

Groupon, Inc.  
Form 10-Q  
October 31, 2014

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-Q  
QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934  
For the quarterly period ended September 30, 2014

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number: 1-35335

Groupon, Inc.

(Exact name of registrant as specified in its charter)

Delaware

27-0903295

(State or other jurisdiction of  
incorporation or organization)

(I.R.S. Employer  
Identification No.)

600 West Chicago Avenue, Suite 400

60654

Chicago, Illinois

(Address of principal executive offices)

(Zip Code)

312-334-1579

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company)  Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

As of October 28, 2014, there were 668,957,164 of the registrant's Class A Common Stock outstanding and 2,399,976 shares of the registrant's Class B Common Stock outstanding.



TABLE OF CONTENTS

PART I. Financial Information	Page
Forward-Looking Statements	<u>3</u>
Item 1. Financial Statements	<u>4</u>
Condensed Consolidated Balance Sheets as of September 30, 2014 (unaudited) and December 31, 2013	<u>4</u>
Condensed Consolidated Statements of Operations for the three and nine months ended September 30, 2014 and 2013 (unaudited)	<u>5</u>
Condensed Consolidated Statements of Comprehensive Income (Loss) for the three and nine months ended September 30, 2014 and 2013 (unaudited)	<u>6</u>
Condensed Consolidated Statement of Stockholders' Equity for the nine months ended September 30, 2014 (unaudited)	<u>7</u>
Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2014 and 2013 (unaudited)	<u>8</u>
Notes to Condensed Consolidated Financial Statements	<u>10</u>
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	<u>36</u>
Item 3. Quantitative and Qualitative Disclosures about Market Risk	<u>82</u>
Item 4. Controls and Procedures	<u>82</u>
PART II. Other Information	
Item 1. Legal Proceedings	<u>84</u>
Item 1A. Risk Factors	<u>84</u>
Item 2. Unregistered sales of equity securities and use of proceeds	<u>99</u>
Item 5. Other Information	<u>99</u>
Item 6. Exhibits	<u>99</u>
Signatures	<u>100</u>
Exhibits	<u>101</u>

PART I. Financial Information

FORWARD LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, including statements regarding our future results of operations and financial position, business strategy and plans and our objectives for future operations. The words "may," "will," "should," "could," "expect," "anticipate," "believe," "estimate," "intend," "continue" and other similar expressions are intended to identify forward-looking statements. We have based these forward-looking statements largely on current expectations and projections about future events and financial trends that we believe may affect our financial condition, results of operations, business strategy, short-term and long-term business operations and objectives, and financial needs. These forward-looking statements involve risks and uncertainties that could cause our actual results to differ materially from those expressed or implied in our forward-looking statements. Such risks and uncertainties include, among others, those discussed in "Item 1A. Risk Factors" of our 2013 Annual Report on Form 10-K and Part II, "Item 1A. Risk Factors" of this Quarterly Report on Form 10-Q, as well as in our condensed consolidated financial statements, related notes, and the other financial information appearing elsewhere in this report and our other filings with the Securities and Exchange Commission. Moreover, we operate in a very competitive and rapidly changing environment. New risks emerge from time to time. It is not possible for our management to predict all risks, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements we may make. We do not intend, and undertake no obligation, to update any of our forward-looking statements after the date of this report to reflect actual results or future events or circumstances. Given these risks and uncertainties, readers are cautioned not to place undue reliance on such forward-looking statements.

As used herein, "Groupon," "we," "our," and similar terms include Groupon, Inc. and its subsidiaries, unless the context indicates otherwise.

## ITEM 1. FINANCIAL STATEMENTS

## GROUPON, INC.

## CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except share and per share amounts)

	September 30, 2014	December 31, 2013
	(unaudited)	
Assets		
Current assets:		
Cash and cash equivalents	\$855,168	\$1,240,472
Accounts receivable, net	124,598	83,673
Deferred income taxes	26,564	27,938
Prepaid expenses and other current assets	243,750	210,415
Total current assets	1,250,080	1,562,498
Property, equipment and software, net	170,534	134,423
Goodwill	441,290	220,827
Intangible assets, net	119,810	28,443
Investments	23,639	20,652
Deferred income taxes, non-current	44,709	35,941
Other non-current assets	22,103	39,226
Total Assets	\$2,072,165	\$2,042,010
Liabilities and Equity		
Current liabilities:		
Accounts payable	\$25,848	\$27,573
Accrued merchant and supplier payables	754,628	752,943
Accrued expenses	223,677	226,986
Deferred income taxes	44,787	47,558
Other current liabilities	134,116	132,718
Total current liabilities	1,183,056	1,187,778
Deferred income taxes, non-current	9,668	10,853
Other non-current liabilities	151,486	131,697
Total Liabilities	1,344,210	1,330,328
Commitments and contingencies (see Note 6)		
Stockholders' Equity		
Class A common stock, par value \$0.0001 per share, 2,000,000,000 shares authorized, 694,272,530 shares issued and 668,185,526 shares outstanding at September 30, 2014 and 670,149,976 shares issued and 665,717,176 shares outstanding at December 31, 2013	70	67
Class B common stock, par value \$0.0001 per share, 10,000,000 shares authorized, 2,399,976 shares issued and outstanding at September 30, 2014 and December 31, 2013	—	—
Common stock, par value \$0.0001 per share, 2,010,000,000 shares authorized, no shares issued and outstanding at September 30, 2014 and December 31, 2013	—	—
Additional paid-in capital	1,814,040	1,584,211
Treasury stock, at cost, 26,087,004 shares at September 30, 2014 and 4,432,800 shares at December 31, 2013	(190,355	) (46,587
Accumulated deficit	(930,748	) (848,870
Accumulated other comprehensive income	34,948	24,830

Edgar Filing: Groupon, Inc. - Form 10-Q

Total Groupon, Inc. Stockholders' Equity	727,955	713,651	
Noncontrolling interests	—	(1,969	)
Total Equity	727,955	711,682	
Total Liabilities and Equity	\$2,072,165	\$2,042,010	

See Notes to unaudited Condensed Consolidated Financial Statements.

GROUPON, INC.  
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
(in thousands, except share and per share amounts)  
(unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Revenue:				
Third party and other	\$399,803	\$394,987	\$1,232,173	\$1,252,966
Direct	357,251	200,072	1,034,094	552,242
Total revenue	757,054	595,059	2,266,267	1,805,208
Cost of revenue:				
Third party and other	61,497	54,001	182,226	179,524
Direct	315,413	181,436	928,314	502,359
Total cost of revenue	376,910	235,437	1,110,540	681,883
Gross profit	380,144	359,622	1,155,727	1,123,325
Operating expenses:				
Marketing	59,935	53,265	203,134	158,319
Selling, general and administrative	325,942	294,074	983,751	904,880
Acquisition-related (benefit) expense, net	(304)	(1,529)	2,078	(2,276)
Total operating expenses	385,573	345,810	1,188,963	1,060,923
(Loss) income from operations	(5,429)	13,812	(33,236)	62,402
Other (expense) income, net	(20,023)	832	(21,886)	(9,830)
(Loss) income before (benefit) provision for income taxes	(25,452)	14,644	(55,122)	52,572
(Benefit) provision for income taxes	(6,434)	15,936	20,181	62,657
Net loss	(19,018)	(1,292)	(75,303)	(10,085)
Net income attributable to noncontrolling interests	(2,190)	(1,288)	(6,575)	(4,061)
Net loss attributable to Groupon, Inc.	\$(21,208)	\$(2,580)	\$(81,878)	\$(14,146)
Net loss per share				
Basic	\$(0.03)	\$(0.00)	\$(0.12)	\$(0.02)
Diluted	\$(0.03)	\$(0.00)	\$(0.12)	\$(0.02)
Weighted average number of shares outstanding				
Basic	669,526,524	666,432,848	675,814,535	662,531,567
Diluted	669,526,524	666,432,848	675,814,535	662,531,567

See Notes to unaudited Condensed Consolidated Financial Statements.

## GROUPON, INC.

## CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(in thousands)

(unaudited)

	Three Months Ended September		Nine Months Ended September	
	30,		30,	
	2014	2013	2014	2013
Net loss	\$ (19,018	) \$ (1,292	) \$ (75,303	) \$ (10,085
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustments	1,827	(1,072	) 9,899	11,416
Available-for-sale securities:				
Net unrealized loss during the period	(425	) (109	) (799	) (19
Reclassification adjustment for impairment included in net loss	831	—	831	—
Net change in unrealized gain (loss) (net of tax effects of \$248 and (\$68) for the three months ended September 30, 2014 and 2013, respectively, and \$23406 and (\$12) for the nine months ended September 30, 2014 and 2013, respectively)		(109	) 32	(19
Other comprehensive income (loss)	2,233	(1,181	) 9,931	11,397
Comprehensive (loss) income	(16,785	) (2,473	) (65,372	) 1,312
Comprehensive income attributable to noncontrolling interests	(2,187	) (1,302	) (6,388	) (4,325
Comprehensive loss attributable to Groupon, Inc.	\$ (18,972	) \$ (3,775	) \$ (71,760	) \$ (3,013

See Notes to unaudited Condensed Consolidated Financial Statements.

GROUPON, INC.  
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY  
(in thousands, except share amounts)  
(unaudited)

	Groupon, Inc. Stockholders' Equity									
	Common Stock			Treasury Stock		Accumulated Deficit	Other Comprehensive Income	Total Groupon Inc. Stockholders' Equity	Non-control- ling Interests	Total
Shares	Amount	Additional Paid-In Capital	Shares	Amount						
Balance at December 31, 2013	672,549,952	\$67	\$1,584,211	(4,432,800 )	\$(46,587 )	\$(848,870)	\$24,830	\$713,651	\$(1,969)	\$713,681
Net loss	—	—	—	—	—	(81,878 )	—	(81,878 )	6,575	(75,303)
Foreign currency translation	—	—	—	—	—	—	10,086	10,086	(187 )	9,899
Unrealized gain on available-for-sale securities, net of tax	—	—	—	—	—	—	32	32	—	32
Common stock issued in connection with acquisition of business, net of issuance costs	13,825,283	2	162,703	—	—	—	—	162,705	—	162,707
Shares issued to settle liability-classified awards and contingent consideration	102,180	—	1,041	—	—	—	—	1,041	—	1,041
Purchase of interests in consolidated subsidiaries	—	—	(6,310 )	—	—	—	—	(6,310 )	2,415	(3,895)
Exercise of stock options	805,225	—	807	—	—	—	—	807	—	807
Vesting of restricted stock units	12,741,462	1	(1 )	—	—	—	—	—	—	—
Shares issued under employee stock purchase plan	857,171	—	5,397	—	—	—	—	5,397	—	5,397
Tax withholdings related to net share settlements of stock-based	(4,208,767 )	—	(33,149 )	—	—	—	—	(33,149 )	—	(33,149)

Edgar Filing: Groupon, Inc. - Form 10-Q

compensation awards										
Stock-based compensation on equity-classified awards	—	—	97,857	—	—	—	—	97,857	—	97,857
Excess tax benefits, net of shortfalls, on stock-based compensation awards	—	—	1,484	—	—	—	—	1,484	—	1,484
Purchases of treasury stock	—	—	—	(21,654,204)	(143,768 )	—	—	(143,768 )	—	(143,768 )
Partnership distributions to noncontrolling interest holders	—	—	—	—	—	—	—	—	(6,834 )	(6,834 )
Balance at September 30, 2014	696,672,506	\$70	\$1,814,040	(26,087,004)	\$(190,355)	\$(930,748)	\$34,948	\$727,955	\$—	\$727,955

See Notes to unaudited Condensed Consolidated Financial Statements.

GROUPON, INC.  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(in thousands)  
(unaudited)

	Nine Months Ended September 30,	
	2014	2013
Operating activities		
Net loss	\$(75,303)	) \$(10,085)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization of property, equipment and software	71,476	49,186
Amortization of acquired intangible assets	36,068	16,131
Stock-based compensation	89,958	89,223
Deferred income taxes	(1,956)	) (1,225)
Excess tax benefits on stock-based compensation	(12,573)	) (12,116)
Loss on equity method investments	459	58
Net gain from changes in fair value of contingent consideration	(1,059)	) (2,276)
Impairment of investments	2,036	—
Change in assets and liabilities, net of acquisitions:		
Restricted cash	6,961	(81)
Accounts receivable	(29,267)	) 8,999
Prepaid expenses and other current assets	(32,397)	) 13,146
Accounts payable	(8,964)	) (25,867)
Accrued merchant and supplier payables	(61,219)	) (72,290)
Accrued expenses and other current liabilities	(27,091)	) (27,790)
Other, net	44,873	15,144
Net cash provided by operating activities	2,002	40,157
Investing activities		
Purchases of property and equipment and capitalized software	(67,461)	) (43,574)
Acquisitions of businesses, net of acquired cash	(117,303)	) (6,349)
Purchases of investments	(6,704)	) (19,583)
Settlement of liabilities related to purchase of additional interests in consolidated subsidiaries	(1,599)	) (1,959)
Purchases of intangible assets	(500)	) (1,520)
Net cash used in investing activities	(193,567)	) (72,985)
Financing activities		
Payments for purchases of treasury stock	(145,395)	) (7,376)
Excess tax benefits on stock-based compensation	12,573	12,116
Taxes paid related to net share settlements of stock-based compensation awards	(32,390)	) (26,504)
Debt issuance costs	(1,029)	) —
Common stock issuance costs in connection with acquisition of business	(158)	) —
Payments of contingent consideration from acquisitions	—	) (780)
Settlements of purchase price obligations related to acquisitions	(3,136)	) (5,000)
Proceeds from stock option exercises and employee stock purchase plan	6,204	6,578
Partnership distribution payments to noncontrolling interest holders	(6,178)	) (4,286)
Payments of capital lease obligations	(3,559)	) (1,001)
Net cash used in financing activities	(173,068)	) (26,253)
Effect of exchange rate changes on cash and cash equivalents	(20,671)	) (10,351)
Net decrease in cash and cash equivalents	(385,304)	) (69,432)
Cash and cash equivalents, beginning of period	1,240,472	1,209,289
Cash and cash equivalents, end of period	\$855,168	\$1,139,857



Non-cash investing and financing activities		
Issuance of common stock in connection with acquisition of business	\$162,862	\$3,051
Contingent consideration liabilities incurred in connection with acquisitions	\$4,006	\$3,567
Equipment acquired under capital lease obligations	\$18,546	\$7,377
Shares issued to settle liability-classified awards and contingent consideration	\$1,041	\$3,394
Liability for purchases of treasury stock	\$120	\$1,638
Liability for purchase consideration	\$359	\$—
Liability for purchase of additional interests in consolidated subsidiaries	\$2,296	\$—
Accounts payable and accrued expenses related to purchases of property and equipment and capitalized software	\$5,508	\$1,713

GROUPON, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

1. DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

Company Information

Groupon, Inc. and subsidiaries (the "Company"), which commenced operations in October 2008, operates online local commerce marketplaces throughout the world that connect merchants to consumers by offering goods and services at a discount. The Company also offers deals on products for which it acts as the merchant of record. Customers can access the Company's deal offerings directly through its websites and mobile applications. The Company also sends emails to its subscribers with deal offerings that are targeted by location and personal preferences.

The Company's operations are organized into three segments: North America, EMEA, which is comprised of Europe, Middle East and Africa, and the remainder of the Company's international operations ("Rest of World"). See Note 12 "Segment Information."

Unaudited Interim Financial Information

The Company has prepared the accompanying condensed consolidated financial statements pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC") for interim financial reporting. These condensed consolidated financial statements are unaudited and, in the Company's opinion, include all adjustments, consisting of normal recurring adjustments and accruals, necessary for a fair presentation of the Company's condensed consolidated balance sheets, statements of operations, comprehensive income (loss), cash flows and stockholders' equity for the periods presented. Operating results for the periods presented are not necessarily indicative of the results to be expected for the full year ending December 31, 2014. Certain information and disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles ("U.S. GAAP") have been omitted in accordance with the rules and regulations of the SEC. These condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and accompanying notes included in the Company's Annual Report on Form 10-K for the year ended December 31, 2013, as filed with the SEC on February 20, 2014.

Principles of Consolidation

The condensed consolidated financial statements include the accounts of the Company and its subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation. The Company's consolidated financial statements were prepared in accordance with U.S. GAAP and include the assets, liabilities, revenue and expenses of all wholly-owned subsidiaries and majority-owned subsidiaries over which the Company exercises control and variable interest entities for which the Company has determined that it is the primary beneficiary. Outside stockholders' interests in subsidiaries are shown on the condensed consolidated financial statements as "Noncontrolling interests." Equity investments in entities in which the Company does not have a controlling financial interest are accounted for under either the equity method, the cost method or as available-for-sale securities, as appropriate.

Reclassifications

Certain reclassifications have been made to the condensed consolidated financial statements of prior periods and the accompanying notes to conform to the current period presentation.

Use of Estimates

The preparation of condensed consolidated financial statements in conformity with U.S. GAAP requires estimates and assumptions that affect the reported amounts and classifications of assets and liabilities, revenue and expenses, and the related disclosures of contingent liabilities in the condensed consolidated financial statements and accompanying notes. Estimates are utilized for, but not limited to, stock-based compensation, income taxes, valuation of acquired goodwill and intangible assets, investments, customer refunds, contingent liabilities and the useful lives of property, equipment and software and intangible assets.

GROUPON, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

Actual results could differ materially from those estimates.

## 2. BUSINESS COMBINATIONS

The Company acquired four businesses during the nine months ended September 30, 2014. These business combinations were accounted for using the acquisition method, and the results of each of those acquired businesses have been included in the condensed consolidated financial statements beginning on the respective acquisition dates. The fair value of consideration transferred in business combinations is allocated to the tangible and intangible assets acquired and liabilities assumed at the acquisition date, with the remaining unallocated amount recorded as goodwill. The allocations of the acquisition price for recent acquisitions have been prepared on a preliminary basis, and changes to those allocations may occur as a result of final working capital adjustments and tax return filings. Acquired goodwill represents the premium the Company paid over the fair value of the net tangible and intangible assets acquired. The Company paid this premium for a number of reasons, including growing the Company's merchant and customer base, acquiring assembled workforces, expanding its presence in international markets, expanding and advancing its product offerings and enhancing technology capabilities. The goodwill from these business combinations is generally not deductible for tax purposes.

For the three and nine months ended September 30, 2014, \$0.7 million and \$3.1 million, respectively, of external transaction costs related to business combinations, primarily consisting of legal and advisory fees, are classified within "Acquisition-related (benefit) expense, net" on the condensed consolidated statements of operations.

LivingSocial Korea, Inc.

On January 2, 2014, the Company acquired all of the outstanding equity interests of LivingSocial Korea, Inc., a Korean corporation and holding company of Ticket Monster Inc. ("Ticket Monster"). Ticket Monster is an e-commerce company based in the Republic of Korea that connects merchants to consumers by offering goods and services at a discount. The primary purpose of this acquisition was to grow the Company's merchant and customer base and expand its presence in the Korean e-commerce market. The aggregate acquisition-date fair value of the consideration transferred for the Ticket Monster acquisition totaled \$259.4 million, which consisted of the following (in thousands):

Cash	\$96,496
Issuance of 13,825,283 shares of Class A common stock	162,862
Total	\$259,358

The fair value of the Class A Common Stock issued as consideration was measured based on the stock price upon closing of the transaction on January 2, 2014.

GROUPON, INC.  
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)  
 (unaudited)

The following table summarizes the allocation of the aggregate acquisition price of the Ticket Monster acquisition (in thousands):

Cash and cash equivalents	\$24,768
Accounts receivable	15,832
Deferred income taxes	1,264
Prepaid expenses and other current assets	829
Property, equipment and software	5,944
Goodwill	220,592
Intangible assets: <sup>(1)</sup>	
Subscriber relationships	57,022
Merchant relationships	32,176
Developed technology	571
Trade name	19,325
Other non-current assets	3,033
Total assets acquired	\$381,356
Accounts payable	\$5,951
Accrued merchant and supplier payables	82,934
Accrued expenses	22,700
Other current liabilities	3,482
Deferred income taxes, non-current	1,264
Other non-current liabilities	5,667
Total liabilities assumed	\$121,998
Total acquisition price	\$259,358

(1) The acquired intangible assets have estimated useful lives of between 2 and 5 years.

Ideeli, Inc.

On January 13, 2014, the Company acquired all of the outstanding equity interests of Ideeli, Inc. (d/b/a "Ideel"), a fashion flash site based in the United States. The primary purpose of this acquisition was to expand and advance the Company's product offerings. The aggregate acquisition-date fair value of the consideration transferred for the Ideel acquisition totaled \$42.7 million, which consisted of the following (in thousands):

Cash	\$42,339
Liability for purchase consideration	359
Total	\$42,698

## GROUPON, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

The following table summarizes the allocation of the aggregate acquisition price of the Ideel acquisition (in thousands):

Cash and cash equivalents	\$79
Accounts receivable	988
Deferred income taxes	572
Prepaid expenses and other current assets	22,081
Property, equipment and software	8,173
Goodwill	5,379
Intangible assets: <sup>(1)</sup>	
Subscriber relationships	5,490
Brand relationships	7,100
Trade name	4,500
Deferred income taxes, non-current	7,753
Total assets acquired	\$62,115
Accounts payable	\$1,640
Accrued supplier payables	4,092
Accrued expenses	9,118
Other current liabilities	482
Deferred income taxes, non-current	332
Other non-current liabilities	3,753
Total liabilities assumed	\$19,417
Total acquisition price	\$42,698

(1) The acquired intangible assets have estimated useful lives of between 3 and 5 years.

## Other Acquisitions

The Company acquired two other businesses during the nine months ended September 30, 2014. The primary purpose of these acquisitions was to acquire an experienced workforce, expand and advance product offerings and enhance technology capabilities. The aggregate acquisition-date fair value of the consideration transferred for these acquisitions totaled \$7.5 million, which consisted of the following (in thousands):

Cash	\$3,477
Contingent consideration	4,006
Total	\$7,483

## GROUPON, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

The following table summarizes the allocation of the aggregate purchase price of these other acquisitions (in thousands):

Net working capital (including acquired cash of \$0.2 million)	\$(52	)
Goodwill	6,261	
Intangible assets: <sup>(1)</sup>		
Subscriber relationships	560	
Brand relationships	579	
Developed technology	568	
Deferred income taxes, non-current	(433	)
Total acquisition price	\$7,483	

(1) Acquired intangible assets have estimated useful lives of between 3 and 5 years.

Pro forma results of operations presented below do not include the results of these other acquisitions because the effects of these acquisitions, individually and in the aggregate, were not material to the Company's condensed consolidated results of operations.

## Pro Forma Financial Information

The following unaudited pro forma information presents the combined operating results of the Company for the three and nine months ended September 30, 2013, as if the Company had acquired Ticket Monster and Ideel as of January 1, 2013 (in thousands). Pro forma results of operations have not been presented for the nine months ended September 30, 2014, because the operating results of Ticket Monster and Ideel from January 1, 2014 through their respective acquisition dates were not material to the Company's consolidated results of operations for the nine months ended September 30, 2014. The underlying pro forma results include the historical financial results of the Company and these two acquired businesses adjusted for depreciation and amortization expense associated with the assets acquired. The unaudited pro forma results do not reflect any operating efficiencies or potential cost savings which may result from the consolidation of the operations of the Company and the acquired entities. Accordingly, these unaudited pro forma results are not necessarily indicative of what the actual results of operations of the combined company would have been if the acquisitions had occurred as of January 1, 2013, nor are they indicative of future results of operations.

	Three Months Ended September 30, 2013	Nine Months Ended September 30, 2013
Revenue	\$642,645	\$1,949,406
Net loss	(23,004	)(79,936

The revenue and net loss of Ticket Monster included in our condensed consolidated statements of operations were \$42.8 million and \$6.4 million for the three months ended September 30, 2014, respectively, and \$107.4 million and \$30.3 million for the nine months ended September 30, 2014, respectively. The revenue and net loss of Ideel included in our condensed consolidated statements of operations were \$20.6 million and \$0.5 million for the three months ended September 30, 2014, respectively, and \$58.1 million and \$3.7 million for the nine months ended September 30, 2014, respectively.

## 3. GOODWILL AND OTHER INTANGIBLE ASSETS

The following table summarizes the Company's goodwill activity by segment for the nine months ended September 30, 2014 (in thousands):

## GROUPON, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

	North America	EMEA	Rest of World	Consolidated
Balance as of December 31, 2013	\$85,457	\$115,669	\$19,701	\$220,827
Goodwill related to acquisitions	11,640	—	220,592	232,232
Other adjustments <sup>(1)</sup>	(157	) (9,578	) (2,034	) (11,769
Balance as of September 30, 2014	\$96,940	\$106,091	\$238,259	\$441,290

(1) Represents the impact of changes in foreign exchange rates on goodwill.

The following tables summarize the Company's other intangible assets (in thousands):

Asset Category	September 30, 2014		
	Gross Carrying Value	Accumulated Amortization	Net Carrying Value
Subscriber relationships	\$105,108	\$44,891	\$60,217
Merchant relationships	40,653	16,522	24,131
Trade names	29,980	9,800	20,180
Developed technology	23,415	21,663	1,752
Brand relationships	7,664	1,103	6,561
Other intangible assets	17,199	10,230	6,969
Total	\$224,019	\$104,209	\$119,810

Asset Category	December 31, 2013		
	Gross Carrying Value	Accumulated Amortization	Net Carrying Value
Subscriber relationships	\$45,541	\$30,866	\$14,675
Merchant relationships	9,186	7,991	1,195
Trade names	6,739	6,739	—
Developed technology	23,038	19,547	3,491
Other intangible assets	16,776	7,694	9,082
Total	\$101,280	\$72,837	\$28,443

Amortization of intangible assets is computed using the straight-line method over their estimated useful lives, which range from 1 to 5 years. Amortization expense related to intangible assets was \$11.8 million and \$5.3 million for the three months ended September 30, 2014 and 2013, respectively, and \$36.1 million and \$16.1 million for the nine months ended September 30, 2014 and 2013, respectively. As of September 30, 2014, the Company's estimated future amortization expense related to intangible assets is as follows (in thousands):

Remaining amounts in 2014	\$11,094
2015	39,055
2016	32,912
2017	18,575
2018	18,089
Thereafter	85
Total	\$119,810

## GROUPON, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

## 4. INVESTMENTS

The following table summarizes the Company's investments (dollars in thousands):

	September 30, 2014	Percent Ownership of Voting Stock			December 31, 2013	Percent Ownership of Voting Stock				
Cost and equity method investments:										
Cost method investments	\$ 15,920	6	% to	19	%	\$ 15,788	6	% to	19	%
Equity method investments	1,231	21	% to	50	%	1,690	21	% to	50	%
Total cost and equity method investments	17,151					17,478				
Available-for-sale securities:										
Convertible debt securities	2,030					3,174				
Redeemable preferred shares	4,458	19	% to	23	%	—	19	%		
Total available-for-sale securities	6,488					3,174				
Total investments	\$ 23,639					\$ 20,652				

In February 2014, the Company acquired redeemable preferred shares in an online home services company for \$4.6 million. The shares are accounted for as available-for-sale securities.

The following table summarizes the amortized cost, gross unrealized loss and fair value of the Company's available-for-sale securities as of September 30, 2014 and December 31, 2013 (in thousands):

	September 30, 2014			December 31, 2013		
	Amortized Cost	Gross Unrealized Loss	Fair Value	Amortized Cost	Gross Unrealized Loss	Fair Value
Available-for-sale securities:						
Convertible debt securities	\$ 2,030	\$—	\$ 2,030	\$ 3,370	\$ (196 )	\$ 3,174
Redeemable preferred shares	4,599	(141 )	4,458	—	—	—
Total available-for-sale securities	\$ 6,629	\$ (141 )	\$ 6,488	\$ 3,370	\$ (196 )	\$ 3,174

The Company's investments in available-for-sale securities have been in an unrealized loss position for less than one year as of September 30, 2014.

## Other-Than-Temporary Impairment

An unrealized loss exists when the current fair value of an investment is less than its amortized cost basis. The Company conducts reviews of all of its investments with unrealized losses on a quarterly basis to evaluate whether those impairments are other-than-temporary. This evaluation, which is performed at the individual investment level, consists of several qualitative and quantitative factors regarding the severity and duration of the unrealized loss as well as the Company's intent and ability to hold the investment for a period of time that is sufficient to allow for an anticipated recovery in value. Evidence considered in this evaluation includes the amount of the impairment, the length of time that the investment has been impaired, the factors contributing to the impairment, the financial condition and near-term prospects of the investee, recent operating trends and forecasted performance of the investee, market conditions in the geographic area or industry in which the investee operates, and the Company's strategic plans for holding the investment in relation to the period of time expected for an anticipated recovery in value. Additionally, the Company considers whether it intends to sell the investment or whether it is more likely than not that it will be required to sell the investment before recovery of its amortized cost basis. Investments with unrealized losses that are determined to be other-than-temporary are written down to fair value with a charge to earnings. Unrealized losses that are determined to be temporary in nature are not recorded for cost method investments and equity method investments, while such losses are recorded, net of tax, in accumulated other comprehensive income for available-for-sale securities. The Company recorded a \$1.3 million other-than-temporary impairment of an investment in the convertible debt securities of a nonpublic entity, which is reported within "Other



GROUPON, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

(expense) income, net" on the condensed consolidated statements of operations for the three and nine months ended September 30, 2014. The Company's investment in Life Media Limited ("F-tuan"), an entity with operations based in China, was written down to zero through an other-than-temporary impairment charge as of December 31, 2013, and continues to have an estimated fair value of zero as of September 30, 2014.

#### 5. SUPPLEMENTAL CONSOLIDATED BALANCE SHEETS AND STATEMENTS OF OPERATIONS INFORMATION

The following table summarizes the Company's other (expense) income, net for the three and nine months ended September 30, 2014 and 2013 (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Interest income	\$409	\$487	\$1,151	\$1,348
Interest expense	(277)	(39)	(444)	(187)
Impairment of investments	(1,448)	—	(2,036)	—
Loss on equity method investments	(91)	(25)	(459)	(58)
Foreign exchange (losses) gains, net	(18,638)	326	(20,108)	(11,156)
Other	22	83	10	223
Other (expense) income, net	\$(20,023)	\$832	\$(21,886)	\$(9,830)

The following table summarizes the Company's prepaid expenses and other current assets as of September 30, 2014 and December 31, 2013 (in thousands):

	September 30, 2014	December 31, 2013
Current portion of unamortized tax effects on intercompany transactions	\$23,377	\$28,502
Finished goods inventories	57,301	57,097
Prepaid expenses	42,603	29,404
Restricted cash	11,056	14,579
VAT and income taxes receivable	82,804	52,960
Prepaid marketing	9,832	17,301
Other	16,777	10,572
Total prepaid expenses and other current assets	\$243,750	\$210,415

## GROUPON, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

The following table summarizes the Company's accrued merchant and supplier payables as of September 30, 2014 and December 31, 2013 (in thousands):

	September 30, 2014	December 31, 2013
Accrued merchant payables	\$575,145	\$518,233
Accrued supplier payables <sup>(1)</sup>	179,483	234,710
Total accrued merchant and supplier payables	\$754,628	\$752,943

(1) Amounts include payables to suppliers of inventories and providers of shipping and fulfillment services.

The following table summarizes the Company's accrued expenses as of September 30, 2014 and December 31, 2013 (in thousands):

	September 30, 2014	December 31, 2013
Marketing	\$11,860	\$12,001
Refunds reserve	29,221	38,597
Payroll and benefits	64,751	64,966
Customer credits	46,297	44,728
Professional fees	16,902	18,906
Other	54,646	47,788
Total accrued expenses	\$223,677	\$226,986

The following table summarizes the Company's other current liabilities as of September 30, 2014 and December 31, 2013 (in thousands):

	September 30, 2014	December 31, 2013
Income taxes payable	\$27,020	\$21,994
VAT payable	30,476	37,627
Sales taxes payable	6,229	10,412
Deferred revenue	50,677	47,259
Other	19,714	15,426
Total other current liabilities	\$134,116	\$132,718

The following table summarizes the Company's other non-current liabilities as of September 30, 2014 and December 31, 2013 (in thousands):

	September 30, 2014	December 31, 2013
Long-term tax liabilities	\$108,233	\$109,286
Deferred rent	13,216	9,148
Other	30,037	13,263
Total other non-current liabilities	\$151,486	\$131,697

GROUPON, INC.  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)  
(unaudited)

The following table summarizes the components of accumulated other comprehensive income, net of tax, as of September 30, 2014 and December 31, 2013 (in thousands):

	Foreign currency translation adjustments	Unrealized loss on available-for-sale securities, net of tax	Total
Balance as of December 31, 2013	\$ 24,952	\$ (122 )	\$ 24,830
Other comprehensive income (loss) before reclassification adjustments	10,086	(799 )	9,287
Reclassification adjustment for impairment included in net loss	—	831	831
Other comprehensive income	10,086	32	10,118
Balance as of September 30, 2014	\$ 35,038	\$ (90 )	\$ 34,948

The effects of amounts reclassified from accumulated other comprehensive income (loss) to net loss for the three and nine months ended September 30, 2014 and 2013 are presented within the following line items in the condensed consolidated statements of operations (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,		Condensed Consolidated Statements of Operations Line Item
	2014	2013	2014	2013	
Other-than-temporary impairment of available-for-sale security	\$ 1,340	\$ —	\$ 1,340	\$ —	Other (expense) income, net
Less: Tax effect	(509 )	—	(509 )	—	(Benefit) provision for income taxes
Reclassification adjustment	\$ 831	\$ —	\$ 831	\$ —	

#### 6. COMMITMENTS AND CONTINGENCIES

Except as it relates to commitments under operating leases that were assumed in connection with the Ticket Monster and Ideel acquisitions, as described in Note 2, "Business Combinations," the Company's commitments as of September 30, 2014 did not materially change from the amounts set forth in its 2013 Annual Report on Form 10-K. As of September 30, 2014, estimated future payments under operating leases assumed in connection with the Ticket Monster and Ideel acquisitions for each of the next five years and thereafter are as follows (in thousands):

	Operating leases
2014	\$ 1,348
2015	5,148
2016	4,936
2017	4,342
2018	2,631
Thereafter	11,110
Total minimum lease payments	\$ 29,515

#### Legal Matters

From time to time, the Company is party to various legal proceedings incident to the operation of its business. For example, the Company is currently involved in proceedings by stockholders, former employees, merchants, intellectual property infringement suits and suits by customers (individually or as class actions) alleging, among other things, violation of the Credit Card Accountability, Responsibility and Disclosure Act and state laws governing gift cards, stored value cards and coupons. Additionally,



GROUPON, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

the Company is subject to general customer complaints seeking monetary damages, particularly in its Rest of World segment. The following is a brief description of significant legal proceedings.

