OVERSTOCK.COM, INC
Form 10-Q
October 24, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2013

Or

o 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: 000-49799

OVERSTOCK.COM, INC.
(Exact name of registrant as specified in its charter)

Delaware	87-0634302
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
6350 South 3000 East Salt Lake City, Utah 84121	(801) 947-3100
(Address, including zip code, of Registrant's principal executive offices)	(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), (2) has been subject to such filing requirements for the past 90 days. Yes ý No o

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 ý No o

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 o	Accelerated filer x
Non-accelerated filer o	Smaller reporting company o

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the act). Yes o No ý

There were 23,774,066 shares of the Registrant’s common stock, par value $0.0001, outstanding on October 21, 2013.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS (UNAUDITED)

Overstock.com, Inc.
Consolidated Balance Sheets (Unaudited)
(in thousands)

	September 30, 2013	December 31, 2012
Assets		
Current assets:		
Cash and cash equivalents	$84,862	$93,547
Restricted cash	1,780	1,905
Accounts receivable, net	14,672	19,273
Inventories, net	22,733	26,464
Prepaid inventories, net	1,926	1,912
Prepaids and other assets	13,062	12,897
Total current assets	139,035	155,998
Fixed assets, net	26,892	21,037
Precious metals	8,560	—
Goodwill	2,784	2,784
Other long-term assets, net	2,167	2,166
Total assets	$179,438	$181,985
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	$54,685	$62,416
Accrued liabilities	45,412	47,674
Deferred revenue	29,858	38,411
Total current liabilities	129,955	148,501
Other long-term liabilities	1,147	2,522
Total liabilities	131,102	151,023
Commitments and contingencies (Note 5)	0	0
Stockholders' equity:		
Preferred stock, $0.0001 par value:		
Authorized shares - 5,000		
Issued and outstanding shares - none	—	—
Common stock, $0.0001 par value		
Authorized shares - 100,000		
Issued shares - 26,898 and 26,481		
Outstanding shares - 23,774 and 23,451	2	2
Additional paid-in capital	360,730	356,895
Accumulated deficit	(232,168)	(247,096)
Treasury stock:		
Shares at cost - 3,124 and 3,030	(80,228)	(78,839)
Total stockholders' equity	48,336	30,962
Total liabilities and stockholders' equity	$179,438	$181,985

See accompanying notes to consolidated financial statements.

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Overstock.com, Inc.
Consolidated Statements of Income and Comprehensive Income (Unaudited)
(in thousands, except per share data)

	Three months ended September 30,		Nine months ended September 30,	
	2013	2012	2013	2012
Revenue, net				
Direct	$35,681	$34,215	$113,873	$109,048
Fulfillment partner	265,745	221,137	792,751	648,207
Total net revenue	301,426	255,352	906,624	757,255
Cost of goods sold				
Direct(1)	30,777	30,684	99,768	99,422
Fulfillment partner	211,499	178,126	630,931	520,614
Total cost of goods sold	242,276	208,810	730,699	620,036
Gross profit	59,150	46,542	175,925	137,219
Operating expenses:				
Sales and marketing(1)	22,463	14,899	60,376	42,886
Technology(1)	17,259	16,085	53,339	46,845
General and administrative(1)	15,970	13,828	47,643	43,166
Restructuring	—	(45)	(471)	53
Total operating expenses	55,692	44,767	160,887	132,950
Operating income	3,458	1,775	15,038	4,269
Interest income	34	30	100	86
Interest expense	(33)	(194)	(121)	(655)
Other income, net	165	1,213	360	2,364
Income before income taxes	3,624	2,824	15,377	6,064
Provision for income taxes	91	131	449	182
Net income	$3,533	$2,693	$14,928	$5,882
Net income per common share—basic:				
Net income attributable to common shares—basic	$0.15	$0.11	$0.63	$0.25
Weighted average common shares outstanding—basic	23,766	23,447	23,692	23,382
Net income per common share—diluted:				
Net income attributable to common shares—diluted	$0.14	$0.11	$0.61	$0.25
Weighted average common shares outstanding—diluted	24,446	23,754	24,297	23,511
Comprehensive income	$3,533	$2,693	$14,928	$5,882

(1) Includes stock-based compensation as follows (Note 7):

Cost of goods sold — direct	$37	$74	$117	$200
Sales and marketing	44	108	123	260
Technology	33	218	235	585
General and administrative	695	580	1,902	1,579
Total	$809	$980	$2,377	$2,624

See accompanying notes to consolidated financial statements.

