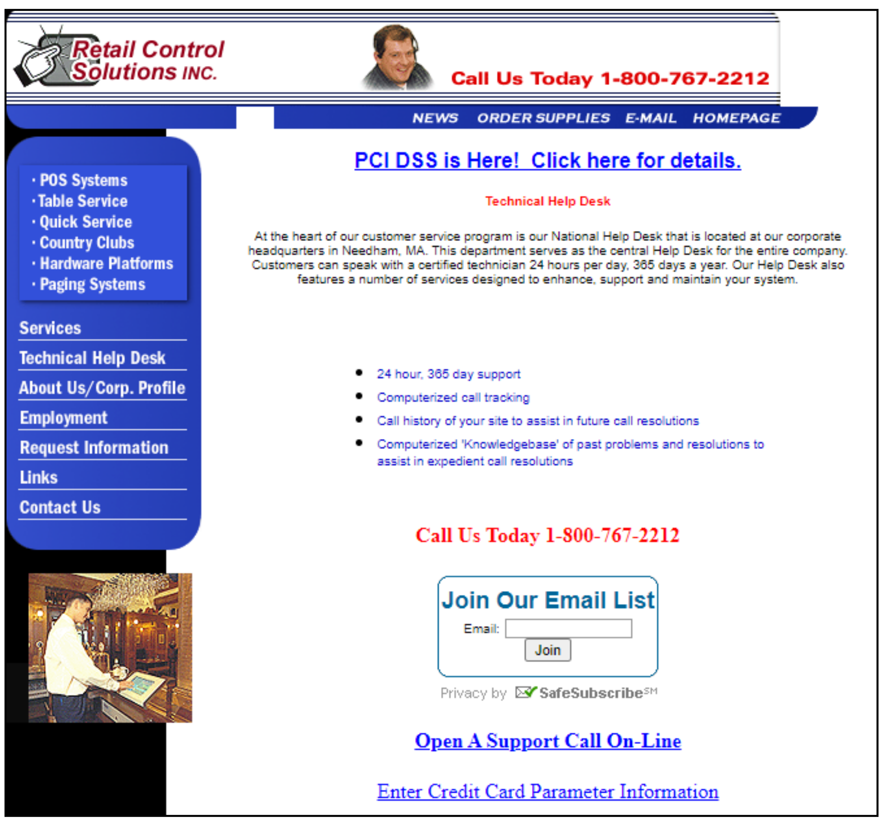
Source: Q4 2022 Shareholder Letter, Capital IQ, Blue Orca estimates

Low-Quality Distributor M&A Suggests Financial Engineering as Primary Motivation

We believe that, with most investors blind to the extent to which near-term EBITDA growth would be driven superficially by the accounting around distributor acquisitions, **Shift4's acquisitions flattered earnings and made the stock look more attractive at a moment at which FOUR was reaching new precipitous lows, just as the margin loan would have been at high risk for a catastrophic margin call**. We see little other compelling reason for Shift4 to acquire third-party resellers, which our research suggests are extremely low-quality M&A targets.

Note that distributors do not appear to be attractive businesses: these are people-intensive organizations which, as the servicer of Shift4's merchants throughout the life of their customer relationship, are effectively cost centers for the Company. They almost universally have little meaningful IP. They are simply an outsourced sales force whose incentive structure happens to hit Shift4's income statement at the COGS level. We don't see why Shift4 would have any interest in acquiring these "businesses" aside from taking the opportunity to inflate EBITDA.

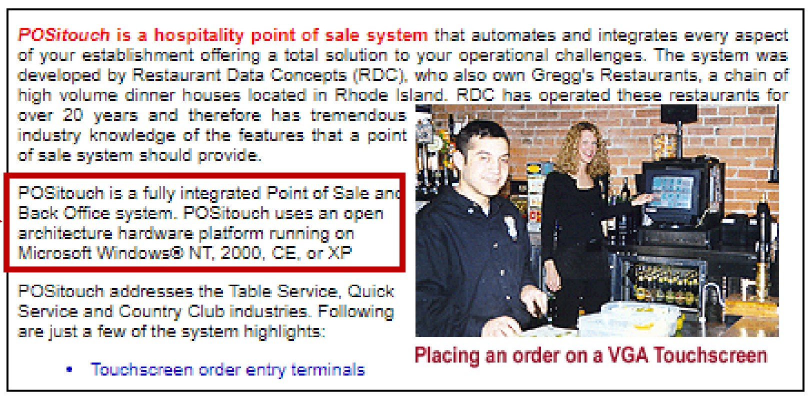
Consider some of the resellers which Shift4 bought up in its recent round of acquisitions. Among those large enough to be named in its filings was Retail Control Solutions, Inc. ("RCS"). Its homepage looks straight out of 1995, best viewed in Netscape. It was still live just weeks before the publication of this report. While Shift4 was wise enough to redirect from http://rcs-usa.com/ to https://www.skytab.com/ after the deal was done, as it did with its other acquisitions, it until recently failed to kill RCS's *actual* home page, http://rcs-usa.com/helpdesk.html, leaving its antediluvian website up for all to see. While it is no longer live, you can find a recently cached version of the site without images here, and a fully navigable version on the Wayback Machine here (from 2017, but we can confirm that this is exactly how the site appeared until as recently as March 2023). Below is a screenshot of how it appeared until just weeks ago.



RCS website as of March 2023. Archived at the Wayback Machine.

This is an actual screenshot from the reseller's website, giving the appearance of a low-tech late 90s RadioShack enthusiast.

Hilariously, RCS proudly reported that POSitouch, one of the Shift4 POS systems offered by RCS, "uses an open architecture hardware platform running on Microsoft Windows® NT, 2000, CE, or XP."



This was one of the distributors large and prominent enough to have *gone reported* in Shift4's filings. In acquiring 50% of its independent sales force, the Company acquired dozens of small, local resellers, many of which are little more than unsophisticated one-man shows with almost zero web presence – and which, consequently, were not individually disclosed by Shift4. Somehow, RCS was supposed to be more of the more impressive ones, about which Shift4 felt comfortable being public.

We are also concerned that Shift4 used this recent round of distributor acquisitions to provide a relative of the CEO with an unusually large personal windfall. The most recent 10-K discloses that, in its round of third-party reseller acquisitions, it bought out the residual commissions of a relative of the CEO for \$3.6 million. For a single individual to have racked up this much in residual commissions as an independent distributor is itself eyebrow-raising. We think Shift4 should provide greater transparency around this deal. Who is the relative? How large was his regional footprint as a reseller? How many merchants, and what volume of transactions, was he servicing?

2022 10-K

> In June 2022, the Company entered into a \$3.6 million residual commission buyout agreement with a relative of the Founder, consisting of an initial payment of \$2.5 million in cash and \$0.6 million in shares of the Company's Class A common stock, and a contingent payment of \$0.5 million in cash payable after 12 months, subject to certain conditions related to the performance of the acquired assets.

Source: 2022 10-K

But this also raises a larger question around the Company's relationship with supposedly independent third-party distributors. Though this relative was technically an independent reseller, why was the business relationship between him and Shift4 – apparently a sizable one – not previously reported among the Company's related party transactions? The revelation that a family member was previously earning sizable commissions through his relationship with Shift4 makes us wonder whether any other similar arrangements exist.

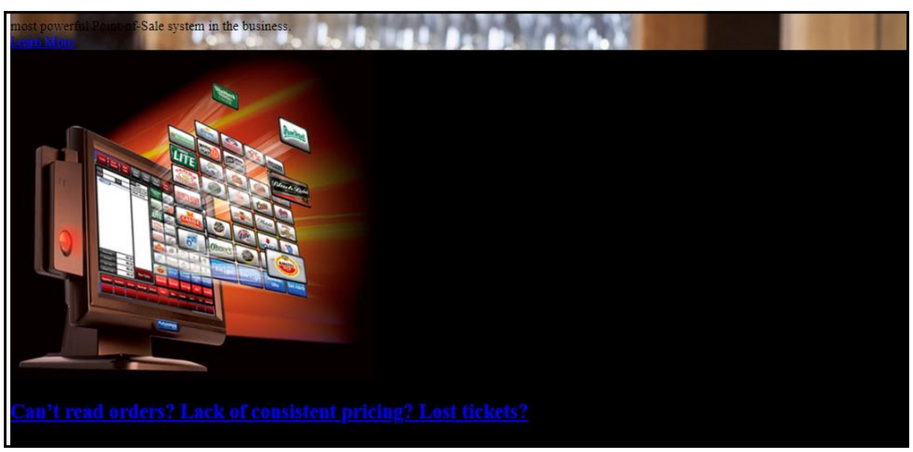
For the resellers not specifically identified by Shift4, we believe that we identified a number of them by combing LinkedIn for regional sales managers who started working with Shift4 during or around Q3 2022, and identifying those who had previously run or worked for small regional distributors that appear to have been wound down at the same time. We also identified a number of small businesses and individual proprietorships whose state registrations were transferred to Shift4's CEO and GC around this time, indicating that these resellers were part of the Q3 2022 M&A. We believe, based on the preponderance of the evidence, that these resellers were included in the residual commission buyouts.

We find that many of the distributors recently acquired by Shift4 appear to be businesses run by just one or two people, and sometimes by family members, with minimal IP and, to us, little to offer as an acquisition target except the ability to capitalize a major component of COGS.

Consider, for example, Southern Point of Sale LLC out of Hammond, LA, which appears to have been manned by all of two people – both now Shift4 salesmen, per their LinkedIn pages – and Long Beach Cash Register Co., for which we can find neither a website nor even business records, but whose sole member self-reports as a Local Sales Manager for Shift4 as of September 2022, amidst the string of reseller acquisitions. We assume he effectively operated as a sole proprietor.

It's important to note that you won't find these "businesses" mentioned anywhere in Company filings. Shift4 might argue that they are simply too small to disclose individually, but we think that the Company is more than happy to use this excuse as a cop-out to avoid having to reveal them to the market. Investors simply aren't able to identify most of the distributors acquired by Shift4 without taking creative and time-consuming measures to do so.

Among these distributors, for example, is Apex Solutions of Toledo, whose President and Owner became a Local Manager for Shift4 in July 2022, per his LinkedIn page. Its former website appears janky, not unlike RCS's, and it linked to ancient POS demo YouTube videos such as this and this.