On February 8, 2012, the Company issued a press release announcing its expected financial results for the fourth quarter of 2011. After finalizing its year-end financial statements, the Company announced on March 30, 2012 revised financial results, as well as a material weakness in its internal control over financial reporting related to deficiencies in its financial statement close process. The revisions resulted in a reduction to fourth quarter 2011 revenue of \$14.3 million. The revisions also resulted in an increase to fourth quarter operating expenses that reduced operating income by \$30.0 million, net income by \$22.6 million and earnings per share by \$0.04. Following this announcement, the Company and several of its current and former directors and officers were named as parties to the following outstanding securities and stockholder derivative lawsuits all arising out of the same alleged events and facts.

The Company is currently a defendant in a proceeding pursuant to which, on October 29, 2012, a consolidated amended class action complaint was filed against the Company, certain of its directors and officers, and the underwriters that participated in the initial public offering of the Company's Class A common stock. Originally filed in April 2012, the case is currently pending before the United States District Court for the Northern District of Illinois: *In re Groupon, Inc. Securities Litigation*. The complaint asserts claims pursuant to Sections 11 and 15 of the Securities Act of 1933 and Sections 10(b) and 20(a) of the Securities Exchange Act of 1934. Allegations in the consolidated amended complaint include that the Company and its officers and directors made untrue statements or omissions of material fact by issuing inaccurate financial statements for the fiscal quarter and the fiscal year ending December 31, 2011 and by failing to disclose information about the Company's financial controls in the registration statement and prospectus for the Company's initial public offering of Class A common stock and in the Company's subsequently-issued earnings release dated February 8, 2012. The class action lawsuit seeks an unspecified amount of monetary damages, reimbursement for fees and costs incurred in connection with the actions, including attorneys' fees, and various other forms of monetary and non-monetary relief. The plaintiff filed an amended motion for class certification on December 4, 2013. On March 18, 2014, the court entered a scheduling order setting deadlines for fact discovery by March 13, 2015, expert discovery by August 31, 2015, and dispositive motions by October 30, 2015. On May 2, 2014, defendants filed a motion requesting exclusion of the opinions of plaintiff's proposed market efficiency expert in resolving the motion for class certification. The court held a hearing on the motion to exclude plaintiff's expert on September 11, 2014 and ordered that the parties file post-hearing briefings. On September 23, 2014, before the parties had commenced the ordered post-hearing briefing, the court entered an order granting plaintiff's motion for class certification. On October 1, 2014, the Company filed a petition for leave to appeal that order in the United States Court of Appeals for the Seventh Circuit. The petition is currently pending.

In addition, federal and state purported stockholder derivative lawsuits have been filed against certain of the Company's current and former directors and officers. The federal purported stockholder derivative lawsuit was originally filed in April 2012 and a consolidated stockholder derivative complaint, filed on July 30, 2012, is currently pending in the United States District Court for the Northern District of Illinois: *In re Groupon Derivative Litigation*. Plaintiffs assert claims for breach of fiduciary duty and abuse of control. The state derivative cases are currently pending before the Chancery Division of the Circuit Court of Cook County, Illinois: *Orrego v. Lefkofsky, et al.*, was filed on April 5, 2012; and *Kim v. Lefkofsky, et al.*, was filed on May 25, 2012. The state derivative complaints generally allege that the defendants breached their fiduciary duties by purportedly mismanaging the Company's business by, among other things, failing to utilize proper accounting controls and, in the case of one of the state derivative lawsuits, by engaging in alleged insider trading of the Company's Class A common stock and misappropriating information. In addition, one state derivative case asserts a claim for unjust enrichment. The derivative lawsuits purport to seek to recoup for the Company an unspecified amount of monetary damages allegedly sustained by the Company, restitution from defendants, reimbursement for fees and costs incurred in connection with

the actions, including attorneys' fees, and various other forms of monetary and non-monetary relief. On June 20, 2012, the Company and the individual defendants filed a motion requesting that the court stay the consolidated federal derivative action pending resolution of the consolidated federal class actions. On July 31, 2012, the court granted defendants' motion in part, and stayed the consolidated federal derivative action pending a separate resolution of upcoming motions to dismiss in the consolidated federal class actions. On June 15, 2012, the state plaintiffs filed a motion to consolidate the state derivative actions, which was granted on July 2, 2012, and on July 5, 2012, the plaintiffs filed a motion for appointment of co-lead plaintiffs and co-lead counsel, which was granted on July 27, 2012. No consolidated complaint has been filed in the state derivative action. On September 14, 2012, the court granted a motion filed by the parties requesting that the court stay the state derivative actions pending the federal court's resolution of anticipated motions to dismiss in the consolidated federal class action. On April 18, 2013, the state court appointed a lead plaintiff and approved its selection of lead counsel and local counsel for the purported class. Following entry of the court's order denying defendants' motions to dismiss in *In re Groupon*

GROUPON, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

Securities Litigation, the courts in both the state and federal derivative actions granted motions requesting that the respective courts extend the litigation stays currently in place pending further developments in In re Groupon, Inc. Securities Litigation.

The Company intends to defend all of the securities and stockholder derivative lawsuits vigorously.

In 2010, the Company was named as a defendant in a series of class actions that came to be consolidated into a single case in the U.S. District Court for the Southern District of California. The consolidated case is referred to as In re Groupon Marketing and Sales Practices Litigation. The Company denies liability, but the parties agreed to settle the litigation for \$8.5 million before any determination had been made on the merits or with respect to class certification. Because the case had been filed as a class action, the parties were required to provide proper notice and obtain court approval for the settlement. During that process, certain individuals asserted various objections to the settlement. The parties to the case opposed the objections and on December 14, 2012, the district court approved the settlement over the various objections.

Subsequent to the entry of the order approving settlement, certain of the objectors filed a notice of appeal, contesting the settlement and appealing the matter to the Ninth Circuit of the U.S. Court of Appeals, where the case remains pending. The Company believes that the settlement is valid and intends to oppose the appeal. Plaintiffs also maintain that the settlement is valid and will be opposing the appeal. The settlement, however, is not effective during the pendency of the appeal. The Company does not know when the appeal will be resolved. Depending on the outcome of the appeal, it is possible that the settlement will be rejected, or that there will be further proceedings in the appellate court or district court, or that the settlement will be enforced at that time without further objections or proceedings. In addition, third parties have from time to time claimed, and others may claim in the future, that the Company has infringed their intellectual property rights. The Company is subject to intellectual property disputes, and expects that it will increasingly be subject to intellectual property infringement claims as its services expand in scope and complexity. The Company has in the past litigated such claims, and several of these claims are currently pending. The Company may also become more vulnerable to third party claims as laws such as the Digital Millennium Copyright Act are interpreted by the courts, and as the Company becomes subject to laws in jurisdictions where the underlying laws with respect to the potential liability of online intermediaries are either unclear or less favorable. The Company believes that additional lawsuits alleging that it has violated patent, copyright or trademark laws will be filed against it. Intellectual property claims, whether meritorious or not, are time consuming and costly to resolve, could require expensive changes in the Company's methods of doing business, or could require it to enter into costly royalty or licensing agreements.

The Company is also subject to, or in the future may become subject to, a variety of regulatory inquiries across the jurisdictions where the Company conducts its business, including, for example, consumer protection, marketing practices, tax and privacy rules and regulations. Any regulatory actions against the Company, whether meritorious or not, could be time consuming, result in costly litigation, damage awards, injunctive relief or increased costs of doing business through adverse judgment or settlement, require the Company to change its business practices in expensive ways, require significant amounts of management time, result in the diversion of significant operational resources or otherwise harm the Company's business.

The Company establishes an accrued liability for loss contingencies related to legal and regulatory matters when the loss is both probable and estimable. This accrual represents management's best estimate of probable loss and in such cases, there may be an exposure to loss in excess of the amounts accrued. For each matter described above, there is inherent and significant uncertainties based on, among other factors, the stage of the proceedings, developments in the applicable facts of law, or the lack of a specific damage claim. In addition, for some matters for which a loss is probable or reasonably possible, an estimate of the amount of loss or range of loss is not possible, and we may be unable to estimate the possible loss or range of losses that could potentially result from the application of non-monetary remedies. Currently, the Company is unable to reasonably estimate the amount of reasonably possible losses in excess of the amounts accrued for the securities and stockholder derivative lawsuits. For the remaining

matters described above, the Company believes that the amount of reasonably possible losses in excess of the amounts accrued would not have a material adverse effect on its business, consolidated financial position, results of operations or cash flows. The Company's accrued liabilities for loss contingencies related to legal and regulatory matters may change in the future as a result of new developments, including, but not limited to, the occurrence of new legal matters, changes in the law or regulatory environment, adverse or favorable rulings, newly discovered facts relevant to the matter, or changes in the strategy for the matter. Regardless of the outcome, litigation can have an adverse impact on the Company because of defense and settlement costs, diversion of management resources and other factors.

GROUPON, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

#### Indemnifications

In the normal course of business to facilitate transactions related to its operations, the Company indemnifies certain parties, including employees, lessors, service providers and merchants, with respect to various matters. The Company has agreed to hold certain parties harmless against losses arising from a breach of representations or covenants, or other claims made against those parties. These agreements may limit the time within which an indemnification claim can be made and the amount of the claim. The Company is also subject to increased exposure to various claims as a result of its acquisitions, particularly in cases where the Company is entering into new businesses in connection with such acquisitions. The Company may also become more vulnerable to claims as it expands the range and scope of its services and is subject to laws in jurisdictions where the underlying laws with respect to potential liability are either unclear or less favorable. In addition, the Company has entered into indemnification agreements with its officers and directors, and the Company's bylaws contain similar indemnification obligations to agents.

It is not possible to determine the maximum potential amount under these indemnification agreements due to the limited history of prior indemnification claims and the unique facts and circumstances involved in each particular agreement. Historically, any payments that the Company has made under these agreements have not had a material impact on the operating results, financial position or cash flows of the Company.

#### 7. REVOLVING CREDIT AGREEMENT

In August 2014, the Company entered into a three-year senior secured revolving credit agreement (the "Credit Agreement") that provides for aggregate principal borrowings of up to \$250.0 million. Borrowings under the Credit Agreement bear interest, at the Company's option, at a rate per annum equal to the Alternate Base Rate or Adjusted LIBO Rate (each as defined in the Credit Agreement) plus an additional margin ranging between 0.25% and 2.00%. The Company is required to pay quarterly commitment fees ranging from 0.20% to 0.35% per annum of the average daily amount available under the Credit Agreement. The Credit Agreement also provides for the issuance of up to \$45.0 million in letters of credit, provided that the sum of outstanding borrowings and letters of credit do not exceed the maximum funding commitment of \$250.0 million.

The Credit Agreement is secured by substantially all of the Company's and its subsidiaries' tangible and intangible assets, including a pledge of 100% of the outstanding capital stock of substantially all of its direct and indirect domestic subsidiaries and 65% of the shares or equity interests of first-tier foreign subsidiaries and each U.S. entity whose assets substantially consist of capital stock and/or intercompany debt of one or more foreign subsidiaries, subject to certain exceptions. Certain of the Company's domestic subsidiaries are guarantors under the Credit Agreement.

The Credit Agreement contains various customary restrictive covenants that limit the Company's ability to, among other things: incur additional indebtedness; enter into sale or leaseback transactions; make investments, loans or advances; grant or incur liens on assets; sell assets; engage in mergers, consolidations, liquidations or dissolutions; engage in transactions with affiliates; and make dividend payments. The Credit Agreement requires the Company to maintain compliance with specified financial covenants, comprised of a minimum fixed charge coverage ratio, a maximum leverage ratio, and a minimum liquidity ratio, each as set forth in the Credit Agreement. The Company is also required to maintain, as of the last day of each fiscal quarter, unrestricted cash of at least \$400.0 million, including \$200.0 million in accounts held with lenders under the Credit Agreement or their affiliates. Non-compliance with these covenants may result in termination of the commitments under the Credit Agreement and any then outstanding borrowings may be declared due and payable immediately. The Company has the right to terminate the Credit Agreement or reduce the available commitments at any time.

As of September 30, 2014, the Company had no borrowings or letters of credit outstanding under the Credit Agreement and was in compliance with all covenants.

#### 8. STOCKHOLDERS' EQUITY AND STOCK-BASED COMPENSATION

Common Stock

The Company's Certification of Incorporations authorizes three classes of common stock: Class A common stock, Class B common stock and common stock. No shares of common stock will be issued or outstanding until October 31, 2016, at which time all outstanding shares of Class A common stock and Class B common stock will automatically convert into shares of common

## GROUPON, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

stock. In addition, the Company's Certification of Incorporation authorizes shares of undesignated preferred stock, the rights, preferences and privileges of which may be designated from time to time by the Board.

## Share Repurchase Programs

The Board has authorized the Company to purchase up to \$300.0 million of its outstanding Class A common stock through August 2015. The timing and amount of any share repurchases is determined based on market conditions, share price and other factors, and the program may be discontinued or suspended at any time. During the three and nine months ended September 30, 2014, the Company purchased 1,349,712 shares and 21,654,204 shares, respectively, of Class A common stock for an aggregate purchase price of \$8.3 million and \$143.8 million (including fees and commissions), respectively, under the share repurchase program. As of September 30, 2014, up to \$109.6 million of Class A common stock remains available for repurchase under the share repurchase program.

## Groupon, Inc. Stock Plans

The Groupon, Inc. Stock Plans (the "Plans") are administered by the Compensation Committee of the Board, which determines the number of awards to be issued, the corresponding vesting schedule and the exercise price for options. As of September 30, 2014, 45,500,684 shares were available for future issuance under the Plans.

The Company recognized stock-based compensation expense of \$34.6 million and \$26.9 million for the three months ended September 30, 2014 and 2013, respectively, and \$90.0 million and \$89.2 million for the nine months ended September 30, 2014 and 2013, respectively, related to stock awards issued under the Plans, acquisition-related awards and subsidiary awards. The Company also capitalized \$2.8 million and \$2.2 million of stock-based compensation for the three months ended September 30, 2014 and 2013, respectively, and \$7.9 million and \$6.9 million of stock-based compensation for the nine months ended September 30, 2014 and 2013, respectively, in connection with internally-developed software.

As of September 30, 2014, a total of \$230.1 million of unrecognized compensation costs related to unvested stock awards and unvested acquisition-related awards are expected to be recognized over a remaining weighted average period of 1.4 years.

## Employee Stock Purchase Plan

The Company is authorized to grant up to 10,000,000 shares of common stock under its employee stock purchase plan ("ESPP"). For the nine months ended September 30, 2014 and 2013, 857,171 and 774,288 shares of common stock were issued under the ESPP, respectively.

## Stock Options

The table below summarizes the stock option activity for the nine months ended September 30, 2014:

	Options	Weighted- Average Exercise Price	Weighted- Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (in thousands) <sup>(1)</sup>
Outstanding at December 31, 2013	3,355,054	\$ 1.11	6.04	\$ 35,742
Exercised	(805,225)	) \$ 1.00		
Forfeited	(59,489)	) \$ 2.41		
Outstanding at September 30, 2014	2,490,340	\$ 1.14	5.30	\$ 13,796
Exercisable at September 30, 2014	2,484,486	\$ 1.13	5.30	\$ 13,789

The aggregate intrinsic value of options outstanding and exercisable represents the total pretax intrinsic value (the difference between the fair value of the Company's stock on the last day of each period and the exercise price, (1) multiplied by the number of options where the fair value exceeds the exercise price) that would have been received by the option holders had all option holders exercised their options as of September 30, 2014 and December 31, 2013, respectively.



## GROUPON, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

## Restricted Stock Units

The table below summarizes activity regarding unvested restricted stock units under the Plans for the nine months ended September 30, 2014:

	Restricted Stock Units	Weighted- Average Grant Date Fair Value (per share)
Unvested at December 31, 2013	41,648,055	\$8.06
Granted	22,885,522	\$7.83
Vested	(12,741,462	) \$7.97
Forfeited	(9,586,804	) \$8.00
Unvested at September 30, 2014	42,205,311	\$8.03

## Performance Share Units

The Company completed its acquisition of Ticket Monster on January 2, 2014, as described in Note 2 "Business Combinations," and approximately 2,000,000 performance share units were granted to certain key employees of that subsidiary. The vesting of these awards into shares of the Company's Class A common stock is contingent upon the subsidiary's achievement of specified financial targets over three annual performance periods for the years ending December 31, 2014, 2015 and 2016 and is subject to continued employment at the end of each performance period. If the financial targets for a performance period are not achieved, no shares will be issued for that performance period. The grant date fair value of the performance share units was \$8.07 per share.

## Restricted Stock Awards

The Company has granted restricted stock awards in connection with prior period business combinations.

Compensation expense on these awards is recognized on a straight-line basis over the requisite service periods.

The table below summarizes activity regarding unvested restricted stock for the nine months ended September 30, 2014:

	Restricted Stock	Weighted- Average Grant Date Fair Value (per share)
Unvested at December 31, 2013	97,677	\$14.00
Vested	(48,890	) \$14.45
Forfeited	(13,129	) \$17.07
Unvested at September 30, 2014	35,658	\$15.59

## 9. INCOME TAXES

The Company's tax provision for interim periods is determined using an estimate of its annual effective tax rate, adjusted for discrete items.

For the three months ended September 30, 2014, the Company recorded an income tax benefit of \$6.4 million on pre-tax losses of \$25.5 million, for an effective tax rate of 25.3%. For the three months ended September 30, 2013, the Company recorded income tax expense of \$15.9 million on pre-tax income of \$14.6 million, for an effective tax rate of 108.8%.

For the nine months ended September 30, 2014, the Company recorded income tax expense of \$20.2 million on pre-tax losses of \$55.1 million, for an effective tax rate of (36.6)%. For the nine months ended September 30, 2013, the Company recorded income tax expense of \$62.7 million on pre-tax income of \$52.6 million, for an effective tax rate of 119.2%.

## GROUPON, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

The Company's U.S. statutory rate is 35%. Significant factors impacting the effective tax rate for the three and nine months ended September 30, 2014 and 2013 included losses in jurisdictions that the Company is not able to benefit due to uncertainty as to the realization of those losses, amortization of the tax effects of intercompany sales of intellectual property and nondeductible stock-based compensation expense. Additionally, the effective tax rate for the three and nine months ended September 30, 2014 included a \$7.7 million decrease to the Company's liabilities for uncertain tax positions, as discussed in the following paragraph.

The Company is currently undergoing income tax audits in multiple jurisdictions. There are many factors, including factors outside of the Company's control, which influence the progress and completion of these audits. For the three and nine months ended September 30, 2014, the Company decreased its liabilities for uncertain tax positions and income tax expense by \$7.7 million as a result of new information that impacted its estimates of amounts that are more-likely-than-not of being realized upon ultimate settlement. As of September 30, 2014, the Company believes that it is reasonably possible that additional changes of up to \$35.5 million in unrecognized tax benefits may occur within the next 12 months upon closing of income tax audits or the expiration of applicable statutes of limitations.

As of September 30, 2014, unamortized tax effects of intercompany transactions of \$23.4 million and \$1.5 million are included within "Prepaid expenses and other current assets" and "Other non-current assets," respectively, on the condensed consolidated balance sheet. As of December 31, 2013, unamortized tax effects of intercompany transactions of \$28.5 million and \$20.4 million are included within "Prepaid expenses and other current assets" and "Other non-current assets," respectively, on the condensed consolidated balance sheet. As of September 30, 2014, the estimated future amortization of the tax effects of intercompany transactions is \$6.2 million for the remainder of 2014 and \$18.7 million for 2015. These amounts exclude the benefits, if any, for tax deductions in other jurisdictions that the Company may be entitled to as a result of the related intercompany transactions.

## 10. FAIR VALUE MEASUREMENTS

Fair value is defined under U.S. GAAP as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. As such, fair value is a market-based measurement that is determined based on assumptions that market participants would use in pricing an asset or a liability.

To increase the comparability of fair value measures, the following hierarchy prioritizes the inputs in valuation methodologies used to measure fair value:

Level 1 - Measurements that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 - Measurements that include other inputs that are directly or indirectly observable in the marketplace.

Level 3 - Measurements derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable. These fair value measurements require significant judgment.

In determining fair value, the Company uses various valuation approaches within the fair value measurement framework. The valuation methodologies used for the Company's assets and liabilities measured at fair value and their classification in the valuation hierarchy are summarized below:

Cash equivalents - Cash equivalents primarily consist of AAA-rated money market funds with overnight liquidity and no stated maturities. The Company classified cash equivalents as Level 1 due to the short-term nature of these instruments and measured the fair value based on quoted prices in active markets for identical assets.

Available-for-sale securities - The Company has investments in redeemable preferred shares and convertible debt securities issued by nonpublic entities. The Company measures the fair value of available-for-sale securities using the discounted cash flow method, which is an income approach, and the probability-weighted expected return method, which is an income approach that incorporates probability-weighted outcomes.

The Company has classified its investments in available-for-sale securities as Level 3 due to the lack of observable market data over fair value inputs such as cash flow projections, discount rates and probability-weightings. Increases in projected



GROUPON, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

cash flows and decreases in discount rates contribute to increases in the estimated fair values of available-for-sale securities, whereas decreases in projected cash flows and increases in discount rates contribute to decreases in their fair values. Additionally, increases in the probabilities of favorable investment outcomes, such as a sale or initial public offering of the investee, and decreases in the probabilities of unfavorable outcomes, such as a default by the investee, contribute to increases in the estimated fair value of available-for-sale securities, whereas decreases in the probabilities of favorable investment outcomes and increases in the probabilities of unfavorable investment outcomes contribute to decreases in their fair values.

Contingent consideration - The Company has contingent obligations to transfer cash payments to the former owners in conjunction with certain acquisitions if specified financial results are met over future reporting periods. Liabilities for contingent consideration (i.e., earn-outs) are measured at fair value each reporting period, with the acquisition-date fair value included as part of the consideration transferred and subsequent changes in fair value are recorded in earnings within "Acquisition-related (benefit) expense, net" on the condensed consolidated statements of operations. The Company uses an income approach to value contingent consideration liabilities, which is determined based on the present value of probability-weighted future cash flows. The Company has generally classified the contingent consideration liabilities as Level 3 due to the lack of relevant observable market data over fair value inputs such as probability-weighting of payment outcomes. Increases in the assessed likelihood of a higher payout under a contingent consideration arrangement contribute to increases in the fair value of the related liability. Conversely, decreases in the assessed likelihood of a higher payout under a contingent consideration arrangement contribute to decreases in the fair value of the related liability. Changes in assumptions could have an impact on the payout of contingent consideration arrangements with a maximum cash payout of \$7.3 million as of September 30, 2014.

GROUPON, INC.  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)  
(unaudited)

The following tables summarize the Company's assets and liabilities that are measured at fair value on a recurring basis (in thousands):

Description	September 30, 2014	Fair Value Measurement at Reporting Date Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>Assets:</b>				
Cash equivalents	\$440,578	\$440,578	\$—	\$—
Available-for-sale securities:				
Convertible debt securities	2,030	—	—	2,030
Redeemable preferred shares	4,458	—	—	4,458
<b>Liabilities:</b>				
Contingent consideration	2,986	—	—	2,986
Description	December 31, 2013	Fair Value Measurement at Reporting Date Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>Assets:</b>				
Cash equivalents	\$585,514	\$585,514	\$—	\$—
Available-for-sale securities:				
Convertible debt securities	3,174	—	—	3,174
Redeemable preferred shares	—	—	—	—
<b>Liabilities:</b>				
Contingent consideration	606	—	—	606

## GROUPON, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

The following table provides a roll-forward of the fair value of recurring Level 3 fair value measurements for the three and nine months ended September 30, 2014 and 2013 (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
<b>Assets</b>				
Available-for-sale securities				
Convertible debt securities:				
Beginning Balance	\$2,630	\$3,233	\$3,174	\$3,087
Total gains (losses) included in other comprehensive income	740	(177	) 196	(31
Total (losses) gains included in other expense (income), net	(1,340	) —	(1,340	) —
Ending Balance	\$2,030	\$3,056	\$2,030	\$3,056
Unrealized (losses) gains still held <sup>(1)</sup>	\$(600	) \$(177	) \$(1,144	) \$(31
Redeemable preferred shares: <sup>(2)</sup>				
Beginning Balance	\$4,544	\$42,539	\$—	\$42,539
Purchase of redeemable preferred shares	—	—	4,599	—
Total (losses) gains included in other comprehensive income	(86	) —	(141	) —
Ending Balance	\$4,458	\$42,539	\$4,458	\$42,539
Unrealized (losses) gains still held <sup>(1)</sup>	\$(86	) \$—	\$(141	) \$—
<b>Liabilities</b>				
Contingent Consideration:				
Beginning Balance	\$4,006	\$6,854	\$606	\$7,601
Issuance of contingent consideration in connection with acquisitions	—	3,537	4,006	3,567
Settlements of contingent consideration liabilities	—	(750	) (424	) (780
Reclass to non-fair value liabilities when no longer contingent	—	—	(143	) —
Total (gains) losses included in earnings <sup>(3)</sup>	(1,020	) (1,529	) (1,059	) (2,276
Ending Balance	\$2,986	\$8,112	\$2,986	\$8,112
Unrealized (gains) losses still held <sup>(1)</sup>	\$(1,020	) \$(1,408	) \$(1,020	) \$(2,155

(1) Represents the unrealized losses or gains recorded in earnings and/or other comprehensive (loss) income during the period for assets and liabilities classified as Level 3 that are still held (or outstanding) at the end of the period.

For the three and nine months ended September 30, 2013, the Company's investments in Life Media Limited (F-tuan) preferred shares were previously classified as cost method investments and have been reclassified to the available-for-sale category in this table. The balance as of September 30, 2013 represents the Company's investments in F-tuan preferred shares, which were written down to zero through an other-than-temporary impairment charge as of December 31, 2013 and continue to have an estimated fair value of zero as of September 30, 2014. The \$4.5 million balance as of September 30, 2014 represents the Company's investment in the preferred shares of an online home services company during the three months ended March 31, 2014, as described in Note 4 "Investments."

(3) Changes in the fair value of contingent consideration liabilities are classified within "Acquisition-related (benefit) expense, net" on the condensed consolidated statements of operations.

Assets and Liabilities Measured at Fair Value on a Nonrecurring Basis

Certain assets and liabilities are measured at fair value on a nonrecurring basis, including assets that are written down to fair value as a result of an impairment. The Company did not record any significant nonrecurring fair value measurements after initial recognition during the three and nine months ended September 30, 2014 and 2013.

GROUPON, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

## Estimated Fair Value of Financial Assets and Liabilities Not Measured at Fair Value

The following table presents the carrying amounts and fair values of financial instruments that are not carried at fair value in the condensed consolidated financial statements (in thousands):

	September 30, 2014		December 31, 2013	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Cost method investments	\$15,920	\$16,037	\$15,788	\$15,573

The fair values of the Company's cost method investments were determined using the market approach or the income approach, depending on the availability of fair value inputs such as financial projections for the investees and market multiples for comparable companies. The Company has classified the fair value measurements of its cost method investments as Level 3 measurements within the fair value hierarchy because they involve significant unobservable inputs such as cash flow projections and discount rates.

The Company's other financial instruments not carried at fair value consist primarily of short term certificates of deposit, accounts receivable, restricted cash, accounts payable, accrued merchant and supplier payables and accrued expenses. The carrying values of these assets and liabilities approximate their respective fair values as of September 30, 2014 and December 31, 2013 due to their short term nature.

## 11. LOSS PER SHARE OF CLASS A AND CLASS B COMMON STOCK

The Company computes loss per share of Class A and Class B common stock using the two-class method. Basic loss per share is computed using the weighted-average number of common shares outstanding during the period. Diluted loss per share is computed using the weighted-average number of common shares and the effect of potentially dilutive equity awards outstanding during the period. Potentially dilutive securities consist of stock options, restricted stock units, unvested restricted stock awards, performance share units and ESPP shares. The dilutive effect of these equity awards are reflected in diluted loss per share by application of the treasury stock method. The computation of the diluted loss per share of Class A common stock assumes the conversion of Class B common stock, if dilutive, while the diluted loss per share of Class B common stock does not assume the conversion of those shares.

The rights, including the liquidation and dividend rights, of the holders of Class A and Class B common stock are identical, except with respect to voting. Under the two-class method, the undistributed earnings for each period are allocated based on the contractual participation rights of the Class A and Class B common shares as if the earnings for the period had been distributed. As the liquidation and dividend rights are identical, the undistributed earnings are allocated on a proportionate basis. Further, as the Company assumes the conversion of Class B common stock, if dilutive, in the computation of the diluted loss per share of Class A common stock, the undistributed earnings are equal to net income for that computation.

GROUPON, INC.  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)  
(unaudited)

The following table sets forth the computation of basic and diluted loss per share of Class A and Class B common stock for the three and nine months ended September 30, 2014 and 2013 (in thousands, except share amounts and per share amounts):

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2014		2013		2014		2013	
	Class A	Class B	Class A	Class B	Class A	Class B	Class A	Class B
Basic loss per share:								
Numerator								
Allocation of net loss	\$(18,950 )	\$(68 )	\$(1,287 )	\$(5 )	\$(75,035 )	\$(268 )	\$(10,049 )	\$(36 )
Less: Allocation of net income attributable to noncontrolling interests	2,182	8	1,283	5	6,552	23	4,046	15
Allocation of net loss attributable to common stockholders	\$(21,132 )	\$(76 )	\$(2,570 )	\$(10 )	\$(81,587 )	\$(291 )	\$(14,095 )	\$(51 )
Denominator								
Weighted-average common shares outstanding	667,126,548	2,399,976	664,032,872	2,399,976	673,414,559	2,399,976	660,131,591	2,399,976
Basic loss per share	\$(0.03 )	\$(0.03 )	\$(0.00 )	\$(0.00 )	\$(0.12 )	\$(0.12 )	\$(0.02 )	\$(0.02 )
Diluted loss per share:								
Numerator								
Allocation of net loss attributable to common stockholders	\$(21,132 )	\$(76 )	\$(2,570 )	\$(10 )	\$(81,587 )	\$(291 )	\$(14,095 )	\$(51 )
Reallocation of net income attributable to common stockholders as a result of conversion of Class B <sup>(1)</sup>	—	—	—	—	—	—	—	—
Allocation of net loss attributable to common stockholders	\$(21,132 )	\$(76 )	\$(2,570 )	\$(10 )	\$(81,587 )	\$(291 )	\$(14,095 )	\$(51 )
Denominator								
Weighted-average common shares outstanding used in	667,126,548	2,399,976	664,032,872	2,399,976	673,414,559	2,399,976	660,131,591	2,399,976

Edgar Filing: Groupon, Inc. - Form 10-Q

basic computation								
Conversion of Class B <sup>(1)</sup>	—	—	—	—	—	—	—	—
Employee stock options <sup>(1)</sup>	—	—	—	—	—	—	—	—
Restricted shares and RSUs <sup>(1)</sup>	—	—	—	—	—	—	—	—
Weighted-average diluted shares outstanding <sup>(1)</sup>	667,126,548	2,399,976	664,032,872	2,399,976	673,414,559	2,399,976	660,131,591	2,399,976
Diluted loss per share	\$ (0.03 )	\$ (0.03 )	\$ (0.00 )	\$ (0.00 )	\$ (0.12 )	\$ (0.12 )	\$ (0.02 )	\$ (0.02 )

Conversion of Class B shares into Class A shares and outstanding equity awards have not been reflected in the (1)diluted loss per share calculation for the three and nine months ended September 30, 2014 and 2013 because the effect would be antidilutive.

GROUPON, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

The following outstanding equity awards are not included in the diluted loss per share calculation above because they would have had an antidilutive effect:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Stock options	2,610,764	5,023,559	2,905,390	6,242,363
Restricted stock units	43,989,496	43,020,496	42,713,167	39,076,490
Restricted stock	36,988	217,005	58,718	357,339
ESPP shares	466,271	334,213	528,796	484,184
Total	47,103,519	48,595,273	46,206,071	46,160,376

In addition to the antidilutive awards as set forth in the table above, the Company also granted approximately 2,000,000 performance share units in connection with its acquisition of Ticket Monster during the nine months ended September 30, 2014. Contingently issuable shares are excluded from the computation of diluted EPS if, based on current period results, the shares would not be issuable if the end of the reporting period were the end of the contingency period. These outstanding performance share units have been excluded from the table above for the nine months ended September 30, 2014 as the performance conditions would not have been satisfied as of the end of the period.

## 12. SEGMENT INFORMATION

The company organizes its operations into three segments: North America, EMEA, which is comprised of Europe, Middle East and Africa, and the remainder of the Company's international operations ("Rest of World"). Segment operating results reflect earnings before stock-based compensation, acquisition-related (benefit) expense, net, other (expense) income, net and (benefit) provision for income taxes. Segment information reported in the tables below represents the operating segments of the Company organized in a manner consistent with which separate information is available and for which segment results are evaluated regularly by the Company's chief operating decision-maker in assessing performance and allocating resources.