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Overstock.com, Inc.
Consolidated Statements of Changes in Stockholders' Equity (Unaudited)
(in thousands)

	Common stock		Additional Paid-in	Accumulated	Treasury stock		
	Shares	Amount	Capital	Deficit	Shares	Amount	Total
Balances at December 31, 2012	26,481	$2	$356,895	$(247,096)	3,030	$(78,839)	$30,962
Net income	—	—	—	14,928	—	—	14,928
Stock-based compensation to employees and directors	—	—	2,377	—	—	—	2,377
Common stock issued upon vesting of restricted stock	334	—	—	—	—	—	—
Exercise of stock options	83	—	1,458	—	—	—	1,458
Purchase of treasury stock	—	—	—	—	94	(1,389)	(1,389)
Balances at September 30, 2013	26,898	$2	$360,730	$(232,168)	3,124	$(80,228)	$48,336

See accompanying notes to consolidated financial statements.

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Overstock.com, Inc.
Consolidated Statements of Cash Flows (Unaudited)
(in thousands)

	Nine months ended September 30,		Twelve months ended September 30,	
	2013	2012	2013	2012
Cash flows from operating activities:				
Net income	$14,928	$5,882	$23,715	$2,473
Adjustments to reconcile net income to net cash provided by (used in) operating activities:				
Depreciation and amortization	10,833	11,935	14,907	15,813
Realized gain from sale of marketable securities	(28)	(8)	(29)	(8)
Loss on disposition of fixed assets	—	72	—	72
Stock-based compensation to employees and directors	2,377	2,624	3,280	3,264
Amortization of debt discount and deferred loan costs	14	55	32	105
Loss on investment in precious metals	475	—	475	—
Loss from early extinguishment of debt	—	—	—	1,199
Restructuring charges (reversals)	(471)	53	(448)	53
Changes in operating assets and liabilities:				
Restricted cash	125	(24)	280	323
Accounts receivable, net	4,601	(519)	(652)	(5,575)
Inventories, net	3,731	1,603	(1,343)	(2,180)
Prepaid inventories, net	(14)	(641)	(258)	(253)
Prepaids and other assets	(2,995)	(314)	(1,387)	2,448
Other long-term assets, net	(445)	(1,160)	448	(1,332)
Accounts payable	(7,779)	(26,958)	11,277	761
Accrued liabilities	(2,308)	(7,478)	4,711	2,981
Deferred revenue	(8,553)	836	1,044	7,634
Other long-term liabilities	(707)	705	(786)	848
Net cash provided by (used in) operating activities	13,784	(13,337)	55,266	28,626
Cash flows from investing activities:				
Purchases of marketable securities	(111)	(69)	(124)	(110)
Purchases of intangible assets	(13)	(6)	(13)	(3)
Sales of marketable securities	291	154	291	154
Investment in precious metals	(5,980)	—	(7,377)	—
Expenditures for fixed assets, including internal-use software and website development	(13,970)	(10,563)	(15,896)	(12,960)
Proceeds from sale of fixed assets	—	56	—	56
Net cash used in investing activities	(19,783)	(10,428)	(23,119)	(12,863)
Cash flows from financing activities:				
Payments on capital lease obligations	(2,563)	(112)	(2,563)	(188)
Payments on line of credit	—	—	(17,000)	—
Capitalized financing costs	—	—	—	(19)
Payments on finance obligations	—	—	—	(21,528)
Paydown on direct financing arrangement	(192)	(175)	(253)	(231)
Proceeds from exercise of stock options	1,458	—	1,458	—
Purchase of treasury stock	(1,389)	(464)	(1,396)	(466)
Net cash used in financing activities	(2,686)	(751)	(19,754)	(22,432)
Net increase (decrease) in cash and cash equivalents	(8,685)	(24,516)	12,393	(6,669)

