

Wirecard: Audits and Revenue Recognition Concern

SHORT @ €97

Analyst: **Mark Hiley**[Wirecard – View All Notes and Models](#)Recommendation: **Short (No Change)**Price: **€97**2-Year Price Target: **€30**Forecast Return: **69%**3m Average Daily Volume: **\$244.3m**Market Cap: **€12bn**Ticker: **WDI GY**

Investment Thesis

- **Changes in revenue recognition policy in the Indian Star Global subsidiary represent a red flag. Wirecard may have reduced revenue in FY'17 under the E&Y audit (€0.6m) before increasing revenue in FY'18 under a new auditor and new revenue recognition policies (€88.1m). This raises questions regarding €87.5m of the organic growth during that period. The nature of Star Global's business as an offline money remittance and FX shop also reminds investors that Wirecard is not necessarily a scalable ecommerce payment processor.**
- **This is not an isolated discovery, and has similarities with patterns at the Systems@Work takeover in 2011.**
- **Multiple changes of auditor remain apparent in subsidiary filings in India.**
- **Wirecard has different auditors within both India and Singapore, whilst timings of audit may create risk for investors. India also has a March year-end, compared to December at the AG.**
- **Subsidiary audits typically complete, and filings occur, considerably after the topco audit. Whilst this is not unusual, it creates further risk in the process. For example, the 2017 accounts were filed at topco well before the audit of the 2016 subsidiary accounts in India and Singapore were completed.**
- **Wirecard currently expects to file FY'18 accounts on 04 April 2019, though there is some risk apparent on the timing due to the negative press coverage introduced by the Financial Times.**
- **Our Short thesis is unchanged; we see Wirecard as a Short today with a €30 price target.**

In this note, we address concerns we have into revenue recognition and auditor changes into Wirecard subsidiaries – specifically the Star Global/India and Systems@Work/Singapore subsidiary.

In addition, ahead of Wirecard releasing FY'18 accounts on 04 April 2019, the company will now be conducting audit and financial consolidation/reporting against the backdrop of a series of very negative public articles published in the Financial Times (FT), an ongoing internal legal investigation (which commenced around May 2018), and a subsequent police investigation in Singapore. This increases the pressure on the individuals that will be involved in the preparation and audit of the statements and raises the risk profile for investors. The specific concerns raised by the FT will necessarily be present in discussions, although the CEO described these as a 'non-issue' on the company's conference call last week (04 February 2019). This is important as investors need 100% trust in Wirecard's financials, which were already opaque. With €12bn market cap, €1.3bn of gross debt, and reporting €264m of adjusted free cash flow in 2017, the stock valuation remains demanding. Every day that passes without the Singaporean police or Wirecard itself reporting back on the fraud allegations and internal investigation is a difficult day for shareholders.

The stock appears to be de-rating according to corporate governance concerns. In this note, we raise a specific concern related to revenue recognition and audit change in one of the Indian subsidiaries – Star Global – and revisit a previous red flag on Systems@Work (Singapore).