## GROUPON, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

Revenue and profit or loss information by reportable segment reconciled to consolidated net loss for the three and nine months ended September 30, 2014 and 2013 were as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
North America				
Revenue <sup>(1)</sup>	\$418,494	\$360,838	\$1,273,487	\$1,077,574
Segment cost of revenue and operating expenses <sup>(2)</sup>	405,910	335,670	1,234,973	962,532
Segment operating income <sup>(2)</sup>	12,584	25,168	38,514	115,042
EMEA				
Revenue <sup>(1)</sup>	230,072	147,950	688,655	491,710
Segment cost of revenue and operating expenses <sup>(2)</sup>	207,643	132,346	619,594	417,222
Segment operating income <sup>(2)</sup>	22,429	15,604	69,061	74,488
Rest of World				
Revenue	108,488	86,271	304,125	235,924
Segment cost of revenue and operating expenses <sup>(2)</sup>	114,660	87,890	352,900	276,105
Segment operating loss <sup>(2)</sup>	(6,172)	(1,619)	(48,775)	(40,181)
Consolidated				
Revenue	757,054	595,059	2,266,267	1,805,208
Segment cost of revenue and operating expenses <sup>(2)</sup>	728,213	555,906	2,207,467	1,655,859
Segment operating income <sup>(2)</sup>	28,841	39,153	58,800	149,349
Stock-based compensation	34,574	26,870	89,958	89,223
Acquisition-related (benefit) expense, net	(304)	(1,529)	2,078	(2,276)
(Loss) income from operations	(5,429)	13,812	(33,236)	62,402
Other (expense) income, net	(20,023)	832	(21,886)	(9,830)
(Loss) income before (benefit) provision for income taxes	(25,452)	14,644	(55,122)	52,572
(Benefit) provision for income taxes	(6,434)	15,936	20,181	62,657
Net loss	\$(19,018)	\$(1,292)	\$(75,303)	\$(10,085)

North America includes revenue from the United States of \$409.3 million and \$349.1 million for the three months ended September 30, 2014 and 2013, respectively, and \$1,242.4 million and \$1,039.7 million for the nine months ended September 30, 2014 and 2013, respectively. Beginning in September 2013, direct revenue transactions in the EMEA Goods category have been transacted through a Switzerland-based subsidiary. As a result, EMEA includes revenue from Switzerland of \$117.7 million and \$312.0 million for the three and nine months ended September 30, 2014, respectively.

Segment cost of revenue and operating expenses and segment operating income (loss) exclude stock-based compensation and acquisition-related (benefit) expense, net. This presentation corresponds to the measure of segment profit or loss that the Company's chief operating decision-maker uses in assessing segment performance and making resource allocation decisions. The following table summarizes the Company's stock-based compensation expense and acquisition-related (benefit) expense, net by reportable segment for the three and nine months ended September 30, 2014 and 2013 (in thousands):

Three Months Ended September 30,				Nine Months Ended September 30,			
2014		2013		2014		2013	
Stock-based compensation	Acquisition-related	Stock-based compensation	Acquisition-related	Stock-based compensation	Acquisition-related	Stock-based compensation	Acquisition-related
\$28,493	\$ (304)	\$21,082	\$ (984)	\$74,179	\$ 1,934	\$69,494	\$ (1,364)

Edgar Filing: Groupon, Inc. - Form 10-Q

North America									
EMEA	2,687	—	2,616	(545 )	7,187	144	9,082	(912 )	
Rest of World	3,394	—	3,172	—	8,592	—	10,647	—	
Consolidated	\$34,574	\$ (304 )	\$26,870	\$ (1,529 )	\$89,958	\$ 2,078	\$89,223	\$ (2,276 )	

32

---

## GROUPON, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

Acquisition-related (benefit) expense, net for the North America segment includes external transaction costs and gains and losses relating to contingent consideration obligations incurred by U.S. legal entities relating to purchases of businesses that became part of the EMEA and Rest of World segments, which is consistent with the attribution used for internal reporting purposes.

The following table summarizes the Company's total assets by reportable segment as of September 30, 2014 and December 31, 2013 (in thousands):

	September 30, 2014	December 31, 2013
North America <sup>(1)</sup>	\$978,814	\$1,267,158
EMEA	543,257	616,126
Rest of World <sup>(1)</sup>	550,094	158,726
Consolidated total assets	\$2,072,165	\$2,042,010

North America contains assets from the United States of \$940.8 million and \$1,231.3 million as of September 30, 2014 and December 31, 2013, respectively. Rest of World contains assets from the Republic of Korea, including (1) those assets acquired as a part of our acquisition of Ticket Monster described in Note 2 "Business Combinations," of \$395.0 million as of September 30, 2014. There were no other individual countries that represented more than 10% of consolidated total assets as of September 30, 2014 and December 31, 2013, respectively.

## Category Information

The Company offers goods and services through three primary categories: Local Deals ("Local"), Groupon Goods ("Goods") and Groupon Getaways ("Travel"). The Company also earns advertising revenue, payment processing revenue, point of sale revenue, reservation revenue and commission revenue. Revenue and gross profit from these other sources were previously considered to be distinct from our primary categories and were aggregated with revenue and gross profit from Travel, our smallest category. In recent periods, these other revenue sources have been increasingly viewed by management as a component of the Local category, as they are primarily generated through the Company's relationships with local and national merchants. Accordingly, the Company updated its presentation of category information, effective beginning with the quarter ended March 31, 2014, to include other revenue and gross profit within the Local category in the tables below, and the prior period category information has been retrospectively adjusted to conform to the current period presentation.

The following table summarizes the Company's third party and other and direct revenue by category for its three reportable segments for the three months ended September 30, 2014 and 2013 (in thousands):

	North America		EMEA		Rest of World		Consolidated	
	Three Months Ended September 30, 2014	Three Months Ended September 30, 2013	Three Months Ended September 30, 2014	Three Months Ended September 30, 2013	Three Months Ended September 30, 2014	Three Months Ended September 30, 2013	Three Months Ended September 30, 2014	Three Months Ended September 30, 2013
Local <sup>(1)</sup> :								
Third party and other	\$161,912	\$161,306	\$90,002	\$92,141	\$45,085	\$51,900	\$296,999	\$305,347
Direct	—	1,040	—	—	—	—	—	1,040
Total	161,912	162,346	90,002	92,141	45,085	51,900	296,999	306,387
Goods:								
Third party	1,139	3,999	14,750	32,008	37,814	17,215	53,703	53,222
Direct	237,816	181,915	108,360	9,271	11,075	7,846	357,251	199,032
Total	238,955	185,914	123,110	41,279	48,889	25,061	410,954	252,254
Travel:								
Third party	17,627	12,578	16,960	14,530	14,514	9,310	49,101	36,418

Edgar Filing: Groupon, Inc. - Form 10-Q

Total revenue           \$418,494   \$360,838   \$230,072   \$147,950   \$108,488   \$86,271   \$757,054   \$595,059

(1) Includes revenue from deals with local merchants, from deals with national merchants, and through local events.

## GROUPON, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

The following table summarizes the Company's third party and other and direct revenue by category for its three reportable segments for the nine months ended September 30, 2014 and 2013 (in thousands):

	North America		EMEA		Rest of World		Consolidated	
	Nine Months Ended September 30,		Nine Months Ended September 30,		Nine Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013	2014	2013	2014	2013
Local <sup>(1)</sup> :								
Third party and other	\$503,659	\$510,284	\$295,607	\$313,959	\$131,610	\$141,163	\$930,876	\$965,406
Direct	—	1,733	—	—	—	—	—	1,733
Total	503,659	512,017	295,607	313,959	131,610	141,163	930,876	967,139
Goods:								
Third party	3,859	11,794	49,070	110,821	112,686	50,262	165,615	172,877
Direct	714,157	511,357	296,342	18,903	23,595	20,249	1,034,094	550,509
Total	718,016	523,151	345,412	129,724	136,281	70,511	1,199,709	723,386
Travel:								
Third party	51,812	42,406	47,636	48,027	36,234	24,250	135,682	114,683

Total revenue \$1,273,487 \$1,077,574 \$688,655 \$491,710 \$304,125 \$235,924 \$2,266,267 \$1,805,208

(1) Includes revenue from deals with local merchants, from deals with national merchants, and through local events.

The following table summarizes the Company's gross profit by category for its three reportable segments for the three months ended September 30, 2014 and 2013 (in thousands):

	North America		EMEA		Rest of World		Consolidated	
	Three Months Ended September 30,		Three Months Ended September 30,		Three Months Ended September 30,		Three Months Ended September 30,	
	2014	2013	2014	2013	2014	2013	2014	2013
Local <sup>(1)</sup> :								
Third party and other	\$138,189	\$139,737	\$83,956	\$81,808	\$38,592	\$44,435	\$260,737	\$265,980
Direct	—	(847 )	—	—	—	—	—	(847 )
Total	138,189	138,890	83,956	81,808	38,592	44,435	260,737	265,133
Goods:								
Third party	951	3,519	12,307	28,036	23,986	11,530	37,244	43,085
Direct	23,002	18,090	19,945	907	(1,109 )	486	41,838	19,483
Total	23,953	21,609	32,252	28,943	22,877	12,016	79,082	62,568
Travel:								
Third party	14,000	11,070	15,440	12,930	10,885	7,921	40,325	31,921

Total gross profit \$176,142 \$171,569 \$131,648 \$123,681 \$72,354 \$64,372 \$380,144 \$359,622

(1) Includes gross profit from deals with local merchants, from deals with national merchants, and through local events.



## GROUPON, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

The following table summarizes the Company's gross profit by category for its three reportable segments for the nine months ended September 30, 2014 and 2013 (in thousands):

	North America		EMEA		Rest of World		Consolidated	
	Nine Months Ended September 30,		Nine Months Ended September 30,		Nine Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013	2014	2013	2014	2013
Local <sup>(1)</sup> :								
Third party and other	\$433,485	\$441,787	\$274,395	\$278,515	\$108,958	\$119,810	\$816,838	\$840,112
Direct	—	(790 )	—	—	—	—	—	(790 )
Total	433,485	440,997	274,395	278,515	108,958	119,810	816,838	839,322
Goods:								
Third party	3,239	10,317	43,019	96,264	72,101	27,507	118,359	134,088
Direct	56,279	50,725	51,967	(239 )	(2,466 )	187	105,780	50,673
Total	59,518	61,042	94,986	96,025	69,635	27,694	224,139	184,761
Travel:								
Third party	42,807	36,472	44,003	42,393	27,940	20,377	114,750	99,242
Total gross profit	\$535,810	\$538,511	\$413,384	\$416,933	\$206,533	\$167,881	\$1,155,727	\$1,123,325

(1) Includes gross profit from deals with local merchants, from deals with national merchants, and through local events.

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis of our financial condition and results of operations should be read together with our condensed consolidated financial statements and related notes included under Part I, Item 1 of this Quarterly Report on Form 10-Q. This discussion contains forward-looking statements about our business and operations. Our actual results may differ materially from those we currently anticipate as a result of many factors, including those we describe under "Risk Factors" and elsewhere in this Quarterly Report.

### Overview

Groupon operates online local commerce marketplaces throughout the world that connect merchants to consumers by offering goods and services at a discount. Traditionally, local merchants have tried to reach consumers and generate sales through a variety of methods, including online advertising, the yellow pages, direct mail, newspaper, radio, television, and promotions. By bringing the brick and mortar world of local commerce onto the Internet, Groupon is helping local merchants to attract customers and sell goods and services. We provide consumers with savings and help them discover what to do, eat, see, buy and where to travel.

Current and potential customers are able to access our deal offerings directly through our websites and mobile applications. We also send emails to our subscribers each day with deal offerings that are targeted by location and personal preferences. We offer deals in three primary categories: Local Deals ("Local"), Groupon Goods ("Goods") and Groupon Getaways ("Travel"). In our Goods category, through which we offer deals on merchandise, we often act as the merchant of record, particularly for deals in North America and for deals in EMEA, which is comprised of Europe, Middle East and Africa, beginning in September 2013. Our revenue from deals where we act as the third party marketing agent is the purchase price paid by the customer for a Groupon voucher ("Groupon") less an agreed upon portion of the purchase price paid to the featured merchants, excluding applicable taxes and net of estimated refunds for which the merchant's share is recoverable. Our direct revenue from deals where we act as the merchant of record is the purchase price paid by the customer, excluding applicable taxes and net of estimated refunds. We generated revenue of \$757.1 million during the three months ended September 30, 2014, as compared to \$595.1 million during the three months ended September 30, 2013. We generated revenue of \$2,266.3 million during the nine months ended September 30, 2014, as compared to \$1,805.2 million during the nine months ended September 30, 2013.

Our operations are organized into three segments: North America, EMEA and the remainder of our international operations ("Rest of World"). See Note 12 "Segment Information" for further information. For the three months ended September 30, 2014, we derived 55.3% of our revenue from our North America segment, 30.4% of our revenue from our EMEA segment and 14.3% of our revenue from our Rest of World segment. For the nine months ended September 30, 2014, we derived 56.2% of our revenue from our North America segment, 30.4% of our revenue from our EMEA segment and 13.4% of our revenue from our Rest of World segment.

We have an accumulated deficit of \$930.7 million as of September 30, 2014. Since our inception, we have made substantial investments in infrastructure and marketing to increase subscriber acquisition and customer activation. In particular, our significant net losses have been driven in part by the rapid expansion of our EMEA and Rest of World segments, which involved investing heavily in upfront marketing, sales and infrastructure related to the build-out of our operations in early stage countries.

On January 2, 2014, we acquired all of the outstanding equity interests of LivingSocial Korea, Inc., including its subsidiary Ticket Monster Inc. ("Ticket Monster"), for an aggregate acquisition price of \$259.4 million, after closing working capital adjustments, of which \$96.5 million was paid in cash and the balance was paid in our Class A common stock. Ticket Monster is an e-commerce company based in the Republic of Korea that connects merchants to consumers by offering goods and services at a discount. The operations of Ticket Monster are reported within our Rest of World segment for the three and nine months ended September 30, 2014. On January 13, 2014, we acquired all of the outstanding equity interests of Ideeli, Inc. (d/b/a "Ideel"), a fashion flash site based in the United States, for an aggregate acquisition price of \$42.7 million in cash. Ideel is focused on women's fashion apparel, accessories and home decor, and the operations of Ideel are reported within our North America segment for the three and nine months ended September 30, 2014.

We have hired advisers to help us explore a range of financing and strategic alternatives for Ticket Monster and certain other markets in our Rest of World segment that would enable us to enhance value for our stockholders.

However, we cannot provide any assurance as to the likelihood, timetable or type of transaction.

## How We Measure Our Business

We measure our business with several financial and operating metrics. We use these metrics to assess the progress of our business, make decisions on where to allocate capital, time and technology investments and assess the long-term performance of our marketplaces. Certain of the financial metrics are reported in accordance with U.S. generally accepted accounting principles ("U.S. GAAP") and certain of these metrics are considered non-GAAP financial measures. As our business evolves, we may make changes to our key financial and operating metrics used to measure our business in future periods. For further information and a reconciliation to the most applicable financial measure under U.S. GAAP, refer to our discussion under Non-GAAP Financial Measures in the "Results of Operations" section.

### Financial Metrics

**Gross billings.** This metric represents the total dollar value of customer purchases of goods and services, excluding applicable taxes and net of estimated refunds. For third party revenue deals, gross billings differs from third party revenue reported in our consolidated statements of operations, which is presented net of the merchant's share of the transaction price. For direct revenue deals, gross billings are equivalent to direct revenue reported in our consolidated statements of operations. We consider this metric to be an important indicator of our growth and business performance as it is a proxy for the dollar volume of transactions generated through our marketplaces. Tracking gross billings on third party revenue deals also allows us to track changes in the percentage of gross billings that we are able to retain after payments to our merchants.

**Revenue.** Third party revenue is derived from deals where we act as the marketing agent and is the purchase price paid by the customer less an agreed upon portion of the purchase price paid to the featured merchant, excluding applicable taxes and net of estimated refunds for which the merchant's share is recoverable. Direct revenue, when the Company is selling the product as the merchant of record, is the purchase price paid by the customer, excluding applicable taxes and net of estimated refunds.

**Gross profit.** Gross profit reflects the net margin earned after deducting our cost of revenue from our revenue. Due to the lack of comparability between third party revenue, which is presented net of the merchant's share of the transaction price, and direct revenue, which is reported on a gross basis, we believe that gross profit is an important measure for evaluating our performance.

**Adjusted EBITDA.** Adjusted EBITDA is a non-GAAP financial measure that comprises net income (loss) excluding income taxes, interest and other non-operating items, depreciation and amortization, stock-based compensation and acquisition-related (benefit) expense, net. We exclude stock-based compensation expense and depreciation and amortization because they are primarily non-cash in nature, and we believe that non-GAAP financial measures excluding these items provide meaningful supplemental information about our operating performance and liquidity. Acquisition-related (benefit) expense, net is comprised of the change in the fair value of contingent consideration arrangements and external transaction costs related to business combinations, primarily consisting of legal and advisory fees. Our definition of Adjusted EBITDA may differ from similar measures used by other companies, even when similar terms are used to identify such measures. We believe that Adjusted EBITDA is a meaningful measure for evaluating our operating performance. For further information and a reconciliation to the most applicable financial measure under U.S. GAAP, refer to our discussion under Non-GAAP Financial Measures in the "Results of Operations" section.

**Free cash flow.** Free cash flow is a non-GAAP financial measure that comprises net cash (used in) provided by operating activities less purchases of property and equipment and capitalized software. We use free cash flow, and ratios based on it, to conduct and evaluate our business because, although it is similar to cash flow from operations, we believe that it typically represents a more useful measure of cash flows because purchases of fixed assets, software developed for internal use and website development costs are necessary components of our ongoing operations. Free cash flow is not intended to represent the total increase or decrease in our cash balance for the applicable period. For further information and a reconciliation to the most applicable financial measure under U.S. GAAP, refer to our discussion under Non-GAAP Financial Measures in the "Results of Operations" section.

The following table presents the above Financial Metrics for the three and nine months ended September 30, 2014 and 2013 (in thousands):



	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Gross billings	\$1,860,735	\$1,342,648	\$5,496,992	\$4,164,223
Revenue	757,054	595,059	2,266,267	1,805,208
Gross profit	380,144	359,622	1,155,727	1,123,325
Adjusted EBITDA	66,987	62,302	166,344	214,666
Free cash flow	25,413	(26,969)	(65,459)	(3,417)

#### Operating Metrics

**Active customers.** We define active customers as unique user accounts that have purchased a voucher or product from us during the trailing twelve months. We consider this metric to be an important indicator of our business performance as it helps us to understand how the number of customers actively purchasing our deals is trending.

**Gross billings per average active customer.** This metric represents the trailing twelve months gross billings generated per average active customer. This metric is calculated as the total gross billings generated in the trailing twelve months, divided by the average number of active customers in such time period. Although we believe total gross billings, not trailing twelve months gross billings per average active customer, is a better indication of the overall growth of our marketplaces over time, trailing twelve months gross billings per average active customer provides an opportunity to evaluate whether our growth is primarily driven by growth in total customers or in spend per customer in any given period.

**Units.** This metric represents the number of vouchers and products purchased from us by our customers, before refunds and cancellations. We consider unit growth to be an important indicator of the total volume of business conducted through our marketplaces.

Our Active customers and Gross billings per average active customer for the trailing twelve months ("TTM") ended September 30, 2014 and 2013 were as follows:

	Trailing twelve months ended September 30,	
	2014	2013 <sup>(1)</sup>
TTM Active customers (in thousands)	52,750	42,566
TTM Gross billings per average active customer	\$148.77	\$139.03

TTM active customers for the period ended September 30, 2013 has been reduced from 43.5 million active customers previously reported to 42.6 million to correct that operational information. This correction increased (1) TTM gross billings per average active customer for the period ended September 30, 2013 from \$136.99 previously reported to \$139.03.

The increase in active customers for the trailing twelve months ended September 30, 2014, as compared to the prior year period, was primarily attributable to the acquisitions of Ticket Monster and Ideel.

Our Units for the three and nine months ended September 30, 2014 and 2013 were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Units (in thousands)	88,192	45,862	254,698	137,433

The increase in units for the three and nine months ended September 30, 2014, as compared to the prior year period, was primarily attributable to the acquisitions of Ticket Monster and Ideel.

#### Factors Affecting Our Performance

**Deal sourcing and quality.** We consider our merchant relationships to be a vital part of our business model and have made significant investments in order to expand the variety of tools that we can provide to our merchants. We depend on our ability to attract and retain merchants that are prepared to offer products or services on compelling terms, particularly as we attempt to expand our product and service offerings in order to create more complete online marketplaces for local commerce. In North

America and many of our foreign markets, we offer deals in which the merchant has a continuous presence on our websites and mobile applications by offering vouchers on an ongoing basis for an extended period of time. Currently, a substantial majority of our merchants in North America elect to offer deals in this manner, and we expect that trend to continue. These marketplaces, which we refer to as "pull" marketplaces, enable customers to search for specific types of deals on our websites and mobile applications. However, merchants have the ability to withdraw their extended deal offerings, and we generally do not have noncancelable long-term arrangements to guarantee availability of deals. In order to attract merchants that may not have run deals on our platform or would have run deals on a competing platform, we have periodically been willing to accept lower deal margins across all three of our segments and we expect that trend to continue. This has contributed to lower deal margins during the three and nine months ended September 30, 2014, as compared to the prior year period. If new merchants do not find our marketing and promotional services effective, or if our existing merchants do not believe that utilizing our services provides them with a long-term increase in customers, revenue or profit, they may stop making offers through our marketplaces or they may only continue offering deals if we accept lower margins.

**International operations.** Our international operations represent a substantial portion of our business and have increased as a percentage of our total revenue. For the three months ended September 30, 2014 and 2013, 30.4% and 24.9% of our revenue was generated from our EMEA segment, respectively, and 14.3% and 14.5% of our revenue was generated from our Rest of World segment, respectively. For the nine months ended September 30, 2014 and 2013, 30.4% and 27.2% of our revenue was generated from our EMEA segment, respectively, and 13.4% and 13.1% of our revenue was generated from our Rest of World segment, respectively. Operating a global business requires management attention and resources and requires us to localize our services to conform to a wide variety of local cultures, business practices, laws and regulations. The different commercial and regulatory environments in other countries may make it more difficult for us to successfully operate our business. In addition, many of the automation tools and technology enhancements that we have implemented in our North America segment are close to being fully implemented in most EMEA countries but have not been substantially rolled out to the countries in our Rest of World segment. Revenue from our EMEA segment increased for the three and nine months ended September 30, 2014, as compared to the prior year period, and the percentage of total revenue generated by our EMEA segment increased on a year-over-year basis. Revenue from our Rest of World segment increased for the three and nine months ended September 30, 2014, as compared to the prior year period. On a year-over-year basis, the percentage of total revenue generated by our Rest of World segment increased for the nine months ended September 30, 2014 and decreased for the three months ended September 30, 2014. Revenue from our North America segment increased for the three and nine months ended September 30, 2014, as compared to the prior year period, and the percentage of total revenue generated by our North America segment decreased on a year-over-year basis. The decrease in North America revenue as a percentage of total revenue was primarily due to the increase in direct revenue transactions from our Groupon Goods business in EMEA, as direct revenue is presented on a gross basis in our consolidated statements of operations.

**Marketing activities.** We must continue to acquire and retain customers in order to increase revenue and attempt to achieve profitability. If consumers do not perceive our Groupon offerings to be attractive, or if we fail to introduce new or more relevant deals, we may not be able to acquire or retain customers. In addition, as we build-out more complete marketplaces, our success will depend on our ability to increase consumer awareness of deals available through those marketplaces. As discussed under "Components of Results of Operations," we consider order discounts, free shipping on qualifying merchandise sales and reducing margins on our deals to be marketing-related activities, even though these activities are not presented as marketing expenses in our consolidated statements of operations. We have, and expect to continue to, reduce our deal margins when we believe that by doing so we can offer our customers a product or service from a merchant who might not have otherwise been willing to conduct business through our marketplaces. We use this as a marketing tool because we believe that in some instances this is an effective method of retaining or activating a customer, as compared to other methods of retention or activation, such as traditional advertising or discounts.

**Investment in growth.** We have aggressively invested, and intend to continue to invest, in our products and infrastructure to support our growth. We anticipate that we will make substantial investments in the foreseeable future as we continue to increase the number and variety of deals we offer each day, broaden our customer base, expand our

marketing channels, expand our operations, hire additional employees and develop our technology. Additionally, we believe that our efforts to automate our internal processes through investments in technology should allow us to improve our cost structure over time, as we are able to more efficiently run our business and minimize manual processes.

We recently announced the launch of an iPad®-based platform for merchants, which we refer to as "Gnome," that will streamline the voucher redemption process. Gnome can also be used in connection with our credit card payment processing service. In addition, we have begun to add additional content about local merchants to our websites and mobile applications, including merchants who have not offered deals through our marketplace. This new content, which we refer to as "Pages," is intended to provide customers with the ability to discover more local businesses and deal offerings through our websites and mobile applications. While we believe that both of these initiatives will contribute to the future success of our business, we do not expect that they will generate a material amount of revenue in the near term.

Competitive pressure. A substantial number of companies that attempt to replicate our business model have emerged around the world. In addition to such competitors, we expect to increasingly compete against other large Internet and technology based businesses that have launched initiatives which are directly competitive to our core business, our other merchant offerings such as payment processing and point of sale, and other initiatives such as Gnome and Pages. We also expect to compete against other Internet sites that are focused on specific communities or interests and offer coupons or discount arrangements related to such communities or interests. Increased competition in the future may adversely impact our gross billings, revenue and profit margins.

Growth of Groupon Goods. Our Groupon Goods category has experienced significant revenue growth in recent periods. This category has lower margins than our Local category, primarily as a result of shipping and fulfillment costs related to direct revenue transactions. The percentage of revenue generated from our Goods category was 54.3% and 42.4% for the three months ended September 30, 2014 and 2013, respectively, and 52.9% and 40.1% for the nine months ended September 30, 2014 and 2013, respectively. We are often the merchant of record for transactions in our Goods category, particularly in North America and also in EMEA beginning in September 2013, such that the resulting direct revenue is reported on a gross basis in our consolidated statements of operations. Growth in direct revenue results in a smaller increase to income and cash flows than growth in third party revenue because direct revenue includes the entire amount of gross billings, before deducting the cost of the related inventory, while third party revenue is net of the merchant's share of the transaction price. Gross profit as a percentage of revenue on direct revenue transactions in our Goods category was 11.7% and 10.2% for the three and nine months ended September 30, 2014, respectively. As direct revenue transactions in our Goods category have become a larger component of our overall business in recent periods, the significant revenue growth generated by those transactions has not resulted in comparable growth in gross profit, operating income or cash flows.

#### Components of Results of Operations

##### Third Party and Other Revenue

Third party revenue arises from transactions in which we are acting as a third party marketing agent and consists of the net amount we retain from the sale of Groupons after paying an agreed upon portion of the purchase price to the featured merchant, excluding applicable taxes and net of estimated refunds for which the merchant's share is recoverable. Other revenue primarily consists of advertising revenue, payment processing revenue, point of sale revenue and commission revenue.

##### Direct Revenue

Direct revenue arises from transactions, primarily in our Goods category, in which we are the merchant of record and consists of the gross amount we receive from the customer, excluding applicable taxes and net of estimated refunds.

##### Cost of Revenue

Cost of revenue is comprised of direct and certain indirect costs incurred to generate revenue. For direct revenue transactions, cost of revenue includes the cost of inventory, shipping and fulfillment costs and inventory markdowns. Fulfillment costs are comprised of third party logistics provider costs, as well as rent, depreciation, personnel costs and other costs of operating our own fulfillment center, which began operations in the fourth quarter of 2013. For third party revenue transactions, cost of revenue includes estimated refunds for which the merchant's share is not recoverable. Other costs incurred to generate revenue, which include credit card processing fees, editorial costs, certain technology costs, web hosting, and other processing fees, are allocated to cost of third party revenue, direct revenue and other revenue in proportion to gross billings during the period.

Technology costs within cost of revenue include the payroll and stock based compensation expense related to the Company's technology support personnel who are responsible for operating and maintaining the infrastructure of the Company's websites. Technology costs within cost of revenue also include a portion of amortization expense from internal-use software, primarily related to website development. Other technology-related costs within cost of revenue include email distribution costs. Editorial costs included in cost of revenue consist of payroll and stock based compensation expense related to the Company's editorial personnel, as these staff members are primarily dedicated to drafting and promoting deals.

##### Marketing

Marketing expense consists primarily of targeted online marketing costs, such as sponsored search, advertising on social networking sites, email marketing campaigns, affiliate programs and, to a lesser extent, offline marketing costs such as television,

radio and print advertising. Additionally, marketing payroll and stock based compensation expense are classified as marketing expense. We record these costs within "Marketing" on the consolidated statements of operations when incurred. From time to time, we offer deals with well-known national merchants for subscriber acquisition and customer activation purposes, for which the amount we owe the merchant for each voucher sold exceeds the transaction price paid by the customer. Our gross billings from those transactions generate no third party revenue and our net cost (i.e., the excess of the amount owed to the merchant over the amount paid by the customer) is classified as marketing expense. Our marketing activities also include elements that are not presented as "Marketing" on our consolidated statements of operations, such as order discounts, free shipping on qualifying merchandise sales and accepting lower margins on our deals. Marketing is the primary method by which we acquire customers and, as such, is a critical part of our growth strategy.

#### Selling, General and Administrative

Selling expenses reported within "Selling, general and administrative" on the consolidated statements of operations consist of payroll, stock-based compensation expense and sales commissions for sales representatives, as well as costs associated with supporting the sales function such as technology, telecommunications and travel. General and administrative expenses consist of payroll and stock-based compensation expense for employees involved in general corporate functions, including accounting, finance, tax, legal and human resources, among others. Additional costs included in general and administrative include customer service and operations, depreciation and amortization, rent, professional fees, litigation costs, travel and entertainment, charitable contributions, recruiting, office supplies, maintenance, certain technology costs and other general corporate costs.

#### Acquisition Related (Benefit) Expense, Net

Acquisition-related (benefit) expense, net includes the change in the fair value of contingent consideration arrangements related to business combinations. See Note 10 "Fair Value Measurements." For the three and nine months ended September 30, 2014, acquisition-related (benefit) expense, net also includes external transaction costs related to business combinations, primarily consisting of legal and advisory fees.

#### Other (Expense) Income, Net

Other (expense) income, net includes interest income on our cash and cash equivalents, interest expense on capital leases and the revolving credit agreement, impairment of investments, gains and losses on equity method investments and foreign currency transaction gains and losses, primarily resulting from intercompany balances with our subsidiaries that are denominated in foreign currencies.

Edgar Filing: Groupon, Inc. - Form 10-Q

Results of Operations

Comparison of the Three Months Ended September 30, 2014 and 2013:

	Three Months Ended September 30,	
	2014	2013
	(in thousands)	
Revenue:		
Third party and other	\$ 399,803	\$ 394,987
Direct	357,251	200,072
Total revenue	757,054	595,059
Cost of revenue:		
Third party and other	61,497	54,001
Direct	315,413	181,436
Total cost of revenue	376,910	235,437
Gross profit	380,144	359,622
Operating expenses:		
Marketing	59,935	53,265
Selling, general and administrative	325,942	294,074
Acquisition-related (benefit) expense, net	(304)	) (1,529)
Total operating expenses	385,573	345,810
(Loss) income from operations	(5,429)	) 13,812
Other (expense) income, net	(20,023)	) 832
(Loss) income before (benefit) provision for income taxes	(25,452)	) 14,644
(Benefit) provision for income taxes	(6,434)	) 15,936
Net loss	(19,018)	) (1,292)
Net income attributable to noncontrolling interests	(2,190)	) (1,288)
Net loss attributable to Groupon, Inc.	\$(21,208)	) \$(2,580)



Classification of stock-based compensation within cost of revenue and operating expenses

Cost of revenue and operating expenses include stock-based compensation as follows:

	Three Months Ended September 30, 2014		2013	
	Statement of Operations line item  (in thousands)	Stock-based compensation included in line item	Statement of Operations line item	Stock-based compensation included in line item
Total cost of revenue	\$376,910	\$1,181	\$235,437	\$386
Operating expenses:				
Marketing	\$59,935	\$2,505	\$53,265	\$2,512
Selling, general and administrative	325,942	30,888	294,074	23,972
Acquisition-related (benefit) expense, net	(304 )	—	(1,529 )	—
Total operating expenses	\$385,573	\$33,393	\$345,810	\$26,484

Foreign exchange rate neutral operating results

The effect on our gross billings, revenue, cost of revenue and operating expenses, and loss from operations for the three months ended September 30, 2014 from changes in exchange rates versus the U.S. dollar was as follows:

	Three Months Ended September 30, 2014		
	At Avg. Q3 2013 Rates <sup>(1)</sup> (in thousands)	Exchange Rate Effect <sup>(2)</sup>	As Reported
Gross billings	\$1,840,983	\$19,752	\$1,860,735
Revenue	\$756,712	\$342	\$757,054
Cost of revenue and operating expenses	761,982	501	762,483
Loss from operations	\$(5,270 )	\$(159 )	\$(5,429 )

(1) Represents the financial statement balances that would have resulted had exchange rates in the reporting period been the same as those in effect in the comparable prior year period.

(2) Represents the increase or decrease in reported amounts resulting from changes in exchange rates from those in effect in the comparable prior year period.

Gross Billings

Gross billings represents the total dollar value of customer purchases of goods and services, excluding applicable taxes and net of estimated refunds. Gross billings for the three months ended September 30, 2014 and 2013 were as follows:

	Three Months Ended September 30, 2014		2013	
	(in thousands)			
Gross billings:				
Third party	\$1,496,663		\$1,138,373	
Direct	357,251		200,072	
Other	6,821		4,203	
Total gross billings	\$1,860,735		\$1,342,648	

For third party revenue deals, gross billings differs from third party revenue reported in our consolidated statements of operations, which is presented net of the merchant's share of the transaction price. For direct revenue deals and other revenue, gross billings are equivalent to direct revenue and other revenue reported in our consolidated statements of operations. Gross billings increased by \$518.1 million to \$1,860.7 million for the three months ended September 30, 2014, as compared to \$1,342.6 million for the three months ended September 30, 2013, primarily due to the acquisition of Ticket Monster which contributed \$370.3 million in gross billings for the three months ended September 30, 2014. The increase was comprised of a \$358.3 million increase in gross billings from third party revenue transactions and a \$157.2 million increase in gross billings from direct revenue transactions. The increase in gross billings was driven by an increase in active customers and the volume of transactions, as we have continued to build our marketplaces and increase our offerings to customers. The favorable impact on gross billings from year-over-year changes in foreign exchange rates for the three months ended September 30, 2014 was \$19.8 million. We offer goods and services through three primary categories: Local, Goods and Travel within our North America, EMEA and Rest of World segments. We also earn advertising revenue, payment processing revenue, point of sale revenue and commission revenue. Gross billings, revenue, cost of revenue and gross profit from these other sources were previously considered to be distinct from our primary categories and were aggregated with gross billings, revenue, cost of revenue and gross profit from Travel, our smallest category. In recent periods, these other revenue sources have been increasingly viewed by management as a component of the Local category, as they are primarily generated through our relationships with local and national merchants. Accordingly, we updated our presentation of category information, effective beginning with the quarter ended March 31, 2014, to include other gross billings, revenue, cost of revenue and gross profit within the Local category in the tables below, and the prior period category information has been retrospectively adjusted to conform to the current period presentation. The increase in our gross billings was comprised of a \$279.7 million increase in our Goods category, a \$123.0 million increase in our Local category and a \$115.4 million increase in our Travel category.