Cash and cash equivalents, beginning of period	93,547	96,985	72,469	79,138
Cash and cash equivalents, end of period	$84,862	$72,469	$84,862	$72,469
Supplemental disclosures of cash flow information:				
Cash paid during the period:				
Interest paid	$56	$436	$202	$991
Taxes paid	598	139	758	139
Non-cash investing and financing activities:				
Fixed assets, including internal-use software and website development, costs financed through accounts payable and accrued liabilities	$89	$581	$10	$278
Equipment acquired under capital lease obligations	2,563	—	2,563	—

See accompanying notes to consolidated financial statements.

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Overstock.com, Inc.
Notes to Unaudited Consolidated Financial Statements

1. BASIS OF PRESENTATION

As used herein, “Overstock,” “Overstock.com,” “O.co,” “we,” “our” and similar terms include Overstock.com, Inc. and its subsidiaries, unless the context indicates otherwise. We have prepared the accompanying unaudited consolidated financial statements pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”) regarding interim financial reporting. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements and should be read in conjunction with Management’s Discussion and Analysis of Financial Condition and Results of Operations and our audited annual consolidated financial statements and related notes included in our Annual Report on Form 10-K for the year ended December 31, 2012. The accompanying unaudited consolidated financial statements reflect all adjustments, consisting only of normal recurring adjustments, which are, in our opinion, necessary for a fair presentation of results for the interim periods presented. Preparing financial statements requires us to make estimates and assumptions that affect the amounts that are reported in the consolidated financial statements and accompanying disclosures. Although these estimates are based on our best knowledge of current events and actions that we may undertake in the future, actual results may be different from the estimates. The results of operations for the three and nine months ended September 30, 2013 are not necessarily indicative of the results to be expected for any future period or the full fiscal year.

2. ACCOUNTING POLICIES

Principles of consolidation

The accompanying consolidated financial statements include our accounts and the accounts of our wholly-owned subsidiaries. All intercompany account balances and transactions have been eliminated in consolidation.

Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires estimates and assumptions that affect the reported amounts of assets and liabilities, revenues and expenses, and related disclosures of contingent liabilities in the consolidated financial statements and accompanying notes. Estimates are used for, but not limited to, investment valuation, receivables valuation, revenue recognition, sales returns, incentive discount offers, inventory valuation, depreciable lives of fixed assets and internally-developed software, goodwill valuation, intangible valuation, income taxes, stock-based compensation, performance-based compensation, restructuring liabilities and contingencies. Actual results could differ materially from those estimates.

Cash equivalents

We classify all highly liquid instruments, including money market funds with a remaining maturity of three months or less at the time of purchase, as cash equivalents. Cash equivalents were $58.1 million and $76.2 million at September 30, 2013 and December 31, 2012, respectively.

Restricted cash

We consider cash that is legally restricted and cash that is held as a compensating balance for letter of credit arrangements as restricted cash. Restricted cash was $1.8 million and $1.9 million at September 30, 2013 and December 31, 2012, respectively.

Fair value of financial instruments

Our financial instruments, including cash, cash equivalents, restricted cash, accounts receivable, accounts payable and accrued liabilities are carried at cost, which approximates their fair value because of the short-term maturity of these instruments.

We account for our assets and liabilities using a hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources,

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while unobservable inputs reflect our market assumptions. These two types of inputs have created the following fair-value hierarchy:

- Level 1—Quoted prices for identical instruments in active markets;
- Level 2—Quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-derived valuations in which all significant inputs and significant value drivers are observable in active markets; and
- Level 3—Valuations derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable.

This hierarchy requires us to minimize the use of unobservable inputs and to use observable market data, if available, when determining fair value.