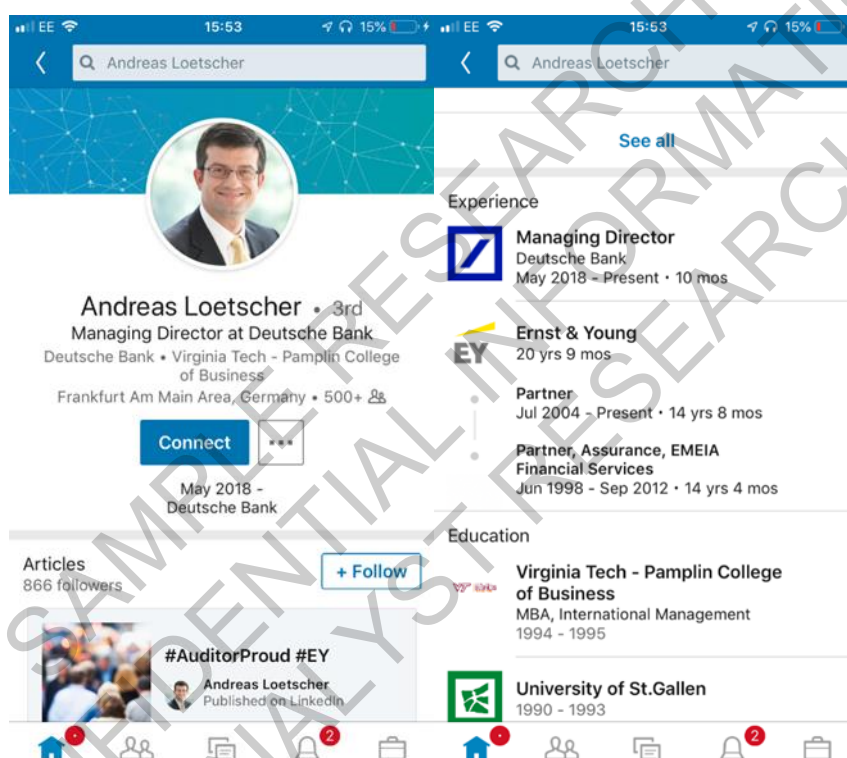
Germany Audits

There will be a relatively new CFO and likely a new primary signatory from Ernst & Young (E&Y) for this year's topco audit. Burkhard Ley, the previous CFO, did not sign the 2017 accounts as he left the role of CFO at the end of the year (Alexander von Knoop signed in 2017 as he replaced Mr Ley with effect from 01 January 2018). Mr Von Knoop is a Wirecard insider and would naturally have prior knowledge of the accounts.

Wirecard is audited by E&Y, which approved the 2017 topco report and issued an unqualified opinion. The board meeting held on 11 April 2018 examined the statements and reports and approved them. Wirecard is scheduled to publish its annual report on 04 April 2019 for the year to December 2018. Markus Braun (CEO), Alexander von Knoop (new CFO), Jan Marsalek (COO), and Susanne Steidl (CPO) signed the accounts for 2017.

E&Y's responsible auditor was Andreas Loetscher (since 2015). According to his LinkedIn profile, he moved to Deutsche Bank to be a Managing Director in May 2018, although the profile also shows him still active as a partner at E&Y (Exhibit 1). He appears to have spent over 20 years at E&Y (14 as a partner). He seems to have joined Deutsche Bank at roughly the same time as the FT claims the whistleblower report was submitted by Wirecard's lawyers in Singapore. This set of topco accounts could therefore require a new primary signatory. E&Y has been the sole auditor of Wirecard AG and the Group since 2011 (although we now note that another auditor now covers one of the Singapore subsidiaries, with some different auditors in India). Last year, there was a secondary signatory, Martin Dahmen, who appears to be a senior 26-year partner at E&Y. E&Y audits one of the two Singapore subsidiaries; it appears it has not yet filed the 2017 accounts at Singapore company's house.

Exhibit 1: Wirecard's Primary Auditor May Have Moved to Deutsche Bank in May 2018



Source: LinkedIn Search, Accessed February 2019

Wirecard's payment to E&Y increased substantially in FY'17 (from €1.339m to €2.178m), which is not unusual considering the larger scope of the business after the acquisitions of Indian and Citigroup assets. In general, we consider rising audit fees a red flag.

India Audits

When we previously examined the Indian acquisitions in 2016-17, we identified multiple changes of auditor either side of the Wirecard takeovers. Wirecard acquired four businesses in India (Visa Processing Services, Hermes I Tickets Pvt Ltd, GI Technologies Pvt Ltd, and Star Global). Between 31 March 2015 and 16 October 2017, there were, collectively, five auditors involved and nine relinquishments of audit responsibility. This is a clear red flag for us.

Exhibit 2: Multiple Changes of Auditor in India (August 2015 – September 2017)

Auditor Changes				
Wirecard (former) entity	Auditor	Date	Reason/Action	Partner
Visa Processing Services (Wirecard India)	BSR & Associates LLP	31st March 2015	Do not wish to continue	Ashwin Suvarna
Visa Processing Services (Wirecard India)	SR Batliboi & Associates LLP	26th September 2016	Sign Accounts	Aniruddh Sankaran
Hermes I Tickets Pvt Ltd	Kuriachan & Nova	24th August 2015	Preoccupation in other assignments	VP Kuriachan
Hermes I Tickets Pvt Ltd	V Krishnan & Co	31st August 2015	Resignation not in position to continue	K Ulaganaathan Shankar
GI Technologies Pvt Ltd	Kuriachan & Nova	5th June 2016	Preoccupation in other assignments	VP Kuriachan
Hermes I Tickets Pvt Ltd	Kuriachan & Nova	15th June 2016	Preoccupation in other assignments	VP Kuriachan
Hermes I Tickets Pvt Ltd	V Krishnan & Co	15th June 2016	Preoccupation in other assignments	K Ulaganaathan Shankar
Hermes I Tickets Pvt Ltd	CNGSN & Associates LLP	19th August 2016	Appointment	
Star Global	SR Batliboi & Associates LLP	5th September 2016	Appointment	
Hermes I Tickets Pvt Ltd	CNGSN & Associates LLP	29th September 2016	Sign Accounts	
Star Global	SR Batliboi & Associates LLP	12th July 2017	Inability to continue	NS Bharath
Hermes I Tickets Pvt Ltd	CNGSN & Associates LLP	16th October 2017	Preoccupation and other commitments	R. Thurumalmarugan
GI Technologies Pvt Ltd	CNGSN & Associates LLP	16th October 2017	Preoccupation and other commitments	R. Thurumalmarugan

