**GROUPON’S FIRST 10-K: APRIL FOOL’S!**

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What’s all the hoopla about Groupon’s latest “revision” to its financial reports and lack of internal controls? Why is everyone acting so surprised? You should have known something was up when the Groupon’s 10K was so long in coming after earnings were originally released on February 8th. Moreover, we warned you all in [“Trust No One, Particularly Not Groupon’s Accountants,”](http://blogs.smeal.psu.edu/grumpyoldaccountants/archives/281) that this day would soon come. Remember this?

*It is absolutely ludicrous to think that Groupon is anywhere close to having an effective set of internal controls over financial reporting having done 17 acquisitions in a little over a year. When a company expands to 45 countries, grows merchants from 212 to 78,466, and expands its employee base from 37 to 9,625 in only two years, there is little doubt that internal controls are not working somewhere. Any M&A expert will agree. And don’t forget that Groupon admitted to having an inexperienced accounting and reporting staff.*

We just can’t resist: TOLD YOU SO! We just wonder what took E&Y so long to figure this out…after all, as Groupon’s auditors, they get to see the Company’s books and records, and we don’t. Maybe it’s just a case of not being able to see the forest for all of the trees. That’s not very comforting is it?

And could it be any more appropriate that this latest “revision” release comes so close to April Fool’s Day?

For those of you that have real lives and may have missed it, here’s what happened:

* On February 8, 2012, Groupon issued a press release reporting revenues of $506.5 million, free cash flows of $155.1 million, and operating profits of $15.0 million (among other things). See the [Company’s 8K filed](http://www.sec.gov/Archives/edgar/data/1490281/000110465912007814/a12-4452_18k.htm) on this date for more details.
* Then, this past Friday after the markets’ close, the Company announced a “revision” to its original earnings press release. 2011 revenues and operating profits were both revised downward, revenues down to $492.2 million and operating profits flipping to a loss of $15 million. See [Groupon’s 8K filed on March 30, 2012](http://www.sec.gov/Archives/edgar/data/1490281/000110465912022869/a12-8401_38ka.htm) for more details.
* But the biggest “surprise,” or confirmation of trouble, can be found in Item 9A of the [Company’s 2011 10K](http://www.sec.gov/Archives/edgar/data/1490281/000144530512000922/groupon10-k.htm), also filed on March 30, where Groupon admits to having a material weakness in internal control over financial reporting. The following Company admissions are particularly damning:

*We did not maintain financial close process and procedures that were adequately designed, documented and executed to support the accurate and timely reporting of our financial results.*

*We did not maintain effective controls to provide reasonable assurance that accounts were complete and accurate and agreed to detailed support, and that account reconciliations were properly performed, reviewed and approved.*

*We did not have adequate policies and procedures in place to ensure the timely, effective review of estimates, assumptions and related reconciliations and analyses, including those related to customer refund reserves. As noted previously, our original estimate disclosed on February 8 of the reserve for customer refunds proved to be inadequate after we performed additional analysis.*

So, what should all this mean for investors and market regulators? Well, first of all, the Groupon’s earnings revision which was prompted by an increased reserve requirement for customer refunds, highlights the subjectivity and uncertainty associated with any accounting assumptions (or judgments) made by relatively “new” companies, operating in “new” industries, with inexperienced management: *yes, internet companies!* ***In short, internet company accounting is suspect given all the unsupported assertions and assumptions that must be made to comply with generally accepted accounting principles, not to mention the likely internal control weakness issue.***

Next, we question whether there is any real corporate governance at Groupon whatsoever. Usually, when material weaknesses surface, heads roll…not at Groupon! Instead, the board of directors rewarded the Company’s chief financial officer with a salary increase and bonus. According to a [Groupon 8K filed on March 19, 2012](http://www.sec.gov/Archives/edgar/data/1490281/000110465912019265/a12-7395_18k.htm):

*Mr. Child’s base salary was increased from $350,000 to $380,000 per year. This increase will be effective on April 1, 2012…Mr. Child’s annual bonus guarantee of $350,000 will remain in place for 2012, and he will receive half of the guaranteed bonus in June 2012. The remainder of the guarantee plus any additional bonus earned under the plan will be paid in the first quarter of 2013.*

Absolutely unbelievable! Not only does the guy who is responsible for the aforementioned system of internal control bust get to keep his job, but he gets a raise and a bonus! Need we say more?

Finally, do you really believe that this material weakness in internal control (and related refund issue) mysteriously appeared in the fourth quarter of 2011? Of course not, but by assigning it to the fourth quarter of 2011, Groupon and E&Y can avoid the embarrassment of admitting that the financial statements included in the Company’s IPO filing were incorrect. This is probably not a bad strategy from their perspective given the impending securities litigation that is now lurking.

In closing, we just want to remind you of another warning we issued in September of 2011 in [“Is Groupon ‘Cooking Its Books?’”](http://blogs.smeal.psu.edu/grumpyoldaccountants/archives/301): ***weak control environments offer managers the opportunity to manipulate reported financial results with impunity.*** No one will know, not even the auditors.

Being old and grumpy, we have seen this movie before, and we know how it ends. But it’s still entertaining. Please pass the popcorn.

*This essay reflects the opinion of the authors and not necessarily the opinions of The Pennsylvania State University, The American College, or Villanova University.*