The fair value of these financial instruments was determined using the following levels of inputs as of September 30, 2013 (in thousands):

	Fair Value Measurements at September 30, 2013:			
	Total	Level 1	Level 2	Level 3
Assets:				
Cash equivalents - Money market mutual funds	$58,078	$58,078	$—	$—
Trading securities held in a “rabbi trust” (1)	110	110	—	—
Total assets	$58,188	$58,188	$—	$—
Liabilities:				
Deferred compensation accrual “rabbi trust” (2)	$240	$240	$—	$—
Total liabilities	$240	$240	$—	$—

The fair value of these financial instruments was determined using the following levels of inputs as of December 31, 2012 (in thousands):

	Fair Value Measurements at December 31, 2012:			
	Total	Level 1	Level 2	Level 3
Assets:				
Cash equivalents - Money market mutual funds	$76,248	$76,248	$—	$—
Trading securities held in a “rabbi trust” (1)	264	264	—	—
Total assets	$76,512	$76,512	$—	$—
Liabilities:				
Deferred compensation accrual “rabbi trust” (2)	$266	$266	$—	$—
Restructuring (3)	65	—	—	65
Total liabilities	$331	$266	$—	$65

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(1) — Trading securities held in a rabbi trust are included in Other current and long-term assets in the consolidated balance sheets.

(2) — Non qualified deferred compensation in a rabbi trust is included in Accrued liabilities and Other long-term liabilities in the consolidated balance sheets.

(3) — The fair value was determined based on the income approach, in which we used internal cash flow projections over the life of the underlying lease agreements discounted based on a credit adjusted risk-free rate of return. See the roll forward related to the restructuring accrual at Note 3—Restructuring Expense.

Restricted investments

We have a Non Qualified Deferred Compensation Plan (the “NQDC Plan”) for senior management. Deferred compensation amounts are invested in mutual funds held in a “rabbi trust” and are restricted for payment to the participants of the NQDC Plan. We account for our investments held in the trust in accordance with Accounting Standards Codification

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(“ASC”) No. 320 “Investments — Debt and Equity Securities”. The investments held in the trust are classified as trading securities. The fair value of the investments held in the trust totaled $110,000 at September 30, 2013 and are included in Other current and long-term assets in the consolidated balance sheets. Our gains and losses on these investments were immaterial for the three and nine months ended September 30, 2013 and 2012.

Accounts receivable

Accounts receivable consist primarily of trade amounts due from customers and from uncleared credit card transactions at period end. Accounts receivable are recorded at invoiced amounts and do not bear interest.

Allowance for doubtful accounts

From time to time, we grant credit to some of our business customers on normal credit terms (typically 30 days). We perform credit evaluations of our business customers’ financial condition and payment history and maintain an allowance for doubtful accounts receivable based upon our historical collection experience and expected collectability of accounts receivable. The allowance for doubtful accounts receivable was $160,000 and $797,000 at September 30, 2013 and December 31, 2012, respectively. The decrease in the allowance for doubtful accounts was primarily due to write-offs of accounts receivable during the nine months ended September 30, 2013, which had no effect on results of operations for the period as the items had been previously reserved.

Concentration of credit risk

Cash equivalents include short-term, highly liquid instruments with maturities at date of purchase of three months or less. At September 30, 2013 and December 31, 2012, two banks held the majority of our cash and cash equivalents. We do not believe that, as a result of this concentration, we are subject to any unusual financial risk beyond the normal risk associated with commercial banking relationships.

Financial instruments that potentially subject us to significant concentrations of credit risk consist primarily of cash equivalents and receivables. We invest our cash primarily in money market securities which are uninsured.

Our accounts receivable are derived primarily from revenue earned from customers located in the United States. We maintain an allowance for doubtful accounts based upon the expected collectability of accounts receivable.

Valuation of inventories

Inventories, consisting of merchandise purchased for resale, are accounted for using a standard costing system which approximates the first-in-first-out (“FIFO”) method of accounting, and are valued at the lower of cost or market. We write down our inventory for estimated obsolescence and to lower of cost or market value based upon assumptions about future demand and market conditions. If actual market conditions are less favorable than those projected by management, additional inventory write-downs may be required. Once established, the original cost of the inventory less the related inventory allowance represents the new cost basis of such products. Reversal of the allowance is recognized only when the related inventory has been sold or scrapped.

Prepaid inventories, net

Prepaid inventories represent inventories paid for in advance of receipt. Prepaid inventories were $1.9 million and $1.9 million at September 30, 2013 and December 31, 2012, respectively.