Source: Company Filings (www.mca.gov.in)

Changes of auditors after takeovers are not unusual however, and Wirecard should naturally want to align audit in India to the E&Y affiliate; SR Batliboi. SR Batliboi is a JV (of Ernst & Young and S.R. Batliboi). [E&Y lists 12 firms & affiliates](#) in India at 05 January 2018. However, SR Batliboi only audited Visa Processing Services and another Wirecard business for one year (Star Global), in India.

We already noted that SR Batliboi cited 'inability to continue' for the Star Global audit on 12 July 2017. SR Batliboi was in place on Visa Processing Services (Wirecard India) for signing on 26 September 2016.

Updates from Latest Filings

N.B. We have attached copies of the relevant Star Global accounts and audit resignations on our website.

- Hermes I Tickets** (acquired from with GI Retail): This is the largest Indian entity, which recorded revenue of €32m in the subsidiary filing to March 2017 (down from revenue levels of March 2016). **Suresh Surana and Associates** was the auditor of FY'17, after the resignation of **CNGSN** (audited FY'16 accounts, appointed 19 August 2016), which, in turn, came in after the resignation of both **Kuriachan & Nova** (24 August 2015 and 15 June 2016) and **V Krishna & Co** (31 August 2015 and 15 June 2016). We see filings for Hermes I Tickets and Wirecard Sales International GmbH for FY'17 implying Hermes was amalgamated into the GmbH, which subsequently filed in India. Hermes' income increased materially (by nearly 3x to €10m) due to a materially lower expenditure line. Of the revenue reported, 68% was generated from 'Airline booking and hosting business', whilst the profit gain is due to a reduction in 'cost of materials consumed' from INR235,59,13,011 to INR56,66,84,222 in the year. Hermes does not, so far, appear to have filed Mar-18 accounts. We are interested to see revenue disclosures in due course due to our analysis below on Star Global. To our knowledge, E&Y has not audited Hermes, which is strange as it was the largest entity in India and important for the group. Investors may ask how the same auditor can resign twice – a good question – and we attach copies of the resignation letters to this note.
- GI Technology Private Limited** (60% owned by Wirecard, which paid €14m for the stake): After an AGM on 22 December 2017, the company appointed a new auditor (Suresh Surana & Associates), which signed the March 2018 accounts on 29 September 2018. CNGSN had previously resigned on 16 October 2017 (post Wirecard's deal). This is a small company registering €2m revenue (from interest income and charges on domestic money remittance), which is losing money and has contracts with other Wirecard businesses. The business is funded with a ~€7m loan from Hermes. The directors state that the weak financial performance was due to lower-interest income and are refocusing on fintech products for the banking industry. In its investor presentation from September 2017, Wirecard suggests GI Technology has 'award-winning performance' – the company financials suggest differently. The price paid also looks high in this context, although Wirecard will likely view this as a strategic platform investment in India.

Exhibit 3: GI Technology Reports €2m Revenue, Wirecard Claims 'Award-winning performance'