#### Gross Billings by Segment

Gross billings by segment for the three months ended September 30, 2014 and 2013 were as follows:

	Three Months Ended September 30,		2013	% of total	
	2014	% of total			
	(dollars in thousands)				
Gross billings:					
North America	\$774,286	41.6	% \$664,999	49.5	%
EMEA	489,423	26.3	443,318	33.0	
Rest of World	597,026	32.1	234,331	17.5	
Total gross billings	\$1,860,735	100.0	% \$1,342,648	100.0	%

Edgar Filing: Groupon, Inc. - Form 10-Q

Gross billings by category and segment for the three months ended September 30, 2014 and 2013 were as follows (in thousands):

	North America		EMEA		Rest of World		Consolidated	
	Three Months Ended September 30,		Three Months Ended September 30,		Three Months Ended September 30,		Three Months Ended September 30,	
	2014	2013	2014	2013	2014	2013	2014	2013
Local <sup>(1)</sup> :								
Third party and other <sup>(2)</sup>	\$446,573	\$404,873	\$218,615	\$207,803	\$190,254	\$118,718	\$855,442	\$731,394
Direct	—	1,040	—	—	—	—	—	1,040
Total	446,573	405,913	218,615	207,803	190,254	118,718	855,442	732,434
Goods:								
Third party	5,077	12,650	82,646	160,578	278,135	71,127	365,858	244,355
Direct	237,816	181,915	108,360	9,271	11,075	7,846	357,251	199,032
Total	242,893	194,565	191,006	169,849	289,210	78,973	723,109	443,387
Travel:								
Third party <sup>(2)</sup>	84,820	64,521	79,802	65,666	117,562	36,640	282,184	166,827
Total gross billings	\$774,286	\$664,999	\$489,423	\$443,318	\$597,026	\$234,331	\$1,860,735	\$1,342,648

(1) Includes gross billings from deals with local merchants, from deals with national merchants, and through local events.

During the three months ended March 31, 2014, the Company began classifying other gross billings as a (2) component of the Local category. Other gross billings were previously aggregated with the Travel category. The prior period category information has been retrospectively adjusted to conform to the current period presentation.

North America

North America segment gross billings increased by \$109.3 million to \$774.3 million for the three months ended September 30, 2014, as compared to \$665.0 million for the three months ended September 30, 2013. The increase in gross billings includes a \$48.3 million increase in our Goods category, which included \$20.6 million of gross billings from our Ideel acquisition. The increase in gross billings also includes a \$40.7 million increase in our Local category and a \$20.3 million increase in our Travel category. The increase in gross billings in the North America segment resulted from an increase in active customers, partially offset by lower gross billings per average active customer and increased order discounts for the three months ended September 30, 2014, as compared to the prior year period. We believe that increases in transaction activity by active customers who make purchases on mobile devices and in the number of deals that we offered contributed to the growth in billings for our North America segment. In addition, we have continued to refine our approach to targeting customers and have undertaken marketing initiatives to increase consumer awareness of deals available through our marketplaces, which we believe contributed to the billings growth. Historically, our customers often purchased a Groupon voucher when they received our email with a limited-time offer, even though they may not have intended to use the voucher in the near term. The growth in recent periods of our marketplaces of deals has enabled customers to wait until they are ready to use the related vouchers before making purchases. We believe that this shift in purchasing behavior adversely impacted gross billings in recent periods. However, we believe that the potential impact of these changes in the timing of customer purchases on our billings growth has become less significant because the prior year period includes the effects of those purchasing trends and therefore is more comparable to the current year period.

EMEA

EMEA segment gross billings increased by \$46.1 million to \$489.4 million for the three months ended September 30, 2014, as compared to \$443.3 million for the three months ended September 30, 2013. The increase in gross billings was comprised of a \$21.2 million increase in our Goods category, resulting from increased unit sales in this category for the three months ended September 30, 2014, as compared to the prior year period. The increase in gross billings

was also comprised of a \$10.8 million increase in our Local category and a \$14.1 million increase in our Travel category, resulting from increased unit sales in these categories. The increase in gross billings in the EMEA segment also resulted from an increase in active customers and higher gross billings per average active customer for the three months ended September 30, 2014, as compared to the prior year period.

The favorable impact on gross billings from year-over-year changes in foreign exchange rates for the three months ended September 30, 2014 was \$2.2 million.

#### Rest of World

Rest of World segment gross billings increased by \$362.7 million to \$597.0 million for the three months ended September 30, 2014, as compared to \$234.3 million for the three months ended September 30, 2013. The increase in gross billings was attributable to our acquisition of Ticket Monster, which contributed \$370.3 million in gross billings for the three months ended September 30, 2014, and also generated increased unit sales and an increase in active customers for the three months ended September 30, 2014, as compared to the prior year period. The increase in gross billings was comprised of a \$210.2 million increase in our Goods category, a \$71.5 million increase in our Local category and an \$80.9 million increase in our Travel category. The favorable impact on gross billings from year-over-year changes in foreign exchange rates for the three months ended September 30, 2014 was \$18.1 million. On a pro forma basis, the combined gross billings of our Rest of World segment, as if the Company had acquired Ticket Monster as of January 1, 2013, were \$464.6 million for the three months ended September 30, 2013. This pro forma gross billings amount is not necessarily indicative of what the actual results of the combined company would have been if the acquisition had occurred as of January 1, 2013, nor is it indicative of future results.

#### Revenue

We generate revenue from third party revenue deals, direct revenue deals and other transactions. Revenue for the three months ended September 30, 2014 and 2013 was as follows:

	Three Months Ended September 30,	
	2014	2013
	(in thousands)	
Revenue:		
Third party	\$392,982	\$390,784
Direct	357,251	200,072
Other	6,821	4,203
Total revenue	\$757,054	\$595,059

Revenue increased by \$162.0 million to \$757.1 million for the three months ended September 30, 2014, as compared to \$595.1 million for the three months ended September 30, 2013. This increase was primarily attributable to the \$157.2 million increase in direct revenue from transactions in our Goods category where we are the merchant of record and for which revenue is reported on a gross basis. The increase in revenue was also due to a \$2.6 million increase in other revenue and a \$2.2 million increase in third party revenue. The increase in revenue was attributable to increased unit sales and an increase in active customers for the three months ended September 30, 2014 as compared to the prior year period. We also increased the number of merchant relationships and the volume of deals we offer to our customers. Our acquisitions of Ticket Monster and Ideel contributed \$42.8 million and \$20.6 million of revenue, respectively, for the three months ended September 30, 2014. The favorable impact on revenue from year-over-year changes in foreign exchange rates for the three months ended September 30, 2014 was \$0.3 million.

#### Third Party Revenue

Third party revenue increased by \$2.2 million to \$393.0 million for the three months ended September 30, 2014, as compared to \$390.8 million for the three months ended September 30, 2013. The increase in third party revenue is primarily due to a \$12.7 million increase in our Travel category, which resulted from a \$115.4 million increase in gross billings, partially offset by a reduction in the percentage of gross billings that we retained after deducting the merchant's share to 17.4% for the three months ended September 30, 2014, as compared to 21.8% for the three months ended September 30, 2013. The increase in third party revenue was partially offset by an \$11.0 million decrease in our Local category. Although third party billings in our Local category increased by \$121.4 million, the percentage of gross billings that we retained after deducting the merchant's share decreased to 34.2% for the three months ended September 30, 2014, as compared to 41.4% for the three months ended September 30, 2013. Our acquisition of Ticket Monster contributed \$42.8 million of revenue, primarily third party revenue, for the three months ended September 30, 2014. The decrease in the percentage of gross billings that we retained after deducting the merchant's share primarily reflects the impact of Ticket Monster's lower deal margins.



### Direct Revenue

Direct revenue increased by \$157.2 million to \$357.3 million for the three months ended September 30, 2014, as compared to \$200.1 million for the three months ended September 30, 2013. Direct revenue for the three months ended September 30, 2014 includes \$20.6 million from our Ideel acquisition. We are often the merchant of record for transactions in the Goods category, particularly in North America and also in EMEA beginning in September 2013, such that the resulting revenue is reported on a gross basis within direct revenue. Growth in direct revenue results in a smaller increase in income from operations than growth in third party revenue because direct revenue includes the entire amount of gross billings, before deducting the cost of the related inventory, while third party revenue is net of the merchant's share of the transaction price. Additionally, our Goods category has lower margins than our Local category, primarily as a result of shipping and fulfillment costs related to direct revenue transactions.

We believe that direct revenue deals in our Goods category will increase in the future in the EMEA and Rest of World segments as we continue to build out our global supply chain infrastructure.

### Other Revenue

Other revenue increased by \$2.6 million to \$6.8 million for the three months ended September 30, 2014, as compared to \$4.2 million for the three months ended September 30, 2013, primarily due to increases in payment processing revenue and commission revenue. Other revenue also includes point of sale revenue. These other revenue sources were not significant for the three months ended September 30, 2014 and 2013, and we do not expect them to be material in the near term.

### Revenue by Segment

Revenue by segment for the three months ended September 30, 2014 and 2013 was as follows:

	Three Months Ended September 30,				
	2014	% of total	2013	% of total	
	(dollars in thousands)				
North America:					
Third party and other	\$180,678	23.9	% \$177,883	29.9	%
Direct	237,816	31.4	182,955	30.7	
Total segment revenue	418,494	55.3	360,838	60.6	
EMEA:					
Third party and other	121,712	16.1	138,679	23.3	
Direct	108,360	14.3	9,271	1.6	
Total segment revenue	230,072	30.4	147,950	24.9	
Rest of World:					
Third party and other	97,413	12.9	78,425	13.2	
Direct	11,075	1.4	7,846	1.3	
Total segment revenue	108,488	14.3	86,271	14.5	
Total revenue	\$757,054	100.0	% \$595,059	100.0	%

Edgar Filing: Groupon, Inc. - Form 10-Q

Revenue by category and segment for the three months ended September 30, 2014 and 2013 was as follows (in thousands):

	North America		EMEA		Rest of World		Consolidated	
	Three Months Ended September 30,		Three Months Ended September 30,		Three Months Ended September 30,		Three Months Ended September 30,	
	2014	2013	2014	2013	2014	2013	2014	2013
Local <sup>(1)</sup> :								
Third party and other <sup>(2)</sup>	\$161,912	\$161,306	\$90,002	\$92,141	\$45,085	\$51,900	\$296,999	\$305,347
Direct revenue	—	1,040	—	—	—	—	—	1,040
Total	161,912	162,346	90,002	92,141	45,085	51,900	296,999	306,387
Goods:								
Third party	1,139	3,999	14,750	32,008	37,814	17,215	53,703	53,222
Direct revenue	237,816	181,915	108,360	9,271	11,075	7,846	357,251	199,032
Total	238,955	185,914	123,110	41,279	48,889	25,061	410,954	252,254
Travel:								
Third party <sup>(2)</sup>	17,627	12,578	16,960	14,530	14,514	9,310	49,101	36,418
Total revenue	\$418,494	\$360,838	\$230,072	\$147,950	\$108,488	\$86,271	\$757,054	\$595,059

(1) Includes revenue from deals with local merchants, from deals with national merchants, and through local events.

During the three months ended March 31, 2014, the Company began classifying other revenue as a component of (2) the Local category. Other revenue was previously aggregated with the Travel category. The prior period category information has been retrospectively adjusted to conform to the current period presentation.

North America

North America segment revenue increased by \$57.7 million to \$418.5 million for the three months ended September 30, 2014, as compared to \$360.8 million for the three months ended September 30, 2013. The increase in revenue primarily resulted from a \$55.9 million increase in direct revenue from our Goods category, which includes \$20.6 million of direct revenue from Ideel, which we acquired in January 2014. Direct revenue, which is recorded on a gross basis, is derived primarily from selling products through our Goods category where we are the merchant of record. Revenue in our Travel category also increased by \$5.0 million, which resulted from a \$20.3 million increase in gross billings and an increase in the percentage of gross billings that we retained after deducting the merchant's share to 20.8% for the three months ended September 30, 2014, as compared to 19.5% for the three months ended September 30, 2013. Third party and other revenue in our Local category increased \$0.6 million, which resulted from a \$41.7 million increase in gross billings, partially offset by a reduction in the percentage of gross billings that we retained after deducting the merchant's share to 36.3% for the three months ended September 30, 2014, as compared to 39.8% for the three months ended September 30, 2013. This decrease in the percentage of gross billings that we retained after deducting the merchant's share reflects the overall results of individual deal-by-deal negotiations with merchants and can vary significantly from period-to-period. We were willing to accept lower deal margins in our Local category, as compared to the prior year period, in order to improve the quality and increase the number of deals offered to customers by offering more attractive terms to merchants. The overall increase in revenue in our North America segment was also due to an increase in active customers, partially offset by lower gross billings per average active customer and increased order discounts for the three months ended September 30, 2014, as compared to the prior year period.

We believe that increases in transaction activity on mobile devices and in the number of deals that we offered contributed to the growth in revenue for our North America segment. In addition, we have continued to refine our approach to targeting customers and have undertaken marketing initiatives to increase consumer awareness of deals available through our marketplaces, which we believe contributed to the revenue growth.

EMEA

EMEA segment revenue increased by \$82.1 million to \$230.1 million for the three months ended September 30, 2014, as compared to \$148.0 million for the three months ended September 30, 2013. The increase in revenue primarily resulted from a \$99.1 million increase in direct revenue from our Goods category. Revenue from transactions in our Goods category in our

EMEA segment were primarily presented on a net basis within third party revenue in the prior year period, as we were not typically the merchant of record for those transactions outside of the United States. However, we began increasing the number of product deals offered in our EMEA segment for which we are the merchant of record beginning in September 2013. As a result, the proportion of direct revenue deals in the Goods category of our EMEA segment increased in the third quarter of 2014 as compared to the prior year period, and we expect that the proportion of direct revenue deals in the Goods category of our EMEA segment will continue to increase in future periods.

The increase in direct revenue in our Goods category was partially offset by a \$17.3 million decrease in third party revenue in our Goods category, which resulted from a \$77.9 million decrease in gross billings and a decrease in the percentage of gross billings that we retained after deducting the merchant's share to 17.8% for the three months ended September 30, 2014, as compared to 19.9% for the three months ended September 30, 2013. The increase in revenue was also partially offset by a \$2.1 million decrease in third party and other revenue from our Local category, which resulted from a decrease in the percentage of gross billings that we retained after deducting the merchant's share to 41.2% for the three months ended September 30, 2014, as compared to 44.3% for the three months ended September 30, 2013. These decreases in the percentage of gross billings that we retained during the three months ended September 30, 2014 reflect the overall results of individual deal-by-deal negotiations with our merchants and can vary significantly from period-to-period. We were willing to accept lower deal margins, as compared to the prior year period, in order to improve the quality and increase the number of deals offered to our customers by offering more attractive terms to merchants.

The overall increase in revenue in our EMEA segment was also due to increased unit sales, an increase in active customers and higher gross billings per average active customer for the three months ended September 30, 2014, as compared to the prior year period. The favorable impact on revenue from year-over-year changes in foreign exchange rates for the three months ended September 30, 2014 was \$0.9 million.

#### Rest of World

Rest of World segment revenue increased by \$22.2 million to \$108.5 million for the three months ended September 30, 2014, as compared to \$86.3 million for the three months ended September 30, 2013. The increase in revenue was attributable to our acquisition of Ticket Monster, which contributed \$42.8 million in revenue for the three months ended September 30, 2014. Revenue from our Goods category increased by \$23.8 million for the three months ended September 30, 2014, as compared to the prior year period, due to a \$20.6 million increase in third party revenue, which resulted from a \$207.0 million increase in gross billings, partially offset by a reduction in the percentage of gross billings that we retained after deducting the merchant's share to 13.6% for the three months ended September 30, 2014, as compared to 24.2% in the prior year period. The increase in third party revenue from our Goods category was attributable to the Ticket Monster acquisition, and the decrease in the percentage of gross billings that we retained after deducting the merchant's share primarily reflects the impact of Ticket Monster's lower deal margins. In our Rest of World segment, revenue from transactions in our Goods category are primarily presented on a net basis within third party revenue, as we have not typically been the merchant of record for those transactions outside of the United States and EMEA.

The increase in revenue from our Rest of World segment included a \$5.2 million increase in revenue from our Travel category, which resulted from an \$80.9 million increase in gross billings, partially offset by a reduction in the percentage of gross billings that we retained after deducting the merchant's share to 12.3% for the three months ended September 30, 2014, as compared to 25.4% in the prior year period. Although gross billings on third party and other revenue transactions in our Local category increased by \$71.5 million, third party and other revenue in our Local category decreased by \$6.8 million, which resulted from a reduction in the percentage of gross billings that we retained after deducting the merchant's share to 23.7% for the three months ended September 30, 2014, as compared to 43.7% for the three months ended September 30, 2013. The decrease in the percentage of gross billings that we retained after deducting the merchant's share primarily reflects the impact of Ticket Monster's lower deal margins. The unfavorable impact on revenue from year-over-year changes in foreign exchange rates for the three months ended September 30, 2014 was \$0.4 million.



## Cost of Revenue

Cost of revenue on third party, direct revenue and other deals for the three months ended September 30, 2014 and 2013 was as follows:

	Three Months Ended September 30,	
	2014	2013
	(in thousands)	
Cost of revenue:		
Third party	\$57,736	\$51,276
Direct	315,413	181,436
Other	3,761	2,725
Total cost of revenue	\$376,910	\$235,437

Cost of revenue is comprised of direct and certain indirect costs incurred to generate revenue. For direct revenue deals, cost of revenue includes the cost of inventory, shipping and fulfillment costs and inventory markdowns. Fulfillment costs are comprised of third party logistics provider costs, as well as rent, depreciation, personnel costs and other costs of operating our own fulfillment center, which began operations in the fourth quarter of 2013. For third party revenue transactions, cost of revenue includes estimated refunds for which the merchant's share is not recoverable. Other costs incurred to generate revenue, which include credit card processing fees, editorial costs, certain technology costs, web hosting and other processing fees, are allocated to cost of third party revenue, direct revenue, and other revenue in proportion to gross billings during the period. As a result of the significant growth we have experienced from direct revenue transactions relative to our total gross billings for the three months ended September 30, 2014, as compared to the prior year period, an increased share of those allocable costs has been allocated to cost of direct revenue in our condensed consolidated statement of operations for the three months ended September 30, 2014.

Cost of revenue increased by \$141.5 million to \$376.9 million for the three months ended September 30, 2014, as compared to \$235.4 million for the three months ended September 30, 2013, which was attributable to the growth in direct revenue from our Goods category. The increase in cost of revenue was primarily driven by the cost of inventory and related shipping costs on direct revenue deals, which were not as significant during the prior year period. We currently outsource a majority of our inventory fulfillment activities in the United States to third party logistics providers. However, we expect to reduce our usage of those third parties in future periods by transitioning additional inventory fulfillment work in the United States to internal resources. For example, we launched our own fulfillment center in the fourth quarter of 2013. Additionally, to further reduce the involvement of third party logistics providers in the fulfillment process in the United States, we have increased our use of arrangements in which the suppliers of our product offerings ship merchandise directly to our customers. We are also refining our inventory management practices to better allocate inventories among warehouses in different geographic regions throughout the United States to reduce shipping distances to customers and increase units per order. We believe that these initiatives will ultimately reduce our fulfillment costs and improve the margins on direct revenue transactions in our Goods category. However, we may incur increased fulfillment costs from time to time as we enhance our internal processes and continue to transition fulfillment work from third party logistics providers.

## Cost of Revenue by Segment

Cost of revenue by segment for the three months ended September 30, 2014 and 2013 was as follows:

	Three Months Ended September 30,		2013			
	2014	% of total		% of total		
(dollars in thousands)						
North America:						
Third party and other	\$27,538	7.3	%	\$23,557	10.0	%
Direct	214,814	57.0		165,712	70.4	
Total segment cost of revenue	242,352	64.3		189,269	80.4	
EMEA:						
Third party and other	10,009	2.7		15,905	6.8	
Direct	88,415	23.4		8,364	3.5	
Total segment cost of revenue	98,424	26.1		24,269	10.3	
Rest of World:						
Third party and other	23,950	6.4		14,539	6.2	
Direct	12,184	3.2		7,360	3.1	
Total segment cost of revenue	36,134	9.6		21,899	9.3	
Total cost of revenue	\$376,910	100.0	%	\$235,437	100.0	%

Cost of revenue by category and segment for the three months ended September 30, 2014 and 2013 was as follows (in thousands):

	North America		EMEA		Rest of World		Consolidated	
	Three Months Ended September 30,		Three Months Ended September 30,		Three Months Ended September 30,		Three Months Ended September 30,	
	2014	2013	2014	2013	2014	2013	2014	2013
Local <sup>(1)</sup> :								
Third party and other <sup>(2)</sup>	\$23,723	\$21,569	\$6,046	\$10,333	\$6,493	\$7,465	\$36,262	\$39,367
Direct	—	1,887	—	—	—	—	—	1,887
Total	23,723	23,456	6,046	10,333	6,493	7,465	36,262	41,254
Goods:								
Third party	188	480	2,443	3,972	13,828	5,685	16,459	10,137
Direct	214,814	163,825	88,415	8,364	12,184	7,360	315,413	179,549
Total	215,002	164,305	90,858	12,336	26,012	13,045	331,872	189,686
Travel:								
Third party <sup>(2)</sup>	3,627	1,508	1,520	1,600	3,629	1,389	8,776	4,497
Total cost of revenue	\$242,352	\$189,269	\$98,424	\$24,269	\$36,134	\$21,899	\$376,910	\$235,437

(1) Includes cost of revenue from deals with local merchants, from deals with national merchants, and through local events.

During the three months ended March 31, 2014, the Company began classifying other cost of revenue as a (2) component of the Local category. Other cost of revenue was previously aggregated with the Travel category. The prior period category information has been retrospectively adjusted to conform to the current period presentation.

## North America

North America cost of revenue increased by \$53.1 million to \$242.4 million for the three months ended September 30, 2014, as compared to \$189.3 million for the three months ended September 30, 2013. The increase in cost of revenue was primarily driven by the cost of inventory and shipping costs related to direct revenue deals in our Goods category, due to the growth of that category as compared to the prior year period. Cost of revenue for the three months ended September 30, 2014 includes \$18.0 million from the Ideel acquisition.



## EMEA

EMEA cost of revenue increased by \$74.2 million to \$98.4 million for the three months ended September 30, 2014, as compared to \$24.3 million for the three months ended September 30, 2013. The increase in cost of revenue was primarily driven by the cost of inventory and shipping and fulfillment costs related to direct revenue deals in our Goods category, as we began increasing the number of product deals offered in our EMEA segment for which we are the merchant of record beginning in September 2013.

## Rest of World

Rest of World cost of revenue increased by \$14.2 million to \$36.1 million for the three months ended September 30, 2014, as compared to \$21.9 million for the three months ended September 30, 2013. Cost of revenue for the three months ended September 30, 2014 includes \$17.9 million from the Ticket Monster acquisition, which primarily consists of credit card processing fees.

## Gross Profit

Gross profit for the three months ended September 30, 2014 and 2013 was as follows:

	Three Months Ended September 30,	
	2014	2013
	(in thousands)	
Gross profit:		
Third party	\$335,246	\$339,508
Direct	41,838	18,636
Other	3,060	1,478
Total gross profit	\$380,144	\$359,622

Gross profit increased by \$20.5 million to \$380.1 million for the three months ended September 30, 2014, as compared to \$359.6 million for the three months ended September 30, 2013. This increase in gross profit resulted from the \$162.0 million increase in revenue during the three months ended September 30, 2014, partially offset by the \$141.5 million increase in cost of revenue. The acquisitions of Ticket Monster and Ideel contributed \$24.9 million and \$2.6 million of gross profit, respectively, for the three months ended September 30, 2014.

Gross profit as a percentage of revenue decreased to 50.2% for the three months ended September 30, 2014, as compared to 60.4% for the three months ended September 30, 2013. The decrease in gross profit as a percentage of revenue during the three months ended September 30, 2014, as compared to the prior year period, was primarily attributable to the increase in direct revenue. Direct revenue primarily relates to deals in our Goods category, which typically have lower margins than deals in our Local and Travel categories. Additionally, direct revenue and the related cost of revenue are presented on a gross basis in our consolidated statements of operations, which contributes to lower gross profit as a percentage of revenue.

Gross profit on third party revenue decreased by \$4.3 million to \$335.2 million for the three months ended September 30, 2014, as compared to \$339.5 million for the three months ended September 30, 2013. This decrease in gross profit resulted from the \$6.5 million increase in the cost of third party revenue, partially offset by the \$2.2 million increase in third party revenue. Gross profit as a percentage of revenue on third party revenue deals decreased to 85.3% for the three months ended September 30, 2014, as compared to 86.9% for the three months ended September 30, 2013.

Gross profit on direct revenue increased by \$23.2 million to \$41.8 million for the three months ended September 30, 2014, as compared to \$18.6 million for the three months ended September 30, 2013. This increase in gross profit resulted from the \$157.2 million increase in direct revenue to \$357.3 million for the three months ended September 30, 2014, as compared to \$200.1 million for the three months ended September 30, 2013, partially offset by the \$134.0 million increase in cost of revenue on direct revenue deals to \$315.4 million for the three months ended September 30, 2014, as compared to \$181.4 million for the three months ended September 30, 2013. Gross profit as a percentage of revenue on direct revenue deals increased to 11.7% for the three months ended September 30, 2014, as compared to 9.3% for the three months ended September 30, 2013. The increase in gross profit as a percentage of revenue on direct revenue deals was attributable, in part, to lower shipping and fulfillment costs as a percentage of direct revenue, partially offset by increased cost of inventory sold as a percentage of direct revenue.



## Gross Profit by Segment

Gross profit by segment for the three months ended September 30, 2014 and 2013 was as follows:

	Three Months Ended September 30,		2013		
	2014	% of total		% of total	
(dollars in thousands)					
North America:					
Third party and other	\$ 153,140	40.3	% \$ 154,326	42.9	%
Direct	23,002	6.1	17,243	4.8	
Total gross profit	176,142	46.4	171,569	47.7	
EMEA:					
Third party and other	111,703	29.4	122,774	34.1	
Direct	19,945	5.2	907	0.3	
Total gross profit	131,648	34.6	123,681	34.4	
Rest of World:					
Third party and other	73,463	19.3	63,886	17.8	
Direct	(1,109	) (0.3	) 486	0.1	
Total gross profit	72,354	19.0	64,372	17.9	
Total gross profit	\$ 380,144	100.0	% \$ 359,622	100.0	%

Gross profit by category and segment for the three months ended September 30, 2014 and 2013 was as follows (in thousands):

	North America		EMEA		Rest of World		Consolidated	
	Three Months Ended September 30,		Three Months Ended September 30,		Three Months Ended September 30,		Three Months Ended September 30,	
	2014	2013	2014	2013	2014	2013	2014	2013
Local <sup>(1)</sup> :								
Third party and other <sup>(2)</sup>	\$ 138,189	\$ 139,737	\$ 83,956	\$ 81,808	\$ 38,592	\$ 44,435	\$ 260,737	\$ 265,980
Direct	—	(847	) —	—	—	—	—	(847
Total	138,189	138,890	83,956	81,808	38,592	44,435	260,737	265,133
Goods:								
Third party	951	3,519	12,307	28,036	23,986	11,530	37,244	43,085
Direct	23,002	18,090	19,945	907	(1,109	) 486	41,838	19,483
Total	23,953	21,609	32,252	28,943	22,877	12,016	79,082	62,568
Travel:								
Third party <sup>(2)</sup>	14,000	11,070	15,440	12,930	10,885	7,921	40,325	31,921
Total gross profit	\$ 176,142	\$ 171,569	\$ 131,648	\$ 123,681	\$ 72,354	\$ 64,372	\$ 380,144	\$ 359,622

<sup>(1)</sup> Includes gross profit from deals with local merchants, from deals with national merchants, and through local events.

During the three months ended March 31, 2014, the Company began classifying other gross profit as a component <sup>(2)</sup> of the Local category. Other gross profit was previously aggregated with the Travel category. The prior period category information has been retrospectively adjusted to conform to the current period presentation.

## North America

North America gross profit increased by \$4.6 million to \$176.1 million for the three months ended September 30, 2014, as compared to \$171.6 million for the three months ended September 30, 2013. The increase in gross profit was comprised of a



\$2.9 million increase in our Travel category and a \$2.3 million increase in our Goods category, partially offset by a \$0.7 million decrease in our Local category.

#### EMEA

EMEA gross profit increased by \$8.0 million to \$131.6 million for the three months ended September 30, 2014, as compared to \$123.7 million for the three months ended September 30, 2013. The increase in gross profit was comprised of a \$3.3 million increase in our Goods category, a \$2.5 million increase in our Travel category, and a \$2.1 million increase in our Local category.

#### Rest of World

Rest of World gross profit increased by \$8.0 million to \$72.4 million for three months ended September 30, 2014, as compared to \$64.4 million for the three months ended September 30, 2013. The increase in gross profit was comprised of a \$10.9 million increase in our Goods category and a \$3.0 million increase in our Travel category, partially offset by a \$5.8 million decrease in our Local category.

#### Marketing

For the three months ended September 30, 2014 and 2013, marketing expense was \$59.9 million and \$53.3 million, respectively. Marketing expense by segment as a percentage of segment revenue and as a percentage of total marketing expense for the three months ended September 30, 2014 and 2013 was as follows:

	Three Months Ended September 30,					
	2014	% of Segment Revenue	% of Total Marketing	2013	% of Segment Revenue	% of Total Marketing
	(dollars in thousands)					
North America	\$31,155	7.4	% 52.0	% \$27,100	7.5	% 50.9
EMEA	17,289	7.5	28.8	16,807	11.4	31.6
Rest of World	11,491	10.6	19.2	9,358	10.8	17.5
Marketing	\$59,935	7.9	100.0	% \$53,265	9.0	100.0

Marketing expense increased by \$6.7 million to \$59.9 million for the three months ended September 30, 2014, as compared to \$53.3 million for the three months ended September 30, 2013. Marketing expense as a percentage of revenue decreased to 7.9% for the three months ended September 30, 2014, as compared to 9.0% for the three months ended September 30, 2013. We evaluate marketing expense as a percentage of revenue because it gives us an indication of how well our marketing spend is driving revenue growth.

Our subscriber acquisition and customer activation marketing activities also include elements that are not presented as "Marketing" on our consolidated statements of operations, such as order discounts, free shipping on qualifying merchandise sales and accepting lower margins on our deals. Marketing is the primary method by which we acquire customers, and as such, is an important part of our business.

#### North America

North America marketing expense increased by \$4.1 million to \$31.2 million for the three months ended September 30, 2014, as compared to \$27.1 million for the three months ended September 30, 2013. The increase in marketing expense was primarily attributable to our initiatives to grow our active customer base and increase awareness of the pull marketplace. For the three months ended September 30, 2014, marketing expense as a percentage of revenue for our North America segment decreased to 7.4%, as compared to 7.5% for the three months ended September 30, 2013.

## EMEA

EMEA marketing expense for the three months ended September 30, 2014 remained relatively consistent as compared to the three months ended September 30, 2013. For the three months ended September 30, 2014, marketing expense as a percentage of revenue for our EMEA segment decreased to 7.5%, as compared to 11.4% for the three months ended September 30, 2013.

## Rest of World

Rest of World marketing expense increased by \$2.1 million to \$11.5 million for the three months ended September 30, 2014, as compared to \$9.4 million for the three months ended September 30, 2013. The increase in marketing expense was primarily attributable to our acquisition of Ticket Monster, as we incurred \$4.7 million of marketing expenditures for the three months ended September 30, 2014 in connection with our initiatives to grow the business. For the three months ended September 30, 2014, marketing expense as a percentage of revenue for our Rest of World segment decreased to 10.6%, as compared to 10.8% for the three months ended September 30, 2013.

## Selling, General and Administrative

Selling, general and administrative expense increased by \$31.9 million to \$325.9 million for the three months ended September 30, 2014, as compared to \$294.1 million for the three months ended September 30, 2013. This increase was attributable to the Ticket Monster and Ideel acquisitions. Wages and benefits (excluding stock-based compensation) within selling, general and administrative expense increased by \$15.9 million for the three months ended September 30, 2014, as compared to the prior year period, primarily due to the additional employees from those acquisitions. Depreciation and amortization recorded within selling, general and administrative expense increased by \$13.1 million for the three months ended September 30, 2014, which includes increased amortization expense related to intangible assets acquired as part of those acquisitions.

Selling, general and administrative expense as a percentage of revenue was 43.1% for the three months ended September 30, 2014, as compared to 49.4% for the three months ended September 30, 2013, respectively. Although revenue increased by \$162.0 million, or 27.2%, for the three months ended September 30, 2014, as compared to the prior year period, selling, general and administrative expense increased by \$31.9 million, or 10.8%. We are continuing to refine our sales management and administrative processes, including through automation and ongoing regionalization of back-office functions, in connection with our efforts to generate increased operating efficiencies.

## Acquisition Related (Benefit) Expense, Net

For the three months ended September 30, 2014, we incurred a net acquisition-related benefit of \$0.3 million due to a benefit of \$1.0 million related to changes in the fair value of contingent consideration, partially offset by \$0.7 million of external transaction costs. For the three months ended September 30, 2013, the net acquisition-related benefit of \$1.5 million also related to changes in the fair value of contingent consideration. See Note 10 "Fair Value Measurements" for information about fair value measurements of contingent consideration arrangements.