Prepaids and other assets

Prepaids and other assets represent expenses paid prior to receipt of the related goods or services, including advertising, license fees, maintenance, packaging, insurance, and other miscellaneous costs. Total prepaids and other assets were $13.1 million at September 30, 2013 and $12.9 million, including precious metals of $3.1 million, at December 31, 2012.

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Fixed assets

Fixed assets, which include assets such as technology infrastructure, internal-use software, website development, furniture and fixtures and leasehold improvements, are recorded at cost and depreciated using the straight-line method over the estimated useful lives of the related assets or the term of the related capital lease, whichever is shorter, as follows:

	Life (years)
Computer software	2-4
Computer hardware	3-4
Furniture and equipment	3-5

Leasehold improvements are amortized over the shorter of the term of the related leases or estimated useful lives.

Depreciation and amortization expense is classified within the corresponding operating expense categories on the consolidated statements of income as follows (in thousands):

	Three months ended September 30,		Nine months ended September 30,	
	2013	2012	2013	2012
Cost of goods sold - direct	$87	$123	$292	$350
Technology	2,937	3,371	9,595	10,570
General and administrative	283	345	946	1,015
Total depreciation and amortization, including internal-use software and website development	$3,307	$3,839	$10,833	$11,935

Internal-use software and website development

Included in fixed assets is the capitalized cost of internal-use software and website development, including software used to upgrade and enhance our Website and processes supporting our business. We capitalize costs incurred during the application development stage of internal-use software and amortize these costs over the estimated useful life of two to three years. Costs incurred related to design or maintenance of internal-use software are expensed as incurred.

During the three months ended September 30, 2013 and 2012, we capitalized $3.3 million and $3.0 million, respectively, of costs associated with internal-use software and website development, both developed internally and acquired externally. Amortization of costs associated with internal-use software and website development was $1.8 million and $2.0 million for those respective periods. During the nine months ended September 30, 2013 and 2012, we capitalized $8.1 million and $6.8 million, respectively, of such costs and had amortization of $5.9 million and $6.3 million for those respective periods.

Leases

We account for lease agreements as either operating or capital leases depending on certain defined criteria. In certain of our lease agreements, we receive rent holidays and other incentives. We recognize lease costs on a straight-line basis without regard to deferred payment terms, such as rent holidays, that defer the commencement date of required payments. Additionally, tenant improvement allowances are amortized as a reduction in rent expense over the term of the lease. Leasehold improvements are capitalized at cost and amortized over the lesser of their expected useful life or the life of the lease, without assuming renewal features, if any, are exercised.

Treasury stock

We account for treasury stock under the cost method and include treasury stock as a component of stockholders' equity.

Other long-term assets

Other long-term assets consist primarily of long-term prepaid expenses.

Impairment of long-lived assets

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We review property and equipment and other long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset group may not be recoverable. Recoverability is measured by comparison of the assets' carrying amount to future undiscounted net cash flows the asset group is expected to generate. Cash flow forecasts are based on trends of historical performance and management's estimate of future performance, giving consideration to existing and anticipated competitive and economic conditions. If such asset group is considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds their fair values. There were no impairments to long-lived assets recorded during the three months ended September 30, 2013 and the year ended December 31, 2012.

Precious Metals

Our investments in precious metals were $8.6 million at September 30, 2013. At December 31, 2012, our investments in precious metals were $3.1 million and were included in Prepaids and other assets in our Consolidated Balance Sheets. At September 30, 2013 these investments were comprised of $4.5 million in gold and $4.1 million in silver and are stored at an off-site secure facility. Because these assets consist of actual precious metals, rather than financial instruments, we account for them as a cost method investment initially recorded at cost (including transaction fees) and then adjusted to the lower of cost of market based on an average unit cost. On an interim basis, we recognize decreases in the value of these assets caused by market declines. Subsequent increases in the value of these assets through market price recoveries during the same fiscal year are recognized in the later interim period, but may not exceed the total previously recognized decreases in value during the same year. Gains or losses resulting from changes in the value of our precious metal assets are recorded in Other income, net in our Consolidated Statements of Income and Comprehensive Income. Losses on investments in precious metals were $93,000 and $475,000 for the three and nine months ended September 30, 2013, respectively. There were no losses on investments in precious metals for the three and nine months ended September 30, 2012.

