

Top 10 Red Flags for Fraud at Speedway Motorsports, Inc. (NYSE:TRK)

In 2004 TRK surprised the investment community by forming Oasis Trading Group (www.oasistradinggroup.com) which brought up the obvious question: Why would a company that holds NASCAR events invest in an oil trading (emphasis on trading) and exploration business? Management was looking for a way out of the financial troubles – they got involved with trading gas and oil hoping that one fantastic trade would bail them out. That business didn't go well, and the company is in more financial trouble than ever. There are plenty of signs pointing to fraud and mismanagement at this company, and below are our top ten.

1. **False Filing to Mislead Investors:** In the most recent 10-K filed with the Securities and Exchange Commission, Speedway claimed that it had requested NASCAR to move a Sprint Cup Series race to the Kentucky Speedway as soon as possible. NASCAR says no such request has been received. The truth is that NASCAR has been involved in litigation with the former owners of the Kentucky Speedway, and isn't interested in scheduling a Sprint Cup event there until it's settled.

Why would management make up such a thing? These big events are key to Speedway's survival, but without a big event, the purchase of the Kentucky Speedway is nothing but a financial drag on the company. And more importantly when do these material misrepresentations add up to grave concern at Speedway Motorsports, Inc.? This misrepresentation, along with additional ones below show just how desperate this company is to keep up appearances.

2. **Misleading Statement About Revenue From Key Customer:**

In 2008, Speedway earned \$168 million, or 28% of its total revenues, from NASCAR television broadcasting revenues. The company has estimated the revenue under that contract will total \$174 million in 2009.

When asked during the most recent conference call whether there is "any variable component to the TV contract" or "a risk that if ratings do get bad that it could be renegotiated," president and COO Marcus Smith stated:

"Good question and the answer is no, there's no variable based on ratings. And over the lifetime of the contract and depending on the climate of the economy and the business, when the discussion comes up for an extension and renegotiation that will determine what happens in the next several years of the TV agreement."

Yet while he state there's no variable component to the contract, that's not really the case. The latest 10-K states:

"Future changes in race schedules would impact broadcasting revenues. Similar to many televised sports, overall seasonal averages for motorsports may increase or decrease from year to year, and television ratings for certain individual events may fluctuate from year to year for any number of reasons. While this long-term rights

agreement will likely result in annual revenue increases over the contract period, associated annual increases in purse and sanction fees paid to NASCAR may continue. The Company's share of the television broadcast revenues are contracted, and purse and sanction fees are negotiated, with NASCAR on an annual basis."

The 10-K makes it clear that there is variation in this contract, and so revenues could go up or down. Mr. Smith is not being forthright in answering these questions about the contract, and we have to ask why.

- 3. Pledged Stock Shares Put the Company at Risk and Provide "Cooking the Books"**
Fraud Motive: According to the most recent proxy, O. Bruton Smith and Sonic Financial (a company owned primarily by Mr. Smith) collectively own more than 29 million shares (67.5%) of the company's outstanding common stock. Over 10.5 million of those shares have been pledged as collateral for loans. About half of the pledged shares are for loans made to Sonic Automotive (another company of which Mr. Smith is majority owner), and the other half are pledged on debt for which no information is provided.

Sonic Automotive is in serious financial trouble, and its auditors have advised that the 2008 audited financial statements might need a "going concern" qualification. The company is likely to not survive the next year. Sonic Automotive has apparently violated lending covenants, which would clearly put this pledged stock in jeopardy.

Having the majority shareholder and head of the company so closely tied into other failing businesses can't bode well for Speedway. The financial dealings of Smith are clearly intermingled, and the collective financial pressure is enormous. And perhaps most importantly this 'stock pledging' collateral is a built-in motive for fraud because in order to prevent a loan covenant violation or the loan being called (which would have far reaching impact), the temptation exists to do whatever it takes to prop the stock up—even if it means a coordinated effort like that seen when Marcus Smith's resume blunder took place (noted in point 10 below).

- 4. Covering Up Declining Attendance and Viewership:** The story told by the company differs from independent sources of data. During the most recent conference call, Speedway executives represented the following:

William R. Brooks: "Joe, the attendances that I was referring to that was the same year-over-year – similar year-over-year relates to the Sprint Cup events. The attendance at the other series has been down year-over-year. Based on the public comments that other promoters have made, they have had attendance that's been fairly similar to the prior year but again the weekend revenues have been less for the reasons that I mentioned before."

Marcus G. Smith: "Yes, Joe, they've [TV ratings] held strong. We've had solid ratings for Sprint Cup Nationwide and the Truck series. They've held their place in rankings. We've been up and down, but it's pretty even with last year."