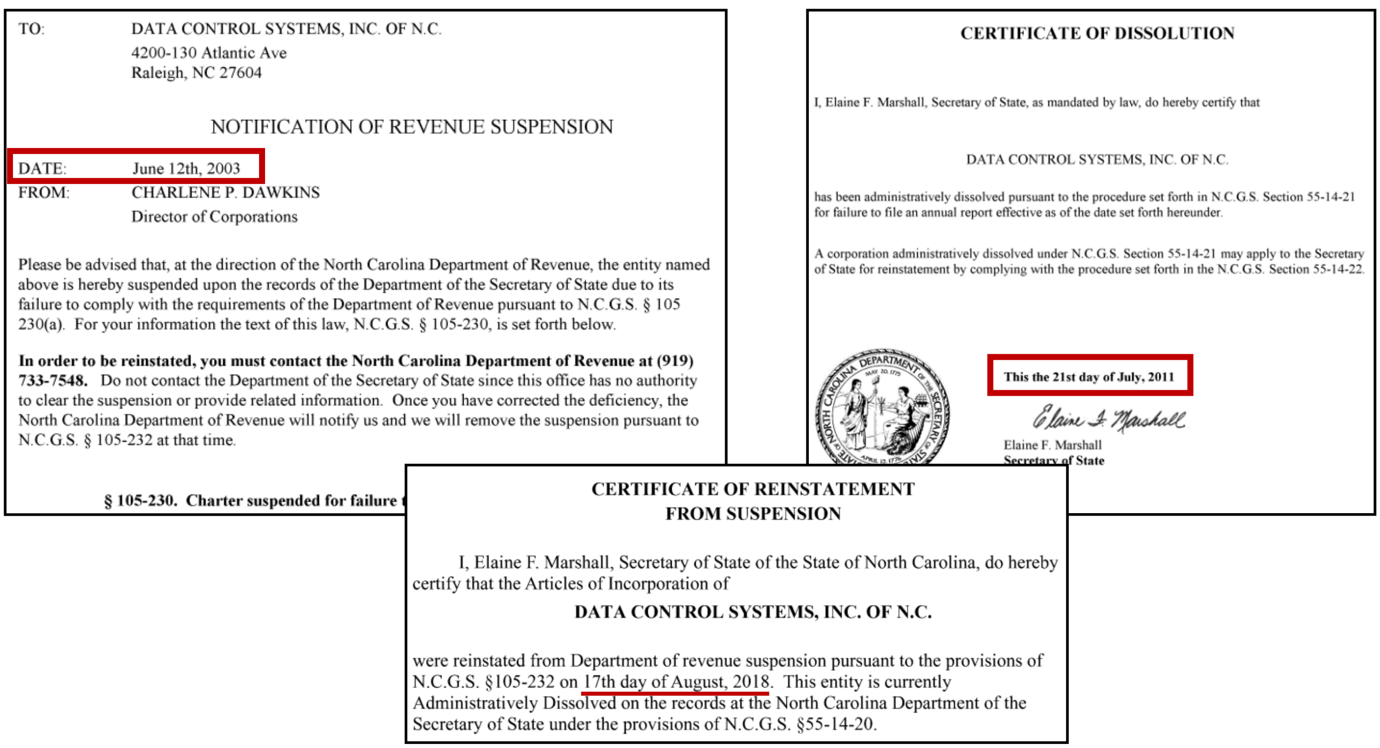


Source: Apex Solutions (archived at the Wayback Machine)

Also see Gibbs Retail Systems, whose website is still up, but which was bought out by Shift4 per the former owner's retirement announcement on his business' recently removed Facebook page ("unexpectedly," according to the post, which is now down, but the text of which is still viewable in the source code of a recently cached version of the page). At least one of its employees now self-reports as a Shift4 employee on his LinkedIn page. Its website looks a bit more professional, but it appears to show that the business focused more on selling security systems and drive-thru technology than POS systems.

Source: Gibbs Retail Systems

We also identified a number of small third-party resellers whose registrations were recently transferred to Shift4, and which appear to be of similarly low-quality, if not worse, than the above. Consider, for example, Data Control Systems, Inc. of N.C., which was registered to its founders from 1994-2022, and is now registered to Shift4's CEO and GC. Formed as a small father-son business in 1994, it failed to file annual reports between 1998 and 2017. It was suspended by the state of North Carolina in 2003 and forcibly dissolved in 2011. This was rectified only in 2018, when the company filed outstanding reports dating back to 1998.



TO: DATA CONTROL SYSTEMS, INC. OF N.C.
4200-130 Atlantic Ave
Raleigh, NC 27604

NOTIFICATION OF REVENUE SUSPENSION

DATE: June 12th, 2003
FROM: CHARLENE P. DAWKINS
Director of Corporations

Please be advised that, at the direction of the North Carolina Department of Revenue, the entity named above is hereby suspended upon the records of the Department of the Secretary of State due to its failure to comply with the requirements of the Department of Revenue pursuant to N.C.G.S. § 105 230(a). For your information the text of this law, N.C.G.S. § 105-230, is set forth below.

In order to be reinstated, you must contact the North Carolina Department of Revenue at (919) 733-7548. Do not contact the Department of the Secretary of State since this office has no authority to clear the suspension or provide related information. Once you have corrected the deficiency, the North Carolina Department of Revenue will notify us and we will remove the suspension pursuant to N.C.G.S. § 105-232 at that time.

§ 105-230. Charter suspended for failure

CERTIFICATE OF DISSOLUTION

I, Elaine F. Marshall, Secretary of State, as mandated by law, do hereby certify that

DATA CONTROL SYSTEMS, INC. OF N.C.

has been administratively dissolved pursuant to the procedure set forth in N.C.G.S. Section 55-14-21 for failure to file an annual report effective as of the date set forth hereunder.

A corporation administratively dissolved under N.C.G.S. Section 55-14-21 may apply to the Secretary of State for reinstatement by complying with the procedure set forth in the N.C.G.S. Section 55-14-22.

This the 21st day of July, 2011

Elaine F. Marshall
Elaine F. Marshall
Secretary of State

CERTIFICATE OF REINSTATEMENT FROM SUSPENSION

I, Elaine F. Marshall, Secretary of State of the State of North Carolina, do hereby certify that the Articles of Incorporation of

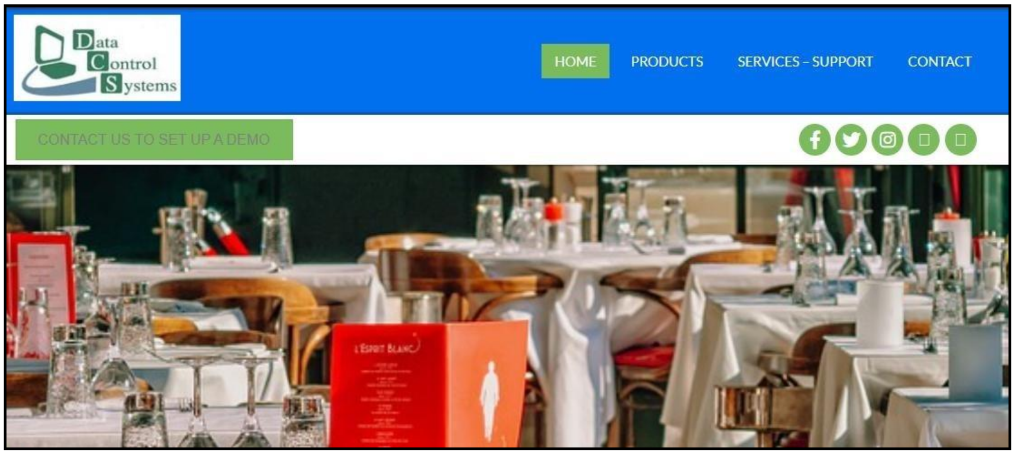
DATA CONTROL SYSTEMS, INC. OF N.C.

were reinstated from Department of revenue suspension pursuant to the provisions of N.C.G.S. §105-232 on 17th day of August, 2018. This entity is currently Administratively Dissolved on the records at the North Carolina Department of the Secretary of State under the provisions of N.C.G.S. §55-14-20.

Source: North Carolina Business Register

How did Data Control Systems legally operate from 2003 through 2017? How did it file taxes if it wasn't recognized by the state as a registered entity?

Whatever the case, its website was not much more appealing than RCS's, now down as of late 2022 but archived here.



Source: DC POS, archived at the Wayback Machine

Why did Shift4 bother spending $256 million in Q3 alone to buy a motley collection of small resellers, some of which appear not even to be focused exclusively on selling POS systems, only to have some of their former owners retire immediately thereafter? These moves simply seem to give Shift4 the benefit of moving the residual commissions tied to these businesses out of COGS, instead capitalizing them as residual commission buyouts.

The Company, at different times, tried to justify the deals by citing, in no particular order, a desire to in-source merchant servicing (without providing a clear reason), to incentivizing its sales force to sell its SkyTab system to more customers (which they would have been anyways), to avoiding channel conflict between sellers of its various different POS systems (which, if ever a problem, must have been so since 2017-18, when it rolled up its multiple POS systems under private equity firm Searchlight Capital Partners, even though Shift4 seemed to suggest that this was a new phenomenon, or at least one not worth fighting for a full five years), to the mere fact that "they know us well" ("they attend our holiday parties," said its CSO at an investor conference). To us, none of these reasons seem compelling or convincing, and the Company's mixed messaging makes them seem even less so.

We see little credible rationale for in-sourcing this hodgepodge of independent resellers and customer relationship managers besides capitalizing a large quantity of future COGS, for which Shift4 was willing to shell out $80 million for six "restaurant technology partners" and $256 million for residual commission buyouts all at once, in Q3 2022. In our opinion, we see this as a naked attempt to game Shift4's financials and flatter earnings without improving Company fundamentals in any way.

And we again note that it was executed just as FOUR was hitting its 2022 lows, when the margin loan would have been in its most precarious state, and just in time for the financial flattery to be fully integrated into Q4 earnings, the announcement of which was due to coincide with the planned insider sale of up to 2 million shares.

While Shift4 claims that it will be more selective in buying out distributors going forward, we note that it continues to allocate capital towards reseller acquisitions, spending $7 million on residual commission buyouts in Q4. Considering the relative size of residual commissions as a component of COGS through Shift4's history, Shift4 could continue to pull levers through distributor M&A to a point at which, at the extreme, it could inflate gross profit by as much as 45%, and Adj. EBITDA by as much as 69%.