## (Loss) Income from Operations

The loss from operations for the three months ended September 30, 2014 was \$5.4 million, as compared to income from operations for the three months ended September 30, 2013 of \$13.8 million. The change in (loss) income from operations for the three months ended September 30, 2014, as compared to the prior year period, was primarily due to the increase in selling, general and administrative expense of \$31.9 million and marketing expense of \$6.7 million, partially offset by the increase in gross profit of \$20.5 million. The unfavorable impact on the loss from operations from year-over-year changes in foreign exchange rates for the three months ended September 30, 2014 was \$0.2 million.

## North America

Segment operating income in our North America segment, which excludes stock-based compensation and acquisition-related (benefit) expense, net, decreased by \$12.6 million to \$12.6 million for the three months ended September 30, 2014, as compared to \$25.2 million for the three months ended September 30, 2013. The decrease in segment operating income was attributable to an increase in segment operating expenses, partially offset by an increase in segment gross profit.



## EMEA

Segment operating income in our EMEA segment, which excludes stock-based compensation and acquisition-related (benefit) expense, net, increased by \$6.8 million to \$22.4 million for the three months ended September 30, 2014, as compared to \$15.6 million for the three months ended September 30, 2013. The increase in segment operating income was attributable to an increase in segment gross profit, partially offset by an increase in segment operating expenses.

## Rest of World

Segment operating loss in our Rest of World segment, which excludes stock-based compensation and acquisition-related (benefit) expense, net, increased by \$4.6 million to a loss of \$6.2 million for the three months ended September 30, 2014, as compared to a loss of \$1.6 million for the three months ended September 30, 2013. The increased segment operating loss was attributable to an increase in segment operating expenses, partially offset by an increase in segment gross profit.

## Other (Expense) Income, Net

Other (expense) income, net was an expense of \$20.0 million for the three months ended September 30, 2014, as compared to income of \$0.8 million for the three months ended September 30, 2013. The current period expense was primarily comprised of \$18.6 million in foreign currency transaction losses and \$1.4 million of other-than-temporary impairments related to minority investments. The foreign currency transaction losses primarily represent unrealized losses on intercompany balances with our subsidiaries that are denominated in foreign currencies. The foreign currency losses on those intercompany balances primarily resulted from the significant decline in the Euro against the U.S. dollar from an exchange rate of 1.3654 on June 30, 2014 to 1.2598 on September 30, 2014. For the three months ended September 30, 2013, other income, net was primarily comprised of \$0.4 million of interest income, net and \$0.3 million of foreign currency transaction gains.

## Provision for Income Taxes

For the three months ended September 30, 2014, we recorded an income tax benefit of \$6.4 million, as compared to income tax expense of \$15.9 million for the three months ended September 30, 2013.

The effective tax rate was 25.3% for the three months ended September 30, 2014, as compared to 108.8% for the three months ended September 30, 2013. Significant factors impacting our effective tax rate for the three months ended September 30, 2014 and 2013 included losses in jurisdictions that we are not able to benefit due to uncertainty as to the realization of those losses, amortization of the tax effects of intercompany sales of intellectual property and nondeductible stock-based compensation expense. Additionally, the effective tax rate for the three months ended September 30, 2014 included a \$7.7 million decrease to our liabilities for uncertain tax positions, as discussed below. We expect that our consolidated effective tax rate in future periods will continue to differ significantly from the U.S. federal income tax rate as a result of our tax obligations in jurisdictions with profits and valuation allowances in jurisdictions with losses. Our consolidated effective tax rate in future periods will also be adversely impacted by the amortization of the tax effects of intercompany transactions, including intercompany sales of intellectual property that we expect to undertake in the future.

We are currently undergoing income tax audits in multiple jurisdictions. There are many factors, including factors outside of our control, which influence the progress and completion of these audits. For the three months ended September 30, 2014, we decreased our liabilities for uncertain tax positions and income tax expense by \$7.7 million as a result of new information that impacted our estimates of amounts that are more-likely-than not of being realized upon ultimate settlement. As of September 30, 2014, we believe that it is reasonably possible that additional changes of up to \$35.5 million in unrecognized tax benefits may occur within the next 12 months upon closing of income tax audits or the expiration of applicable statutes of limitations.

## Results of Operations

Comparison of the Nine Months Ended September 30, 2014 and 2013:

	Nine Months Ended September 30,	
	2014	2013
	(in thousands)	
Revenue:		
Third party and other	\$1,232,173	\$1,252,966
Direct	1,034,094	552,242
Total revenue	2,266,267	1,805,208
Cost of revenue:		
Third party and other	182,226	179,524
Direct	928,314	502,359
Total cost of revenue	1,110,540	681,883
Gross profit	1,155,727	1,123,325
Operating expenses:		
Marketing	203,134	158,319
Selling, general and administrative	983,751	904,880
Acquisition-related expense (benefit), net	2,078	(2,276)
Total operating expenses	1,188,963	1,060,923
(Loss) income from operations	(33,236)	) 62,402
Other (expense) income, net	(21,886)	) (9,830)
(Loss) income before provision for income taxes	(55,122)	) 52,572
Provision for income taxes	20,181	62,657
Net loss	(75,303)	) (10,085)
Net income attributable to noncontrolling interests	(6,575)	) (4,061)
Net loss attributable to Groupon, Inc.	\$(81,878)	) \$(14,146)

## Classification of stock-based compensation within cost of revenue and operating expenses

Cost of revenue and operating expenses include stock-based compensation as follows:

	Nine Months Ended September 30,			
	2014		2013	
	Statement of Operations line item  (in thousands)	Stock-based compensation included in line item	Statement of Operations line item	Stock-based compensation included in line item
Total cost of revenue	\$1,110,540	\$2,601	\$681,883	\$1,615
Operating expenses:				
Marketing	\$203,134	\$7,102	\$158,319	\$7,011
Selling, general and administrative	983,751	80,255	904,880	80,597
Acquisition-related expense (benefit), net	2,078	—	(2,276)	) —
Total operating expenses	\$1,188,963	\$87,357	\$1,060,923	\$87,608

## Foreign exchange rate neutral operating results

The effect on our gross billings, revenue, cost of revenue and operating expenses, and (loss) income from operations for the nine months ended September 30, 2014 from changes in exchange rates versus the U.S. dollar was as follows:

	Nine Months Ended September 30,		As Reported
	2014		
	At Avg. Q3 2013 YTD Rates <sup>(1)</sup> (in thousands)	Exchange Rate Effect <sup>(2)</sup>	
Gross billings	\$5,458,250	\$38,742	\$5,496,992
Revenue	\$2,261,643	\$4,624	\$2,266,267
Cost of revenue and operating expenses	2,297,204	2,299	2,299,503
(Loss) income from operations	\$(35,561)	) \$2,325	\$(33,236)

<sup>(1)</sup> Represents the financial statement balances that would have resulted had exchange rates in the reporting period been the same as those in effect in the comparable prior year period.

<sup>(2)</sup> Represents the increase or decrease in reported amounts resulting from changes in exchange rates from those in effect in the comparable prior year period.

## Gross Billings

Gross billings represents the total dollar value of customer purchases of goods and services, excluding applicable taxes and net of estimated refunds. Gross billings for the nine months ended September 30, 2014 and 2013 were as follows:

	Nine Months Ended September 30,	
	2014	2013
	(in thousands)	
Gross billings:		
Third party	\$4,444,576	\$3,602,033
Direct	1,034,094	552,242
Other	18,322	9,948
Total gross billings	\$5,496,992	\$4,164,223

For third party revenue deals, gross billings differs from third party revenue reported in our consolidated statements of operations, which is presented net of the merchant's share of the transaction price. For direct revenue deals and other revenue, gross billings are equivalent to direct revenue and other revenue reported in our consolidated statements of operations. Gross billings increased by \$1,332.8 million to \$5,497.0 million for the nine months ended September 30, 2014, as compared to \$4,164.2 million for the nine months ended September 30, 2013, primarily due to the acquisition of Ticket Monster which contributed \$983.8 million in gross billings for the nine months ended September 30, 2014. The increase was comprised of an \$842.5 million increase in gross billings from third party revenue transactions and a \$481.9 million increase in gross billings from direct revenue transactions. The increase in gross billings was driven by an increase in active customers and the volume of transactions, as we have continued to build our marketplaces and increase our offerings to customers. The favorable impact on gross billings from year-over-year changes in foreign exchange rates for the nine months ended September 30, 2014 was \$38.7 million.

We offer goods and services through three primary categories: Local, Goods and Travel within our North America, EMEA and Rest of World segments. We also earn advertising revenue, payment processing revenue, point of sale revenue and commission revenue. Gross billings, revenue, cost of revenue and gross profit from these other sources were previously considered to be distinct from our primary categories and were aggregated with gross billings, revenue, cost of revenue and gross profit from Travel, our smallest category. In recent periods, these other revenue sources have been increasingly viewed by management as a component of the Local category, as they are primarily generated through our relationships with local and national merchants. Accordingly, we updated our presentation of category information, effective beginning with the quarter ended March 31, 2014, to include other gross billings, revenue, cost of revenue and gross profit within the Local category in the tables below, and the prior period category information has been retrospectively adjusted to conform to the current period presentation. The increase in our gross billings was comprised of an \$879.4 million increase in our Goods category, a \$227.3 million increase in our Local category and a \$226.1 million increase in our Travel category.

#### Gross Billings by Segment

Gross billings by segment for the nine months ended September 30, 2014 and 2013 were as follows:

	Nine Months Ended September 30,		2013	% of total	
	2014	% of total			%
	(dollars in thousands)				
Gross billings:					
North America	\$2,354,900	42.8	% \$2,058,523	49.4	%
EMEA	1,486,266	27.0	1,417,886	34.0	
Rest of World	1,655,826	30.2	687,814	16.6	
Total gross billings	\$5,496,992	100.0	% \$4,164,223	100.0	%

Gross billings by category and segment for the nine months ended September 30, 2014 and 2013 were as follows (in thousands):

	North America		EMEA		Rest of World		Consolidated	
	Nine Months Ended September 30,		Nine Months Ended September 30,		Nine Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013	2014	2013	2014	2013
Local <sup>(1)</sup> :								
Third party and other <sup>(2)</sup>	\$1,364,891	\$1,308,051	\$708,022	\$709,956	\$528,324	\$354,193	\$2,601,237	\$2,372,200
Direct	—	1,733	—	—	—	—	—	1,733
Total	1,364,891	1,309,784	708,022	709,956	528,324	354,193	2,601,237	2,373,933
Goods:								
Third party	19,250	45,445	268,634	467,733	830,006	208,895	1,117,890	722,073
Direct	714,157	511,357	296,342	18,903	23,595	20,249	1,034,094	550,509
Total	733,407	556,802	564,976	486,636	853,601	229,144	2,151,984	1,272,582
Travel:								
Third party <sup>(2)</sup>	256,602	191,937	213,268	221,294	273,901	104,477	743,771	517,708
Total gross billings	\$2,354,900	\$2,058,523	\$1,486,266	\$1,417,886	\$1,655,826	\$687,814	\$5,496,992	\$4,164,223

(1) Includes gross billings from deals with local merchants, from deals with national merchants, and through local events.

During the three months ended March 31, 2014, the Company began classifying other gross billings as a (2) component of the Local category. Other gross billings were previously aggregated with the Travel category. The prior period category information has been retrospectively adjusted to conform to the current period presentation.

#### North America

North America segment gross billings increased by \$296.4 million to \$2,354.9 million for the nine months ended September 30, 2014, as compared to \$2,058.5 million for the nine months ended September 30, 2013. The increase in gross billings was comprised of a \$176.6 million increase in our Goods category, which included \$58.1 million of gross billings from our Ideel acquisition. The increase in gross billings also includes a \$64.7 million increase in our Travel category and a \$55.1 million increase in our Local category. The increase in gross billings in the North America segment resulted from an increase in active customers, partially offset by lower gross billings per average active customer and increased order discounts for the nine months ended September 30, 2014, as compared to the prior year period. We believe that increases in transaction activity by active customers who make purchases on mobile devices and in the number of deals that we offered contributed to the growth in billings for our North America segment. In addition, we have continued to refine our approach to targeting customers and have undertaken marketing initiatives to increase consumer awareness of deals available through our marketplaces, which we believe contributed to the billings growth.

Historically, our customers often purchased a Groupon voucher when they received our email with a limited-time offer, even though they may not have intended to use the voucher in the near term. The growth in recent periods of our marketplaces of deals has enabled customers to wait until they are ready to use the related vouchers before making purchases. We believe that this shift in purchasing behavior adversely impacted gross billings in recent periods. However, we believe that the potential impact of these changes in the timing of customer purchases on our billings growth has become less significant because the prior year period includes some of the effects of those purchasing trends and therefore is becoming more comparable to the current year period.

#### EMEA

EMEA segment gross billings increased by \$68.4 million to \$1,486.3 million for the nine months ended September 30, 2014, as compared to \$1,417.9 million for the nine months ended September 30, 2013. The increase in gross

billings was comprised of a \$78.3 million increase in our Goods category, resulting from increased unit sales in this category for the nine months ended September 30, 2014, as compared to the prior year period. The increase in gross billings in the EMEA segment also resulted from an increase in active customers and higher gross billings per average active customer for the nine months ended September 30,

2014, as compared to the prior year period. The increase in Goods gross billings was partially offset by an \$8.0 million decrease in our Travel category and a \$1.9 million decrease in our Local category. The favorable impact on gross billings from year-over-year changes in foreign exchange rates for the nine months ended September 30, 2014 was \$38.8 million.

#### Rest of World

Rest of World segment gross billings increased by \$968.0 million to \$1,655.8 million for the nine months ended September 30, 2014, as compared to \$687.8 million for the nine months ended September 30, 2013. The increase in gross billings was attributable to our acquisition of Ticket Monster, which contributed \$983.8 million in gross billings for the nine months ended September 30, 2014, and also generated increased unit sales and an increase in active customers for the nine months ended September 30, 2014, as compared to the prior year period. The increase in gross billings was comprised of a \$624.5 million increase in our Goods category, a \$174.1 million increase in our Local category and a \$169.4 million increase in our Travel category. The increase in gross billings in the Rest of World segment was primarily due to an increase in active customers and higher gross billings per average active customer for the nine months ended September 30, 2014, as compared to the prior year period. The favorable impact on gross billings from year-over-year changes in foreign exchange rates for the nine months ended September 30, 2014 was \$1.9 million.

On a pro forma basis, the combined gross billings of our Rest of World segment, as if the Company had acquired Ticket Monster as of January 1, 2013, were \$1,306.0 million for the nine months ended September 30, 2013. This pro forma gross billings amount is not necessarily indicative of what the actual results of the combined company would have been if the acquisition had occurred as of January 1, 2013, nor is it indicative of future results. Pro forma gross billings for the nine months ended September 30, 2013 includes \$618.2 million from Ticket Monster. This amount differs from the \$572.7 million of gross billings disclosed in the Company's press release announcing the acquisition on January 2, 2014 in order to conform to the Company's classification of the merchant's share of VAT on third party revenue transactions.

#### Revenue

We generate revenue from third party revenue deals, direct revenue deals and other transactions. Revenue for the nine months ended September 30, 2014 and 2013 was as follows:

	Nine Months Ended September 30,	
	2014	2013
	(in thousands)	
Revenue:		
Third party	\$1,213,851	\$1,243,018
Direct	1,034,094	552,242
Other	18,322	9,948
Total revenue	\$2,266,267	\$1,805,208

Revenue increased by \$461.1 million to \$2,266.3 million for the nine months ended September 30, 2014, as compared to \$1,805.2 million for the nine months ended September 30, 2013. This increase was attributable to the \$481.9 million increase in direct revenue from transactions in our Goods category, where we are the merchant of record and for which revenue is reported on a gross basis. The increase in revenue was partially offset by a \$29.2 million decrease in third party revenue. The net increase in revenue was attributable to increased unit sales and an increase in active customers for the nine months ended September 30, 2014, as compared to the prior year period. We also increased the number of merchant relationships and the volume of deals we offer to our customers. Our acquisitions of Ticket Monster and Ideel contributed \$107.4 million and \$58.1 million of revenue, respectively, for the nine months ended September 30, 2014. The favorable impact on revenue from year-over-year changes in foreign exchange rates for the nine months ended September 30, 2014 was \$4.6 million.

#### Third Party Revenue

Third party revenue decreased by \$29.2 million to \$1,213.9 million for the nine months ended September 30, 2014, as compared to \$1,243.0 million for the nine months ended September 30, 2013. The decrease in third party revenue is primarily due to a \$42.9 million decrease in our Local category. Although third party gross billings in our Local category increased \$220.7 million, the percentage of gross billings that we retained after deducting the merchant's

share decreased to 35.3% for the nine months ended September 30, 2014, as compared to 40.4% for the nine months ended September 30, 2013. The decrease in third party revenue in the current period was also due to a \$7.3 million decrease in our Goods category, which resulted from a reduction

in the percentage of gross billings that we retained after deducting the merchant's share to 14.8% for the nine months ended September 30, 2014, as compared to 23.9% in the prior year period. The decrease in third party revenue was partially offset by a \$21.0 million increase in our Travel category, which resulted from a \$226.1 million increase in gross billings, partially offset by a reduction in the percentage of gross billings that we retained after deducting the merchant's share to 18.2% for the nine months ended September 30, 2014, as compared to 22.2% for the nine months ended September 30, 2013. Our acquisition of Ticket Monster contributed \$107.4 million of revenue, primarily third party revenue, for the nine months ended September 30, 2014. The decrease in the percentage of gross billings that we retained after deducting the merchant's share primarily reflects the impact of Ticket Monster's lower deal margins.

#### Direct Revenue

Direct revenue increased by \$481.9 million to \$1,034.1 million for the nine months ended September 30, 2014, as compared to \$552.2 million for the nine months ended September 30, 2013. Direct revenue for the nine months ended September 30, 2014 includes \$58.1 million from our Ideel acquisition. We are often the merchant of record for transactions in our Goods category, particularly in North America and also in EMEA beginning in September 2013, such that the resulting revenue is reported on a gross basis within direct revenue. Growth in direct revenue will result in a smaller increase in income from operations than growth in third party revenue because direct revenue includes the entire amount of gross billings, before deducting the cost of the related inventory, while third party revenue is net of the merchant's share of the transaction price. Additionally, our Goods category has lower margins than our Local category, primarily as a result of shipping and fulfillment costs related to direct revenue transactions.

We believe that direct revenue deals in our Goods category will increase in the future in the EMEA and Rest of World segments as we continue to build out our global supply chain infrastructure.

#### Other Revenue

Other revenue increased by \$8.4 million to \$18.3 million for the nine months ended September 30, 2014, as compared to \$9.9 million for the nine months ended September 30, 2013, primarily due to increases in payment processing revenue, advertising revenue and commission revenue. Other revenue also includes point of sale revenue. Those other revenue sources were not significant for the nine months ended September 30, 2014 and 2013, and we do not expect them to be material in the near term.

#### Revenue by Segment

Revenue by segment for the nine months ended September 30, 2014 and 2013 was as follows:

	Nine Months Ended September 30,				
	2014	% of total	2013	% of total	
	(dollars in thousands)				
North America:					
Third party and other	\$559,330	24.7	% \$564,484	31.3	%
Direct	714,157	31.5	513,090	28.4	
Total segment revenue	1,273,487	56.2	1,077,574	59.7	
EMEA:					
Third party and other	392,313	17.3	472,807	26.2	
Direct	296,342	13.1	18,903	1.0	
Total segment revenue	688,655	30.4	491,710	27.2	
Rest of World:					
Third party and other	280,530	12.4	215,675	11.9	
Direct	23,595	1.0	20,249	1.2	
Total segment revenue	304,125	13.4	235,924	13.1	
Total revenue	\$2,266,267	100.0	% \$1,805,208	100.0	%

Edgar Filing: Groupon, Inc. - Form 10-Q

Revenue by category and segment for the nine months ended September 30, 2014 and 2013 was as follows (in thousands):

	North America		EMEA		Rest of World		Consolidated	
	Nine Months Ended September 30,		Nine Months Ended September 30,		Nine Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013	2014	2013	2014	2013
Local <sup>(1)</sup> :								
Third party and other <sup>(2)</sup>	\$503,659	\$510,284	\$295,607	\$313,959	\$131,610	\$141,163	\$930,876	\$965,406
Direct revenue	—	1,733	—	—	—	—	—	1,733
Total	503,659	512,017	295,607	313,959	131,610	141,163	930,876	967,139
Goods:								
Third party	3,859	11,794	49,070	110,821	112,686	50,262	165,615	172,877
Direct revenue	714,157	511,357	296,342	18,903	23,595	20,249	1,034,094	550,509
Total	718,016	523,151	345,412	129,724	136,281	70,511	1,199,709	723,386
Travel:								
Third party <sup>(2)</sup>	51,812	42,406	47,636	48,027	36,234	24,250	135,682	114,683
Total revenue	\$1,273,487	\$1,077,574	\$688,655	\$491,710	\$304,125	\$235,924	\$2,266,267	\$1,805,208

(1) Includes revenue from deals with local merchants, from deals with national merchants, and through local events.

During the three months ended March 31, 2014, the Company began classifying other revenue as a component of (2) the Local category. Other revenue was previously aggregated with the Travel category. The prior period category information has been retrospectively adjusted to conform to the current period presentation.

#### North America

North America segment revenue increased by \$195.9 million to \$1,273.5 million for the nine months ended September 30, 2014, as compared to \$1,077.6 million for the nine months ended September 30, 2013. The increase in revenue primarily resulted from a \$202.8 million increase in direct revenue from our Goods category, which includes \$58.1 million of direct revenue from Ideel, which we acquired in January 2014. Direct revenue, which is recorded on a gross basis, is derived primarily from selling products through our Goods category where we are the merchant of record. Revenue in our Travel category also increased by \$9.4 million, which resulted from a \$64.7 million increase in gross billings, partially offset by a reduction in the percentage of gross billings that we retained after deducting the merchant's share to 20.2% for the nine months ended September 30, 2014, as compared to 22.1% for the nine months ended September 30, 2013. The increase in North America segment revenue was partially offset by a \$6.6 million decrease in third party and other revenue in our Local category, which resulted from a reduction in the percentage of gross billings that we retained after deducting the merchant's share to 36.9% for the nine months ended September 30, 2014, as compared to 39.0% for the nine months ended September 30, 2013. These decreases in the percentage of gross billings that we retained after deducting the merchant's share reflects the overall results of individual deal-by-deal negotiations with merchants and can vary significantly from period-to-period. We were willing to accept lower deal margins in order to improve the quality and increase the number of deals offered to customers by offering more attractive terms to merchants. The overall increase in revenue in our North America segment was also due to an increase in active customers, partially offset by lower gross billings per average active customer and increased order discounts for the nine months ended September 30, 2014, as compared to the prior year period.

We believe that increases in transaction activity on mobile devices and in the number of deals that we offered contributed to the growth in revenue for our North America segment. In addition, we have continued to refine our approach to targeting customers and have undertaken marketing initiatives to increase consumer awareness of deals available through our marketplaces, which we believe contributed to the revenue growth.

#### EMEA

EMEA segment revenue increased by \$196.9 million to \$688.7 million for the nine months ended September 30, 2014, as compared to \$491.7 million for the nine months ended September 30, 2013. The increase in revenue primarily resulted from a \$277.4 million increase in direct revenue from our Goods category. Revenue from transactions in the Goods category in our

EMEA segment were primarily presented on a net basis within third party revenue in the prior year period, as we were not typically the merchant of record for those transactions outside of the United States. However, we began increasing the number of product deals offered in our EMEA segment for which we are the merchant of record beginning in September 2013. As a result, the proportion of direct revenue deals in the Goods category of our EMEA segment increased for the nine months ended September 30, 2014 as compared to the prior year period, and we expect that the proportion of direct revenue deals in the Goods category of our EMEA segment will continue to increase in future periods.

The increase in direct revenue in our Goods category was partially offset by a \$61.8 million decrease in third party revenue in our Goods category, which resulted from a \$199.1 million decrease in gross billings and a decrease in the percentage of gross billings that we retained after deducting the merchant's share to 18.3% for the nine months ended September 30, 2014, as compared to 23.7% for the nine months ended September 30, 2013. The increase in EMEA segment revenue was partially offset by an \$18.4 million decrease in third party and other revenue from our Local category, which primarily resulted from a decrease in the percentage of third party and other gross billings that we retained after deducting the merchant's share to 41.8% for the nine months ended September 30, 2014, as compared to 44.2% for the nine months ended September 30, 2013. These decreases in the percentage of third party and other gross billings that we retained during the nine months ended September 30, 2014 reflect the overall results of individual deal-by-deal negotiations with our merchants and can vary significantly from period-to-period. We were willing to accept lower deal margins, as compared to the prior year period, in order to improve the quality and increase the number of deals offered to our customers by offering more attractive terms to merchants.

The overall increase in revenue in our EMEA segment was also due to increased unit sales, an increase in active customers and higher gross billings per average active customer for the nine months ended September 30, 2014, as compared to the prior year period. The favorable impact on revenue from year-over-year changes in foreign exchange rates for the nine months ended September 30, 2014 was \$18.1 million.

#### Rest of World

Rest of World segment revenue increased by \$68.2 million to \$304.1 million for the nine months ended September 30, 2014, as compared to \$235.9 million for the nine months ended September 30, 2013. The increase in revenue was attributable to our acquisition of Ticket Monster, which contributed \$107.4 million in revenue for the nine months ended September 30, 2014. Revenue from our Goods category increased by \$65.8 million for the nine months ended September 30, 2014, as compared to the prior year period, due to a \$62.4 million increase in third party revenue, which resulted from a \$621.1 million increase in gross billings, partially offset by a reduction in the percentage of gross billings that we retained after deducting the merchant's share to 13.6% for the nine months ended September 30, 2014, as compared to 24.1% in the prior year period. The increase in third party revenue from our Goods category was attributable to the Ticket Monster acquisition, and the decrease in the percentage of gross billings that we retained after deducting the merchant's share primarily reflects the impact of Ticket Monster's lower deal margins. In our Rest of World segment, revenue from transactions in our Goods category are primarily presented on a net basis within third party revenue, as we have not typically been the merchant of record for those transactions outside of the United States and EMEA.

The increase in revenue from our Rest of World segment included a \$12.0 million increase in revenue from our Travel category, which resulted from an \$169.4 million increase in gross billings, partially offset by a reduction in the percentage of gross billings that we retained after deducting the merchant's share to 13.2% for the nine months ended September 30, 2014, as compared to 23.2% in the prior year period. Although gross billings on third party and other revenue transactions in our Local category increased by \$174.1 million, third party and other revenue in our Local category decreased by \$9.6 million, which resulted from a reduction in the percentage of third party and other gross billings that we retained after deducting the merchant's share to 24.9% for the nine months ended September 30, 2014, as compared to 39.9% for the nine months ended September 30, 2013. The decrease in the percentage of gross billings that we retained after deducting the merchant's share primarily reflects the impact of Ticket Monster's lower deal margins. The unfavorable impact on revenue from year-over-year changes in foreign exchange rates for the nine months ended September 30, 2014 was \$12.9 million.



## Cost of Revenue

Cost of revenue on third party, direct revenue and other deals for the nine months ended September 30, 2014 and 2013 was as follows:

	Nine Months Ended September 30,	
	2014	2013
	(in thousands)	
Cost of revenue:		
Third party	\$ 170,186	\$ 175,580
Direct	928,314	502,359
Other	12,040	3,944
Total cost of revenue	\$ 1,110,540	\$ 681,883

Cost of revenue is comprised of direct and certain indirect costs incurred to generate revenue. For direct revenue deals, cost of revenue includes the cost of inventory, shipping and fulfillment costs and inventory markdowns. Fulfillment costs are comprised of third party logistics provider costs, as well as rent, depreciation, personnel costs and other costs of operating our own fulfillment center, which began operations in the fourth quarter of 2013. For third party revenue transactions, cost of revenue includes estimated refunds for which the merchant's share is not recoverable. Other costs incurred to generate revenue, which include credit card processing fees, editorial costs, certain technology costs, web hosting and other processing fees, are allocated to cost of third party revenue, direct revenue, and other revenue in proportion to gross billings during the period. As a result of the significant growth we have experienced from direct revenue transactions relative to our total gross billings for the nine months ended September 30, 2014, as compared to the prior year period, an increased share of those allocable costs has been allocated to cost of direct revenue in our condensed consolidated statement of operations for the nine months ended September 30, 2014.

Cost of revenue increased by \$428.7 million to \$1,110.5 million for the nine months ended September 30, 2014, as compared to \$681.9 million for the nine months ended September 30, 2013, which was attributable to the growth in direct revenue from our Goods category. The increase in cost of revenue was primarily driven by the cost of inventory and related shipping and fulfillment costs on direct revenue deals, which were not as significant during the prior year period. We currently outsource a majority of our inventory fulfillment activities in the United States to third party logistics providers. However, we expect to reduce our usage of those third parties in future periods by transitioning additional inventory fulfillment work in the United States to internal resources. For example, we launched our own fulfillment center in the fourth quarter of 2013. Additionally, to further reduce the involvement of third party logistics providers in the fulfillment process in the United States, we have increased our use of arrangements in which the suppliers of our product offerings ship merchandise directly to our customers. We are also refining our inventory management practices to better allocate inventories among warehouses in different geographic regions throughout the United States to reduce shipping distances to customers and increase units per order. We believe that these initiatives will ultimately reduce our fulfillment costs and improve the margins on direct revenue transactions in our Goods category. However, we may incur increased fulfillment costs from time to time as we enhance our internal processes and continue to transition fulfillment work from third party logistics providers.

Cost of Revenue by Segment

Cost of revenue by segment for the nine months ended September 30, 2014 and 2013 was as follows:

	Nine Months Ended September 30,		2013		
	2014	% of total		% of total	
(dollars in thousands)					
North America:					
Third party and other	\$79,799	7.2	% \$75,908	11.1	%
Direct	657,878	59.2	463,155	68.0	
Total segment cost of revenue	737,677	66.4	539,063	79.1	
EMEA:					
Third party and other	30,896	2.8	55,635	8.2	
Direct	244,375	22.0	19,142	2.8	
Total segment cost of revenue	275,271	24.8	74,777	11.0	
Rest of World:					
Third party and other	71,531	6.4	47,981	7.0	
Direct	26,061	2.4	20,062	2.9	
Total segment cost of revenue	97,592	8.8	68,043	9.9	
Total cost of revenue	\$1,110,540	100.0	% \$681,883	100.0	%

Cost of revenue by category and segment for the nine months ended September 30, 2014 and 2013 was as follows (in thousands):

	North America		EMEA		Rest of World		Consolidated	
	Nine Months Ended		Nine Months Ended		Nine Months Ended		Nine Months Ended	
	September 30,	September 30,						
	2014	2013	2014	2013	2014	2013	2014	2013
Local <sup>(1)</sup> :								
Third party and other <sup>(2)</sup>	\$70,174	\$68,497	\$21,212	\$35,444	\$22,652	\$21,353	\$114,038	\$125,294
Direct	—	2,523	—	—	—	—	—	2,523
Total	70,174	71,020	21,212	35,444	22,652	21,353	114,038	127,817
Goods:								
Third party	620	1,477	6,051	14,557	40,585	22,755	47,256	38,789
Direct	657,878	460,632	244,375	19,142	26,061	20,062	928,314	499,836
Total	658,498	462,109	250,426	33,699	66,646	42,817	975,570	538,625
Travel:								
Third party <sup>(2)</sup>	9,005	5,934	3,633	5,634	8,294	3,873	20,932	15,441
Total cost of revenue	\$737,677	\$539,063	\$275,271	\$74,777	\$97,592	\$68,043	\$1,110,540	\$681,883

(1) Includes cost of revenue from deals with local merchants, from deals with national merchants, and through local events.

During the three months ended March 31, 2014, the Company began classifying other cost of revenue as a (2) component of the Local category. Other cost of revenue was previously aggregated with the Travel category. The prior period category information has been retrospectively adjusted to conform to the current period presentation.

North America

North America cost of revenue increased by \$198.6 million to \$737.7 million for the nine months ended September 30, 2014, as compared to \$539.1 million for the nine months ended September 30, 2013. The increase in cost of revenue was primarily driven by the cost of inventory and shipping costs related to direct revenue deals in our Goods category, due to the growth of that category as compared to the prior year period. Cost of revenue for the nine months ended September 30, 2014 includes \$50.3 million from the Ideel acquisition.



## EMEA

EMEA cost of revenue increased by \$200.5 million to \$275.3 million for the nine months ended September 30, 2014, as compared to \$74.8 million for the nine months ended September 30, 2013. The increase in cost of revenue was primarily driven by the cost of inventory related to direct revenue deals in our Goods category, as we began increasing the number of product deals offered in our EMEA segment for which we are the merchant of record beginning in September 2013.

## Rest of World

Rest of World cost of revenue increased by \$29.5 million to \$97.6 million for the nine months ended September 30, 2014, as compared to \$68.0 million for the nine months ended September 30, 2013. Cost of revenue for the nine months ended September 30, 2014 includes \$38.8 million from the Ticket Monster acquisition, which primarily consists of credit card processing fees.

## Gross Profit

Gross profit for the nine months ended September 30, 2014 and 2013 was as follows:

	Nine Months Ended September 30,	
	2014	2013
	(in thousands)	
Gross profit:		
Third party	\$1,043,665	\$1,067,438
Direct	105,780	49,883
Other	6,282	6,004
Total gross profit	\$1,155,727	\$1,123,325

Gross profit increased by \$32.4 million to \$1,155.7 million for the nine months ended September 30, 2014, as compared to \$1,123.3 million for the nine months ended September 30, 2013. This increase in gross profit resulted from the \$461.1 million increase in revenue during the nine months ended September 30, 2014, partially offset by the \$428.7 million increase in cost of revenue. The acquisitions of Ticket Monster and Ideel contributed \$68.6 million and \$7.8 million of gross profit, respectively, for the nine months ended September 30, 2014.

Gross profit as a percentage of revenue decreased to 51.0% for the nine months ended September 30, 2014, as compared to 62.2% for the nine months ended September 30, 2013. The decrease in gross profit as a percentage of revenue during the nine months ended September 30, 2014, as compared to the prior year period, was primarily attributable to the increase in direct revenue. Direct revenue primarily relates to deals in our Goods category, which typically have lower margins than deals in our Local and Travel categories. Additionally, direct revenue and the related cost of revenue are presented on a gross basis in our consolidated statements of operations, which contributes to lower gross profit as a percentage of revenue.