Yet Nielsen ratings show that NASCAR broadcasts are down double digits. NASCAR This Week reported that two races were promoted as sell-outs, but had thousands of empty seats. "Official" numbers apparently don't even tell the whole story about attendance at racing events. Clearly Speedway is heavily dependent on attendance and viewership for its survival, yet is covering up the true outlook.

- 5. Losses in Oil and Gas Investments:** In 2004, Speedway departed from its core business and became involved in the oil and gas industry via an entity called Oasis Trading Group. This was not explicitly disclosed in Speedway filings until two years later, in 2006. According to a 2007 disclosure, Speedway recorded a receivable from Oasis for its "...reimbursable share of loss associated with the recoverability assessment of amounts due from these two foreign entities." It appears that Speedway bears the true risk of loss with this entity, but Oasis stood to receive 30% to 50% of any profits generated from the oil and gas business.

In 2008, Speedway wrote off the line of business, which had accumulated losses of over \$50 million. Why were Speedway shareholders subjected to such a business which wasn't adequately disclosed until two years into it, and why did they have to bear the risk of these losses? The answer often lies in what financial wrong management is trying to write. Risky, unrelated businesses are often a way to "solve" the financial problems of the core business—like our YouTube video says—"The Cure." Executive management probably thought they were one big trade away from straightening out their finances.

- 6. Dividend Change to Benefit Insiders:** This year Speedway declared a quarterly dividend. In prior years, there has only been an annual dividend paid after the close of the year. The acceleration of dividend payments as a result of this change means that O. Bruton Smith and Sonic Financial received about \$2.6 million from the company months sooner, and that additional dividend payments throughout this year (likely of similar amounts) will get to them quicker. Is it possible that Mr. Smith wants to be sure he gets his dividend payments even if the company gets in even more financial trouble later this year? Why not take that money received from dividends and turn it back over to the stockholders to pay down outstanding money still due the company from Sonic Financial or the Oasis Trading debacle?
- 7. Detrimental Related Party Transactions:** Speedway and Sonic Financial share some expenses, according to a filing by Speedway. As of December 31, 2008, Sonic Financial owed Speedway \$5.1 million. At one point, Sonic Financial owed Speedway \$5.3 million, but that was reduced by about \$247,000 for amounts Speedway owed to Sonic Financial. It appears as if Sonic Financial is not making payments on what is owed to Speedway. The precarious financial position of both Sonic Financial and Sonic Automotive is not disclosed in Speedway's filings, although it would appear to be a very material fact.

Related party transactions are often troublesome, especially in a situation like this, in which one party (Speedway) seems to be bearing all the risk. Sonic Financial (owned primarily by Smith) is benefiting and Speedway and its shareholders are being harmed by this arrangement.

8. **Lack of Board Independence:** Bernie Madoff was a one man show. So was Barry Minkow while CEO of ZZZZ Best, in that a single person possessed the authority to authorize the company to do virtually anything. Statement of Auditing Standard 99 makes it clear that when members of management have too much control in an organization, it is easy for them to override controls that might otherwise prevent the manipulation of financial and other data.

In the case of Speedway Motorsports, Inc there are seven members on the board of directors. Three of them are company employees, while one is also a director of Sonic Automotive. It's not unusual for companies to have insiders and outsiders sit on the board of directors. However, in the case of Speedway, it is clear that there are numerous conflicts of interest and several instances of self-dealing that is detrimental to the outside shareholders of the company. Management simply cannot be trusted to look out for the interests of the other shareholders. And by serving as company management and board members, it is far easier for them to manipulate the numbers to benefit themselves.

9. **High Debt Load Threatens the Company's Survival:** At the end of 2008, Speedway reported long term debt of \$685 million. \$350 million of the total is on a revolving credit facility which expires in 2010. While carrying such a high debt load, the earnings are expected to be down dramatically in 2009 if you believe management's numbers. If you think there is a motive to inflate the numbers being presented to the public, the outlook is even more grim. Continued declines in business will make it very difficult to refinance the debt, if Speedway is even able to survive. All this means that there is only one line of defense left. The stock price. It cannot be allowed to drop as it secures what is left of this over-encumbered pool of entities.
10. **Falsified Executive Credentials:** President and CEO, Marcus Smith, was recently found to have lied about his credentials. It was reported by the company that he had a degree from the University of North Carolina at Chapel Hill, yet he never graduated. Even worse, when asked about the phony degree, Smith responded that he "believed" he graduated. The cover-up may be just as bad as the original lie.