Pro-Forma Full-Year Impact of Third-Party Distributor In-Sourcing: 100% In-Sourced

$, m	Actual Results			Pro-Forma, 100% of Residual Commissions Removed from COGS		
	2019	2020	2021	2019	2020	2021
Gross Profit	173.4	177.8	278.4	173.4	177.8	278.4
Less: Depreciation of Leased Equipment	(0.2)	(9.8)	(21.8)	(0.2)	(9.8)	(21.8)
Gross Profit (New Methodology)	173.2	168.0	256.6	173.2	168.0	256.6
Plus: Residual Commissions	-	-	-	*55.0*	*60.0*	*115.0*
Pro-Forma Gross Profit	173.2	168.0	256.6	228.2	228.0	371.6
Less: Operating Expenses[3]	(177.6)	(225.6)	(305.8)	(177.6)	(225.6)	(305.8)
Depreciation & Amortization[3]	62.6	84.2	104.4	62.6	84.2	104.4
Other Items	1.0	(16.0)	0.1	1.0	(16.0)	0.1
Pro-Forma EBITDA	59.2	10.6	55.3	114.2	70.6	170.3
Total Adjustments	30.6	77.1	111.9	30.6	77.1	111.9
Pro-Forma Adj. EBITDA	89.8	87.7	167.2	144.8	147.7	282.2
Gross Profit Inflation %	-	-	-	***31.8%***	***35.7%***	***44.8%***
Adj. EBITDA Inflation %	-	-	-	***61.2%***	***68.4%***	***68.8%***

Source: Company Filings, Blue Orca estimates

Between the dramatic financial consequences of its distributor M&A, the lack of an otherwise coherent rationale around the deals, and their convenient timing, we view these acquisitions with heavy suspicion. In our view, buying out resellers who for years had been part of an almost exclusively independent sales force is likely an instance of financial engineering that inflates gross profit and EBITDA by capitalizing COGS, which the Company kick-started at a moment when its stock dangled precariously near all-time lows, and when the risk of a margin call on the CEO's loan would have been near its highest.

[3] "Depreciation & Amortization" includes depreciation and amortization from both COGS and SG&A. "Depreciation & Amortization" and "Operating Expenses" are unadjusted for incremental amortization from residual commission buyouts, which would simultaneously increase operating expenses and decrease D&A, and have no net impact on EBITDA.

3. Cash Flow Manipulation Massively Inflates Operating Cash Flow

Shift4 reported surprisingly high operating cash flows of $139.5 million in Q4, blowing its previous quarterly high of $65.1 million in Q3 2022 out of the water. On paper, this lent credence to Shift4's narrative that the Company is becoming stronger and more cash-generative. It also came at the perfect time for the CEO, who quietly began his month-long divestment of up to 2 million shares tied to his first VPF contract immediately after Q4 earnings.

Yet dig deeper and this supposedly impressive result on cash flows appears entirely manufactured, in our opinion, using gimmicky cash movements around quarter-end.

Because Shift4 does not qualify as a member bank among major credit card issuers, it must use a sponsor bank to access these payment networks. But, as it bills some of its customers on a monthly rather than daily basis, it must maintain a deposit at its sponsor bank to cover potential overdrafts. This deposit stood at $76.5 million towards the end of Q4.

Sometime before the end of Q4 2022, Shift4 withdrew its entire deposit, claiming to be in negotiations for lower collateral requirements with its sponsor bank. Slipped into its Q4 shareholder letter was an ambiguous note to its cash flow statement stating that "In December 2022, the Company received all funds held in its sponsor bank merchant settlement account that were previously deposited to cover the overdraft at the sponsor bank," and that it "expects to finalize an agreement…to not be required to deposit funds in the future…."

Q4 2022 Shareholder Letter

(A) This adjustment reflects changes in our accounts receivable balances which are typically relieved shortly after quarter-end. Balances are expected to fluctuate based on volume and calendar timing. In December 2022, the Company received all funds held in its sponsor bank merchant settlement account that were previously deposited to cover the overdraft at the sponsor bank. Although the Company expects to finalize an agreement with the sponsor bank in the near term to not be required to deposit funds in the future, the Company has not yet reached an agreement.

Source: *Q4 2022 Shareholder Letter*

In short, Shift4, under the guise of lobbying its sponsor bank for a new deal that excuses it from maintaining deposits, **pocketed its old deposit of $76.5 million and reported it as an addition to operating cash flow.**

Yet this maneuver appears, in our opinion, to be pure financial gimmickry. The very next month after recalling its deposit (and recognizing it as an addition to its now-juiced operating cash flow), **Shift4 appears to have returned a substantial chunk of the deposit just after the end of the fiscal year.**

In Shift4's 10-K, issued the morning *after* earnings (on which shares of FOUR rose more than 10% with the seemingly positive results), the Company admitted that, subsequent to the quarter's December 31 closing date, it re-deposited a substantial portion of the withdrawn cash (this time $33 million) into its sponsor bank to cover potential overdrafts.

2022 10-K

Because the Company is not a "member bank" as defined in certain of the payment networks' rules, the Company is not eligible for primary membership in certain payment networks and are therefore unable to directly access them. Instead, those payment networks require the Company to be sponsored by a member bank as a service provider, which the Company has accomplished through a sponsorship agreement with its sponsor bank. In order to cover overdraft obligations at the sponsor bank, prior to December 2022, the Company had funds deposited in a sponsor bank merchant settlement account to facilitate gross card transaction deposits for those customers the Company bills on a monthly, versus a daily basis. This amount fluctuated based upon end-to-end payment volumes and timing of billing cycles. As of December 31, 2021, the Company had $53.3 million in funds deposited at the sponsor bank included within "Accounts Receivable" on its Consolidated Balance Sheets. In December 2022, the Company received all funds held in this account that were previously deposited to cover the overdraft at the sponsor bank. Although the Company expects to finalize an agreement with the sponsor bank in the near term to not be required to deposit funds in the future, the Company has not yet reached an agreement. As such, in January 2023, the Company deposited $33 million to its sponsor bank merchant settlement account to cover the overdraft as of December 31, 2022. The Company will continue to maintain a deposit with the sponsor bank to cover overdrafts until an amendment is finalized.

Source: *2022 10-K*

Simply by delaying the return of its deposit until January 2023, after the books for Q4 2022 were closed, Shift4 was able to report the full December withdrawal of $76.5 million as a windfall to operating cash flow. Had it simply *reduced* the value of its deposit before quarter-close, the windfall would have been far smaller. But by withdrawing the full deposit, then placing a new, smaller deposit at its sponsor bank, it was able to post a massive $76.5 million gain to operating cash flow.

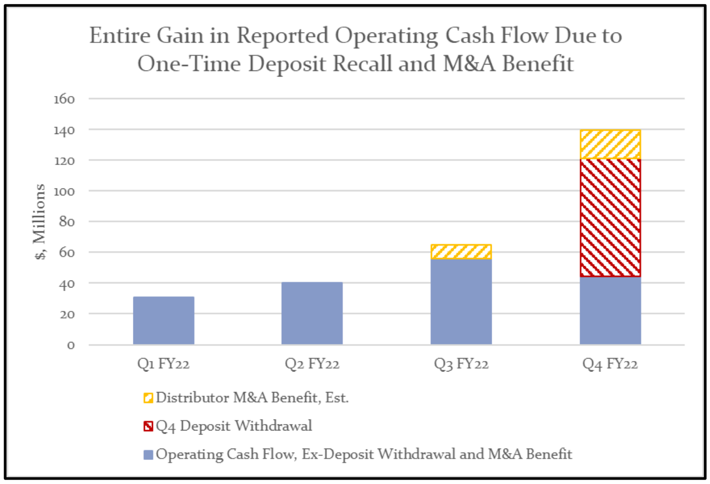
This gimmickry has an outsized impact on reported cash flow. **By shifting around money across its various bank accounts, we calculate that Shift4 was able to turn what would have been an operating cash flow *contraction* into a Q-o-Q *doubling* of operating cash flow, and to post its highest quarterly operating cash flow figure to date.**

In our view, the brazenness of these maneuvers simply cannot be overstated: Shift4 was able to more than double its quarterly operating cash flow simply by shifting cash from one bank to another and maximized the impact of its cash account movements on operating cash flow by delaying its subsequent deposit back into the initial bank until after quarter-end.

We find it suspicious that the Company chose to undertake this maneuver in Q4 in particular. In so doing, it appears to have been willing to sacrifice operating cash flow in Q1 2023, during which part of the withdrawal will be reversed, in favor of juicing Q4 2022 operating cash flow. It troubles us that this coincided with the CEO's planned liquidation of up to 2 million shares in March 2023 with the unwinding of his first VPF contract.

We think that Shift4's particular level of aggressiveness this quarter is yet another instance of its now-consistent behavior of going out of its way to make Company financials look particularly good precisely when insiders need it most. It happened in Q3 2022, when Shift4 found a way to inflate EBITDA by as much as 34% (based on prior years' residual commissions) with the acquisition of 50% of Shift4's third-party distributors. Shift4 appears to be doing so again in Q4, more than doubling its reported operating cash flow simply by pocketing its deposit from its sponsor bank just prior to massive insider share sales. And this on top of the financial engineering enabled by distributor acquisitions, now fully integrated into earnings, that allowed the Company to report a $12.5 million Q4 Adj. EBITDA beat rather than a $5.8 million miss.

All told, excluding both the Q4 2022 withdrawal and the benefit of capitalizing residual commissions through distributor M&A starting in Q3 2022, we believe that Q3 and Q4 operating cash flow would have been 14% and 68% lower, respectively, than was reported by the Company. By these estimates, operating cash flow for the full year would have been $104.0 million (38%) lower than reported.



Source: Q4 2022 Shareholder Letter, Blue Orca estimates

Ultimately, such cash flows do not represent a material improvement in Shift4's business. Drawing down a deposit and recognizing the inflows as operating cash flows, only to refund the deposit after quarter-end (indeed, the very next month) appears, in our opinion, to be highly aggressive financial gimmickry which had the impact of supporting the Company's stock through a period of heavy insider selling.