Goodwill

Goodwill represents the excess of the purchase price paid over the fair value of the tangible net assets acquired in business combinations.

Goodwill is not amortized but is tested for impairment at least annually. When evaluating whether goodwill is impaired, we make a qualitative assessment to determine if it is more likely than not that its fair value is less than its carrying amount. If the qualitative assessment determines that it is more likely than not that its fair value is less than its carrying amount, we compare the fair value of the reporting unit to which the goodwill is assigned to its carrying amount. If the carrying amount exceeds its fair value, then the amount of the impairment loss must be measured. The impairment loss, if any, is calculated by comparing the implied fair value of the goodwill to its carrying amount. In calculating the implied fair value of goodwill, the fair value of the reporting unit is allocated to the other assets and liabilities within the reporting unit based on estimated fair value. The excess of the fair value of a reporting unit over the amount allocated to its other assets and liabilities is the implied fair value of goodwill. An impairment loss is recognized when the carrying amount of goodwill exceeds its implied fair value.

In accordance with this guidance, we test for impairment of goodwill in the fourth quarter or when we deem that a triggering event has occurred. Goodwill totaled $2.8 million at September 30, 2013 and December 31, 2012. There were no impairments to goodwill recorded during the three months ended September 30, 2013 or the year ended December 31, 2012.

Revenue recognition

We derive our revenue primarily from direct revenue and fulfillment partner revenue from merchandise sales. We also earn revenue from advertising on our shopping and other pages. We have organized our operations into two principal segments based on the primary source of revenue: direct revenue and fulfillment partner revenue (see Note 8—Business Segments).

Revenue is recognized when the following revenue recognition criteria are met: (1) persuasive evidence of an arrangement exists; (2) delivery has occurred or the service has been provided; (3) the selling price or fee revenue earned is fixed or determinable; and (4) collection of the resulting receivable is reasonably assured. Revenue related to merchandise sales is recognized upon delivery to our customers. As we ship high volumes of packages through multiple carriers, it is not practical for us to track the actual delivery date of each shipment. Therefore, we use estimates to determine which shipments are delivered and, therefore, recognized as revenue at the end of the period. Our delivery date estimates are based on average shipping transit times, which are calculated using the following factors: (i) the type of shipping carrier (as carriers have different in-transit times); (ii) the fulfillment source (either our warehouses or those of our fulfillment partners); (iii) the

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delivery destination; and (iv) actual transit time experience, which shows that delivery date is typically one to eight business days from the date of shipment. We review and update our estimates on a quarterly basis based on our actual transit time experience. However, actual shipping times may differ from our estimates.

We evaluate the criteria outlined in ASC Topic 605-45, Principal Agent Considerations, in determining whether it is appropriate to record the gross amount of product sales and related costs or the net amount earned as commissions. When we are the primary obligor in a transaction, are subject to inventory risk, have latitude in establishing prices and selecting suppliers, or have several but not all of these indicators, revenue is recorded gross. If we are not the primary obligor in the transaction and amounts earned are determined using a fixed percentage, revenue is recorded on a net basis. Currently, the majority of both direct revenue and fulfillment partner revenue is recorded on a gross basis, as we are the primary obligor. We present revenue net of sales taxes.

We periodically provide incentive offers to our customers to encourage purchases. Such offers include current discount offers, such as percentage discounts off current purchases and other similar offers, which, when used by customers, are treated as a reduction of revenue.

Based upon our historical experience, revenue typically increases during the fourth quarter because of the holiday retail season.

Direct revenue

Direct revenue is derived from merchandise sales to individual consumers and businesses that are fulfilled from our warehouses. Direct revenue comes from merchandise sales that occur primarily through our Website, but may also occur through offline and other channels.

Fulfillment partner revenue

Fulfillment partner revenue is derived from merchandise sales through our Website which fulfillment partners ship directly to consumers and businesses from warehouses maintained by our fulfillment partners.