Gross profit on third party revenue decreased by \$23.8 million to \$1,043.7 million for the nine months ended September 30, 2014, as compared to \$1,067.4 million for the nine months ended September 30, 2013. This decrease in gross profit resulted from the \$29.2 million decrease in third party revenue, partially offset by the \$5.4 million decrease in the cost of third party revenue. Gross profit as a percentage of revenue on third party revenue deals increased to 86.0% for the nine months ended September 30, 2014, as compared to 85.9% for the nine months ended September 30, 2013.

Gross profit on direct revenue increased by \$55.9 million to \$105.8 million for the nine months ended September 30, 2014, as compared to \$49.9 million for the nine months ended September 30, 2013. This increase in gross profit resulted from the \$481.9 million increase in direct revenue to \$1,034.1 million for the nine months ended September 30, 2014, as compared to \$552.2 million for the nine months ended September 30, 2013, partially offset by the \$426.0 million increase in cost of revenue on direct revenue deals to \$928.3 million for the nine months ended September 30, 2014, as compared to \$502.4 million for the nine months ended September 30, 2013. Gross profit as a percentage of revenue on direct revenue deals increased to 10.2% for the nine months ended September 30, 2014, as compared to 9.0% for the nine months ended September 30, 2013. The increase in gross profit as a percentage of revenue on direct revenue deals was attributable, in part, to lower shipping and fulfillment costs as a percentage of direct revenue, partially offset by increased cost of inventory sold as a percentage of direct revenue.



## Gross Profit by Segment

Gross profit by segment for the nine months ended September 30, 2014 and 2013 was as follows:

	Nine Months Ended September 30, 2014		2013		
		% of total		% of total	
	(dollars in thousands)				
North America:					
Third party and other	\$479,531	41.5	% \$488,576	43.5	%
Direct	56,279	4.9	49,935	4.4	
Total gross profit	535,810	46.4	538,511	47.9	
EMEA:					
Third party and other	361,417	31.3	417,172	37.1	
Direct	51,967	4.5	(239)	—	
Total gross profit	413,384	35.8	416,933	37.1	
Rest of World:					
Third party and other	208,999	18.1	167,694	14.9	
Direct	(2,466)	(0.3)	187	0.1	
Total gross profit	206,533	17.8	167,881	15.0	
Total gross profit	\$1,155,727	100.0	% \$1,123,325	100.0	%

Gross profit by category and segment for the nine months ended September 30, 2014 and 2013 was as follows (in thousands):

	North America		EMEA		Rest of World		Consolidated	
	Nine Months Ended		Nine Months Ended		Nine Months Ended		Nine Months Ended	
	September 30,		September 30,		September 30,		September 30,	
	2014	2013	2014	2013	2014	2013	2014	2013
Local <sup>(1)</sup> :								
Third party and other <sup>(2)</sup>	\$433,485	\$441,787	\$274,395	\$278,515	\$108,958	\$119,810	\$816,838	\$840,112
Direct	—	(790)	—	—	—	—	—	(790)
Total	433,485	440,997	274,395	278,515	108,958	119,810	816,838	839,322
Goods:								
Third party	3,239	10,317	43,019	96,264	72,101	27,507	118,359	134,088
Direct	56,279	50,725	51,967	(239)	(2,466)	187	105,780	50,673
Total	59,518	61,042	94,986	96,025	69,635	27,694	224,139	184,761
Travel:								
Third party <sup>(2)</sup>	42,807	36,472	44,003	42,393	27,940	20,377	114,750	99,242
Total gross profit	\$535,810	\$538,511	\$413,384	\$416,933	\$206,533	\$167,881	\$1,155,727	\$1,123,325

(1) Includes gross profit from deals with local merchants, from deals with national merchants, and through local events.

During the three months ended March 31, 2014, the Company began classifying other gross profit as a component (2) of the Local category. Other gross profit was previously aggregated with the Travel category. The prior period category information has been retrospectively adjusted to conform to the current period presentation.

## North America

North America gross profit decreased by \$2.7 million to \$535.8 million for the nine months ended September 30, 2014, as compared to \$538.5 million for the nine months ended September 30, 2013. The decrease in gross profit was comprised of a \$7.5 million decrease in our Local category and a \$1.5 million decrease in our Goods category, partially offset by a \$6.3 million increase in our Travel category.



## EMEA

EMEA gross profit decreased by \$3.5 million to \$413.4 million for the nine months ended September 30, 2014, as compared to \$416.9 million for the nine months ended September 30, 2013. The decrease in gross profit was comprised of a \$4.1 million decrease in our Local category and a \$1.0 million decrease in our Goods category, partially offset by a \$1.6 million increase in our Travel category.

## Rest of World

Rest of World gross profit increased by \$38.7 million to \$206.5 million for nine months ended September 30, 2014, as compared to \$167.9 million for the nine months ended September 30, 2013. The increase in gross profit was comprised of a \$41.9 million increase in our Goods category and a \$7.6 million increase in our Travel category, partially offset by a \$10.9 million decrease in our Local category.

## Marketing

For the nine months ended September 30, 2014 and 2013, marketing expense was \$203.1 million and \$158.3 million, respectively. Marketing expense by segment as a percentage of segment revenue and as a percentage of total marketing expense for the nine months ended September 30, 2014 and 2013 was as follows:

	Nine Months Ended September 30,						
	2014	% of Segment Revenue	% of Total Marketing	2013	% of Segment Revenue	% of Total Marketing	
	(dollars in thousands)						
North America	\$ 103,494	8.1	% 50.9	% \$ 79,961	7.4	% 50.5	%
EMEA	57,070	8.3	28.1	49,783	10.1	31.4	
Rest of World	42,570	14.0	21.0	28,575	12.1	18.1	
Marketing	\$ 203,134	9.0	100.0	% \$ 158,319	8.8	100.0	%

Marketing expense increased by \$44.8 million to \$203.1 million for the nine months ended September 30, 2014, as compared to \$158.3 million for the nine months ended September 30, 2013. Marketing expense as a percentage of revenue increased to 9.0% for the nine months ended September 30, 2014, as compared to 8.8% for the nine months ended September 30, 2013. We evaluate marketing expense as a percentage of revenue because it gives us an indication of how well our marketing spend is driving revenue growth.

Our subscriber acquisition and customer activation marketing activities also include elements that are not presented as "Marketing" on our consolidated statements of operations, such as order discounts, free shipping on qualifying merchandise sales and accepting lower margins on our deals. Marketing is the primary method by which we acquire customers, and as such, is an important part of our business.

## North America

North America marketing expense increased by \$23.5 million to \$103.5 million for the nine months ended September 30, 2014, as compared to \$80.0 million for the nine months ended September 30, 2013. For the nine months ended September 30, 2014, marketing expense as a percentage of revenue for the North America segment increased to 8.1%, as compared to 7.4% for the nine months ended September 30, 2013. These increases were primarily attributable to an increase in online marketing spend, in connection with our initiatives to grow our active customer base and increase awareness of the pull marketplace.

## EMEA

EMEA marketing expense increased by \$7.3 million to \$57.1 million for the nine months ended September 30, 2014, as compared to \$49.8 million for the nine months ended September 30, 2013. The increase in marketing expense was primarily due to increased spending on online marketing channels, such as display advertising and affiliate programs that utilize third parties to promote our deals online. For the nine months ended September 30, 2014, marketing expense as a percentage of revenue for the EMEA segment decreased to 8.3%, as compared to 10.1% for the nine months ended September 30, 2013.

## Rest of World

Rest of World marketing expense increased by \$14.0 million to \$42.6 million for the nine months ended September 30, 2014, as compared to \$28.6 million for the nine months ended September 30, 2013. For the nine months ended September 30, 2014, marketing expense as a percentage of revenue for the Rest of World segment increased to 14.0%, as compared to 12.1% for the nine months ended September 30, 2013. These increases were primarily attributable to our acquisition of Ticket Monster, as we incurred \$21.0 million of marketing expenditures for the nine months ended September 30, 2014 in connection with our initiatives to grow the business.

## Selling, General and Administrative

Selling, general and administrative expense increased by \$78.9 million to \$983.8 million for the nine months ended September 30, 2014, as compared to \$904.9 million for the nine months ended September 30, 2013. This increase was attributable to the Ticket Monster and Ideel acquisitions. Wages and benefits (excluding stock-based compensation) within selling, general and administrative expense increased by \$57.5 million for the nine months ended September 30, 2014, as compared to the prior year period, primarily due to the additional employees from those acquisitions. Depreciation and amortization recorded within selling, general and administrative expense increased by \$38.0 million for the nine months ended September 30, 2014, which includes increased amortization expense related to intangible assets acquired as part of those acquisitions. These increases were partially offset by lower corporate costs, including lower consulting and legal costs.

Selling, general and administrative expense as a percentage of revenue was 43.4% for the nine months ended September 30, 2014, as compared to 50.1% for the nine months ended September 30, 2013, respectively. Although revenue increased by \$461.1 million, or 25.5%, for the nine months ended September 30, 2014, as compared to the prior year period, selling, general and administrative expense increased by \$78.9 million, or 8.7%. We are continuing to refine our sales management and administrative processes, including through automation and ongoing regionalization of back-office functions, in connection with our efforts to generate increased operating efficiencies.

## Acquisition Related (Benefit) Expense, Net

For the nine months ended September 30, 2014 and 2013, we incurred a net acquisition-related expense of \$2.1 million and a benefit of \$2.3 million, respectively. For the nine months ended September 30, 2014, the net acquisition-related expense included \$3.1 million of external transaction costs, primarily related to the acquisitions of Ticket Monster and Ideel as described in Note 2 "Business Combinations," partially offset by \$1.1 million related to changes in the fair value of contingent consideration. See Note 10 "Fair Value Measurements" for information about fair value measurements of contingent consideration arrangements.

## (Loss) Income from Operations

The loss from operations for the nine months ended September 30, 2014 was \$33.2 million, as compared to income from operations for the nine months ended September 30, 2013 of \$62.4 million. The change in (loss) income from operations for the nine months ended September 30, 2014, as compared to the prior year period, was primarily due to the increase in selling, general and administrative expense of \$78.9 million and marketing expense of \$44.8 million, partially offset by the increase in gross profit of \$32.4 million. The favorable impact on the loss from operations from year-over-year changes in foreign exchange rates for the nine months ended September 30, 2014 was \$2.3 million.

## North America

Segment operating income in our North America segment, which excludes stock-based compensation and acquisition-related (benefit) expense, net, decreased by \$76.5 million to \$38.5 million for the nine months ended September 30, 2014, as compared to \$115.0 million for the nine months ended September 30, 2013. The decrease in segment operating income was attributable to an increase in segment operating expenses and a decrease in segment gross profit.



#### EMEA

Segment operating income in our EMEA segment, which excludes stock-based compensation and acquisition-related(benefit) expense, net, decreased by \$5.4 million to \$69.1 million for the nine months ended September 30, 2014, as compared to \$74.5 million for the nine months ended September 30, 2013. The decrease in segment operating income was attributable to a decrease in segment gross profit and an increase in segment operating expenses.

#### Rest of World

Segment operating loss in our Rest of World segment, which excludes stock-based compensation and acquisition-related (benefit) expense, net, increased by \$8.6 million to a loss of \$48.8 million for the nine months ended September 30, 2014, as compared to a loss of \$40.2 million for the nine months ended September 30, 2013. The increased segment operating loss was attributable to an increase in segment operating expenses, partially offset by an increase in segment gross profit.

#### Other Expense, Net

Other expense, net was \$21.9 million for the nine months ended September 30, 2014, as compared to \$9.8 million for the nine months ended September 30, 2013. The current period loss was primarily comprised of \$20.1 million in foreign currency transaction losses and \$2.0 million of other-than-temporary impairments related to minority investments. The foreign currency transaction losses primarily represent unrealized losses on intercompany balances with our subsidiaries that are denominated in foreign currencies. The foreign currency losses on those intercompany balances primarily resulted from the significant decline in the Euro against the U.S. dollar from an exchange rate of 1.3763 on December 31, 2013 to 1.2598 on September 30, 2014. For the nine months ended September 30, 2013, other income, net was primarily comprised of \$11.2 million of foreign currency transaction losses, partially offset by \$1.2 million of interest income, net.

#### Provision for Income Taxes

For the nine months ended September 30, 2014 and 2013, we recorded income tax expense of \$20.2 million and \$62.7 million, respectively.

The effective tax rate was (36.6)% for the nine months ended September 30, 2014, as compared to 119.2% for the nine months ended September 30, 2013. Significant factors impacting our effective tax rate for the nine months ended September 30, 2014 and 2013 included losses in jurisdictions that we are not able to benefit due to uncertainty as to the realization of those losses, amortization of the tax effects of intercompany sales of intellectual property and nondeductible stock-based compensation expense. Additionally, the effective tax rate for the nine months ended September 30, 2014 included a \$7.7 million decrease to our liabilities for uncertain tax positions, as discussed below. We expect that our consolidated effective tax rate in future periods will continue to differ significantly from the U.S. federal income tax rate as a result of our tax obligations in jurisdictions with profits and valuation allowances in jurisdictions with losses. Our consolidated effective tax rate in future periods will also be adversely impacted by the amortization of the tax effects of intercompany transactions, including intercompany sales of intellectual property that we expect to undertake in the future.

We are currently undergoing income tax audits in multiple jurisdictions. There are many factors, including factors outside of our control, which influence the progress and completion of these audits. For the nine months ended September 30, 2014, we decreased our liabilities for uncertain tax positions and income tax expense by \$7.7 million as a result of new information that impacted our estimates of amounts that are more-likely-than not of being realized upon ultimate settlement. As of September 30, 2014, we believe that it is reasonably possible that additional changes of up to \$35.5 million in unrecognized tax benefits may occur within the next 12 months upon closing of income tax audits or the expiration of applicable statutes of limitations.

### Non-GAAP Financial Measures

In addition to financial results reported in accordance with U.S. GAAP, we have provided the following non-GAAP financial measures: Adjusted EBITDA, free cash flow and foreign exchange rate neutral operating results. These non-GAAP financial measures are used in addition to and in conjunction with results presented in accordance with U.S. GAAP. However, these measures are not intended to be a substitute for those reported in accordance with U.S. GAAP. These measures may be different from non-GAAP financial measures used by other companies, even when similar terms are used to identify such measures.

**Adjusted EBITDA.** Adjusted EBITDA is a non-GAAP financial measure that comprises net loss excluding income taxes, interest and other non-operating items, depreciation and amortization, stock-based compensation and acquisition-related (benefit) expense, net. We exclude stock-based compensation expense and depreciation and amortization because they are primarily non-cash in nature, and we believe that non-GAAP financial measures excluding these items provide meaningful supplemental information about our operating performance and liquidity. Acquisition-related (benefit) expense, net is comprised of the change in the fair value of contingent consideration arrangements and external transaction costs related to business combinations, primarily consisting of legal and advisory fees. Our definition of Adjusted EBITDA may differ from similar measures used by other companies, even when similar terms are used to identify such measures. Adjusted EBITDA is a key measure used by our management and Board of Directors to evaluate operating performance, generate future operating plans and make strategic decisions for the allocation of capital. Accordingly, we believe that Adjusted EBITDA provides useful information to investors and others in understanding and evaluating our operating results in the same manner as our management and Board of Directors.

The following is a reconciliation of Adjusted EBITDA to the most comparable U.S. GAAP financial measure, "Net loss" for the three and nine months ended September 30, 2014 and 2013 (in thousands):

	Three Months Ended September		Nine Months Ended September	
	30,	2013	30,	2013
	2014	2013	2014	2013
Net loss	\$ (19,018	) \$ (1,292	) \$ (75,303	) \$ (10,085
Adjustments:				
Stock-based compensation <sup>(1)</sup>	34,574	26,870	89,958	89,223
Acquisition-related (benefit) expense, net <sup>(2)</sup>	(304	) (1,529	) 2,078	(2,276
Depreciation and amortization	38,146	23,149	107,544	65,317
Other expense (income), net	20,023	(832	) 21,886	9,830
(Benefit) provision for income taxes	(6,434	) 15,936	20,181	62,657
Total adjustments	86,005	63,594	241,647	224,751
Adjusted EBITDA	\$66,987	\$62,302	\$166,344	\$214,666

(1) Represents stock-based compensation expense recorded within "Selling, general and administrative," "Cost of revenue," and "Marketing" on the consolidated statements of operations.

(2) Represents changes in the fair value of contingent consideration related to business combinations and external transaction costs related to business combinations, primarily consisting of legal and advisory fees.

**Free cash flow.** Free cash flow is a non-GAAP financial measure that comprises net cash provided by operating activities less purchases of property and equipment and capitalized software. We use free cash flow, and ratios based on it, to conduct and evaluate our business because, although it is similar to cash flow from operations, we believe that it typically represents a more useful measure of cash flows because purchases of fixed assets, software developed for internal-use and website development costs are necessary components of our ongoing operations. Free cash flow is not intended to represent the total increase or decrease in our cash balance for the applicable period.

Free cash flow has limitations due to the fact that it does not represent the residual cash flow available for discretionary expenditures. For example, free cash flow does not include the cash payments for business acquisitions. In addition, free cash flow reflects the impact of the timing difference between when we are paid by customers and when we pay merchants and suppliers. Therefore, we believe it is important to view free cash flow as a complement to our entire consolidated statements of cash flows.



The following is a reconciliation of free cash flow to the most comparable U.S. GAAP financial measure, "Net cash provided by operating activities," for the three and nine months ended September 30, 2014 and 2013 (in thousands):

	Three Months Ended September		Nine Months Ended September	
	30,		30,	
	2014	2013	2014	2013
Net cash provided by (used in) operating activities	\$45,466	\$(11,905)	\$2,002	\$40,157
Purchases of property and equipment and capitalized software	(20,053)	(15,064)	(67,461)	(43,574)
Free cash flow	\$25,413	\$(26,969)	\$(65,459)	\$(3,417)
Net cash used in investing activities	\$(20,461)	\$(26,444)	\$(193,567)	\$(72,985)
Net cash used in financing activities	\$(16,823)	\$(8,970)	\$(173,068)	\$(26,253)

Foreign exchange rate neutral operating results. Foreign exchange rate neutral operating results show current period operating results as if foreign currency exchange rates had remained the same as those in effect in the comparable prior year period. These measures are intended to facilitate comparisons to our historical performance. For a reconciliation of foreign exchange rate neutral operating results to the most comparable U.S. GAAP financial measure, see "Results of Operations" above.

#### Liquidity and Capital Resources

As of September 30, 2014, we had \$855.2 million in cash and cash equivalents, which primarily consisted of cash, money market accounts and overnight securities.

Since our inception, we have funded our working capital requirements and expansion primarily with cash flows from operations and through public and private sales of common and preferred stock, which have yielded net proceeds of approximately \$1,857.1 million. We generated positive cash flow from operations for the three and nine months ended September 30, 2014 and we expect cash flows from operations to be positive in annual periods for the foreseeable future. We generally use this cash flow to fund our operations, make acquisitions, purchase capital assets, purchase treasury stock and meet our other cash operating needs. Cash flow provided by operations was \$2.0 million and \$40.2 million for the nine months ended September 30, 2014 and 2013, respectively.

We consider the undistributed earnings of our foreign subsidiaries as of September 30, 2014 to be indefinitely reinvested and, accordingly, no U.S. income taxes have been provided thereon. As of September 30, 2014, the amount of cash and cash equivalents held in foreign jurisdictions was approximately \$365.8 million. We have not, nor do we anticipate the need to, repatriate funds to the United States to satisfy domestic liquidity needs arising in the ordinary course of business.

In August 2014, we entered into a three-year senior secured revolving credit agreement (the "Credit Agreement") that provides for aggregate principal borrowings of up to \$250.0 million. Borrowings under the Credit Agreement bear interest, at our option, at a rate per annum equal to the Alternate Base Rate or Adjusted LIBO Rate (each as defined in the Credit Agreement) plus an additional margin ranging between 0.25% and 2.00%. We are required to pay quarterly commitment fees ranging from 0.20% to 0.35% per annum of the average daily amount available under the Credit Agreement. The Credit Agreement also provides for the issuance of up to \$45.0 million in letters of credit, provided that the sum of outstanding borrowings and letters of credit do not exceed the maximum funding commitment of \$250.0 million. Under the terms of the Credit Agreement, we are required to maintain, as of the last day of each fiscal quarter, unrestricted cash of at least \$400.0 million, including \$200.0 million in accounts held with lenders under the Credit Agreement or their affiliates. The Credit Agreement also contains various other operating and financial covenants. See Note 7 "Revolving Credit Facility" for additional information. No borrowings are currently outstanding under the Credit Agreement and we were in compliance with all covenants as of September 30, 2014. Although we can provide no assurances, we believe that our available cash and cash equivalents balance and cash generated from operations should be sufficient to meet our working capital requirements and other capital expenditures for at least the next twelve months.

#### Uses of Cash

On January 2, 2014, we acquired Ticket Monster for an aggregate acquisition price of \$259.4 million, after closing working capital adjustments, of which \$96.5 million was paid in cash and the balance was paid in our Class A common stock. On January

13, 2014, we acquired all of the outstanding equity interests of Ideel for an aggregate acquisition price of \$42.7 million, of which \$42.3 million has been paid for in cash. In the second quarter of 2014, we acquired two other businesses for an aggregate acquisition price of \$7.5 million, of which \$3.5 million has been paid for in cash. We intend to continue to acquire additional businesses and make strategic minority investments in complementary businesses in future periods to grow our customer base, expand our merchant relationships, enhance our technology capabilities and acquire experienced workforces.

In order to support our current and future global expansion, we expect to continue to make significant investments in our technology platforms and business processes, as well as internal tools aimed at improving the efficiency of our operations. We will also continue to invest in sales and marketing as we seek to grow both the number of active deals available through our online local marketplaces and the volume of transactions through those marketplaces.

The Board of Directors has authorized us to purchase up to \$300.0 million of our outstanding Class A common stock through August 2015. The timing and amount of any share repurchases will be determined based on market conditions, share price and other factors, and the program may be discontinued or suspended at any time. Repurchases will be made in compliance with SEC rules and other legal requirements and may be made in part under a Rule 10b5-1 plan, which permits stock repurchases when the Company might otherwise be precluded from doing so. During the nine months ended September 30, 2014, we purchased 21.7 million shares of Class A common stock for an aggregate purchase price of \$143.8 million (including fees and commissions) under the share repurchase program. As of September 30, 2014, up to \$109.6 million of Class A common stock remains available for repurchase under the share repurchase program.

We currently plan to fund investments in business acquisitions, strategic minority investments, technology, and sales and marketing, as well as our share repurchase program, with our available cash and cash equivalents and cash flows generated from our operations. We also have the ability to borrow funds under the Credit Agreement, described above, although we have no immediate plans to do so. We may also seek to raise additional financing, if available on terms that we believe are favorable, to increase the amount of liquid funds that we can access for future acquisitions or other strategic investment opportunities.

#### Cash Flow

Our net cash flows from operating, investing and financing activities for the nine months ended September 30, 2014 and 2013 were as follows:

	Nine Months Ended September 30,	
	2014	2013
	(in thousands)	
Cash provided by (used in):		
Operating activities	\$2,002	\$40,157
Investing activities	(193,567	) (72,985
Financing activities	(173,068	) (26,253
Effect of changes in exchange rates on cash and cash equivalents	(20,671	) (10,351
Net decrease in cash and cash equivalents	\$(385,304	) \$(69,432

#### Cash Provided by Operating Activities

Cash provided by operating activities primarily consists of our net loss adjusted for certain items, including depreciation and amortization, stock based compensation, deferred income taxes and the effect of changes in working capital and other items.

Our current merchant arrangements are structured as either a redemption payment model or a fixed payment model defined as follows:

Redemption payment model - We typically pay our merchants upon redemption for the majority of deals in our EMEA and Rest of World segments. Under our redemption merchant payment model, we collect payments at the time our customers purchase Groupons and make payments to our merchants at a subsequent date. Using this payment model, merchants are not paid until the customer redeems the Groupon that has been purchased. If a customer does not redeem the Groupon under this payment model, we retain all of the gross billings from the unredeemed Groupon. The redemption model generally improves our overall cash flow because we do not pay our merchants until the customer redeems the Groupon.



Fixed payment model - We typically pay our merchants under the fixed payment model for the majority of deals in North America. For third party revenue deals in which the merchant has a continuous presence on our websites and mobile applications by offering deals for an extended period of time, which currently represents a substantial majority of our third party revenue deals in North America, we remit payments to the merchant on an ongoing basis, generally bi-weekly, throughout the term of the offering. For direct revenue deals in our Goods category, payment terms with our suppliers typically range from net 30 days to net 60 days. Under the fixed payment model, merchants are paid regardless of whether the Groupon is redeemed.

We experience fluctuations in accrued merchant and supplier payables associated with our normal revenue-generating activities, including both third party and direct revenue sales transactions, that can cause volatility in working capital levels and impact cash balances more or less than our operating income or loss would indicate. Revenue from our Goods category has grown rapidly in recent periods, both in absolute dollars and as a percentage of the Company's overall revenue. This category has lower margins than our Local category, primarily as a result of shipping and fulfillment costs on direct revenue transactions. As a result of those lower margins, the amount of cash that we ultimately retain from direct revenue transactions in our Goods category after paying the related inventory, shipping and fulfillment costs is less than the amount that we ultimately retain from third party revenue transactions in our Local category after paying the merchant's share. However, the impact of transactions in our Goods category on our operating cash flows varies from period to period. For example, the cash flows from transactions in that category are impacted by seasonality, with strong cash inflows typically generated during the fourth quarter holiday season followed by subsequent cash outflows when payments are made to suppliers of the merchandise.

For the nine months ended September 30, 2014, our net cash provided by operating activities was \$2.0 million, which consisted of a \$184.4 million net increase for certain non-cash items, partially offset by a \$107.1 million net decrease related to changes in working capital and other assets and liabilities and a \$75.3 million net loss. The net decrease in cash resulting from changes in working capital activities primarily consisted of a \$61.2 million decrease in accrued merchant and supplier payables, a \$32.4 million increase in prepaid expenses and other current assets, a \$29.3 million increase in accounts receivable, a \$27.1 million decrease in accrued expenses and other current liabilities and a \$9.0 million decrease in accounts payable, partially offset by a \$44.9 million net increase from other items, which include \$20.1 million of foreign currency transaction losses, primarily related to intercompany balances denominated in foreign currencies, and the net change in non-current assets and liabilities. The \$61.2 million decrease in accrued merchant and supplier payables was primarily due to the timing of payments to suppliers of merchandise and the seasonally high levels of Goods transactions in the fourth quarter of 2013. The net adjustments for certain non-cash items include \$107.5 million of depreciation and amortization expense and \$90.0 million of stock-based compensation expense, partially offset by \$12.6 million of excess tax benefits on stock-based compensation.

For the nine months ended September 30, 2013, our net cash provided by operating activities was \$40.2 million, which consisted of a \$139.0 million net increase for certain non-cash items, partially offset by an \$88.7 million net decrease related to changes in working capital and other assets and liabilities and a \$10.1 million net loss. The net adjustments for certain non-cash items include \$89.2 million of stock-based compensation expense and \$65.3 million of depreciation and amortization expense, partially offset by \$12.1 million of excess tax benefits on stock-based compensation. The net decrease in cash resulting from changes in working capital activities primarily consisted of a \$72.3 million decrease in accrued merchant and supplier payables, a \$27.8 million decrease in accrued expenses and other current liabilities and a \$25.9 million decrease in accounts payable, partially offset by a \$13.1 million decrease in prepaid expenses and other current assets and a \$9.0 million decrease in accounts receivable. The \$72.3 million decrease in accrued merchant and supplier payables was primarily attributable to payments to suppliers of merchandise in early 2013 related to Goods transactions from November and December of 2012.

#### Cash Used in Investing Activities

Cash used in investing activities primarily consists of capital expenditures, acquisitions of businesses and minority investments.

For the nine months ended September 30, 2014, our net cash used in investing activities of \$193.6 million consisted of \$117.3 million in net cash paid for acquisitions as described in Note 2, "Business Combinations," \$67.5 million in capital expenditures, including capitalized internally-developed software, \$6.7 million in purchases of investments, \$1.6 million related to the purchase of additional interests in consolidated subsidiaries and \$0.5 million in purchases of

intangible assets.

For the nine months ended September 30, 2013, our net cash used in investing activities of \$73.0 million primarily consisted of \$43.6 million in capital expenditures, including capitalized internally-developed software, \$19.6 million in purchases of investments, \$6.3 million in net cash paid for acquisitions, \$2.0 million related to the settlement of the liability related to the purchase of an additional interest in a consolidated subsidiary and \$1.5 million in purchases of intangible assets.

#### Cash Used in Financing Activities

For the nine months ended September 30, 2014, our net cash used in financing activities of \$173.1 million was driven primarily by purchases of treasury stock under our share repurchase program of \$145.4 million and taxes paid related to net share settlements of stock-based compensation awards of \$32.4 million. Our net cash used in financing activities was also due to partnership distributions to noncontrolling interest holders of \$6.2 million, payments of capital lease obligations of \$3.6 million, settlements of purchase price obligations related to acquisitions of \$3.1 million and debt issuance costs of \$1.0 million, partially offset by \$12.6 million of excess tax benefits related to stock-based compensation and \$6.2 million of proceeds from stock option exercises and our employee stock purchase plan.

For the nine months ended September 30, 2013, our net cash used in financing activities of \$26.3 million was driven primarily by taxes paid related to net share settlements of stock-based compensation awards of \$26.5 million. We also paid \$7.4 million for the purchase of treasury stock under the share repurchase program. Our net cash used in financing activities was also due to settlements of purchase price obligations related to acquisitions of \$5.0 million, partnership distributions to noncontrolling interest holders of \$4.3 million and payments of capital lease obligations of \$1.0 million, partially offset by \$12.1 million of excess tax benefits related to stock-based compensation and \$6.6 million of proceeds from stock option exercises and our employee stock purchase plan.

#### Free Cash Flow

Free cash flow, a non-GAAP financial measure, was \$(65.5) million and \$(3.4) million for the nine months ended September 30, 2014, and 2013, respectively. The decrease in free cash flow for the nine months ended September 30, 2014, as compared to the prior year period, was due to the \$38.2 million decrease in our operating cash flow and higher capital expenditures. For further information and a reconciliation to the most applicable financial measure under U.S. GAAP, refer to our discussion under "Non-GAAP Financial Measures" above.

### Contractual Obligations and Commitments

Except for commitments under operating leases that were assumed in connection with the Ticket Monster and Ideel acquisitions, as described in Note 2, "Business Combinations," our commitments as of September 30, 2014 did not materially change from the amounts set forth in our 2013 Annual Report on Form 10-K. As of September 30, 2014, estimated future payments under operating leases assumed in connection with the Ticket Monster and Ideel acquisitions for each of the next five years and thereafter are as follows (in thousands):

	Operating leases
2014	\$ 1,348
2015	5,148
2016	4,936
2017	4,342
2018	2,631
Thereafter	11,110
Total minimum lease payments	\$29,515

### Off-Balance Sheet Arrangements

We did not have any off-balance sheet arrangements as of September 30, 2014.

### Critical Accounting Policies and Estimates

Management's Discussion and Analysis of Financial Condition and Results of Operations is based upon our condensed consolidated financial statements, which have been prepared in accordance with U.S. generally accepted accounting principles ("U.S. GAAP"). Our significant accounting policies are discussed in Note 2 "Summary of Significant Accounting Policies" in the notes to the consolidated financial statements included in our 2013 Annual Report on Form 10-K for the year ended December 31, 2013, as filed with the U.S. Securities and Exchange Commission ("SEC") on February 20, 2014.

The preparation of consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts and classifications of assets and liabilities, revenue and expense, and related disclosure of contingent liabilities. Management bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. If actual amounts are ultimately different from previous estimates, the revisions are included in our results of operations for the period in which the actual amounts become known.

An accounting policy is deemed to be critical if it requires an accounting estimate to be made based on assumptions about matters that are highly uncertain at the time the estimate is made, and if different estimates that reasonably could have been used, or changes in the accounting estimates that are reasonably likely to occur periodically, could materially impact the financial statements. Management believes its critical accounting policies that reflect its more significant estimates and assumptions are policies related to revenue recognition, refunds, goodwill and long-lived assets, income taxes and other-than-temporary impairments.

### Revenue Recognition

We recognize revenue when the following criteria are met: persuasive evidence of an arrangement exists; delivery has occurred; the selling price is fixed or determinable; and collection is reasonably assured.

### Third party revenue recognition

We generate third party revenue, where we act as the third party marketing agent, by offering goods and services provided by third party merchants at a discount through our online local commerce marketplaces that connect merchants to consumers. Our marketplaces include deals offered in three primary categories: Local, Goods and Travel. Customers purchase the discount vouchers ("Groupons") from us and redeem them with merchants.

The revenue recognition criteria are met when the customer purchases a deal, the Groupon has been electronically delivered to the purchaser and a listing of Groupons sold has been made available to the merchant. At that time, our obligations to the merchant, for which we are serving as a marketing agent, are substantially complete. Our remaining obligations, which are limited to remitting payment to the merchant and continuing to make available on our website information about Groupons sold that was previously provided to the merchant, are inconsequential or perfunctory. For a portion of the hotel deals offered through our online local marketplaces, we facilitate the booking of rooms by taking reservations through our websites and managing any subsequent changes to those reservations. We defer the revenue on those deals until the customer's stay occurs.

We record as revenue the net amount we retain from the sale of Groupons after deducting the portion of the purchase price that is payable to the featured merchant, excluding applicable taxes and net of estimated refunds for which the merchant's share is recoverable. Revenue is recorded on a net basis because we are acting as a marketing agent of the merchant in the transaction.

For merchant payment arrangements that are structured under a redemption model, merchants are not paid until the customer redeems the Groupon that has been purchased. If a customer does not redeem the Groupon under this payment model, we retain all the gross billings. We record incremental revenue from unredeemed Groupons and derecognize the related accrued merchant payable when our legal obligation to the merchant expires, which we believe is shortly after deal expiration in most jurisdictions that have payment arrangements structured under a redemption model.

#### Direct revenue recognition

We evaluate whether it is appropriate to record the gross amount of our sales and related costs by considering a number of factors, including, among other things, whether we are the primary obligor under the arrangement, have inventory risk and have latitude in establishing prices.