Source: Wirecard Investor Presentation September 2017

- **Visa Processing Services** (renamed **Wirecard India Private Limited**): This business was acquired in 2015 and provides access to prepaid card issuing across the Wirecard ecosystem. Although this was acquired in India, the headquarters are detailed in Wirecard's filings as in Singapore. It was acquired for \$16m cash. This entity was audited by E&Y's affiliate **S.R. Batliboi** (which signed the March 2016 accounts on 28 September 2017). Accounts are signed by Ng Fook Sun in Singapore as a director (see section below on Wirecard Singapore Pte Ltd). This is a small business providing services to other Wirecard entities and is essentially the license holder for Visa Prepaid card issuing.
- **Star Global** (renamed **Wirecard Forex India Private Limited**): There is a different auditor here (**S Viswanathan LLP**) and Star Global was acquired alongside the Hermes/GI deals (although we do not believe it was part of GI Retail), from the Emerging Markets Investment Fund 1A (announced October 2015, completed February 2016). The new auditor signed on 10 August 2018, but the previous auditor had been S.R. Batliboi (the E&Y affiliate). It seems unusual that E&Y is no longer auditing this company, and in fact, **only came in for one year for the audit** – we discuss this in more detail below. This was a business with less than 20 employees when March 2016 accounts were reported, and was loss-making at the time. We do not know how much Wirecard separately paid for this business. Importantly, it holds an FFMC license with the Reserve Bank of India and it is a money changer and FX dealer.
 - Revenue recognised in the FY'18 accounts shows it doubled from €44.8m (Mar-17) to €88.1m (Mar-18), which appears to be an exceptional performance under Wirecard's ownership and contributes 5-10% of the growth reported in the AG last year. These revenue numbers are visible in the Viswanathan audit in the Mar-18 filings.
 - However, upon further inspection, operating expenses are running at almost the same amount. We can see from the Star Global income statement INR665,25,21,097 total revenue and INR664,75,31,973 total expenses, with a small loss (after interest, tax and other costs) for the period. We infer that at least at the subsidiary level, Wirecard is now recognising the money-changing and remittances on a gross basis rather than the net commission. If this interpretation is correct, the revenue in the AG could have been increased due to the accounting at the Indian subsidiary level. In a payment processor, revenue should be the net 'take' or 'commission' on the gross cash value.
 - There is a very interesting note in the Star Global accounts indicating that a change in revenue recognition has been applied for voluntary revision of turnover recognition. The Mar-17 revenue that was submitted of €0.6m was 'causing problems for the holding company to consolidate their balance sheet'. This is because under the E&Y audit, reported revenue was reduced to the net basis, which was out of line with prior year gross basis and the gross basis considered in the FY'18 report.

Exhibit 4: Revenue Recognition Changes in Star Global Highlighted by Auditors

30. DISCLOSURE ON APPLICATION FILED BEFORE NATIONAL COMPANY LAW TRIBUNAL.
The Financial Statements of your Company from the date of Incorporation up to 31.03.2016 had reproduced the Turnover/ Sales and purchase separately. However, for the year ended March 31, 2017, your Company had adopted a different method of presentation of the financial statements i.e. Total revenue being Sales less Purchases / Stock (tabled below) as compared to practice followed for the previous years.

At the time of consolidation of accounts of your Company with its Holding Company, it was brought to the knowledge of the Company that though there is no deviation, the net turnover as mentioned in the accounts submitted for March 31, 2017 is not in line with its earlier year accounts, which is causing problem for the holding company to consolidate their balance sheet.

Hence your Company has filed an application before the Hon'ble National Company Law Tribunal, bench at Bengaluru for the voluntary revision of financial statements and board's report for the financial year ended 31.03.2017 vide C.P. No 166/BB/2018 in order to make the following changes in the financial statements as it would help in the consolidation of the financials with the Holding Company

Particulars	As at Mar 31, 2017	As at Mar 31, 2016
Sale / Surrender of currency, card, TC, TT	3,297,297,410	2,309,302,804

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Card Forex India Private Limited Standalone Financial Statements for period 01/04/2017 to 31/03/2018

Purchase / Settlement of Currency, Card, TC, TT	3,256,662,626	2,277,505,766
Changes in Stock of currency, Card, TC, TT	(1,166,559)	3,982,210
Revenue for the year	41,801,343	27,814,828

The application for the proposed change is pending before the Hon'ble National Company Law Tribunal, bench at Bengaluru. Upon sanction of the application by the Hon'ble National Company Law Tribunal, bench at Bengaluru, an Extra-ordinary General Meeting shall be convened by the Company in order to inform the members in detail about the changes made in the financial statements and also to adopt the revised Financial Statements and Directors Report for the year ended 31.03.2017.

Also, the next date for hearing this application is fixed on 3rd day of September 2018.

Source: Star Global Filings

Star Global Consequences

If our initial conclusions on Star Global are correct, this implies that Wirecard's revenue contains gross revenue from money-changing business and is subject to audit debate. Star Global revenue of €88.1m (Mar-18) represented >5% of group revenue (LTM to Mar-18), ~12% of Asia Pacific revenue. As Wirecard has been highly-acquisitive and this is a repeating pattern, this gives us cause for concern more broadly on revenue recognition and organic growth. Investors and analysts focus on revenue growth for growth stocks such as Wirecard. We are now deepening our work to understand the possible EBITDA and cash impact, if any.

Looking at the Star Global (Wirecard Forex India Private Limited) accounts, we can see revenue recognition as shown in Exhibit 5. We do not see accounts prior to the March 2015 fiscal year. In any case, Star Global was a small money exchange business with less than 20 employees at the time.