4. Aggressive Accounting Maneuvers Inflate Earnings Significantly

Beyond the financial maneuvers facilitated by Shift4's distributor M&A, the Company employs a number of aggressive accounting tactics – some of which it has maintained for years, and on which it has already faced SEC scrutiny, but some of which are new as of last quarter. **We estimate that, all told, these moves – together with the distributor acquisitions – inflated 2022 gross profit by 13%, Adj. EBITDA by 34%, and operating income by close to 3x, and gave the appearance of a much more palatable (though still high) 4.0x Net Debt / Adj. EBITDA against what we believe to be a more realistic 5.3x.**

Depreciation and Amortization Schedule Management Inflates EBIT Significantly

We observe in Shift4's most recent 10-K that, in the immediate wake of its large round of distributor acquisitions, Shift4 extended the depreciation and amortization periods of many of the intangible assets tied to these deals, among other assets:

- Residual commission buyouts from 3 years to 4-8 years (33-167%)
- Merchant relationships from 8 to 12 years (50%)
- Acquired technology from 9 to 10 years (11%)
- Capitalized customer acquisition costs from 3 to 4 years (33%)
- Equipment for lease from 3 to 4 years (33%)

Residual Commission Buyouts, Net

Residual commission buyouts, net consisted of the following:

	Weighted Average Amortization Period (in years)	December 31, 2022 Carrying Value	Accumulated Amortization	Net Carrying Value
Residual commission buyouts from asset acquisitions	4	$ 334.5	$ (42.6)	$ 291.9
Residual commission buyouts from business combinations	8	12.6	(0.6)	12.0
Total residual commission buyouts		$ 347.1	$ (43.2)	$ 303.9

	Weighted Average Amortization Period (in years)	December 31, 2021 Carrying Value	Accumulated Amortization	Net Carrying Value
Residual commission buyouts from asset acquisitions	3	$ 20.3	$ (6.5)	$ 13.8
Total residual commission buyouts		$ 20.3	$ (6.5)	$ 13.8

Other Intangible Assets, Net

Other intangible assets, net consisted of the following:

	Weighted Average Amortization Period (in years)	December 31, 2022 Carrying Value	Accumulated Amortization	Net Carrying Value
Merchant relationships	12	$ 196.3	$ (36.4)	$ 159.9
Acquired technology	10	123.1	(64.1)	59.0
Trademarks and trade names	13	27.2	(3.8)	23.4
Capitalized software development costs	3	80.3	(15.8)	64.5
Total other intangible assets, net		$ 426.9	$ (120.1)	$ 306.8

	Weighted Average Amortization Period (in years)	December 31, 2021 Carrying Value	Accumulated Amortization	Net Carrying Value
Merchant relationships	8	$ 200.1	$ (133.7)	$ 66.4
Acquired technology	9	113.2	(54.9)	58.3
Trademarks and trade names	18	20.3	(3.8)	16.5
Capitalized software development costs	4	42.6	(9.1)	33.5
Total other intangible assets, net		$ 376.2	$ (201.5)	$ 174.7

Capitalized Customer Acquisition Costs, Net

Capitalized customer acquisition costs, net were $36.1 million and $35.1 million at December 31, 2022 and 2021, respectively. These amounts consist of upfront processing bonuses with a gross carrying value of $72.3 million and $69.1 million less accumulated amortization of $36.2 million and $34.0 million at December 31, 2022 and 2021, respectively.

Capitalized customer acquisition costs had a weighted average amortization period of four and three years at December 31, 2022 and 2021, respectively.

Equipment for Lease, Net

Equipment for lease, net consisted of the following:

	Weighted Average Depreciation Period (in years)	December 31, 2022		
		Carrying Value	Accumulated Depreciation	Net Carrying Value
Equipment under lease	4	$ 107.7	$ (40.3)	$ 67.4
Equipment held for lease (a)	N/A	13.3	—	13.3
Total equipment for lease, net		$ 121.0	$ (40.3)	$ 80.7

	Weighted Average Depreciation Period (in years)	December 31, 2021		
		Carrying Value	Accumulated Depreciation	Net Carrying Value
Equipment under lease	3	$ 72.9	$ (24.2)	$ 48.7
Equipment held for lease (a)	N/A	9.7	—	9.7
Total equipment for lease, net		$ 82.6	$ (24.2)	$ 58.4

(a) Represents equipment that was not yet initially deployed to a merchant and, accordingly, is not being depreciated.

Source: [2022 10-K]

With the vast majority (over 90%) of Shift4's amortizable or depreciable assets attributable to these accounts, we estimate that extending these amortization periods will slash Shift4's depreciation and amortization by nearly a third going forward.

Deflating D&A Expense by Extending Amortization Schedules

$, m	Net Carrying Value	% of Total	Depreciation / Amortization Period, 2021	Depreciation / Amortization Period, 2022	% Change	Weighted % Impact on D&A
Residual Commission Buyouts	291.9	39.6%	3 years	4 years	33.3%	13.2%
Residual Commission Buyouts from Business Combinations	12.0	1.6%	3 years	8 years	166.7%	2.7%
Merchant Relationships	159.9	21.7%	8 years	12 years	50.0%	10.8%
Acquired Technology	59.0	8.0%	9 years	10 years	11.1%	0.9%
Trademarks and Trade Names	23.4	3.2%	18 years	13 years	-27.8%	-0.9%
Capitalized Software Development Costs	64.5	8.8%	3 years	4 years	-25.0%	-2.2%
Capitalized Customer Acquisition Costs	36.1	4.9%	3 years	4 years	33.3%	1.6%
Equipment Under Lease	67.4	9.2%	3 years	4 years	33.3%	3.1%
PP&E	22.3	3.0%	[Varies]	[No Change]	-	-
TOTAL	***736.5***	***100.0%***	-	-	-	**29.3%**

Source: [2022 10-K]

Shift4's recent tinkering with its depreciation and amortization periods will have a massive impact on earnings in future years. With the sell-side projecting Company EBIT and D&A to be $166.8 million and $113.5 million, respectively, **we estimate that Shift4's extensions of its D&A periods by 29.3% will decrease its D&A expense by an expected $47.0 million, inflating EBIT versus current consensus by 39% in 2023.**

Amortization Schedule Extension Will Massively Inflate Operating Income

$, m	Value / Inflation %
D&A, 2023 Consensus Estimate (CapIQ)	113.5
Deflation %	29.3%
D&A Adjusted for Deflation	160.5
Deflation of D&A	***47.0***
EBIT, 2023 Consensus Estimate (CapIQ)	166.8
EBIT Adjusted for D&A Deflation	119.8
Inflation of EBIT, %	***39.3%***

Source: Capital IQ, Blue Orca estimates

The impact of Shift4's toying with its amortization periods is jaw-dropping. While Shift4's 2022 10-K disclosed the full-year impact of the altered amortization periods on D&A costs associated with residual commission buyouts, equipment under lease, and capitalized customer acquisition costs, it must be emphasized that, since the changes took effect on October 1, the *entirety* of these impacts can be attributed to Q4. The annualized impact of these items going forward will be far more substantial, and will materially inflate Shift4's EBITDA.

Residual Commission Buyouts, Net

Residual commission buyouts primarily represent amounts paid to a software partner to buy out their future residual commission streams. The typical payment to the partner is comprised of a lump sum payment due immediately and a contingent payment following the buyout agreement dependent on attrition rates and/or other financial metrics within the respective merchant portfolios. Amortization is computed using the straight-line method. Prior to October 1, 2022, residual commission buyouts associated with asset acquisitions, which represent the majority of the Company's residual commission buyouts, were amortized over an estimated useful life of three years. Effective October 1, 2022, residual commission buyouts associated with asset acquisitions are amortized over an estimated useful life of four years, which decreased amortization expense by $6.9 million for the year ended December 31, 2022. This change in estimate increased basic and diluted net income per share by $0.08 for the year ended December 31, 2022.

Depreciation and amortization expense

Depreciation and amortization expense was $96.5 million for the year ended December 31, 2022, compared to $62.2 million for the year ended December 31, 2021, an increase of $34.3 million or 55.1%. The increase was primarily driven by higher residual commission buyout amortization of $36.9 million due to the significant amount of residual commission buyouts completed in 2022, net of the change in useful life from three years to four years of $6.9 million. In addition, equipment under lease increased $6.6 million in the year ended December 31, 2022, compared to the year ended December 31, 2021, net of the change in useful life from three years to four years of $3.5 million. This is offset by a decline in other intangible asset amortization of $9.7 million in the year ended December 31, 2022, compared to the year ended December 31, 2021, driven by intangibles that reached the end of their useful life, offset by new intangible assets as a result of the acquisitions in 2022.

Capitalized Customer Acquisition Costs

The Company incurs costs to obtain payment processing contracts with customers, primarily in the form of upfront processing bonuses provided to the Company's internal sales team and to the Company's software partners, which consist of independent software vendors and value-added resellers. The Company recognizes as an asset the incremental costs of obtaining a contract with a customer if it expects to recover the costs. Capitalized customer acquisition costs are amortized ratably over the estimated life of the customer, which was generally three to five years prior to October 1, 2022 and four years subsequent to October 1, 2022. This change in estimate decreased amortization expense by $1.6 million and increased basic and diluted net income per share by $0.02 for the year ended December 31, 2022.

Source: [2022 10-K]

Furthermore, we note that Shift4 did not disclose the impact of all amortization period changes on D&A. In particular, it did not disclose the impact of their extension of the amortization period for merchant relationships by 50%, which we estimate is alone responsible for a 10.8% change in Company-wide D&A.

$, m	Impact of Amortization Schedule Adjustment on Q4 2022 D&A
Residual Commission Buyouts (Disclosed)	(6.9)
Equipment Under Lease (Disclosed)	(3.5)
Capitalized Customer Acquisition Costs (Disclosed)	(1.6)
Merchant Relationships (Not Disclosed – Estimate)	(4.7)
All Others (Not Disclosed – Estimate)	1.0
TOTAL	***(15.7)***

Source: 2022 10-K, Blue Orca estimates

Taking into account the impacts of all changes in amortization and depreciation schedules – both those disclosed and omitted by the Company – we estimate that Shift4 inflated Q4 2022 EBIT by a massive $15.7 million, which accounts for more than half of its reported Q4 EBIT of $30 million. When we also adjust for the aforementioned $18.3 million Q4 COGS tailwind achieved through Shift4's aggressive distributor acquisitions, we estimate that, without Shift4's aggressive accounting maneuvers during the quarter, Q4 EBIT would have come in at just $12.0 million.

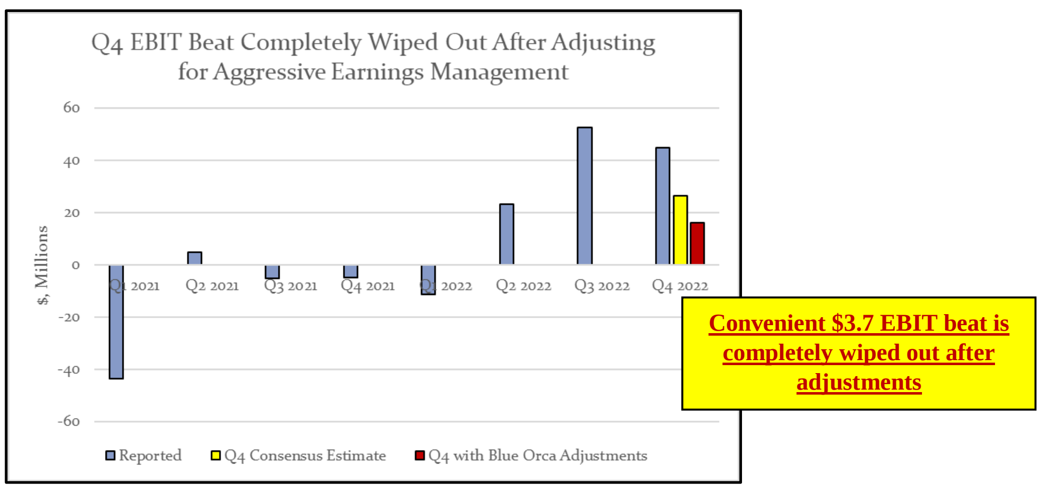
We estimate that, by extending its depreciation and amortization periods and acquiring third-party distributors, Shift4 was able to inflate Q4 EBIT by a massive $18.0 million. In doing so, it was able to post its second highest quarterly operating profit ever, and conveniently just enough to beat expectations by $3.7 million.