Direct revenue is derived primarily from selling consumer products through our Goods category where we are the merchant of record. We are the primary obligor in these transactions, are subject to general inventory risk and have latitude in establishing prices. Accordingly, direct revenue is recorded on a gross basis, excluding applicable taxes and net of estimated refunds. For purposes of evaluating whether product revenue should be recognized on a gross basis, unmitigated general inventory risk is a strong indicator of whether a seller has the risks and rewards of a principal to the sale transaction. U.S. GAAP specifies that general inventory risk exists if a seller either takes title to a product before that product is ordered by a customer (that is, maintains the product in inventory) or will take title to the product if it is returned by the customer (that is, back-end inventory risk) and the customer has a right of return. We have unmitigated general inventory risk on our direct revenue transactions. Currently, that general inventory risk is primarily in the form of back-end inventory risk. However, we had \$57.3 million of finished goods inventory on hand as of September 30, 2014, and in future periods we may increase the levels of inventory on hand for our Goods category. For Goods transactions where we are performing a service by acting as a marketing agent of the merchant, revenue is recorded on a net basis and is presented within third party revenue.

Direct revenue, including associated shipping revenue, is recorded when title passes to the customer. In connection with our rollout of increased direct revenue deals outside the United States, a global change was made to customer terms and conditions in the fourth quarter of 2013 to specify that title to products transfers upon delivery. As a result of this change, we began recognizing direct revenue upon delivery, rather than shipment.

#### Discounts

We provide discount offers to encourage purchases of goods and services through our marketplaces. We record discounts as a reduction of revenue.

#### Refunds

We estimate future refunds utilizing a statistical model that incorporates the following data inputs and factors: historical refund experience developed from millions of deals featured on our website, the relative risk of refunds based on expiration date, deal value, deal category and other qualitative factors that could impact the level of future refunds, such as introductions of new deals, discontinuations of legacy deals and expected changes, if any, in our practices in response to refund experience or economic trends that might impact customer demand. The portion of customer refunds for which the merchant's share is not recoverable on third party revenue deals is estimated based on the refunds that are expected to be issued after expiration of the related vouchers, the refunds that are expected to be

issued due to the merchant bankruptcy or poor customer experience, and whether the payment terms of the related merchant contracts are structured using a redemption payment model or a fixed payment model.

We accrue costs associated with refunds within "Accrued expenses" on the consolidated balance sheets. The cost of

refunds for third party revenue where the amounts payable to the merchant are recoverable and for all direct revenue is presented on the consolidated statements of operations as a reduction to revenue. The cost of refunds for third party revenue for which the merchant's share is not recoverable is presented as a cost of revenue.

We assess the trends that could affect our estimates on an ongoing basis and make adjustments to the refund reserve calculations if it appears that changes in circumstances, including changes to the Company's refund policies, may cause future refunds to differ from our original estimates. If actual results are not consistent with the estimates or assumptions stated above, we may need to change our future estimates, and the effects could be material to the condensed consolidated financial statements.

#### Impairment Assessments of Goodwill and Long-Lived Assets

A component of our growth strategy has been to acquire and integrate businesses that complement our existing operations. We account for business combinations using the acquisition method and allocate the acquisition price of acquired companies to the tangible and intangible assets acquired and liabilities assumed based upon their estimated fair values at the acquisition date. The difference between the acquisition price and the fair value of the net assets acquired is recorded as goodwill.

In determining the fair value of assets acquired and liabilities assumed in business combinations and for determining fair values in impairment tests, we use one of the following recognized valuation methods: the income approach (including discounted cash flows), the market approach and the cost approach. Our significant estimates in those fair value measurements include identifying business factors such as size, growth, profitability, risk and return on investment and assessing comparable revenue and operating income multiples. Further, when measuring fair value based on discounted cash flows, we make assumptions about risk-adjusted discount rates, future price levels, rates of increase in revenue, cost of revenue, and operating expenses, weighted average cost of capital, rates of long-term growth, and income tax rates. Valuations are performed by management or third party valuation specialists under management's supervision, where appropriate. We believe that the estimated fair values assigned to the assets acquired and liabilities assumed and for determining fair value in business combinations and impairment tests are based on reasonable assumptions that marketplace participants would use. However, such assumptions are inherently uncertain and actual results could differ from those estimates.

Goodwill is allocated to our reporting units at the date the goodwill is initially recorded. Once goodwill has been allocated to the reporting units, it no longer retains its identification with a particular acquisition and becomes identified with the reporting unit in its entirety. Accordingly, the fair value of the reporting unit as a whole is available to support the recoverability of its goodwill.

We evaluate goodwill for impairment annually on October 1 or more frequently when an event occurs or circumstances change that indicates the carrying value may not be recoverable. We have the option to assess goodwill for impairment by first performing a qualitative assessment to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If we determine that it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then the two-step goodwill impairment test is not required to be performed. If we determine that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, we perform the two-step goodwill impairment test. In the first step, the fair value of the reporting unit is compared to its book value including goodwill. If the fair value of the reporting unit is in excess of its book value, the related goodwill is not impaired and no further analysis is necessary. If the fair value of the reporting unit is less than its book value, there is an indication of potential impairment and a second step is performed. When required, the second step of testing involves calculating the implied fair value of goodwill for the reporting unit. The implied fair value of goodwill is determined in the same manner as goodwill recognized in a business combination, which is the excess of the fair value of the reporting unit determined in step one over the fair value of its net assets and identifiable intangible assets as if the reporting unit had been acquired. If the carrying value of the reporting unit's goodwill exceeds the implied fair value of that goodwill, an impairment loss is recognized in an amount equal to that excess. For reporting units with a negative book value (i.e., excess of liabilities over assets), we evaluate qualitative factors to determine whether it is necessary to perform the second step of the goodwill impairment test. As of September 30, 2014, our market capitalization of \$4.5 billion substantially exceeded our consolidated net book value of \$728.0 million.

Long lived assets, such as property, equipment and software, net and intangible assets, net, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset or asset group may not be recoverable. If circumstances require that a long lived asset or asset group be tested for possible impairment, we first compare the undiscounted cash flows expected to be generated by that long-lived asset or asset group to its carrying amount. If the carrying amount of the long lived asset or asset group is not recoverable on an undiscounted cash flow basis, an impairment is recognized to the extent that the carrying amount exceeds its fair value.

Future changes in our assumptions or the interrelationship of those assumptions may negatively impact future valuations.

In future measurements of fair value, adverse changes in assumptions could result in an impairment of goodwill or long-lived assets that would require a non-cash charge to the consolidated statements of operations and may have a material effect on our financial condition and operating results.

#### Income Taxes

We account for income taxes using the asset and liability method, under which deferred income tax assets and liabilities are recognized based upon anticipated future tax consequences attributable to differences between financial statement carrying values of assets and liabilities and their respective tax bases. We regularly review deferred tax assets to assess whether it is more likely than not that the deferred tax assets will be realized and, if necessary, establish a valuation allowance for portions of such assets to reduce the carrying value.

For purposes of assessing whether it is more likely than not that our deferred tax assets will be realized, we consider the following four sources of taxable income for each tax jurisdiction: (a) future reversals of existing taxable temporary differences, (b) projected future earnings, (c) taxable income in carryback years, to the extent that carrybacks are permitted under the tax laws of the applicable jurisdiction, and (d) tax planning strategies, which represent prudent and feasible actions that a company ordinarily might not take, but would take to prevent an operating loss or tax credit carryforward from expiring unused. To the extent that evidence about one or more of these sources of taxable income is sufficient to support a conclusion that a valuation allowance is not necessary, other sources need not be considered. Otherwise, evidence about each of the sources of taxable income is considered in arriving at a conclusion about the need for and amount of a valuation allowance. We have incurred significant losses in recent years and had accumulated deficits of \$930.7 million and \$848.9 million as of September 30, 2014 and December 31, 2013, respectively. A cumulative loss in the most recent three-year period is a significant piece of negative evidence that is difficult to overcome when assessing the realizability of deferred tax assets. Outside of the United States, we have only recognized deferred tax assets to the extent that they will be realizable either through future reversals of existing taxable temporary differences or through taxable income in carryback years for the applicable jurisdictions. Due to our cumulative losses outside of the United States, we have recognized valuation allowances against deferred tax assets that are not supported by those objective sources of taxable income. As of September 30, 2014, we have not recognized deferred tax assets without a valuation allowance outside of the United States when the only sources of taxable income are projected future earnings or tax planning strategies. For certain jurisdictions where applicable tax law imposes limitations that may prevent us from realizing our deferred tax assets through the scheduled reversal of taxable temporary differences, we have recorded valuation allowances in excess of the net deferred tax asset balances.

We are subject to taxation in the United States, various state and foreign jurisdictions. Significant judgment is required in determining the worldwide provision for income taxes and recording the related income tax assets and liabilities. During the ordinary course of business, there are many transactions and calculations for which the ultimate tax determination is uncertain. For example, our effective tax rate could be adversely affected by earnings being lower than anticipated in countries where we have lower statutory rates and higher than anticipated in countries where we have higher statutory rates, by changes in foreign currency exchange rates, by changes in the valuation of our deferred tax assets and liabilities, or by changes in the relevant tax, accounting and other laws, regulations, principles and interpretations. Our practice for accounting for uncertainty in income taxes is to recognize the financial statement benefit of a tax position only after determining that the relevant tax authority would more likely than not sustain the position following an audit. For tax positions meeting the more likely than not criteria, the amount recognized in the financial statements is the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement with the relevant tax authority.

We are subject to audit in various jurisdictions, and such jurisdictions may assess additional income tax against us. Although we believe our tax estimates are reasonable, the final determination of any tax audits and any related litigation could be materially different from income tax provision accruals and, therefore, could materially affect our operating results or cash flows in the period(s) in which that determination is made.

#### Other-than-Temporary Impairment of Investments

An unrealized loss exists when the current fair value of an investment is less than its amortized cost basis. We conduct reviews of all of our investments with unrealized losses on a quarterly basis to evaluate whether those impairments are other-than-temporary. This evaluation, which is performed at the individual investment level, considers qualitative

and quantitative factors regarding the severity and duration of the unrealized loss, as well as our intent and ability to hold the investment for a period of time that is sufficient to allow for an anticipated recovery in value. Evidence considered in this evaluation includes the amount of the impairment, the length of time that the investment has been impaired, the factors contributing to the impairment, the financial condition and near-term prospects of the investee, recent operating trends and forecasted performance of the investee, market conditions in the geographic area or industry in which the investee operates, and our strategic plans for holding the investment in

relation to the period of time expected for an anticipated recovery in value. Additionally, we consider whether we intend to sell the investment or whether it is more likely than not that we will be required to sell the investment before recovery of its amortized cost basis. Investments with unrealized losses that are determined to be other-than-temporary are written down to fair value with a charge to earnings. Unrealized losses that are determined to be temporary in nature are not recorded for cost method investments and equity method investments, while such losses are recorded, net of tax, in accumulated other comprehensive income (loss) for available-for-sale securities.

#### Recently Issued Accounting Standards

In May 2014, the Financial Accounting Standards Board issued Accounting Standards Update ("ASU") 2014-09, Revenue from Contracts with Customers. This ASU is a comprehensive new revenue recognition model that requires a company to recognize revenue to depict the transfer of goods or services to a customer at an amount that reflects the consideration it expects to receive in exchange for those goods or services. The ASU is effective for annual periods beginning after December 15, 2016 and interim periods within those annual periods. Management is still assessing the impact of adoption on its condensed consolidated financial statements.

There are no additional accounting standards that have been issued but not yet adopted that we believe will have a material impact on our consolidated financial position or results of operations.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We have operations both within the United States and internationally, and we are exposed to market risks in the ordinary course of our business, including the effect of foreign currency fluctuations, interest rate changes and inflation. Information relating to quantitative and qualitative disclosures about these market risks is set forth below.

#### Foreign Currency Exchange Risk

We transact business in various foreign currencies other than the U.S. dollar, principally the Euro, Korean won, British pound sterling, Japanese yen and Brazilian real, which exposes us to foreign currency risk. For the three months ended September 30, 2014, we derived approximately 30.4% and 14.3% of our revenue from our EMEA and Rest of World segments, respectively. For the nine months ended September 30, 2014, we derived approximately 30.4% and 13.4% of our revenue from our EMEA and Rest of World segments, respectively. Revenue and related expenses generated from our international operations are generally denominated in the local currencies of the corresponding countries. The functional currency of our subsidiaries that either operate or support these markets is generally the same as the corresponding local currency. The results of operations of, and certain of our intercompany balances associated with, our international operations are exposed to foreign exchange rate fluctuations. Upon consolidation, as exchange rates vary, our revenue and other operating results may differ materially from expectations, and we may record significant gains or losses on the re-measurement of intercompany balances.

We assess our foreign currency exchange risk based on hypothetical changes in rates utilizing a sensitivity analysis that measures the potential impact on working capital based on a 10% change (increase and decrease) in currency rates. We use a current market pricing model to assess the changes in the value of the U.S. dollar on foreign currency denominated monetary assets and liabilities. The primary assumption used in this model is a hypothetical 10% weakening or strengthening of the U.S. dollar against those currency exposures as of September 30, 2014 and December 31, 2013.

As of September 30, 2014, our net working capital deficit (defined as current assets less current liabilities) from subsidiaries that are subject to foreign currency translation risk was \$134.3 million. The potential increase in this working capital deficit from a hypothetical 10% adverse change in quoted foreign currency exchange rates would be \$13.4 million. This compares to a \$168.2 million working capital deficit subject to foreign currency exposure as of December 31, 2013, for which a 10% adverse change would have resulted in a potential increase in this working capital deficit of \$16.8 million.

#### Interest Rate Risk

Our cash and cash equivalents primarily consist of cash and money market funds. Our exposure to market risk for changes in interest rates is limited because our cash and cash equivalents have a short-term maturity and are used primarily for working capital purposes. In August 2014, the Company entered into a three-year Credit Agreement that provides for aggregate principal borrowings up to \$250.0 million. As of September 30, 2014, there were no borrowings outstanding under the Credit Agreement. Because our Credit Agreement bears interest at a variable rate, we will be exposed to market risk relating to changes in interest rates, once we draw down under the Credit Agreement. We also have long-term borrowings, which consist of \$14.3 million of long-term capital lease obligations, and investments in convertible debt securities issued by nonpublic entities that are classified as available-for-sale. We believe that the interest rate risk on the long-term capital lease obligations and investments is not significant.

#### Impact of Inflation

We believe that our results of operations are not materially impacted by moderate changes in the inflation rate. Inflation and changing prices did not have a material effect on our business, financial condition or results of operations for the three and nine months ended September 30, 2014 and 2013.

### ITEM 4. CONTROLS AND PROCEDURES

#### Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and our Chief Financial Officer, has evaluated the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act), as of the end of the period covered by this Quarterly Report on Form 10-Q.



Based on this evaluation, our management concluded that, as of September 30, 2014, our disclosure controls and procedures are effective to provide reasonable assurance that information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

#### Changes in Internal Control over Financial Reporting

There was no change in our internal control over financial reporting identified in connection with the evaluation required by Rule 13a-15(d) and 15d-15(d) of the Exchange Act that occurred during the period covered by this Quarterly Report on Form 10-Q that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

#### Limitations on Effectiveness of Controls and Procedures

In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. In addition, the design of disclosure controls and procedures must reflect the fact that there are resource constraints and that management is required to apply its judgment in evaluating the benefits of possible controls and procedures relative to their costs.

## PART II. OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

For a description of our material pending legal proceedings, please see Note 6 "Commitments and Contingencies" of the Notes to the accompanying unaudited Condensed Consolidated Financial Statements included in Part I, Item 1 of this Quarterly Report on Form 10-Q.

#### ITEM 1A. RISK FACTORS

Our business, prospects, financial condition, operating results and the trading price of our Class A common stock could be materially adversely affected by any of these risks, as well as other risks not currently known to us or that we currently consider immaterial.

##### Risks Related to Our Business

Our revenue and operating results may continue to be volatile.

Our revenue and operating results will continue to vary from quarter to quarter due to the rapidly evolving nature of our business. We believe that our revenue growth and ability to achieve and maintain profitability will depend, among other factors, on our ability to:

- acquire new customers and retain existing customers;
- attract new merchants and retain existing merchants who wish to offer deals through the sale of Groupons;
- effectively address and respond to challenges in international markets;
- expand the number, variety and relevance of products and deals we offer, particularly as we attempt to build a more complete local marketplace;
- increase the awareness of our brand domestically and internationally;
- successfully achieve the anticipated benefits of business combinations or acquisitions, including our acquisitions of Ticket Monster and Ideel;
- provide a superior customer service experience for our customers and merchants;
- respond to changes in consumer and merchant access to and use of the Internet and mobile devices;
- react to challenges from existing and new competitors; and
- respond to seasonal changes in supply and demand.

In addition, our margins and profitability may depend on our product sales mix, our geographic revenue mix and merchant pricing terms. For example, sales in our Goods category, which typically carry lower margins than sales in our Local category, have grown faster in recent periods, which has resulted in lower margins and profitability during those periods. Accordingly, our profitability may vary significantly from quarter to quarter.

Our strategy to become a complete local commerce marketplace may not be successful and may expose us to additional risks.

One of our key objectives is to expand upon our traditional daily deals business by building out a more extensive local commerce marketplace. This strategy has required us to devote significant resources to attracting and retaining merchants who are willing to run deals on a continuous basis with us in order to build a significant inventory for our customers, as well as continuing management focus and attention. We have accepted, and expect to continue to accept, a lower portion of the gross billings from some of our merchants as we expand our marketplace. In addition, we are continuously refining our process for presenting the most relevant deals to our customers based on their personal preferences. If we are not successful in pursuing these objectives, our business, financial position and results of operations could be harmed.

Our international operations are subject to increased challenges, and our inability to adapt to the varied commercial and regulatory landscapes of our international markets may adversely affect our business.

Our ability to grow our business in our international markets requires management attention and resources and requires us to localize our services to conform to a wide variety of local cultures, business practices, laws and policies. The different commercial and Internet infrastructure in other countries may make it more difficult for us to replicate our business model. In many countries, we compete with local companies that understand the local market better than we do, and we may not benefit from first-to-market advantages. We are subject to risks of doing business internationally, including the following:

- our ability to maintain merchant and customer satisfaction such that our marketplace will continue to attract high quality merchants;

- our ability to successfully respond to macroeconomic challenges, including by optimizing our deal mix to take into account consumer preferences at a particular point in time;

- strong local competitors, many of whom have been in the market longer than us;

- different regulatory requirements, including regulation of gift cards and coupon terms, Internet services, professional selling, distance selling, bulk emailing, privacy and data protection, banking and money transmitting, that may limit or prevent the offering of our services in some jurisdictions, cause unanticipated compliance expenses or limit our ability to enforce contractual obligations;

- difficulties in integrating with local payment providers, including banks, credit and debit card networks and electronic funds transfer systems;

- different employee/employer relationships and the existence of workers' councils and labor unions;

- shorter payment cycles and greater problems in collecting accounts receivable;

- higher Internet service provider costs;

- seasonal reductions in business activity;

- expenses associated with localizing our products, including offering customers the ability to transact business in the local currency; and

- differing intellectual property laws.

We are subject to complex foreign and U.S. laws and regulations that apply to our international operations, including data privacy and protection requirements, the Foreign Corrupt Practices Act, the UK Anti-Bribery Act and similar local laws prohibiting certain payments to government officials, banking and payment processing regulations, and anti-competition regulations, among others. The cost of complying with these various and sometimes conflicting laws and regulations is substantial. We have implemented policies and procedures to ensure compliance with these laws and regulations, however, we cannot assure you that our employees, contractors, or agents will not violate our policies. Changing laws, regulations and enforcement actions in the U.S. and throughout the world could harm our business.

If, as we continue to expand internationally, we are unable to successfully replicate our business model due to these and other commercial and regulatory constraints in our international markets, our business may be adversely affected.

Our financial results will be adversely affected if we are unable to execute on our marketing strategy. Our marketing strategy is primarily focused on customer activation and mobile application downloads, as well as to increasing awareness of our shift to a more complete local commerce marketplace. We increased our marketing expense to \$203.1 million during the first three quarters of 2014 as compared to \$158.3 million during the first three quarters of 2013. If our assumptions regarding our marketing efforts and strategies prove incorrect, our ability to generate profits from our investments may be less than we have assumed. In such case, we may need to increase expenses or otherwise alter our strategy and our results of operations could be negatively impacted. If we are unable to successfully respond to changes in the market, our business could be harmed. We have operated at a substantial scale for only a limited period of time. Given the limited history, we are constantly evolving our strategy and may not always be successful in doing so. We expect that the market will evolve in ways which may be difficult to predict. For example, we believe that in some of our markets, including North America, investments in new subscriber acquisition are less productive and the continued growth of our revenue will require more focus on increasing or maintaining the rate at which our existing customers purchase Groupons and our ability to expand the number and variety of deals that we offer. It is also possible that merchants or customers could broadly determine that they no longer believe in the value of our current services or marketplace. In the event of these or any other changes to the market, our continued success will depend on our ability to successfully adjust our strategy to meet the changing market dynamics. If we are unable to successfully adapt to changes in our markets, our business, financial condition and results of operations could suffer a material negative impact. If we fail to retain our existing customers or acquire new customers, our revenue and business will be harmed. We must continue to retain and acquire customers that make purchases on our platform in order to increase revenue and achieve consistent profitability. As our customer base continues to evolve, it is possible that the composition of our customers may change in a manner that makes it more difficult to generate revenue to offset the loss of existing customers and the costs associated with acquiring and retaining customers. If customers do not perceive our offerings to be attractive or if we fail to introduce new and more relevant deals, we may not be able to retain or acquire customers at levels necessary to grow our business and profitability. If we are unable to acquire new customers in numbers sufficient to grow our business and offset the number of existing active customers that cease to make purchases, the revenue we generate may decrease and our operating results will be adversely affected. Our future success depends upon our ability to retain and add high quality merchants. We depend on our ability to attract and retain merchants that are prepared to offer products or services on compelling terms through our marketplace and provide our customers with a good experience. We do not have long-term arrangements to guarantee the availability of deals that offer attractive quality, value and variety to customers or favorable payment terms to us. In addition, if we are unsuccessful in our efforts to introduce services to merchants as part of our initiatives to achieve adoption of "Gnome," our iPad®-based platform for merchants, we will not experience a corresponding growth in our merchant pool sufficient to offset the cost of these initiatives. We must continue to attract and retain merchants in order to increase revenue and profitability. If new merchants do not find our marketing and promotional services effective, or if existing merchants do not believe that utilizing our services provides them with a long-term increase in customers, revenue or profits, they may stop making offers through our marketplace. In addition, we may experience attrition in our merchants in the ordinary course of business resulting from several factors, including losses to competitors and merchant closures or bankruptcies. If we are unable to attract new merchants in numbers sufficient to grow our business, or if merchants are unwilling to offer products or services with compelling terms through our marketplace or offer favorable payment terms to us, our operating results will be adversely affected. If our efforts to market, advertise and promote products and services from our existing merchants are not successful, or if our existing merchants do not believe that utilizing our services provides them with a long-term increase in customers, revenue or profits, we may not be able to retain or attract merchants in sufficient numbers to grow our business or we may be required to incur significantly higher marketing expenses or reduce margins in order to attract new merchants. A significant increase in merchant attrition or decrease in merchant growth would have an adverse effect on our business, financial condition and results of operations. We may be subject to breaches of our information technology systems, which could harm our relationships with our customers and merchants, subject us to negative publicity and litigation, and cause substantial harm to our business.

In operating a global online business, we and our third party service providers maintain significant proprietary information and manage large amounts of personal data and confidential information about our employees, customers and merchants. Because

86

---

of our high profile and the number of customer records we maintain, we and the third party providers are at an increased risk of attacks on our systems.

Our risk and exposure to these matters remains heightened because of, among other things, the evolving nature of these threats, our prominent size and scale, the large number of transactions that we process, our payment processing and point of sale offerings, our expanded geographic footprint and international presence, our use of open source software and technologies, the outsourcing of some of our business operations and continued threats of cyber-attacks.

Although cybersecurity and the continued development and enhancement of our controls, processes and practices designed to protect our systems, computers, software, data and networks from attack, damage or unauthorized access are a high priority for us, this may not successfully protect our systems against all vulnerabilities, including technologies developed to bypass our security measures. In addition, outside parties may attempt to fraudulently induce employees, merchants or customers to disclose sensitive information in order to gain access to our secure systems and networks. For example, in May 2013, a hacker accessed a database of our Taiwan subscribers containing usernames and passwords.

As cyber threats continue to evolve, we may be required to expend significant additional resources to continue to modify or enhance our protective measures or to investigate and remediate any information security vulnerabilities.

Further, because the techniques used to gain access to, or sabotage, systems often are not recognized until launched against a target, we may be unable to anticipate the correct methods necessary to defend against these types of attacks. Any actual breach, the perceived threat of a breach or a perceived breach, could cause our customers and merchants to cease doing business with us, subject us to lawsuits, regulatory fines or other action or liability, which would harm our business, financial condition and results of operations.

We may incur losses in the future as we expand our business.

We had an accumulated deficit of \$930.7 million as of September 30, 2014. We anticipate that our financial results will be impacted as we continue to invest in our growth, through increased spending in some areas and through accepting a lower portion of the proceeds from our deals, as we attempt to add more merchants to our marketplace. These efforts may prove more difficult than we currently anticipate, and we may not succeed in realizing the benefits of these efforts in a short time frame, or at all. Many of our efforts to generate revenue from our business are new and unproven, and any failure to increase our revenue, as well as any changes in our mix of sales between our higher and lower margin categories, could prevent us from attaining or increasing, or could reduce, our profitability. We cannot be certain that we will be able to attain or increase profitability on a quarterly or annual basis. If we are unable to effectively manage these risks and difficulties as we encounter them, our business, financial condition and results of operations may suffer.

We operate in a highly competitive industry with relatively low barriers to entry, and must compete successfully in order to grow our business.

We expect competition in e-commerce generally, and group buying in particular, to continue to increase. A substantial number of group buying sites that attempt to replicate our business model are operating around the world. In addition to such competitors, we expect to increasingly compete against other large businesses who offer deals similar to ours as an add-on to their core business. We also expect to compete against other Internet sites and mobile applications that serve niche markets and interests. In some of our categories, such as goods, travel and entertainment, we compete against much larger companies who have more resources and significantly larger scale. In addition, we compete with traditional offline coupon and discount services, as well as newspapers, magazines and other traditional media companies who provide coupons and discounts on products and services.

We believe that our ability to compete successfully depends upon many factors both within and beyond our control, including the following:

- the size and composition of our customer base and the number of merchants we feature;
- the timing and market acceptance of deals we offer, including the developments and enhancements to those deals offered by us or our competitors;
- customer and merchant service and support efforts;
- selling and marketing efforts;
- ease of use, performance, price and reliability of services offered either by us or our competitors;
- our ability to generate large volumes of sales, particularly with respect to goods and travel deals;



- our ability to cost-effectively manage our operations; and
- our reputation and brand strength relative to our competitors.

Many of our current and potential competitors have longer operating histories, significantly greater financial, marketing and other resources and larger customer bases than we do. These factors may allow our competitors to benefit from their existing customer base with lower customer acquisition costs or to respond more quickly than we can to new or emerging technologies and changes in consumer habits. These competitors may engage in more extensive research and development efforts, undertake more far-reaching marketing campaigns and adopt more aggressive pricing policies, which may allow them to build larger customer bases or generate revenue from their customer bases more effectively than we do. Our competitors may offer deals that are similar to the deals we offer or that achieve greater market acceptance than the deals we offer. This could attract customers away from our websites and applications, reduce our market share and adversely impact our gross margin. In addition, we are dependent on some of our existing or potential competitors for banner advertisements and other marketing initiatives to acquire new customers. Our ability to utilize their platforms to acquire new customers may be adversely affected if they choose to compete more directly with us or prevent us from using their services.

If we are unable to maintain favorable terms with our merchants, our revenue may be adversely affected.

The success of our business depends in part on our ability to retain and increase the number of merchants who use our service, particularly as we continue to grow our marketplace. Currently, when a merchant works with us to offer a deal for its products or services, it receives an agreed-upon portion of the total proceeds from each Groupon sold, and we retain the rest. If merchants decide that utilizing our services no longer provides an effective means of attracting new customers or selling their goods and services, they may require a higher portion of the total proceeds from each Groupon sold.

In addition, we expect to face increased competition from other Internet and technology-based businesses. We also have seen that some competitors will accept lower margins, or negative margins, to attract attention and acquire new customers. If competitors engage in group buying initiatives in which merchants receive a higher portion of the revenue than we currently offer, or if we target merchants who will only agree to run deals if they receive a higher portion of the proceeds, we may be forced to take a lower portion of the gross billings.

Our operating cash flow and results of operations could be adversely impacted if we change our merchant payment terms or our revenue does not grow.

Our merchant payment terms and revenue growth have historically provided us with operating cash flow to fund our working capital needs. Our merchant arrangements are generally structured such that we collect cash up front when our customers purchase Groupons and make payments to our merchants at a subsequent date, either on a fixed schedule or upon redemption by customers. We currently pay our merchants upon redemption in many deals in our international markets, but we may continue to move toward offering payments on a fixed schedule in those markets. We believe that seasonal fluctuations will continue to impact our cash flows, particularly as a result of the growth of our Goods category. Our operating cash flow for the nine months ended September 30, 2014 was adversely impacted by a \$61.2 million decrease in accrued merchant and supplier payables, which was primarily due to the timing of payments to suppliers of merchandise and the seasonally high levels of Goods transactions in the fourth quarter of 2013. Our operating cash flows have been adversely impacted by lower growth or declines in our Local category in recent periods. We have used the operating cash flow provided by our merchant payment terms and revenue growth to fund our working capital needs. If we offer our merchants more favorable or accelerated payment terms or our revenue does not grow in the future, our operating cash flow and results of operations could be adversely impacted and we may have to seek alternative financing to fund our working capital needs.

Our success is dependent upon our ability to provide a superior mobile experience for our customers, and our customers' continued ability to access our offerings through mobile devices.

At the present time, more than 50% of our global transactions are completed on mobile devices. Over 100 million people have downloaded our mobile applications worldwide. In order to continue to grow our mobile transactions, it is critical that our applications work well with a range of mobile technologies, systems, networks and standards. Our business may be adversely affected if our customers choose not to access our offerings on their mobile devices or use mobile devices that do not offer access to our mobile applications.



Our business depends on our ability to maintain and scale the network infrastructure necessary to send our emails and operate our websites, mobile applications and transaction processing systems, and any significant disruption in service on our email infrastructure, websites, mobile applications or transaction processing systems could result in a loss of subscribers, customers or merchants.

Customers access our deals through our websites and mobile applications, as well as via emails that are often targeted by location, purchase history and personal preferences. Our reputation and ability to acquire, retain and serve our current customers and potential customers are dependent upon the reliable performance of our websites, mobile applications, email delivery and transaction processing systems and the underlying network infrastructure. As our customer base and the amount of information shared on our websites and applications continue to grow, we will need an increasing amount of network capacity and computing power. We have spent and expect to continue to spend substantial amounts on data centers and equipment and related network infrastructure to handle the traffic on our websites and applications. The operation of these systems is expensive and complex and could result in operational failures. In the event that our subscriber base or the amount of traffic and transactions on our websites and applications grows more quickly than anticipated, we may be required to incur significant additional costs.

Interruptions in these systems, whether due to system failures, computer viruses, physical or electronic break-ins or otherwise (including spam filters preventing emails from reaching current and potential customers), could affect the security or availability of our websites and applications, and prevent our customers from accessing our services. If we do not maintain or expand our network infrastructure successfully or if we experience operational failures, we could lose current and potential customers and merchants, which could harm our operating results and financial condition. In addition, a substantial portion of our network infrastructure is hosted by third party providers. Any failure of these providers to handle existing or increased traffic and transactions could significantly harm our business. Any financial or other difficulties these providers face may adversely affect our business, and we exercise little control over these providers, which increases our vulnerability to problems with the services they provide.

If our emails are not delivered and accepted, or are routed by email providers in a less favorable way than other emails, our business may be substantially harmed.

If email providers implement new or more restrictive email delivery policies it may become more difficult to deliver emails to customers. For example, certain email providers, including Google, categorize our emails as "promotional," and these emails are directed to an alternate, and less readily accessible, section of a customer's inbox. If email providers materially limit or halt the delivery of our emails, or if we fail to deliver emails to customers in a manner compatible with email providers' email handling or authentication technologies, our operating results and financial condition could be substantially harmed. In addition, if we are placed on "spam" lists or lists of entities that have been involved in sending unwanted, unsolicited emails, our ability to contact customers through email could be significantly restricted.

We purchase and sell some products from indirect suppliers, which increases our risk of litigation and other losses.

We source merchandise both directly from brand owners and indirectly from retailers and third party distributors, and we often take title to the goods before we offer them for sale to our customers. Further, some brand owners, retailers and third party distributors may be unwilling to offer products for sale on the Internet or through Groupon in particular, which could have an adverse impact on our ability to source and offer popular products. By selling merchandise sourced from parties other than the brand owners, we are subject to an increased risk that the merchandise may be damaged or non-authentic, which could result in potential liability under applicable laws, regulations, agreements and orders, and increase the amount of returned merchandise. In addition, brand owners may take legal action against us, which even if we prevail could result in costly litigation, generate adverse publicity for us, and have a material adverse impact on our business, financial condition and results of operations.

We are subject to inventory management and order fulfillment risks as a result of our Goods category.

We purchase much of the merchandise that we offer for sale to our customers, and we expect to increase the percentage of merchandise that we offer directly for sale as compared to merchandise that our customers purchase directly from third parties. The demand for products can change for a variety of reasons, including customer preference, quality, seasonality, and the perceived value from customers of purchasing the product through us. In addition, this is a relatively new business for us, and therefore we have a limited historical basis upon which to predict customer demand for the products. If we are unable to adequately predict customer demand and efficiently manage

our inventory, we could either have an excess or a shortage of inventory, either of which would have a material adverse effect on our business.