Consignment

We offer a consignment service to suppliers where the suppliers' merchandise is stored in and shipped from our warehouses. We pay the consignment supplier upon shipment of the consigned merchandise to the consumer. Revenue from consignment service business was less than 1% of total net revenues for the three and nine months ended September 30, 2013 and 2012, and is included in fulfillment partner segment on a gross basis.

International business

At September 30, 2013, we were offering products to customers in over 100 countries and non-U.S. territories. We do not have sales operations outside the United States, and are using a U.S. based third party to provide logistics and fulfillment for all international orders. Revenue generated from our international business is included in either direct or fulfillment partner revenue, depending on whether the product is shipped from our warehouses or from a fulfillment partner. International sales were less than 1% of total net revenues for the three and nine months ended September 30, 2013 and 2012.

Ecommerce marketplace channels

During 2012, we began offering some of our products for sale in online marketplaces of other Internet retailers' websites, which allows us to reach a broader potential customer base. Under the terms of our agreements with these ecommerce marketplace retailers, the retailers typically earn a fee that is a percentage of the selling price of the orders they send us. Revenue generated from these ecommerce marketplace channels is included in either direct or fulfillment partner revenue, on a gross basis, depending on whether the product is shipped from our warehouses or from a fulfillment partner. Ecommerce marketplace channels were approximately 2.1% and less than 1% of our total net revenues for the three months ended September 30, 2013 and 2012, respectively, and approximately 2.5% and less than 1% of our total net revenues for the nine months ended September 30, 2013 and 2012, respectively.

Other businesses

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We operate an online site for listing cars for sale as a part of our Website. The cars listing service allows dealers to list vehicles for sale and allows buyers to review vehicle descriptions and post offers to purchase, and provides the means for prospective purchasers to contact sellers for further information and negotiations on the purchase of an advertised vehicle. Revenue from the cars listing business is included in the fulfillment partner segment on a net basis. Revenue from our other businesses is less than 1% of total net revenues for the three and nine months ended September 30, 2013 and 2012.

Club O loyalty program

We have a customer loyalty program called Club O for which we sell annual memberships. We record membership fees as deferred revenue and we recognize revenue ratably over the membership period. The Club O loyalty program allows members to earn reward dollars for qualifying purchases made on our Website. We also have a co-branded credit card program (see “Co-branded credit card revenue” below for more information). Co-branded cardholders are also Club O members and earn additional reward dollars for purchases made on our Website, and from other merchants. Reward dollars earned may be redeemed on future purchases made through our Website. Club O reward dollars expire 90 days after the customer’s Club O membership expires. We account for these transactions as multiple element arrangements and allocate revenue to the elements using their relative fair values. We include the value of reward dollars earned in deferred revenue and we record it as a reduction of revenue at the time the reward dollars are earned.

We recognize revenue for Club O reward dollars when customers redeem their reward dollars as part of a purchase at our Website. We recognize other income when Club O reward dollars expire or the likelihood of reward dollars being redeemed by a customer is remote (“reward dollar breakage”). Reward dollar breakage is currently recognized when the reward dollars expire.

In instances where customers receive free Club O reward dollars not associated with any purchases, we account for these transactions as sales incentives such as coupons and record a reduction of revenue at the time the reward dollars are redeemed.

Co-branded credit card program

We have a co-branded credit card agreement with a commercial bank for the issuance of credit cards bearing the Overstock.com brand, under which the bank pays us fees for new accounts and for customer usage of the cards. The agreement also provides for a customer loyalty program offering reward points that customers will accrue from card usage and can use to make purchases on our Website (see “Club O loyalty program” above for more information). New account fees are recognized as revenue on a straight-line basis over the remaining life of the credit card relationship which runs through April 2015. Credit card usage fees are recognized as revenues as actual credit card usage occurs. Revenues from new account and credit card usage fees were less than 1% of total net revenues for all periods presented.