Q4 2022 EBIT Beat Manufactured via Distributor Acquisitions and D&A Management

$, m	Consensus Estimate (CapIQ)	Reported	Adjustment for Extended D&A Schedules	Residual Commission Adjustment	Plus: Amortization of Q3 Residual Commission Buyouts, Est.	Adjusted for Resid. Commissions, D&A
EBIT	26.3	30.0	(15.7)	(18.3)	16.0	12.0
Beat/Miss	-	3.7	-	-		(14.3)
Beat/Miss, %	-	14.1%	-	-		-54.5%

Source: Q4 2022 Shareholder Letter, Capital IQ, Blue Orca estimates

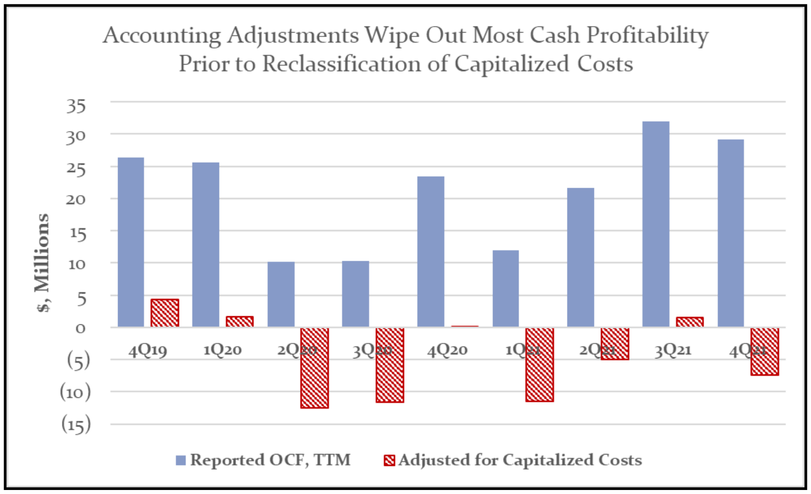
Note: Small differences due to rounding



Source: Company Filings, Capital IQ, Blue Orca estimates

Inappropriately Capitalized Expenses Flatter Earnings

Through Q2 FY22, Shift4 took the aggressive step of capitalizing customer acquisition costs and residual commission buyouts, running them through the investing activities section of the cash flow section rather than expensing them through the income statement, as we believe would be appropriate. In so doing, Shift4 has been able to print a consistently positive operating cash flow figure. However, when we fully load both customer acquisition costs and residual commission buyouts, we observe that nearly all cash profitability is effectively wiped out in the years during which they capitalized both items in the investing section.



Source: Company Filings, Blue Orca estimates
Note: Before restatement of customer acquisition costs as an operating cash item (see below)

This reporting tactic changed only recently, after repeated questioning by the SEC. In May 2022, the SEC asked management to explain its decision to capitalize these costs. This kicked off a months-long back-and-forth between management and the SEC over Shift4's treatment of its customer acquisition costs and residual commission buyouts, through which the SEC appeared to express dissatisfaction with Shift4's responses – at one point asking management in a follow-up letter to "explain in greater detail why you consider capitalized acquisition costs and residual commission buyouts to represent productive assets," suggesting, in our view, that Shift4's first shot at providing a defensible rationale was flatly inadequate.

Only after receiving such not-so-subtle pushback by the SEC did Shift4 acquiesce, but even then it did so only partially: starting in Q3, it classified customer acquisition costs, and only customer acquisition costs, as an operating cash item.

We find this decision strikingly odd: if customer acquisition can be considered a productive asset, it should be capitalized under investing activities. If not, it should be expensed in the income statement. Capitalizing this item under operating activities appears to us an aggressive half-measure with little logical rationale, except that Shift4 wants to have its cake and eat it too: customer acquisition costs will remain excluded from EBITDA.

Importantly, we note that this coincided with the departure of Shift4's former CFO. **After receiving follow-up questions from the SEC regarding Shift4's capitalization of customer acquisition costs and residual commission buyouts, the Company went over a month without responding – but it responded just several days after the departure of its CFO.** We question whether there was internal conflict regarding the Company's capitalized costs prior to his departure, especially in light of the SEC's objections to this aggressive accounting treatment.

We also note that Shift4 did not change its approach to capitalizing residual commission buyouts, arguing that these are lump-sum payments made to third-party distributors to acquire their merchant relationships. This line item was particularly large in Q3 2022, when Shift4 bought out 50% of its independent distributors. Until that point, however, this was a steady stream of spending allocated towards "acquir[ing] all rights to remaining commissions" of distributors' "ongoing merchant relationships." We think it is nonsensical that Shift4 capitalizes this as though it were a "productive asset"; rather, we view it as a bald-faced maneuver to justify reducing COGS by paying off a future stream of expenses up-front and christening it an "acquisition."

Adding this expense back to Shift4's Q3 2022 income statement might not make sense, as the massive $256.4 million outlay would render the income statement meaningless. But we don't think that Shift4 should get credit for more subtly shifting COGS out of the income statement through its more gradual residual buyouts up until that point. We therefore treat these buyouts as just another component of COGS associated with normal distributor reimbursement, which it is.

The SEC also took issue with Shift4's tactic of not including depreciation for equipment under lease in COGS. Rather than make the suggested change, Shift4 instead opted to reclassify COGS as COGS "excluding depreciation of equipment under lease," and ceased reporting a "gross profit" figure in its GAAP filings – a more lenient option permitted under SAB Topic 11.B.

Our read of the correspondence suggests that Shift4 tried desperately to maintain the most favorable reporting practices possible, resisting SEC pushback for months and, even then, electing only the least onerous of remedies available to it. This should come as no surprise, as we estimate that **Shift4's aggressive accounting allowed it to inflate reported gross profit and Adj. EBITDA over recent years by as much as 13% and 36%, respectively.**

Aggressive Accounting Practices Massively Inflate Earnings Before SEC Pushback

$, m	Reported Results			Adjusted for Aggressive Accounting Maneuvers		
	2019	2020	2021	2019	2020	2021
Gross Profit	173.4	177.8	278.4	173.4	177.8	278.4
Less: Depreciation of Leased Equipment	-	-	-	(0.2)	(9.8)	(21.8)
Less: Residual Commission Buyouts	-	-	-	*(3.3)*	*(3.9)*	*(10.4)*
Pro-Forma Gross Profit	173.4	177.8	278.4	169.9	164.1	246.2
Less: Pro-Forma Operating Expenses	(177.8)	(235.4)	(327.6)	(177.6)	(225.6)	(305.8)
Less: Customer Acquisition Costs	-	-	-	*(18.7)*	*(19.4)*	*(26.2)*
Pro-Forma Operating Income	(4.4)	(57.6)	(49.2)	(26.4)	(80.9)	(85.8)
Pro-Forma EBITDA	59.2	10.6	55.3	37.2	(12.7)	18.7
Pro-Forma Adj. EBITDA	89.8	87.7	167.2	67.8	64.4	130.6
Gross Profit Inflation, %	***2.1%***	***8.3%***	***13.1%***	-	-	-
Adj. EBITDA Inflation, %	***32.4%***	***36.2%***	***28.0%***	-	-	-

Source: Company Filings, Blue Orca estimates

Some of Shift4's maneuvers were reined in after Shift4 received pushback from the SEC in 2022. However, as shown in the table below, we think Shift4 more than made up for this by finding new accounting levers to pull in its acquisitions of distributor M&A and D&A schedule management, leaving earnings even more inflated by Q4 2022 than they were in years prior.

Summary: Aggressive Earnings Management Inflates Earnings and Obscures Leverage

Even after Shift4 reined in a number of its aggressive accounting maneuvers at the behest of the SEC, we believe it more than made up for these adjustments by taking advantage of its distributor M&A and amended amortization schedules to report massively inflated earnings for the year. **We estimate that, between its inappropriately capitalized costs (even excluding the one-off $256.4 million of residual commission buyouts associated with the Q3 reseller acquisitions), amended amortization schedules, and removal of residual commissions through its distributor M&A, Shift4 inflated gross profit by 13%, operating income by close to 200%, and Adj. EBITDA by 34%.**

This puts the Company's *actual* leverage at a far higher 5.3x Net Debt / Adj. EBITDA than the Street is currently led to believe (4.0x), leaving it in a far more precarious state and hindering its ability to execute on future M&A – without which we think Shift4 will struggle to meet expected top-line growth.

Total Impact of Aggressive Earnings Management in 2022

$, m	Actual	Adjusted for Earnings Management
Reported Gross Profit (Old Methodology)	470.2	470.2
Less: Depreciation of Equipment Under Lease	(28.4)	(28.4)
Less: Deflated Depreciation due to Dep. Schedule Change	-	*(3.5)*
Gross Profit (New Methodology)	441.8	438.3
Less: Residual Commission Buyouts (Ex-Q3)	-	*(19.1)*
Less: Residual Commissions Removed via M&A (Q3)	-	*(10.4)*
Less: Residual Commissions Removed via M&A (Q4)	-	*(18.3)*
Pro-Forma Gross Profit	441.8	390.5
Less: Pro-Forma Operating Expenses	(347.1)	(347.1)
Less: Capitalized Customer Acquisition Costs	-	*(25.2)*
Less: Deflated D&A due to D&A Schedule Changes	-	*(12.2)*
Plus: Incremental D&A from Reseller M&A	-	*26.7*
Pro-Forma Operating Income	94.7	32.7
Plus: D&A (Reported)	149.1	149.1
Plus: D&A Increase from Schedule Changes	-	*15.7*
Less: Incremental D&A from Reseller M&A	-	*(26.7)*
Plus: Other Items	13.9	13.9
Pro-Forma EBITDA	257.7	184.7
Plus: Adjustments	32.0	32.0
Pro-Forma Adj. EBITDA	289.7	216.7
Gross Profit Inflation, %	***13.1%***	-
Operating Income Inflation, %	***190.0%***	-
Adj. EBITDA Inflation, %	***33.7%***	-
Net Debt / Adj. EBITDA	***4.0x***	***5.3x***

Source: Company Filings, Blue Orca estimates

5. Aggressive and Misleading CEO Statements Prop Up the Stock

During the UBS TMT Conference on December 7, 2022, **Shift4's CEO brazenly announced that he's "incredibly frustrated" that the stock is "way too cheap," and that he would "absolutely" consider taking the Company private**, offering little rationale aside from his displeasure with FOUR's price level, and offering no obvious commitment to following through on his claim.