Purchasing the goods ourselves prior to the sale also means that we will be required to fulfill orders on a timely, efficient and cost-effective basis. Many other online retailers have significantly larger inventory balances and therefore are able to rely on

past experience and economies of scale to optimize their order fulfillment. Because we rely on third party logistics providers for order fulfillment and delivery, many parts of our supply chain are outside our control. Delays or inefficiencies in our processes, or those of our third party logistics providers, could subject us to additional costs, as well as customer dissatisfaction, which would adversely affect our business. Additionally, we assume the risks of inventory damage, theft and obsolescence, as well as risks of price erosion for these products. These risks are especially significant because some of the merchandise we sell is characterized by seasonal trends, fashion trends, obsolescence and price erosion and because we sometimes make large purchases of particular types of inventory. Our success will depend on our ability to sell our inventory rapidly, the ability of our buying staff to purchase inventory at attractive prices relative to its resale value and our ability to manage customer returns and other costs. If we are unsuccessful in any of these areas, we may be forced to sell our inventory at a discount or loss.

The integration of our international operations with our North American technology platform may result in business interruptions.

We currently use a common technology platform in our North America segment to operate our business and are close to fully implementing this platform in most EMEA countries but have not yet substantially rolled out this platform to the countries in our Rest of World segment. Such changes to our technology platform and related software carry risks such as cost overruns, project delays and business interruptions and delays. If we experience a material business interruption as a result of this process, it could have a material adverse effect on our business, financial position and results of operations and could cause the market value of our Class A common stock to decline.

We are involved in pending litigation and an adverse resolution of such litigation may adversely affect our business, financial condition, results of operations and cash flows.

We are involved in litigation regarding, among other matters, patent, consumer, securities and employment issues. Litigation can be expensive, time-consuming and disruptive to normal business operations. The results of complex legal proceedings are often uncertain and difficult to predict. An unfavorable outcome with respect to any of these lawsuits could have a material adverse effect on our business, financial condition, results of operations or cash flows. For additional information regarding these and other lawsuits in which we are involved, see Note 6 "Commitments and Contingencies" to the condensed consolidated financial statements.

An increase in our refund rates could reduce our liquidity and profitability.

Customers have the ability to receive a refund of their purchase price upon the occurrence of specified events. As we increase our revenue and expand our product offerings, our refund rates may exceed our historical levels. For example, as a result of a shift in our deal mix and higher price point offers that began in the fourth quarter of 2011, our refund rates became higher than historical levels. A downturn in general economic conditions may also increase our refund rates. An increase in our refund rates could significantly reduce our liquidity and profitability.

Because we do not have control over our merchants and the quality of products or services they deliver, we rely on a statistical model that incorporates the following data inputs and factors to estimate future refunds: historical refund experience developed from millions of deals featured on our website, the relative risk of refunds based on expiration date, deal value, deal category and other qualitative factors that could impact the level of future refunds, such as introductions of new deals, discontinuations of legacy deals and expected changes, if any, in our practices in response to refund experience or economic trends that might impact customer demand. Our actual level of refund claims could prove to be greater than the level of refund claims we estimate. If our refund reserves are not adequate to cover future refund claims, this inadequacy could have a material adverse effect on our liquidity and profitability.

Our standard agreements with our merchants generally limit the time period during which we may seek reimbursement for customer refunds or claims. Our customers may make claims for refunds with respect to which we are unable to seek reimbursement from our merchants. Our inability to seek reimbursement from our merchants for refund claims could have an adverse effect on our liquidity and profitability.

The loss of one or more key members of our management team, or our failure to attract, integrate and retain other highly qualified personnel in the future could harm our business.

In order to be successful, we must attract, retain and motivate executives and other key employees, including those in managerial, technical and sales positions. Hiring and retaining qualified executives, engineers and qualified sales representatives are critical to our success, and competition for experienced and well qualified employees can be intense. In order to attract and retain executives and other key employees in a competitive marketplace, we must

provide a competitive compensation package,

90

---

including cash and share-based compensation. Our primary form of share-based incentive award is restricted stock units. If the anticipated value of such share-based incentive awards does not materialize, if our share-based compensation otherwise ceases to be viewed as a valuable benefit, or if our total compensation package is not viewed as being competitive, our ability to attract, retain, and motivate executives and key employees could be weakened. The failure to successfully hire executives and key employees or the loss of any executives and key employees could have a significant impact on our operations.

An increase in the costs associated with maintaining our international operations could adversely affect our results of operations.

Certain factors may cause our international costs of doing business to exceed our comparable costs in North America. For example, in some countries, expanding our product and service offerings may require a close commercial relationship with one or more local banks, a shared ownership interest with a local entity or registration as a bank under local law. Such requirements may reduce our revenue, increase our costs or limit the scope of our activities in particular countries.

Further, because our international revenue is denominated in foreign currencies, we could become subject to increased difficulties in repatriating money without adverse tax consequences and increased risks relating to foreign currency exchange rate fluctuations. Further, we could be subject to the application of U.S. tax rules to acquired international operations and local taxation of our fees or of transactions on our websites.

We conduct portions of certain functions, including product development, customer support and other operations, in regions outside of North America. Any factors which reduce the anticipated benefits, including cost efficiencies and productivity improvements, associated with providing these functions outside of North America, including increased regulatory costs associated with our international operations, could adversely affect our business.

We may be subject to additional unexpected regulation which could increase our costs or otherwise harm our business.

The application of certain laws and regulations to Groupons, as a new product category, is uncertain. These include laws and regulations such as the CARD Act, and, in certain instances, potentially unclaimed and abandoned property laws. In addition, from time to time, we may be notified of additional laws and regulations which governmental organizations or others may claim should be applicable to our business. If we are required to alter our business practices as a result of any laws and regulations, our revenue could decrease, our costs could increase and our business could otherwise be harmed. In addition, the costs and expenses associated with defending any actions related to such additional laws and regulations and any payments of related penalties, judgments or settlements could adversely impact our profitability. As we expand into new lines of business and new geographies, we will become subject to additional laws and regulations.

We may have exposure to greater than anticipated tax liabilities.

Our income tax obligations are based on our corporate operating structure, including the manner in which we develop, value and use our intellectual property and the scope of our international operations. The tax laws applicable to our international business activities, including the laws of the United States and other jurisdictions, are subject to interpretation. The taxing authorities of the jurisdictions in which we operate may challenge our methodologies for valuing developed technology or intercompany arrangements, which could increase our worldwide effective tax rate and harm our financial position and results of operations. In addition, our future income taxes could be adversely affected by greater earnings in jurisdictions that have higher statutory tax rates, by changes in the valuation of our deferred tax assets and liabilities, or by changes in tax laws, regulations or accounting principles. We are subject to regular review and audit by both U.S. federal and state and foreign tax authorities. Any adverse outcome of such a review or audit could have a negative effect on our financial position and results of operations. In addition, the determination of our worldwide provision for income taxes and other tax liabilities requires significant judgment by management, and there are many transactions where the ultimate tax determination is uncertain. Although we believe that our estimates are reasonable, the ultimate tax outcome may differ from the amounts recorded in our financial statements and may materially affect our financial results in the period or periods for which such determination is made.

The enactment of legislation implementing changes in the U.S. taxation of international business activities or the adoption of other tax reform policies could materially affect our financial position and results of operations.

The current administration has made public statements indicating that it has made international tax reform a priority, and key members of the U.S. Congress have conducted hearings and proposed a wide variety of potential changes. Certain changes to U.S. tax laws, including limitations on the ability to defer U.S. taxation on earnings outside of the United States until those earnings are repatriated to the United States, could affect the tax treatment of our foreign earnings, as well as cash and cash equivalent balances we currently maintain outside of the United States. Due to the large and expanding scale of our international business activities, any changes in the U.S. taxation of such activities may increase our worldwide effective tax rate and harm our

financial position and results of operations.

The implementation of the CARD Act and similar state and foreign laws may harm our business and results of operations.

It is not clear at this time, but Groupons may be considered gift cards, gift certificates, stored value cards or prepaid cards and therefore governed by, among other laws, the CARD Act, and state laws governing gift cards, stored value cards and coupons. Other foreign jurisdictions have similar laws in place, in particular European jurisdictions where the European E-Money Directive regulates the business of electronic money institutions. Many of these laws contain provisions governing the use of gift cards, gift certificates, stored value cards or prepaid cards, including specific disclosure requirements and prohibitions or limitations on the use of expiration dates and the imposition of certain fees. For example, if Groupons are subject to the CARD Act and are not included in the exemption for promotional programs, it is possible that the purchase value, which is the amount equal to the price paid for the Groupon, or the promotional value, which is the add-on value of the Groupon in excess of the price paid, or both, may not expire before the later of (i) five years after the date on which the Groupon was issued or the date on which the customer last loaded funds on the Groupon if the Groupon has a reloadable feature; (ii) the Groupon's stated expiration date (if any); or (iii) a later date provided by applicable state law. We and several merchants are currently defendants in purported class action litigation that has been filed in federal and state court claiming that Groupons are subject to the CARD Act and various state laws governing gift cards and that the defendants have violated these laws by issuing Groupons with expiration dates and other restrictions. In the event that it is determined that Groupons are subject to the CARD Act or any similar state or foreign law or regulation, and are not within various exemptions that may be available to Groupon under the CARD Act or under some of the various state or foreign jurisdictions, our liabilities with respect to unredeemed Groupons may be materially higher than the amounts shown in our financial statements and we may be subject to additional fines and penalties. In addition, if federal or state laws require that the face value of Groupons have a minimum expiration period beyond the period desired by a merchant for its promotional program, or no expiration period, this may affect the willingness of merchants to issue Groupons in jurisdictions where these laws apply.

If we are required to materially increase the estimated liability recorded in our financial statements with respect to unredeemed Groupons, our results from operations could be materially and adversely affected.

In certain states and foreign jurisdictions, Groupons may be considered a gift card. Some of these states and foreign jurisdictions include gift cards under their unclaimed and abandoned property laws which require companies to remit to the government the value of the unredeemed balance on the gift cards after a specified period of time (generally between one and five years) and impose certain reporting and record-keeping obligations. We do not remit any amounts relating to unredeemed Groupons based on our assessment of applicable laws. The analysis of the potential application of the unclaimed and abandoned property laws to Groupons is complex, involving an analysis of constitutional and statutory provisions and factual issues, including our relationship with customers and merchants and our role as it relates to the issuance and delivery of a Groupon. In the event that one or more states or foreign jurisdictions successfully challenges our position on the application of its unclaimed and abandoned property laws to Groupons, or if the estimates that we use in projecting the likelihood of Groupons being redeemed prove to be inaccurate, our liabilities with respect to unredeemed Groupons may be materially higher than the amounts shown in our financial statements. If we are required to materially increase the estimated liability recorded in our financial statements with respect to unredeemed gift cards, our net income could be materially and adversely affected.

Moreover, a successful challenge to our position could subject us to penalties or interest on unreported and unremitted sums, and any such penalties or interest would have a further material adverse impact on our net income.

Government regulation of the Internet and e-commerce is evolving, and unfavorable changes or failure by us to comply with these regulations could substantially harm our business and results of operations.

We are subject to general business regulations and laws as well as regulations and laws specifically governing the Internet and e-commerce. Existing and future regulations and laws could impede the growth of the Internet or other online services. These regulations and laws may involve taxation, tariffs, subscriber privacy, anti-spam, data protection, content, copyrights, distribution, electronic contracts and other communications, consumer protection, the provision of online payment services and the characteristics and quality of services. It is not clear how existing laws governing issues such as property ownership, sales and other taxes, libel and personal privacy apply to the Internet as

the vast majority of these laws were adopted prior to the advent of the Internet and do not contemplate or address the unique issues raised by the Internet or e-commerce. In addition, it is possible that governments of one or more countries may seek to censor content available on our websites and applications or may even attempt to completely block our emails or access to our websites. Adverse legal or regulatory developments could substantially harm our business. In particular, in the event that we are restricted, in whole or in part, from operating in one or more countries, our ability to retain or increase our customer base may be adversely affected and we may not be able to maintain or grow our revenue as anticipated.

New tax treatment of companies engaged in Internet commerce may adversely affect the commercial use of our services and our financial results.

Due to the global nature of the Internet, it is possible that various states or foreign countries might attempt to regulate our transmissions or levy sales, income or other taxes relating to our activities. Tax authorities at the international, federal, state and local levels are currently reviewing the appropriate treatment of companies engaged in Internet commerce. New or revised international, federal, state or local tax regulations may subject us or our customers to additional sales, income and other taxes. We cannot predict the effect of current attempts to impose sales, income or other taxes on commerce over the Internet. New or revised taxes and, in particular, sales taxes, VAT and similar taxes would likely increase the cost of doing business online and decrease the attractiveness of advertising and selling goods and services over the Internet. New taxes could also create significant increases in internal costs necessary to capture data, and collect and remit taxes. Any of these events could have an adverse effect on our business and results of operations.

Failure to comply with federal, state and international privacy laws and regulations, or the expansion of current or the enactment of new privacy laws or regulations, could adversely affect our business.

A variety of federal, state and international laws and regulations govern the collection, use, retention, sharing and security of consumer data. The existing privacy-related laws and regulations are evolving and subject to potentially differing interpretations. In addition, various federal, state and foreign legislative and regulatory bodies may expand current or enact new laws regarding privacy matters. For example, recently there have been Congressional hearings and increased attention to the capture and use of location-based information relating to users of smartphones and other mobile devices. We have posted privacy policies and practices concerning the collection, use and disclosure of subscriber data on our websites and applications. Several Internet companies have incurred substantial penalties for failing to abide by the representations made in their privacy policies and practices. In addition, several states have adopted legislation that requires businesses to implement and maintain reasonable security procedures and practices to protect sensitive personal information and to provide notice to consumers in the event of a security breach. Any failure, or perceived failure, by us to comply with our posted privacy policies or with any data-related consent orders, Federal Trade Commission requirements or orders or other federal, state or international privacy or consumer protection-related laws, regulations or industry self-regulatory principles could result in claims, proceedings or actions against us by governmental entities or others or other liabilities, which could adversely affect our business. In addition, a failure or perceived failure to comply with industry standards or with our own privacy policies and practices could result in a loss of subscribers or merchants and adversely affect our business. Federal, state and international governmental authorities continue to evaluate the privacy implications inherent in the use of third party web "cookies" for behavioral advertising. The regulation of these cookies and other current online advertising practices could adversely affect our business.

We may suffer liability as a result of information retrieved from or transmitted over the Internet and claims related to our service offerings.

We may be, and in certain cases have been, sued for defamation, civil rights infringement, negligence, patent, copyright or trademark infringement, invasion of privacy, personal injury, product liability, breach of contract, unfair competition, discrimination, antitrust or other legal claims relating to information that is published or made available on our websites or service offerings we make available (including provision of an application programming interface platform for third parties to access our website, mobile device services and geolocation applications). This risk is enhanced in certain jurisdictions outside the United States, where our liability for such third party actions may be less clear and we may be less protected. In addition, we could incur significant costs in investigating and defending such claims, even if we ultimately are not found liable. If any of these events occurs, our net income could be materially and adversely affected.

We are subject to risks associated with information disseminated through our websites and applications, including consumer data, content that is produced by our editorial staff and errors or omissions related to our product offerings. Such information, whether accurate or inaccurate, may result in our being sued by our merchants, subscribers or third parties and as a result our revenue and goodwill could be materially and adversely affected.

We may not be able to adequately protect our intellectual property rights or may be accused of infringing intellectual property rights of third parties.

We regard our trademarks, service marks, copyrights, patents, trade dress, trade secrets, proprietary technology, merchant lists, subscriber lists, sales methodology and similar intellectual property as critical to our success, and we rely on trademark, copyright and patent law, trade secret protection and confidentiality and/or license agreements with our employees and others to protect our proprietary rights. Effective intellectual property protection may not be available in every country in which our deals are made available. We also may not be able to acquire or maintain appropriate domain names or trademarks in all countries in

which we do business. Furthermore, regulations governing domain names may not protect our trademarks and similar proprietary rights. We may be unable to prevent third parties from acquiring and using domain names that are similar to, infringe upon or diminish the value of our trademarks and other proprietary rights. We may be unable to prevent third parties from using and registering our trademarks, or trademarks that are similar to, or diminish the value of, our trademarks in some countries.

We may not be able to discover or determine the extent of any unauthorized use of our proprietary rights. Third parties that license our intellectual property rights also may take actions that diminish the value of our proprietary rights or reputation. The protection of our intellectual property may require the expenditure of significant financial and managerial resources. Moreover, the steps we take to protect our intellectual property may not adequately protect our rights or prevent third parties from infringing or misappropriating our proprietary rights. We are currently subject to multiple lawsuits and disputes related to our intellectual property and service offerings. We may in the future be subject to additional litigation and disputes. The costs of engaging in such litigation and disputes are considerable, and there can be no assurances that favorable outcomes will be obtained.

We are currently subject to third party claims that we infringe their proprietary rights or trademarks and expect to be subject to additional claims in the future. Such claims, whether or not meritorious, may result in the expenditure of significant financial and managerial resources, injunctions against us or the payment of damages by us. We may need to obtain licenses from third parties who allege that we have infringed their rights, but such licenses may not be available on terms acceptable to us or at all. These risks have been amplified by the increase in third parties whose sole or primary business is to assert such claims.

Our business depends on a strong brand, and if we are not able to maintain and enhance our brand, or if we receive unfavorable media coverage, our ability to expand our base of customers and merchants will be impaired and our business and operating results will be harmed.

We believe that the brand identity that we have developed has significantly contributed to the success of our business. We also believe that maintaining and enhancing the "Groupon" brand is critical to expanding our base of customers and merchants. Maintaining and enhancing our brand may require us to make substantial investments and these investments may not be successful. If we fail to promote and maintain the "Groupon" brand, or if we incur excessive expenses in this effort, our business, operating results and financial condition will be materially and adversely affected. We anticipate that, as our market becomes increasingly competitive, maintaining and enhancing our brand may become increasingly difficult and expensive. Maintaining and enhancing our brand will depend largely on our ability to be a group buying leader and to continue to provide reliable, trustworthy and high quality deals, which we may not do successfully.

We receive a high degree of media coverage around the world. Unfavorable publicity or consumer perception of our websites, applications, practices or service offerings, or the offerings of our merchants, could adversely affect our reputation, resulting in difficulties in recruiting, decreased revenue and a negative impact on the number of merchants we feature and the size of our customer base, the loyalty of our customers and the number and variety of deals we offer each day. As a result, our business, financial condition and results of operations could be materially and adversely affected.

Acquisitions, dispositions, joint ventures and strategic investments could result in operating difficulties, dilution and other consequences.

We routinely evaluate and consider a wide array of potential strategic transactions, including acquisitions and dispositions of businesses, joint ventures, technologies, services, products and other assets and minority investments, some of which we consummate. These activities can result in operating difficulties, dilution, management distraction and other potentially adverse consequences. We have in the past acquired a number of companies, including Ticket Monster, which we acquired on January 2, 2014 for total consideration of \$259.4 million, and Ideel, which we acquired on January 13, 2014 for total consideration of \$42.7 million. We have also announced our intention to explore and evaluate financing and strategic alternatives with respect to Ticket Monster and certain other markets in our Rest of World segment. However, the Company has not made a decision to pursue any specific strategic transaction, so there can be no assurance that the exploration and evaluation of any such strategic alternatives will result in a transaction and there is no set timetable for the process. Furthermore, if we consummate such a strategic

transaction, we may not successfully realize the anticipated benefits of the transaction.

Acquisitions involve significant risks and uncertainties, including uncertainties as to the future financial performance of the acquired business, difficulties integrating acquired personnel into our business, the potential loss of key employees, customers or suppliers, difficulties in integrating different computer and accounting systems and exposure to unknown or unforeseen liabilities of acquired companies. In addition, the integration of an acquisition could divert management's time and the Company's resources. If we pay for an acquisition or a minority investment in cash, it would reduce our cash available for operations or cause us to incur debt, and if we pay with our stock it could be dilutive to our stockholders. Additionally, we do not have the ability to exert control

over our joint ventures and minority investments, and therefore we are dependent on others in order to realize their potential benefits. Dispositions and attempted dispositions also involve significant risks and uncertainties, such as the risk of destabilizing the applicable operations or the loss of key personnel, as well as uncertainties with respect to the separation of disposed operations, the terms and timing of any dispositions and the ability to obtain necessary governmental or regulatory approvals. Further, we may be unable to successfully complete potential strategic transactions or we may not realize the anticipated benefits of any or all of our strategic transactions, or we may not realize them in the time frame expected.

Our business may be subject to seasonal sales fluctuations which could result in volatility or have an adverse effect on the market price of our Class A common stock.

Our business has been and may continue to be subject to sales seasonality. This seasonality may cause our working capital cash flow requirements to vary from quarter to quarter depending on the variability in the volume and timing of sales. These factors, among other things, make forecasting more difficult and may adversely affect our ability to manage working capital and to predict financial results accurately, which could adversely affect the market price of our Class A common stock.

Failure to deal effectively with fraudulent transactions and customer disputes would increase our loss rate and harm our business.

Groupons are issued in the form of redeemable coupons with unique identifiers. It is possible that consumers or other third parties will seek to create counterfeit Groupons in order to fraudulently purchase discounted goods and services from merchants. While we use advanced anti-fraud technologies, it is possible that criminals will attempt to circumvent our anti-fraud systems using increasingly sophisticated methods. In addition, our service could be subject to employee fraud or other internal security breaches, and we may be required to reimburse customers and/or merchants for any funds stolen or revenue lost as a result of such breaches. Merchants could also request reimbursement, or stop using Groupon, if they are affected by buyer fraud or other types of fraud.

We may incur significant losses from fraud and counterfeit Groupons. We may incur losses from claims that the customer did not authorize the purchase, from merchant fraud, from erroneous transmissions, and from customers who have closed bank accounts or have insufficient funds in them to satisfy payments. In addition to the direct costs of such losses, if they are related to credit card transactions and become excessive, they could potentially result in our losing the right to accept credit cards for payment. If we were unable to accept credit cards for payment, we would suffer substantial reductions in revenue, which would cause our business to suffer. While we have taken measures to detect and reduce the risk of fraud, these measures need to be continually improved and may not be effective against new and continually evolving forms of fraud or in connection with new product offerings. If these measures do not succeed, our business will suffer.

We are subject to payments-related risks.

We accept payments using a variety of methods, including credit card, debit card and gift certificates. As we offer new payment options to customers, we may be subject to additional regulations, compliance requirements and fraud. For certain payment methods, including credit and debit cards, we pay interchange and other fees, which may increase over time and raise our operating costs and lower profitability. We rely on third parties to provide payment processing services, including the processing of credit cards and debit cards, and it could disrupt our business if these companies become unwilling or unable to provide these services to us. We are also subject to payment card association operating rules, certification requirements and rules governing electronic funds transfers, which could change or be reinterpreted to make it difficult or impossible for us to comply. If we fail to comply with these rules or requirements, we may be subject to fines and higher transaction fees and lose our ability to accept credit and debit card payments from customers or facilitate other types of online payments, and our business and operating results could be adversely affected.

We are also subject to or voluntarily comply with a number of other laws and regulations relating to money laundering, international money transfers, privacy and information security and electronic fund transfers. If we were found to be in violation of applicable laws or regulations, we could be subject to civil and criminal penalties or forced to cease our payment processing service business. In addition, events affecting our third party payment processors, including cyber-attacks, Internet or other infrastructure or communications impairment or other events that could

interrupt the normal operation of our payment processors, could have a material adverse effect on our business.

When we process credit card payments for merchants, we may be subject to chargeback liability if our merchants refuse or cannot reimburse chargebacks resolved in favor of their customers.

We offer a credit card payment processing service to merchants. If we process a payment that is successfully disputed by the customer at a later date, the transaction is normally "charged back" to the merchant and the purchase price is credited or otherwise refunded to the cardholder. If we or our clearing bank is unable to collect such amounts from the merchant's account, or if the merchant refuses or is unable, due to closure, bankruptcy or other reasons, to reimburse us for the chargeback, we bear the loss for the amount of the refund paid to the cardholder. Any chargebacks not paid by merchants may adversely affect our financial condition and results of operations. In addition, if our clearing bank terminates our relationship and we are unable to secure a relationship with another clearing bank, we would be unable to process payments.

Federal laws and regulations, such as the Bank Secrecy Act and the USA PATRIOT Act and similar foreign laws, could be expanded to include Groupons.

Various federal laws, such as the Bank Secrecy Act and the USA PATRIOT Act and foreign laws and regulations, such as the European Directive on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing, impose certain anti-money laundering requirements on companies that are financial institutions or that provide financial products and services. For these purposes, financial institutions are broadly defined to include money services businesses such as money transmitters, check cashers and sellers or issuers of stored value cards. Examples of anti-money laundering requirements imposed on financial institutions include subscriber identification and verification programs, record retention policies and procedures and transaction reporting. We do not believe that we are a financial institution subject to these laws and regulations based, in part, upon the characteristics of Groupons and our role with respect to the distribution of Groupons to subscribers. However, the Financial Crimes Enforcement Network, a division of the U.S. Treasury Department tasked with implementing the requirements of the Bank Secrecy Act, recently proposed amendments to the scope and requirements for parties involved in stored value or prepaid access cards, including a proposed expansion of financial institutions to include sellers or issuers of prepaid access cards. In the event that this proposal is adopted as proposed, it is possible that a Groupon could be considered a financial product and that we could be a financial institution. In the event that we become subject to the requirements of the Bank Secrecy Act or any other anti-money laundering law or regulation imposing obligations on us as a money services business, our regulatory compliance costs to meet these obligations would likely increase which could reduce our net income.

State and foreign laws regulating money transmission could be expanded to include Groupons.

Many states and certain foreign jurisdictions impose license and registration obligations on those companies engaged in the business of money transmission, with varying definitions of what constitutes money transmission. We do not currently believe we are a money transmitter given our role and the product terms of Groupons. However, a successful challenge to our position or expansion of state or foreign laws could subject us to increased compliance costs and delay our ability to offer Groupons in certain jurisdictions pending receipt of any necessary licenses or registrations. Our responsibilities as a public company may cause us to incur significant costs, divert management's attention and affect our ability to attract and retain qualified board members and executives.

We are subject to the reporting requirements of the Exchange Act, the Sarbanes-Oxley Act of 2002, including the requirements of Section 404, as well as new rules and regulations subsequently implemented by the Securities and Exchange Commission, or the SEC, the Public Company Accounting Oversight Board and the marketplace rules of the NASDAQ stock market. Compliance with these public company requirements has increased and will continue to increase our legal and financial compliance costs and increase demand on our systems and resources. It also may be more difficult for us to attract and retain qualified persons to serve on our board of directors or as executive officers. In addition, changing laws, regulations and standards relating to public disclosure and corporate governance are creating uncertainty for public companies, increasing legal and financial compliance costs and making some activities more time consuming. These laws, regulations and standards are subject to varying interpretations, and, as a result, their application in practice may evolve over time as new guidance is provided by regulatory and governing bodies. This could result in continuing uncertainty regarding compliance matters and higher costs necessitated by ongoing

revisions to our disclosures and to our governance practices. We have invested, and intend to continue to invest, resources to comply with evolving laws, regulations and standards, and this investment may result in increased general and administrative expenses and a diversion of management's time and attention away from activities that generate revenue and help grow our business.

Our ability to raise capital in the future may be limited, and our failure to raise capital when needed could prevent us from growing.

We may in the future be required to raise capital through public or private financing or other arrangements. Such financing may not be available on acceptable terms, or at all, and our failure to raise capital when needed could harm our business. Additional equity financing may dilute the interests of our common stockholders, and debt financing, if available, may involve restrictive covenants and could reduce our profitability. If we cannot raise funds on acceptable terms, we may not be able to grow our business or respond to competitive pressures.

#### Risks Related to Ownership of Our Class A Common Stock

The trading price of our Class A common stock is highly volatile.

Our Class A common stock began trading on the NASDAQ Global Select Market on November 4, 2011 and since that date has fluctuated from a high of \$31.14 per share to a low of \$2.60 per share. We expect that the trading price of our stock will continue to be volatile due to variations in our operating results and also may change in response to other factors, including factors specific to technology and Internet commerce companies, many of which are beyond our control. Among the factors that could affect our stock price are:

- our financial results;
- any financial projections that we may choose to provide to the public, any changes in these projections or our failure for any reason to meet these projections or projections made by research analysts;
- the amount of shares of our Class A common stock that are available for sale;
- the relative success of competitive products or services;
- the public's response to press releases or other public announcements by us or others, including our filings with the SEC and announcements relating to litigation;
- speculation about our business in the press or the investment community;
- future sales of our Class A common stock by our significant stockholders, officers and directors;
- announcements about our share repurchase program and sales under the program;
- changes in our capital structure, such as future issuances of debt or equity securities;
- our entry into new markets or exit from existing markets;
- regulatory developments in the United States or foreign countries;
- strategic acquisitions, joint ventures or restructurings announced or consummated by us or our competitors;
- strategic dispositions of businesses or other assets announced or consummated by us; and
- changes in accounting principles.

We expect the stock price volatility to continue for the foreseeable future as a result of these and other factors.

Purchases of shares of our Class A common stock pursuant to our stock repurchase program may affect the value of our Class A common stock.

Pursuant to our publicly announced share repurchase program, we are authorized to repurchase up to \$300.0 million of our outstanding Class A common stock through August 2015 and have approximately \$110 million remaining under this authorization as of September 30, 2014. The timing and amount of any share repurchases will be determined based on market conditions, share price and other factors. This activity could increase (or reduce the size of any decrease in) the market price of our Class A common stock at that time.

The concentration of our capital stock ownership with our founders, executive officers, employees and directors and their affiliates will limit stockholders' ability to influence corporate matters.

Our Class B common stock has 150 votes per share and our Class A common stock has one vote per share. As of October 28, 2014, our founders, Eric Lefkofsky, Bradley Keywell and Andrew Mason control 100% of our outstanding Class B common stock and, based on information available to us, approximately 23.6% of our outstanding Class A common stock, representing approximately 50.3% of the voting power of our outstanding capital stock. Messrs. Lefkofsky, Keywell and Mason will therefore have significant influence over management and affairs and over all matters requiring stockholder approval, including the election of directors and significant corporate transactions, such as a merger or other sale of our company or its assets, for the foreseeable future. This concentrated control will limit stockholders' ability to influence corporate matters and, as a result, we may take actions that our stockholders do not view as beneficial. As a result, the market price of our Class A common stock could be adversely affected.

We do not intend to pay dividends for the foreseeable future.

We intend to retain all of our earnings for the foreseeable future to finance the operation and expansion of our business and do not anticipate paying cash dividends. As a result, stockholders can expect to receive a return on their investment in our Class A common stock only if the market price of the stock increases.

Provisions in our charter documents and under Delaware law could discourage a takeover that stockholders may consider favorable.

Provisions in our certificate of incorporation and bylaws, as amended and restated upon the closing of this offering, may have the effect of delaying or preventing a change of control or changes in our management. These provisions include the following:

Our certificate of incorporation provides for a dual class common stock structure. As a result of this structure, our founders will have significant influence over all matters requiring stockholder approval, including the election of directors and significant corporate transactions, such as a merger or other sale of our company or its assets. This concentrated control could discourage others from initiating any potential merger, takeover or other change of control transaction that other stockholders may view as beneficial.

Our board of directors has the right to elect directors to fill a vacancy created by the expansion of the board of directors or the resignation, death or removal of a director, which prevents stockholders from being able to fill vacancies on our board of directors.

Special meetings of our stockholders may be called only by our Executive Chairman of the Board, our Chief Executive Officer, our board of directors or holders of not less than the majority of our issued and outstanding capital stock. This limits the ability of minority stockholders to take certain actions without an annual meeting of stockholders.

Our stockholders may not act by written consent unless the action to be effected and the taking of such action by written consent is approved in advance by our board of directors. As a result, a holder, or holders, controlling a majority of our capital stock would generally not be able to take certain actions without holding a stockholders' meeting.

Our certificate of incorporation prohibits cumulative voting in the election of directors. This limits the ability of minority stockholders to elect director candidates.

Stockholders must provide timely notice to nominate individuals for election to the board of directors or to propose matters that can be acted upon at an annual meeting of stockholders. These provisions may discourage or deter a potential acquiror from conducting a solicitation of proxies to elect the acquiror's own slate of directors or otherwise attempting to obtain control of our company.

- Our board of directors may issue, without stockholder approval, shares of undesignated preferred stock. The ability to authorize undesignated preferred stock makes it possible for our board of directors to issue preferred stock with voting or other rights or preferences that could impede the success of any attempt to acquire us.



## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

## Recent Sales of Unregistered Securities

During the three months ended September 30, 2014, we did not issue any unregistered securities.

## Issuer Purchases of Equity Securities

The Board of Directors has authorized us to purchase up to \$300.0 million of our outstanding Class A common stock through August 2015. The timing and amount of any share repurchases will be determined based on market conditions, share price and other factors, and the program may be discontinued or suspended at any time. We expect to fund the repurchases through cash on hand and future cash flow. We also have the ability to fund share repurchases with borrowings under our Credit Agreement, which we entered into in July 2014. Repurchases will be made in compliance with SEC rules and other legal requirements and may be made in part under a Rule 10b5-1 plan, which permits stock repurchases when the Company might otherwise be precluded from doing so.

During the three months ended September 30, 2014, we purchased 1,349,712 shares of Class A common stock for an aggregate purchase price of \$8.3 million (including fees and commissions) under the share repurchase program. A summary of our Class A common stock repurchases during the three months ended September 30, 2014 under the repurchase program is set forth in the following table:

Date	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Program	Maximum Number (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under Program
July 1-31, 2014	338,200	\$6.40	338,200	\$ 116,000,000
August 1-31, 2014	887,712	5.96	887,712	111,000,000
September 1-30, 2014	123,800	6.88	123,800	110,000,000
Total	1,349,712	\$6.16	1,349,712	\$ 110,000,000

## ITEM 5. OTHER INFORMATION

## ITEM 6. EXHIBITS

See the Exhibit Index immediately following the signature page of this Quarterly Report on Form 10-Q.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized on this 30th day of October 2014.

GROUPON, INC.

By: /s/ Jason E. Child  
Name: Jason E. Child  
Title: Chief Financial Officer

Edgar Filing: Groupon, Inc. - Form 10-Q

EXHIBITS

Exhibit Number	Description
31.1	Certification of Chief Executive Officer pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of Chief Financial Officer pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certifications of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101	Interactive data file

101