Exhibit 5: Revenue in Star Global, from €0.6m (Mar'17) to €88.1m (Mar'18)

INR	Mar-15	Mar-16	Mar-17	Mar-18
Auditor (Date Signed)		S Visawanathan (10/8/16)	S.R. Batliboi (5/9/17)	S Viswanathan (10/8/18)
(Gross) Revenue (INR)	1,853,933,494	2,309,302,804	3,297,297,410	6,634,573,390
Revenue recognised (INR)	1,853,933,494	2,309,302,804	41,801,343	6,634,573,390
net revenue %		100%	1%	100%
Restated Revenue Application		27,814,828	41,801,343	
As % of gross revenue		1.2%	100.0%	
Take rate		1.2%	1.3%	
Profit after Tax	-	10,072,351	272,666	4,888,300
€m	Mar-15	Mar-16	Mar-17	Mar-18
FX rate (INR/€)	77.2	72.3	73.5	75.3
(Gross) Revenue (€m)	24.0	32.0	44.8	88.1
Revenue recognised (€m)		32.0	0.6	88.1

Source: Star Global Filings in India

Key Points

- If our interpretation is correct, we can potentially see how organic revenue growth could be boosted through changes of audit and recognition policy. Star Global was a small business with a volume of gross transactions. By recognising net revenue of €0.6m in Mar-17, then gross revenue of €88.1m in Mar-18, we have reason to believe up to €87.5m of Wirecard's reported revenue and organic growth could be down to accounting restatements (and is obviously subject to the reconciliations occurring higher up in the audits). The differing year-ends, differing audits, late filing dates, and timing of acquisitions (e.g. towards year-ends and completing across audit periods) make it extremely hard to reconcile such financials.
- Star Global was audited by Visawanathan (FY'16 on 10 August 2016), which resigned, to be replaced by Batliboi, which then audited the FY'17 accounts (on 05 September 2017).
- Batliboi changed revenue recognition from €32m in the prior year (FY'16) to €0.6m (FY'17), aligning recognition with net rather than gross revenue. Batliboi then resigned to be replaced by Visawanathan in time for the FY'18 accounts (10 August 2018). Visawanathan then highlights that *'the change in revenue recognition under Batliboi is not in line with earlier year accounts, which is causing problems for the holding company to consolidate their balance sheet'* (FY'18 report).
- Star Global revenue is consolidated into the direct holding company 'Wirecard Sales International Holding GmbH' which was exempt from the duty to prepare consolidated statements. This means we cannot yet see how revenue recognition follows up to the AG via the GmbH holding.

Exhibit 6: Wirecard Sales International Holding GmbH Was Exempt from Filing Last Year

Exemption from the duty to prepare consolidated financial statements

In accordance with Section 291 (1) of the German Commercial Code (HGB), Wirecard Technologies GmbH, Aschheim, Wirecard Acquiring & Issuing GmbH, Aschheim, and Wirecard Sales International Holding GmbH, Aschheim, are exempt from the duty to prepare consolidated financial statements as full compliance with the requirements of Section 291 (2) of the HGB already exists.

In addition, Wirecard has decided to make use of the exemption pursuant to Section 17 of the Irish Companies Act of 1986 not to submit consolidated financial statements of the Irish group to Companies Office in Ireland.

Wirecard AG confirms that the sub-group financial statements of Wirecard Technologies GmbH, Wirecard Acquiring & Issuing GmbH, Wirecard Sales International Holding GmbH and also Wirecard Payment Solutions Holdings Ltd. are included in these financial statements.

Wirecard Sales International Holding GmbH

Aschheim

(District Court Munich, HRB 187465)

Sections 264 (3), 264b HGB for the financial year from 01.01.2017 to 31.12.2017

Wirecard AG (Munich District Court HRB 169227), with its registered office in Aschheim, acting as the sole shareholder of Wirecard Sales International Holding GmbH (District Court Munich, HRB 187465), with its registered office in Aschheim b. Munich unanimously approved the exercise of the exemption option pursuant to Section 264 (3) HGB for the financial year ended 31.12.2017.

Wirecard AG is the parent company required to assume losses in accordance with Section 302 AktG.

Wirecard Sales International Holding GmbH is included as a subsidiary in the consolidated financial statements of Wirecard AG as at 31.12.2017 and disclosed in the notes to § 325 HGB of the Consolidated Financial Statements and hereby notifies the exemption under § 264 (3) HGB in accordance with § 264 (3) Paragraph 4 letter b HGB with.