> For much of Shift4's history, you ran it as a private company. **Would you consider taking it private again? Particularly if you do not get the valuation you believe it to have from the public market** and despite your growth surpassing much of the competition.
>
> - Rayna Kumar – Analyst, UBS

> **Absolutely. It's like, are you kidding me?** I mean, **the company is way too cheap right now.** Um, and, you know, um…I mean, yeah, **I'm a buyer**. You know, if it makes it too easy, and I think, like, you know, it actually is becoming easier and easier….
>
> …I think, like, we're incredibly frustrated. I think the stock is very much underappreciated….
>
> …We'll look at the share price the same as anyone else, and **if it gets too low, then we'll see what we can do.**
>
> - Jared Isaacman – CEO, Shift4

This comes only two years after Shift4 first went public, and, to our knowledge, occurred absent any rumors or public conversation whatsoever around the possibility of Shift4 going private again. For the CEO to announce loudly that "if [FOUR] gets too low, then we'll see what we can do" – effectively issuing a public put on the stock – seems entirely inappropriate and, to us, an act of desperation to avoid experiencing further pressure on his pledged shares.

Critically, we also find it deeply troubling that the CEO claims to be "a buyer" when records show that he has, in fact, been a net seller. His last open-market purchase (of 27,728 shares) before this pronouncement came in June 2022, six months prior to his claim that he was "a buyer," and when FOUR was close to its all-time low in the low $30s.[4] Yet his net holdings *decreased* over the course of 2022 by 1.3 million shares, per his 2021 and 2022 Schedule 13Gs, and his claim that he was a buyer came *just days* before he disposed of another 21,221 (Class C) shares as a gift, per his annual Form 5. And he continues to divest of sizable portions of his holdings, as he disposed of up to 2 million shares throughout the month of March as his first VPF contract wound down.

Again, he last purchased shares in June 2022, when FOUR was close to its all-time low. We take issue with his claim that he was a buyer in December 2022 when he hadn't made any open market purchases for six months, just days before disposing of even more shares (immediately after his "too cheap" pronouncement added $10 to Shift4's share price), and just a couple of months ahead of his pre-planned disposal of up to 2 million shares tied to his VPF contract. For emphasis: he has made zero open market purchases of FOUR shares since claiming to be a buyer.

Why is the CEO telling investors that the Shift4's stock is a screaming buy when he himself is selling?

[4] The CEO's March 2 acquisition of 121,705 shares represents an award of vesting RSUs, not an open market purchase.

Stock Promotion Even as CEO Sells

Absolutely. It's like, are you kidding me? I mean, **the company is way too cheap right now.** Um, and, you know, um…I mean, yeah, **I'm a buyer.**

- Jared Isaacman – CEO, Shift4 (Dec 7, 2022)

NO YOU'RE NOT!

n-Derivative Securities Acquired, Disposed of, or Beneficially Owned

1. Title of Security (Instr. 3)	2. Transaction Date (Month/Day/Year)	2A. Deemed Execution Date, if any (Month/Day/Year)	3. Transaction Code (Instr. 8)		4. Securities Acquired (A) or Disposed Of (D) (Instr. 3, 4 and 5)			5. Amount of Securities Beneficially Owned Following Reported Transaction(s) (Instr. 3 and 4)	6. Ownership Form: Direct (D) or Indirect (I) (Instr. 4)	7. Nature of Indirect Beneficial Ownership (Instr. 4)
			Code	V	Amount	(A) or (D)	Price			
Class A Common Stock	02/27/2023		C(1)		2,000,000	A	$0.00	2,000,000	I	See footnotes(2)(3)
Class B Common Stock	02/27/2023		J(4)		2,000,000	D	$0.00	23,829,016	I	See footnotes(2)(3)
Class A Common Stock	02/27/2023		J(5)		2,000,000	D	(5)(6)	0	I	See footnotes(2)(3)

Source: Feb 27 Form 4

It is particularly concerning to us that Shift4's CEO so explicitly hyped the stock just ahead of his planned VPF unwinding. We see it as no coincidence that the CEO's musings of potentially taking Shift4 private preceded a ~25% run in the Company's stock price over the next several days.

We think that investors must consider Shift4's increasingly aggressive accounting and the CEO's stock promotion through the past several months against the backdrop of the CEO's heavy borrowing against FOUR shares. Shift4's strategically inexplicable acquisitions of third-party distributors, its stubborn refusal to amend its aggressive accounting methodology only until pressed repeatedly by the SEC, and its continued acquisitions of businesses lacking clear synergies with Shift4's core POS offering in an attempt to manufacture growth (including an ill-fated crypto venture), to us make sense only in light of the precarious state of the margin loans throughout 2022, which hung over Shift4's stock like a sword of Damocles.

6. Suspicious Timing Around CFO Departure Raises Major Red Flags

Just as Shift4 was executing its distributor acquisitions and receiving pushback from the SEC regarding its aggressive accounting maneuvers, Shift4 abruptly parted ways with CFO Bradley Herring, who had held the position since 2019. The timing and circumstances raise a host of red flags.

On August 3, 2022, the day before Shift4's Q2 earnings release and conference call, Shift4 issued a news release announcing Herring's departure, effective on August 5. The release was conspicuously silent as to any reason for the sudden and near immediate resignation of the CFO. Moreover, although he did sign and certify the Q2 SEC Form 10-Q, he curiously did not attend the August 4 earnings call despite the fact that his resignation was not effective until August 5. The Company did not explain why he did not attend the earnings call.

And, on the same 8-K announcing his departure, Shift4 announced that he would be replaced immediately by Nancy Disman, a former board member, without her serving in an interim role for any period of time. Notably, as part of Disman's compensation for taking on the CFO role, the Company promised her an extremely generous one-time cash signing bonus of **$3 million**. Disman's cash signing bonus alone is roughly 2x Herring's annual compensation.

8-K (August 3, 2022)

Item 5.02 - Departure of Directors or Certain Officers; Election of Directors; Appointment of Certain Officers; Compensatory Arrangements of Certain Officers.

Departure of Bradley Herring as Chief Financial Officer

On August 3, 2022, Bradley Herring and Shift4 Payments, Inc. (the "***Company***") agreed that Mr. Herring will no longer serve as the Company's Chief Financial Officer, effective August 5, 2022. In connection with Mr. Herring's resignation, the Company entered into a separation and release of claims agreement (the "***Separation Agreement***") with Mr. Herring on August 3, 2022.

Appointment of Nancy Disman as Chief Financial Officer

On August 3, 2022, Nancy Disman tendered her resignation as a Class II director of the board of directors of the Company (the "***Board***") and will step down from the Board and its Audit, Compensation and Nominating and Corporate Governance Committees, in each case effective August 5, 2022.

On August 3, 2022, the Board appointed Ms. Disman as the Company's Chief Financial Officer and principal financial officer, in each case effective August 5, 2022, (the "***Transition Date***").

In connection with the commencement of her employment, Ms. Disman will receive a one-time signing cash bonus of $3,000,000, $2,000,000 of which will be payable on the first payroll date following the Transition Date, $500,000 of which

Source: August 3, 2022 8-K

We also note that, after having received a follow-up letter from the SEC regarding its aggressive accounting on June 21, 2022, it took the Company over a month to respond with a defense of its decisions to capitalize customer acquisition costs and residual commission buyouts. **Not until August 8 – the very next business day after Herring's effective resignation date – did Shift4 finally issue a response to the SEC.**

A CFO resignation shortly after an IPO is often a red flag in itself, to say nothing of the suspicious timeline of events laid out above. We must question what role, if any, Shift4's aggressive financial maneuvers may have played in this series of events.

Material Weakness over Internal Controls a Major Outlier

It comes as no surprise to us Shift4 would inevitably report a material weakness in its internal controls over financial reporting, which it did in Q3 2022 when it restated capitalized customer acquisition costs as an operating cash item – doing so, of course, only after repeated prodding by the SEC.

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our principal executive officer and principal financial officer, evaluated, as of the end of the period covered by this Quarterly Report on Form 10-Q/A, the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act).

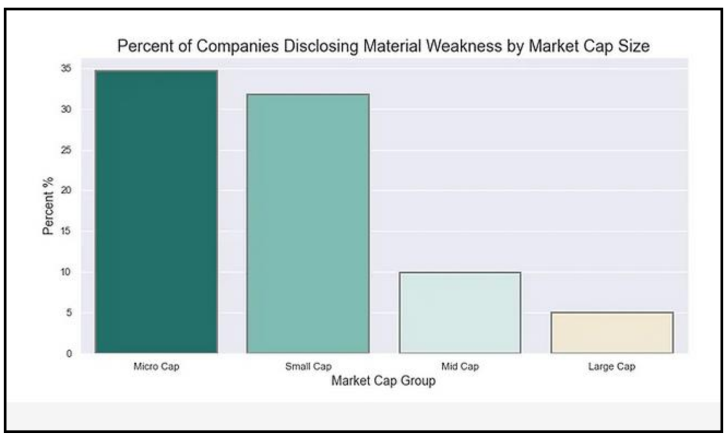
Based on that evaluation, our principal executive officer and principal financial officer concluded that, as of March 31, 2022, due to the material weakness in our internal control over financial reporting described below, our disclosure controls and procedures were not effective at the reasonable assurance level. In light of the material weakness, we performed additional analysis as deemed necessary to ensure that our financial statements were prepared in accordance with U.S. generally accepted principles. Accordingly, management concluded that the financial statements included in this Quarterly Report on Form 10-Q/A present fairly in all material respects our financial position, results of operations and cash flows for each of the periods presented.

A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of our annual or interim financial statements will not be prevented or detected on a timely basis.

Management identified a material weakness related to a lack of an effectively designed control activity over the classification of customer acquisition costs within our Consolidated Statements of Cash Flows. The associated error related to the historical classification of customer acquisition costs within our Consolidated Statements of Cash Flows resulted in the restatement of the Company's previously filed consolidated financial statements as of and for the years ended December 31, 2021, 2020 and 2019 and for each of the quarterly periods ended September 30, 2021, March 31, 2022 and June 30, 2022. Additionally, the material weakness could result in a material misstatement of the aforementioned account balances or disclosures that would result in a material misstatement to the annual or interim consolidated financial statements that would not be prevented or detected.

Source: Q1 2022 10-Q/A

It should be noted that, per Bedrock AI, less than 10% of mid-cap companies reported a material weakness over financial controls between April and October of 2022, and those that do so are 50% more likely to see an impairment to their stock price after reporting the weakness. This compares to 30% of all small-cap companies reporting a material weakness over controls during the same time period.



Source: Bedrock AI

We see Shift4's material weakness as just more evidence that, as discussed later, Shift4 is run much more like a smaller-cap company than a mature, well-run company deserving of its current 16.3x NTM Adj. EBITDA multiple.

That Shift4 would be forced to report a weakness over financial controls almost seems, to us, to be expected in light of the CFO departure and Shift4's aggressive accounting maneuvers and financial gimmicks.

