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Not such a lock

A wave of identity theft and computer-borne financial fraud has hoisted LifeLock—LOCK on the New York Stock Exchange—into the elite ranks of American growth stocks. "Elite" is no part of the LifeLock corporate story, *Grant's* is about to contend. On the company whose CEO famously paraded his own Social Security number in front of the TV cameras just to dare bad actors to steal it (which the taunted thieves actually proceeded to do), this publication is bearish.

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The argument appears to have carried the day with all but one of the nine analysts who follow the company. The shares are valued at 28.9 times trailing net income and 22.7 times the 2015 estimate. Cash per share works out to $2.55; the balance sheet is debt-free. Not since going public in October 2012 has management produced a disappointing quarter. Boldface names—Goldman Sachs, Bessemer Venture Partners, Kleiner Perkins Caufield & Byers—furnished venture capital. Tom Ridge, former head of the Department of Homeland Security, sits on the board of directors.

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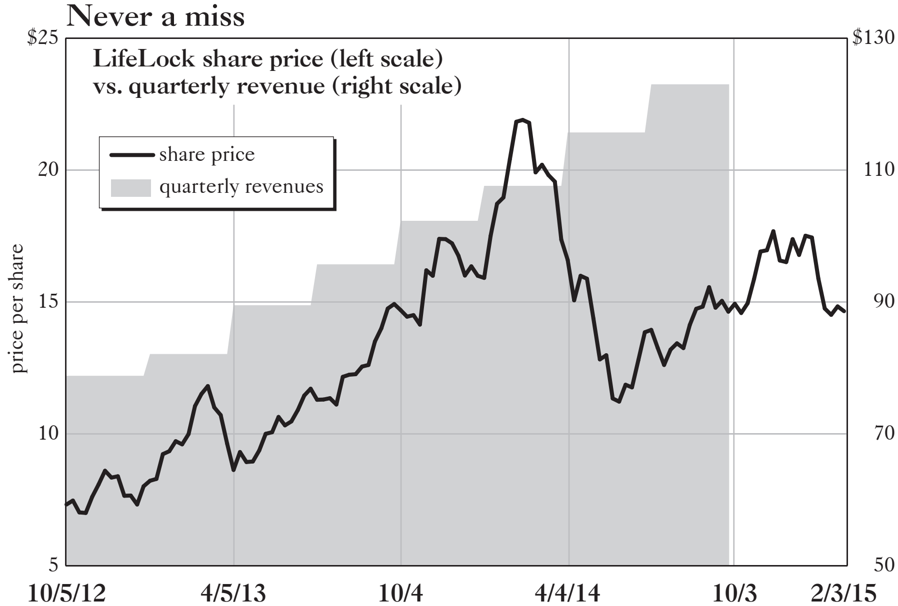
Never a miss



source: The Bloomberg

corporate clients, consumer protection is LifeLock's beating heart.

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Many a business in the Internet age has foundered in failing to compete with services that someone, somewhere can deliver for free. Perhaps such a fateful encounter awaits LifeLock. "Consumers can request their credit reports once a year from each of the three credit bureaus for free," as Lorenz points out. "Anyone can reduce the number of preapproved credit offers at the Consumer Credit Reporting Industry Web site at optoutprescreen.com. Many banks now offer fee alerts for transactions over a size specified by consumers. Anyone can check online registries to see if sex offenders live nearby, again at no cost. MasterCard now offers identity theft alerts, i.e., the core component of LifeLock's product, for free —just go to http://www.mastercard.us/idtheftalerts/ to enroll."

And as for "credit monitoring," said *Consumer Reports* last year in the wake of the Target data breach, it "is not much use for most of what is now called 'identity theft,' which involves old-fashioned credit card theft, because monitoring watches your credit report, not unauthorized charges to your existing accounts."

Did that $1 million LifeLock insurance policy catch your eye? After deducting lawyers' and investigators' fees, and the cost of other 'third-party' services that the company judges to be essential to clean up after the fraud, the hopeful insurance-policy holder is likely to realize not much more than $50,000. You can satisfy yourself on this point by consulting the fine print of the service agreement on the company's Web site.

One might suppose that management could find in its commodious third-party services' budget the funds

LifeLock
(in $ millions unless otherwise indicated)

	12 mo. thru Sept. 30, 2014	2013	2012	2011	2010	2009
Revenue	$448.6	$369.7	$276.4	$193.9	$162.3	$131.4
Cost of services	115.9	100.1	79.9	62.6	51.4	43.1
Gross profit	332.8	269.6	196.5	131.3	110.8	88.3
Operating expenses	317.7	252.4	183.4	126.5	123.5	143.6
Income from operations	15.1	17.2	13.1	4.8	(12.7)	(55.4)
Net interest expense	(0.2)	(0.2)	(3.6)	(0.2)	(1.3)	(1.3)
Other	(0.2)	(0.0)	0.3	(8.7)	(1.4)	(2.0)
Profit before tax	14.7	16.9	9.8	(4.0)	(15.4)	(58.6)
Taxes (benefit)	(37.9)	(37.5)	(13.7)	0.2	0.0	0.0
Income after tax	52.6	54.5	23.5	(4.3)	(15.4)	(58.6)
One time items	0.0	0.0	(17.3)	(18.9)	(16.1)	(10.3)
Net income	52.6	54.5	6.2	(23.2)	(31.5)	(68.9)
Shares in millions	92.4	96.0	62.2	18.7	18.1	17.8
EPS	$0.55	$0.57	$0.09	($1.24)	($1.74)	($3.86)
Cash	238.3	172.6	134.2	28.9	17.6	
Pref. equity	0.0	0.0	0.0	145.2	126.3	
Debt	0.0	0.0	0.0		13.2	
Net debt (cash)	(238.3)	(172.6)	(134.2)	116.3	121.9	