Aschheim in November

The Board

Source: Wirecard Annual Report 2017

Exhibit 7: S Viswanathan Resigns from Audit after Signing on 10 August 2016, S.R. Batliboi Proposed to Be Appointed (E&Y affiliate which then served one year)

12. STATUTORY AUDITORS:

The Company has received a letter from M/s. S. Viswanathan LLP, Chartered Accountants, Bengaluru, expressing their unwillingness to be auditors of the company. Therefore, your Board of Directors have proposed to appoint M/s. S.R. Batliboi & Associates LLP, Chartered Accountants, Chennai, in place of M/s. S. Viswanathan LLP.

M/s. S.R. Batliboi & Associates LLP, Chartered Accountants, Chennai, have confirmed that their appointment as Statutory Auditors, if made, will be in accordance with the provisions of Sections 139 & 141 (3)(g) and applicable provisions of the Company Act 2013 and that they are not disqualified for such appointment.

13. AUDITORS' REPORT:

There are no adverse remarks in the auditors report except the matter relating to provision not made for gratuity. In this connection, it may be noted that since incorporation, the company is incurring loss, besides having less than 20 employees on rolls and change of Management of the company. The new Management is striving its best to promote the business of the company and making provision for gratuity to employees is underway.

Source: Star Global Filings

Exhibit 8a: €88.1m (Rs.6,63,45,73,390) Turnover Achieved under Visawanathan FY'18 Audit**4. BRIEF DESCRIPTION OF THE COMPANY'S WORKING DURING THE YEAR / STATE OF COMPANY'S AFFAIR**

The Company has carried out the business of full-fledged money changers and authorized dealers in foreign currencies and has been able to

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Wirecard Forex India Private Limited Standalone Financial Statements for period 01/04/2017 to 31/03/2018

achieve a total turnover of Rs.6,63,45,73,390 during the year under review and in the previous year the turnover was Rs.3,29,72,97,410. The Company, having its FFMC License upgraded by Reserve Bank of India, is expecting to achieve increased volume of business in the current financial year than in the previous year.

Source: Star Global Filings FY'18

Exhibit 8b: €0.6m (Rs.4,18,01,343) Total Turnover Achieved under Batliboi/E&Y FY'17 Audit

STAR GLOBAL CURRENCY EXCHANGE PRIVATE LIMITED Standalone Financial Statements for period 01/04/2016 to 31/03/2017

4. BRIEF DESCRIPTION OF THE COMPANY'S WORKING DURING THE YEAR/STATE OF COMPANY'S AFFAIR

The Company has carried out the business of full fledged money changers and authorized dealers in foreign currencies and has been able to achieve a total turnover of Rs.4,18,01,343/- during the year under review. The Company having since upgraded its FFMC licence by Reserve Bank of India is expected to handle increased volume of business and obtain better results in the current financial year.

5. CHANGE IN THE NATURE OF BUSINESS, IF ANY

There is no change in the nature of business of the Company.

6. MATERIAL CHANGES AND COMMITMENTS, IF ANY, AFFECTING THE FINANCIAL POSITION OF THE COMPANY WHICH

Source: Star Global Filings FY'17

Exhibit 8c: €32m (Rs.230.93 Crores = Rs.230,93,00,00,000) Turnover Achieved under Visawanathan FY'16 Audit

The company has not transferred any surplus Balance Sheet or has not transferred any amount and kept under reserves and surplus during the year.

4. BRIEF DESCRIPTION OF THE COMPANY'S WORKING DURING THE YEAR/STATE OF COMPANY'S AFFAIR:

The Company has carried out the business of full fledged money changers and authorize dealers in foreign currencies and has been able to achieve a total turnover of Rs . 230 . 93 Crores during the year under review . To meet the working capital requirement to handle increased volume of business , the new Promoters have brought in additional finance to the tune of Rs . 973 , 03 , 000 / - by way of investment in the equity capital of the Company after increasing the Authorized Capital of the Company from RS . 6 crores to RS.15 crores . The Company is submitting necessary application to upgraded by Reserve Bank of India for upgrading its FFMC License to as to enable the Company to handle increased volume of business in the current financial year.

5 : CHANGE IN THE NATURE OF BUSINESS , IF ANY:

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Source: Star Global Filings FY'16

Star Global Conclusions & Thoughts

- Wirecard acquired the Indian assets for a large headline amount of up to €330m, yet it was difficult to see significant financial activities in the acquired companies prior to the acquisition. At the time, only \$1.5m investment in Star Global was visible on the FDI entries in the Indian register.
- As we have seen, Wirecard changed revenue recognition from gross of €44.8m, down to net of €0.6m in the year following the takeover, under the new E&Y affiliate auditor. E&Y is the topco auditor and the Singapore auditor.
- The E&Y affiliate then left, and the new auditor changed revenue back to the gross basis, recognising €88.1m, up from €0.6m in the prior year.
- This change of policy would have the effect of significantly boosting Wirecard's revenue and revenue growth in the year following the takeover, on the assumption that revenue policy followed through the GmbH into the AG.