7. <u>Dismal Corporate Governance</u>

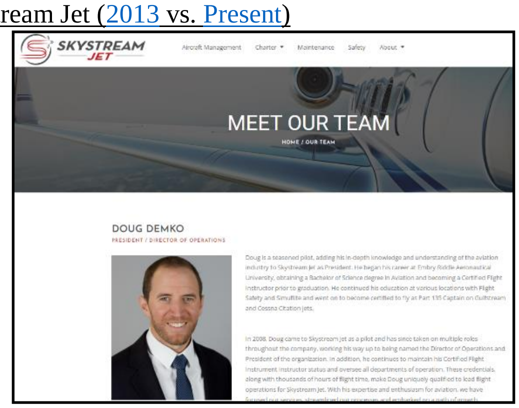
Shift4's board of directors and executive team is full of the CEO's immediate family members and close childhood friends. This includes his father on the board of directors, his brother as Chief Commercial Officer, childhood friends as both Chief Strategy Officer and EVP of Technology, and a flying buddy as COO. In our view, these individuals are far too close to the CEO to serve independently in the interests of shareholders.

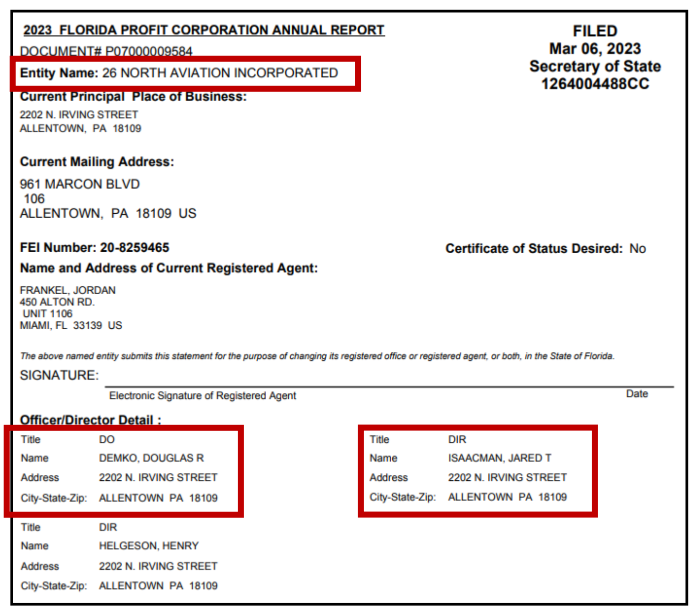
The absence of independent checks and oversight, in our opinion, is especially problematic in light of the CFO resignation, SEC comment letters, and what we believe to be aggressive accounting gimmicks.

We also think that this governance structure provides limited oversight over the CEO's use of Company funds to support his personal activities.

- **Private Jets:** Our research suggests that Shift4 pays the CEO's personally-owned charter jet service, 26 North Aviation (now doing business as Skystream Jet[5]), for private jet flights. COO Doug Demko's LinkedIn also shows that he has been Chairman, President, and Director of Operations of Skystream Jet since 2008.

26 North Aviation Becomes Skystream Jet (2013 vs. Present)





2023 FLORIDA PROFIT CORPORATION ANNUAL REPORT

DOCUMENT# P07000009584

Entity Name: 26 NORTH AVIATION INCORPORATED

FILED
Mar 06, 2023
Secretary of State
1264004488CC

Current Principal Place of Business:
2202 N. IRVING STREET
ALLENTOWN, PA 18109

Current Mailing Address:
961 MARCON BLVD
106
ALLENTOWN, PA 18109 US

FEI Number: 20-8259465

Certificate of Status Desired: No

Name and Address of Current Registered Agent:
FRANKEL, JORDAN
450 ALTON RD.
UNIT 1106
MIAMI, FL 33139 US

The above named entity submits this statement for the purpose of changing its registered office or registered agent, or both, in the State of Florida.

SIGNATURE:
Electronic Signature of Registered Agent Date

Officer/Director Detail :

Title	DO	Title	DIR
Name	DEMKO, DOUGLAS R	Name	ISAACMAN, JARED T
Address	2202 N. IRVING STREET	Address	2202 N. IRVING STREET
City-State-Zip:	ALLENTOWN PA 18109	City-State-Zip:	ALLENTOWN PA 18109
Title	DIR		
Name	HELGESON, HENRY		
Address	2202 N. IRVING STREET		
City-State-Zip:	ALLENTOWN PA 18109		

Source: Florida Business Registry

Furthermore, each of Skystream's aircraft (N82EM, N86MW, and N80EM) are registered with the FAA under either Isaacman's "JDI Holdings LLC" or "AIRDAX LLC," which shares a business address with JDI and Shift4.

[5] Note that http://www.26northaviation.com now redirects to https://skystreamjet.com/.

Shift4's disclosures on these payments have been inconsistent. It did not fully disclose the CEO as the supplier of Shift4's charter services until releasing its Q1 2021 10-Q, before which it described the supplier simply as "a shareholder" (as he is *still* described in the Company's most recent proxy statement).

2020 10-K

> **Related Party Transactions**
>
> The Company has a service agreement with a shareholder of the Company, including access to aircrafts and a property. Total expense for this service, which is included in "General and administrative expenses" in the Consolidated Statements of Operations, were $0.4 million for each of the years ended December 31, 2020, 2019 and 2018. There were no amounts outstanding at December 31, 2020 and 2019. On May 31, 2020, the Company amended the monthly fee and added services in this month-to-month service agreement with a shareholder of the Company.

Source: *2020 10-K*

2021 Proxy Statement (CURRENT)

> **Aircraft and Property Usage**
>
> We have a service agreement with a shareholder of the Company, including access to aircrafts and property. We incurred expenses for this service in the amount of $1.0 million for the year ended December 31, 2021. There were no amounts outstanding at December 31, 2021.

Source: *2021 Proxy Statement*

- **Nebulous "Consulting" Fees:** The 2020 proxy statement states that Rook Holdings, the vehicle through which the CEO maintains his margin loan, received fees for providing "consulting and managing services on an ongoing basis." We struggle to understand how the Company could justifiably pay consulting fees to the CEO's personal borrowing vehicle, and see this as yet another example of poor corporate governance and lack of independent oversight by the board of directors.

- **Amateur Spaceflight Ventures Promoted by Shift4:** Shift4's CEO participated in the Inspiration4 spaceflight, the first all-civilian mission to space, operated by SpaceX. While he purportedly purchased all four seats personally (for ~$50 million each, per *Time*), we note that Shift4 also made a $27.5 million investment in SpaceX in 2021. For a company which does not consistently produce much operating cash, we wonder why any cash would be diverted to non-core investments with such close proximity to the CEO's passion project.

  The CEO also transferred one of the seats on the space flight to Shift4, a non-cash contribution for which it incurred an expense of $2.1 million – seemingly far too low, given the price of the seat. Shift4 recognized another $1.6 million in expenses in relation to the seat's use in promoting and rebranding its 3dcart acquisition as Shift4Shop as part of a public raffle, $0.9 million of which was "reimbursable by the Founder." We worry that Shift4's spending on the CEO's personal spaceflight was even greater than this: the Company's 2021 10-K states that "Company incurred a significant amount of nonrecurring expenses to integrate, rebrand and promote 3dcart to Shift4Shop in conjunction with the Inspiration4 announcement." While Shift4 allocated only $1.6 million directly to the Inspiration4 seat, it recorded another $20.8 million expense for "the integration of 3dcart and its rebranding as Shift4Shop," some of which might have been tied to the raffle of the Inspiration4 seat. The lack of transparency around such expenses is a material red flag, especially given the CFO resignation and the Company's dismal corporate governance.

8. Incinerating Value with Foolish Crypto Investments

As the post-COVID rebound comes to a close for the hospitality sector, the driving force behind Shift4's recent growth has dried up: the Company posted decelerating year-over-year net revenue growth in each quarter between Q2 2021 through Q3 2022, and growth has been roughly flat since. Even during its growth run, Shift4 consistently struggled to post positive operating cash flow after adjusting for capitalized customer acquisition costs. Now that its growth has come back to Earth, we see the Company increasingly funneling what limited cash it does generate into M&A to make up for the top-line deceleration. But we see these efforts as an inevitably futile attempt to meet sell-side growth expectations: with Shift4 struggling to generate consistently positive cash and **already levered at 5.3x net debt / EBITDA (after our adjustments)**, we think it's only a matter of time before Shift4 is forced to turn to dilutive offerings to support M&A if it's to meet top-line expectations, or else allow growth to contract and disappoint.

These deals are so poor and inexplicable that, otherwise, they appear to us as nothing more than an incineration of cash.

Throwing Away Cash into the Crypto Craze

In February 2022, Shift4 acquired The Giving Block, a crypto donation processor for non-profits, for $12.6 million in net cash, $36.4 million in FOUR shares, and a contingent consideration worth up to $246 million. The "technology" provided by this service appears pedestrian and easily replicable: it is effectively a crypto payments widget similar to BitPay and other crypto payment processors oriented towards non-profits rather than for-profit merchants. Shift4 called this acquisition a "very small bet" in an investor conference shortly after the deal was done. But we don't think that excuses it from what appears now to be an ill-timed FOMO bet on crypto: **the ~$50 million up-front consideration paid by the Company for its crypto acquisition is more than it has generated in adjusted free cash flow in any single quarter, save for the latest.**

Shift4 acknowledges that it is "not terribly optimistic about the giving environment" around cryptocurrency, and that The Giving Block's contribution was "not particularly meaningful." But we think this understates the reality of The Giving Block's performance, which, we believe, should come as a surprise to no one given the state of cryptocurrency markets. The contingent consideration tied to the deal, worth up to $246 million, was initially assigned a fair value of $57.8 million. By Q3 2022, it had already been revalued to $20.6 million, and by Q4, it was down to just $10.7 million. The internal outlook for the performance of The Giving Block is clearly not promising. And it is already seeing significant layoffs.