sources: company filings, the Bloomberg

with which to hire a fact checker. Apparently not, as more than a few corporate representations, starting with the tale of how LifeLock came into being (ostensibly as a result of an identity theft perpetrated against co-founder Robert J. Maynard Jr.) don't stand up to scrutiny. For chapter and verse on the checkered LifeLock back story, see the lengthy and thoroughly reported article by Ray Stern in the *Phoenix New Times* almost eight years ago. Accuracy in corporate reporting is still an elusive ideal at LifeLock to judge by the 2014 proxy, which flatters the resumé of CEO Todd Davis by identifying him as a "Certified Identity Theft Risk Management Specialist" (no such record exists), a member of the Crime Prevention Coalition of America (not according to our check), and a "contributing member of the Identity Theft Prevention and Identity Management Standards Panel that worked with the Identity Theft Task Force established by former President Bush" (again, evidence is wanting). Asked for comment, the company declined.

Anomalously for a business with a Goldman Sachs-Bessemer-Kleiner Perkins-Tom Ridge pedigree, LifeLock has had a recurrent series of scrapes with lawyers and regulators. The evident gap between performance and promise is the usual source of conflict. Thus, in a March 2010 settlement with the Federal Trade Commission and 35 state attorneys general, the company agreed to stop making false claims, including the representation that its products provide "complete protection against all forms of identity theft by making customers' personal information useless to identity thieves."

Almost five years later, LifeLock continues to make exactly that kind of claim—"comprehensive identity theft protection" is the slogan on the home page. Whether—as the company insists—the FTC injunction no longer applies because management has tweaked the LifeLock business model is an issue that we look forward to seeing resolved in some future regulatory hearing. The FTC is known to be taking another look at the situation; asked for comment, the commission declined.

If the federal sleuths find themselves running short of material, may *Grant's* suggest that they examine the March/

April 2014 edition of AAA's *Via* magazine? In it, LifeLock seems to advertise protection against "tax return fraud." We say "seems" because the IRS disseminates no data pertaining to any individual's tax returns. What LifeLock could contribute to the security and peace of mind of the tax-paying public is, to us, a mystery.

Like the cobbler's unshod children, according to the FTC complaint, LifeLock's computer systems were themselves vulnerable to hacking. To address the deficiency, the company hired Michael D. Peters as chief information security officer on July 1, 2013. Before the month was out, the company fired him. In a whistle-blower suit filed in March 2014, the ex-employee alleged that LifeLock's substandard security protocols put the well-being of the firm's own phobic customers at risk. (Peters charged that the putative cause of his dismissal, sexual harassment, was the company's malicious invention.)

"This is a company," David Swartz, analyst at Pacific West Land Co. and an owner of puts on LOCK, tells Lorenz "that stores people's Social Security numbers, bank account numbers, credit card numbers—everything. If someone hacks LifeLock, they get everything. The FTC could say they are putting millions of people at risk just by operating, which I believe they are."

A separate legal action brought by another disgruntled former LifeLock employee, Stephen P. Burke, in July 2013, repeated some of Peters' claims. The suit alleges that the volume of account alerts has overwhelmed LifeLock call centers. To quote from Burke's complaint: "The problem of timely informing customers that their credit information was accessed is so widespread that Defendant instituted a code freeze. In essence, Defendant is deliberately 'stepping on the brakes' with regard to sending this critical information to customers on a timely basis, and worse, often choosing to not send these alerts out at all. This practice has been referred to a 'throttling'."

A class action suit brought on Jan. 19 in the Northern District of California charges the company with—among other shortcomings—a failure to "maintain security standards as promised."

Once upon a time, McDonald's kept a running tally of the hamburgers it sold. In a similar vein, LifeLock monitors the cumulative number of alerts it has broadcast. As of March 31, 2014, the tally was 3,615,357. "It seems low enough to lend some circumstantial support to Burke's allegations," Lorenz observes. "Thus, between 2007 and the first quarter 2014, LifeLock had a grand total of 5.3 million customers, implying that each customer, on average, received just 0.68 alerts over a period of seven years. Now, the typical family moves about once every six years, and a change of address in major financial records is something LifeLock claims to monitor. You'd expect that between 2007 through March 31, 2014, at least 2.5 million alerts might have been issued just in connection with moving."

The FTC, as noted, appears to be re-examining its case. On Jan. 17, 2014, the agency met with the company to discuss the Peters' allegations. In the week before the meeting, insiders sold 79,303 shares for $1.4 million. On March 13, the FTC requested more documents and information relating to the company's compliance with the 2010 settlement. On Oct. 29, LifeLock finished sending those papers. If the commission finds that the company has failed to comply with the 2010 settlement, the range of penalties runs from a slap on the wrist to an order to shut down operations and turn out the lights.

With a $1.4 billion market cap and short interest at 12.3% of the float, LOCK is hardly a crowded short. The insiders are heavy sellers of the stock. Nobody has called them stupid.

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Vacation delectation

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James Grant, Editor
August 19, 2015

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"Fiat, boys! I found fiat!"

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