- Our view is that money-changers and FX shops should not be recognising revenue on a gross basis. Rather, they should recognise the net commission, which was ~1.3% (FY'17). This appears to be an area of debate according to the audit reports outlined above.
- A restatement of revenue would potentially have a negative impact on Wirecard's perception by the market. Although we are yet to ascertain the cash and EBITDA impact, we will give this point further thought.
- This accounting methodology and insight may help to explain why Wirecard has been highly acquisitive in emerging markets and raises questions about the definition of organic growth. As Star Global was owned for the full fiscal year March 2017, the growth in revenue of €87.5m could all be included as organic. The sell-side values and considers Wirecard based on the assumptions of Wirecard's stated organic growth (e.g. +28% 9M'18 as shown in the investor presentation). However, if this organic growth could be attributable to accounting changes, then the arguments must be revisited.

Systems@Work Acquisition in 2011

- Gross revenue debate was apparent in some of the other Asian acquisitions in 2011-14. For example, Systems@Work (Singapore) restated revenue from SGD5.879m to SGD17.810m for FY'11, after Wirecard's takeover, alongside a change of auditor.
- Helmi Talib & Co audited the Dec-11 accounts for Systems@Work, whilst E&Y audited the Dec-12 accounts, restating the revenue. A restatement of revenue under E&Y raises questions about differences in revenue recognition under E&Y audits.
- Wirecard acquired Systems@Work on 01 December 2011, paying up to €35m. In 2011 as a whole, Wirecard guided to €7.9m revenue in the annual report disclosures, although it only took €0.4m to the accounts for the one month it owned the company. Systems@Work employed 31 people in 2012.
- In the subsidiary filings, we saw revenues of SGD5.9m (<€4m) in the 2011 statement with the previous auditor. In the next year, we see €11.6m for FY'11, and then a doubling of revenue to €17.1m for FY'12 under E&Y's audit.
- If Wirecard consolidated €17.1m revenue (FY'12) after €7.9m (FY'11 annual report disclosure) under organic growth, this would be material to the numbers at the time. Wirecard reported €395m revenue in FY'12 and grew by €70m (21%) that year.

Exhibit 9: Star Global Restatement Follows Similar Confusing Patterns to Systems@Work Restatements

SYSTEMS@WORK PTE. LTD. AND ITS SUBSIDIARIES

STATEMENT OF COMPREHENSIVE INCOME For the financial year ended 31 December 2011

	Note	Group	
		2011 SGD	2010 SGD
Revenue		5,879,164	5,168,765
Other Items of Income			
Interest Income	4	2,374	2,222
Other Income	5	40,941	127,904
Other Items of Expense			
Employee Benefits Expense	6	(1,806,651)	(1,600,976)
Cost of Services		(2,616,587)	(1,920,861)
Depreciation Expense		(18,686)	(19,386)
Finance Costs	7	-	(240)
Other Expenses		(583,282)	(625,829)
Profit (Loss) Before Tax from Continuing Operations	8	897,273	1,131,599

Systems@Work Pte Ltd and its Subsidiaries

Consolidated Statement of Comprehensive Income for the financial year ended 31 December 2012

	Note	2012 \$	2011 Restated \$
Revenue		26,318,867	17,809,855
Cost of services		(19,169,731)	(14,547,278)
Gross profit		7,149,136	3,262,577
Other items of income			
Interest income	4	1,042	2,374
Other income	5	45,153	40,941
Other items of expense			
Administrative expenses	6	(2,643,156)	(1,825,337)
Other expenses		(612,187)	(583,282)
Profit before tax	7	3,939,988	897,273
Income tax benefit	8	296	-
Profit for the year		3,940,284	897,273

Source: Systems@Work Company Filings

Exhibit 10: Systems@Work Revenue Recognition

In fiscal year 2011, the income statement recognizes net income for the year of EUR 35K and revenues of EUR 352K from the participating interest in Systems@Work. Systems@Work recorded revenues of EUR 7,857K and net income of EUR 3,319K in 2011 as a whole in the structure acquired.

Source: Wirecard Annual Report 2012

Systems@Work subsequently became Wirecard Singapore Pte Ltd. We will now discuss Singapore.