Q1 2022 10-Q/A

(c) The Company agreed to an earnout due to the former shareholders of The Giving Block in April 2023, calculated as a multiple of revenue earned by The Giving Block from March 1, 2022 to February 28, 2023, not to exceed $246.0 million. The earnout will be paid 75% in a combination of RSUs and shares of the Company's Class A common stock and 25% in cash. The fair value of the earnout was included in the initial purchase consideration and will be revalued quarterly until the end of the earnout period as a fair value adjustment within "General and administrative expenses" in the Company's unaudited Condensed Consolidated Statements of Operations. As of March 31, 2022, the fair value of the earnout included in the purchase consideration was $57.8 million, which is recognized in "Accrued expenses and other current liabilities" on the Company's unaudited Condensed Consolidated Balance Sheets. In addition, a portion of the earnout due in April 2023 is considered post-acquisition

Source: Q1 2022 10-Q/A

Q3 2022 10-Q

(c) The Company agreed to an earnout due to the former shareholders of The Giving Block in April 2023, calculated as a multiple of revenue earned by The Giving Block from March 1, 2022 to February 28, 2023, not to exceed $246.0 million. The earnout is expected to be paid 75% in a combination of RSUs and shares of the Company's Class A common stock and 25% in cash. The fair value of the earnout was included in the initial purchase consideration and will be revalued quarterly until the end of the earnout period as a fair value adjustment within "Revaluation of contingent liabilities" in the Company's unaudited Condensed Consolidated Statements of Operations. As of September 30, 2022, the fair value of the earnout was $20.6 million, which is recognized in "Accrued expenses and other current liabilities" on the Company's unaudited Condensed Consolidated Balance Sheets. In addition, a portion of the earnout due in April 2023 is considered post-acquisition compensation

Source: Q3 2022 10-Q

Q4 2022 (2022 10-K)

(c) The Company agreed to an earnout due to the former shareholders of The Giving Block in April 2023, calculated as a multiple of revenue earned by The Giving Block from March 1, 2022 to February 28, 2023, not to exceed $246.0 million. The earnout is expected to be paid 75% in a combination of RSUs and shares of the Company's Class A common stock and 25% in cash. The fair value of the earnout was included in the initial purchase consideration and will be revalued quarterly until the end of the earnout period as a fair value adjustment within "Revaluation of contingent liabilities" in the Company's Consolidated Statements of Operations. As of December 31, 2022, the fair value of the earnout was $10.7 million, which is recognized in "Accrued expenses and other current liabilities" on the Company's Consolidated Balance Sheets.

Source: 2022 10-K

January 18, 2023

The Giving Block cuts about 12% of its workforce

by Yogita Khatri

COMPANIES • JANUARY 18, 2023, 11:30AM EST

Source: The Block

Yet even as the acquisition demonstrably flounders, we note that **Shift4 has not written down the investment whatsoever**: it was assigned a carrying value of $89.3 million of goodwill in Q1, and it continues to be assigned a value of $89.4 million today.

Q1 2022 10-Q/A

Goodwill

The changes in the carrying amount of goodwill were as follows:

Balance at December 31, 2021	$	537.7
The Giving Block Acquisition (Note 3)		89.3
Balance at March 31, 2022	$	627.0

Source: Q1 2022 10-Q/A

Q4 2022 (2022 10-K)

Goodwill

The changes in the carrying amount of goodwill were as follows:

Balance at December 31, 2021	$	537.7
The Giving Block Acquisition (Note 3)		89.4
Online Payments Group Acquisition (Note 3)		49.9
Restaurant Technology Partner Acquisitions (Note 3)		53.4
Effect of foreign currency translation		4.6
Balance at December 31, 2022	$	735.0

Source: 2022 10-K

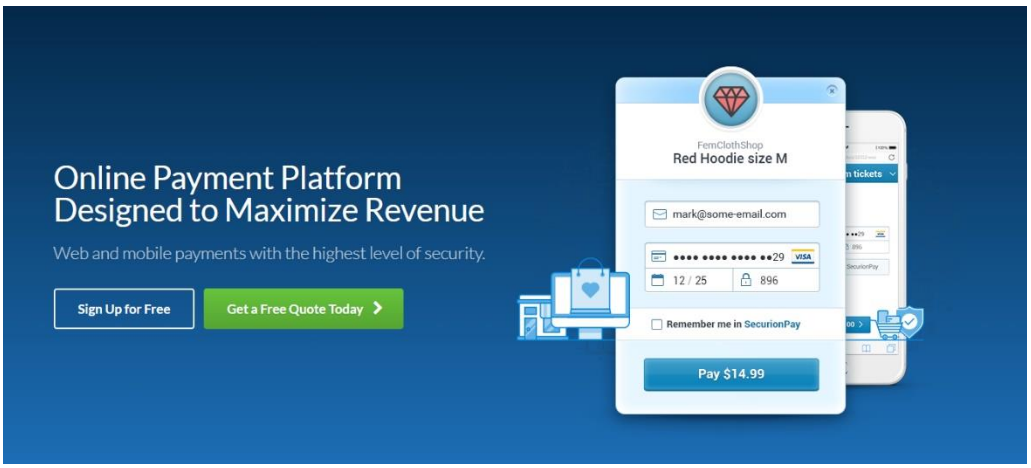
In an environment in which crypto companies are going bust and crypto venture funds blowing up, we find it curious that Shift4 has not taken a write-down on this disaster acquisition. If it's performing so poorly that the fair value of its contingent consideration had to be slashed by over 80%, we think it a goodwill write-down is more than called for.

Even then, we think the acquisition – a flushing-down-the-toilet of cash into a crypto venture – gives us little confidence in the Company going forward.

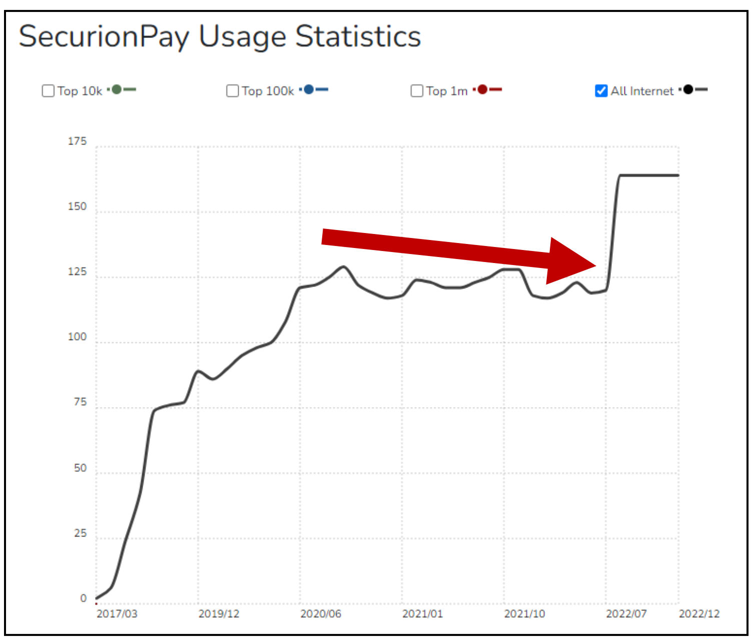
Shift4 Stretching to Keep Growth Alive via M&A

Among other deals made by Shift4 in 2022 was its $104 million acquisition (with a contingent consideration up worth up to $60 million) of a business to which the Company refers only as "a European PSP" (payment service provider) during meetings and calls. Its filings refer to this business as "Online Payments Group AG," a Swiss payment processor which does business under a different name, and has far too generic a formal name for most casual investors to find it with this information alone.

We have identified it as d/b/a SecurionPay. It is yet another mere online payments widget, as we observe from its former website via Wayback Machine. While perhaps giving Shift4 a presence in Europe, it appears to offer no clear advantage beyond this. And web tracking data reveals that it has been underperforming. Of sites tracked by website profiler BuiltWith, growth for SecurionPay topped out in mid-2020, after which it experienced a declining web presence until being purchased by Shift4 in Q3 2022. We assume the subsequent spike and flat-line are due to its being integrated into Shift4.



Source: SecurionPay via the Wayback Machine



Source: BuiltWith

We question why Shift4 refuses to refer to it publicly by its operating name. Is the brand and IP just that inconsequential? Is Shift4 trying to keep its recent performance under wraps? It doesn't give us much confidence either way.

More generally, Shift4 appears to be stretching for growth wherever it can as its core POS market becomes increasingly saturated with higher-tech options. The sell-side continues to forecast top-line growth of ~30% through the coming 2-3 years. However, with the "higher-tech" restaurant POS market increasingly crowded, and facing increasingly competitive peers like Toast, we believe that this number is unreasonably aggressive absent aggressive M&A into adjacent verticals.

Shift4 appears to be adopting just this strategy, as it has increased its push into new adjacent sectors like e-commerce and online payment processing via its acquisitions of 3dcart, Finaro (fka Credorax), and SecurionPay. But online payment processing is truly a new vertical, sharing few obvious synergies with Shift4's core POS offering. If this is to be the driving force behind Shift4's future growth, we question how much runway for continued growth it really has.

In our view, after taking inappropriately capitalized costs into consideration, Shift4 has failed to generate consistently positive cash flow, does not appear to be getting markedly more profitable on a cash basis after adjusting for its recent cash flow manipulation, and is already levered at 5.3x Net Debt / EBITDA (after our adjustments) after taking on over $1 billion in debt since Q3 FY20. With about $740 million worth of cash on its balance sheet, excluding the post-Q4 deposit, Shift4 would appear to have dry powder to work with for M&A. However, with a recent history of doing acquisitions (outside of distributors) at a ~2.5x sales multiple, and currently doing ~$725 million in annual net revenue, we think that Shift4 will be able to continue on its current ~30% annual growth trajectory for at best only a couple of years before it runs up against the limits of its balance sheet – and only then if it commits most or all of its cash to M&A.

We're doubly concerned by Shift4's apparent desire to be cagey about the contribution of acquisitions to Company revenue: on the Q3 2022 earnings call, CSO Taylor Lauber appeared to cut off new CFO Nancy Disman when she was about to disclose SecurionPay's projected Q4 revenue contribution. We suspect that Shift4 will continue to buy sales growth for as long as it can, and not be fully transparent about the contribution of new acquisitions to sales. But we think that it can do so for only so long.

We suspect that Shift4 will do what it takes to make the stock look attractive to investors, even if it means reaching for cheaper M&A targets to keep the growth story alive. In our view of the future, **with its balance sheet already steeply levered and organic growth opportunities limited, we think Shift4 will either have to sacrifice growth by reining in M&A, or issue more shares (or reach for increasingly cheap and unattractive M&A targets) to meet growth expectations. In neither outcome do we think investors should be interested in owning the stock.**

DISCLAIMER

We are short sellers. We are biased. So are long investors. So is Shift4. So are the banks that raised money for the Company. If you are invested (either long or short) in Shift4, so are you. Just because we are biased does not mean that we are wrong. We, like everyone else, are entitled to our opinions and to the right to express such opinions in a public forum. We believe that the publication of our opinions about the public companies we research is in the public interest.

You are reading a short-biased opinion piece. Obviously, we will make money if the price of Shift4 stock declines. This report and all statements contained herein are solely the opinion of BOC Texas, LLC, a Texas limited liability company, and are not statements of fact. Our opinions are held in good faith, and we have based them upon publicly available evidence, which we set out in our research report to support our opinions. We conducted research and analysis based on public information in a manner that any person could have done if they had been interested in doing so. You can publicly access any piece of evidence cited in this report or that we relied on to write this report. Think critically about our report and do your own homework before making any investment decisions. We are prepared to support everything we say, if necessary, in a court of law.

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