Singapore Audits

In the annual report, Wirecard describes Singapore as 'the Asian head office'. There are two primary subsidiaries still filing accounts: Wirecard Asia Holding Pte. Ltd and Wirecard Singapore Pte. Ltd. We believe the Laos and Vietnam subsidiaries are consolidated into Wirecard Singapore. Two other Wirecard entities – Wirecard Pte Ltd (previously Wirecard Asia Pte Ltd) and E-Payment Asia (formerly E-Credit Plus and Wirecard Asia) – have been struck off.

Investors should remember that the entity Wirecard Singapore Pte Ltd was 'also known as' Systems@Work Pte Ltd, which was acquired by Wirecard in late 2011. The FT highlighted loans made to Systems@Work prior to the deal being announced, quoting directly from CEO Braun. PaymentLink Pte Ltd was another Singapore entity that received an audit opinion questioning going concern. This business was acquired by Wirecard from Korvac Group (a Singapore payments company) and PaymentLink in 2013. We believe these assets were amalgamated into Systems@Work from 2015, which then became Wirecard Singapore Pte Ltd, which is audited by E&Y.

Our concerns on Singapore based on filing dates are as follows:

- Firstly, that the Wirecard Asia Holding 2016 accounts (year ending December 2016) were signed on 27 September 2017 by Jan Marsalek (COO) and Ng Fook Sun (Director), audited by RSM Chio Lim LLP. Whereas the Wirecard Singapore 2016 accounts were not signed until 18 June 2018, they were signed by Ng Fook Sun (Director) and Jeffry Ho Kok Hoong (Director), but not Jan Marsalek, and they were audited by Ernst & Young LLP.
 - Wirecard has two different auditors in Singapore. E&Y was signing the accounts on the company where questions have been asked in the past by the FT (Wirecard Singapore was initially incorporated on 05 November 1999, long before Wirecard's takeover when it was Systems@Work), whereas RSM is signing the accounts of the more recently formed legal entity (Wirecard Asia was incorporated on 01 October 2014).
 - The signing of the E&Y-audited entity appears to be slower, signed nearly 18 months after year-end. This is the bigger, more complex entity, filing SGD57m revenue compared to SGD4.2m for Wirecard Asia. In the context of the Wirecard group, Singapore revenue is small (~3%) but Singapore is important as the Asian hub, containing legal and compliance functions.
 - The 2016 accounts were finally filed at ACRA following AGMs on 20 April 2018 and 22 June 2018. This may not be unusual, but it seems slow considering the topco audit of the 2017 accounts was already signed by 11 April 2017. Wirecard finalised their 2017 accounts without the Singapore 2016 accounts even being filed.
 - Auditors often sign topco accounts before subsidiary audits are completed and may rely on basic fact packs supplied from below to complete their own audit. However, the mismatch of timing of audit between subsidiary levels of a large entity can create risk in the audit. Having two different auditors in Singapore can also create risk, as can the multiple auditors and changes we already outlined in India.
 - The Wirecard Asia Holding statements for 2017 were finally filed on the morning of 12 February 2019. At least Wirecard will be doing the topco 2018 audit in the knowledge its Singapore 2017 accounts have been filed. RSM appears to move faster than E&Y, even considering the Citibank assets (another Wirecard acquisition in Asia in 2016-17) were consolidated into these statements for the first time.

- The Wirecard Singapore statements for 2017 have not yet been filed. The 2016 accounts were signed on 18 June 2018, so the late filing may not be completely unusual. However, it does imply that E&Y may not have signed the 2017 accounts in Singapore. The investigations appear to have opened up more broadly during that period according to the FT and Wirecard, so the timings may not be coincidental. However, we do note that E&Y did sign the 2016 accounts after the whistleblower raised concerns in February 2018 (according to the FT).

Additional Considerations

- We are still waiting for Wirecard to feed back to the market on the findings from its internal investigation in Singapore, whilst some comment from the Singapore police can be anticipated following their visit. Wirecard described this as a 'non-issue' on the conference call on 04 February 2019, but the duration of the investigation may indicate otherwise.
- CEO Markus Braun owns 7% of the company (valued at ~€900m) and pledged ~4.2m of these shares in December 2017 (~€400m). We do not know who the primary lender is against this collateral, or the loan-to-value ratio. Broadly speaking, we view borrowing against shares as a soft sale of shares. Mr Braun subsequently bought a small volume of shares (~€5m) in February 2018. A further share price decline may lead to some debate about margin requirements.

Conclusion

Our Short thesis on Wirecard is unchanged. Over many years, we have raised red flags on the accounts — focused on cash conversion, rising gross debt, M&A transactions, and capital intensity. We now have reasons to question the published organic revenue growth and will continue our digging to ascertain the potential impact on earnings and cash flows.

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