Deferred revenue

Customer orders are recorded as deferred revenue prior to delivery of products or services ordered. We record amounts received for Club O membership fees as deferred revenue and we recognize it ratably over the membership period. We record Club O reward dollars earned from purchases as deferred revenue at the time they are earned and we recognize it as revenue upon redemption. If reward dollars are not redeemed, we recognize other income upon expiration. In addition, we sell gift cards and record related deferred revenue at the time of the sale. We sell gift cards without expiration dates and we recognize revenue from a gift card upon redemption of the gift card. If a gift card is not redeemed, we recognize other income when the likelihood of its redemption becomes remote based on our historical redemption experience. We consider the likelihood of redemption to be remote after 36 months.

Sales returns allowance

We inspect returned items when they arrive at our processing facility. We refund the full cost of the merchandise returned and all original shipping charges if the returned item is defective or we or our fulfillment partners have made an error, such as shipping the wrong product.

If the return is not a result of a product defect or a fulfillment error and the customer initiates a return of an unopened item within 30 days of delivery, for most products we refund the full cost of the merchandise minus the original shipping charge and actual return shipping fees. However, we reduce refunds for returns initiated more than 30 days after delivery or that are received at our returns processing facility more than 45 days after initial delivery.

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If our customer returns an item that has been opened or shows signs of wear, we issue a partial refund minus the original shipping charge and actual return shipping fees.

Revenue is recorded net of estimated returns. We record an allowance for returns based on current period revenues and historical returns experience. We analyze actual historical returns, current economic trends and changes in order volume and acceptance of our products when evaluating the adequacy of the sales returns allowance in any accounting period.

The allowance for returns was $7.3 million and $10.6 million at September 30, 2013 and December 31, 2012 respectively. The decrease in allowance for returns at September 30, 2013 compared to December 31, 2012 is primarily due to decreased revenues mostly due to seasonality.

Credit card chargeback allowance

Revenue is recorded net of credit card chargebacks. We maintain an allowance for credit card chargebacks based on current period revenues and historical chargeback experience. The allowance for chargebacks was $48,000 and $182,000 at September 30, 2013 and December 31, 2012, respectively.

Cost of goods sold

Cost of goods sold includes product costs, warehousing costs, outbound shipping costs, handling and fulfillment costs, customer service costs and credit card fees, and is recorded in the same period in which related revenues have been recorded. Cost of goods sold, including product cost and other costs and fulfillment and related costs are as follows (in thousands):

	Three months ended September 30,						Nine months ended September 30,					
	2013			2012			2013			2012		
Total revenue, net	$301,426	100	%	$255,352	100	%	$906,624	100	%	$757,255	100	%
Cost of goods sold												
Product costs and other cost of goods sold	228,963	76	%	196,522	77	%	690,563	76	%	582,436	77	%
Fulfillment and related costs	13,313	4	%	12,288	5	%	40,136	4	%	37,600	5	%
Total cost of goods sold	242,276	80	%	208,810	82	%	730,699	81	%	620,036	82	%
Gross profit	$59,150	20	%	$46,542	18	%	$175,925	19	%	$137,219	18	%

Advertising expense

We expense the costs of producing advertisements the first time the advertising takes place and expense the cost of communicating advertising in the period during which the advertising space or airtime is used. Internet advertising expenses are recognized as incurred based on the terms of the individual agreements, which are generally: 1) a commission for traffic driven to the Website that generates a sale or 2) a referral fee based on the number of clicks on keywords or links to our Website generated during a given period. Advertising expense is included in sales and marketing expenses and totaled $20.2 million and $12.8 million during the three months ended September 30, 2013 and 2012, respectively. For the nine months ended September 30, 2013 and 2012, advertising expenses totaled $53.5 million and $37.0 million, respectively. Prepaid advertising (included in Prepaids and other assets in the accompanying consolidated balance sheets) was $2.1 million and $1.2 million at September 30, 2013 and December 31, 2012, respectively.

Stock-based compensation

We measure compensation expense for all outstanding unvested share-based awards at fair value on date of grant and recognize compensation expense over the service period for awards expected to vest on a straight line basis. The estimation of stock awards that will ultimately vest requires judgment, and to the extent actual results differ from estimates, such amounts will be recorded as an adjustment in the period estimates are revised. We consider many factors when estimating expected forfeitures, including types of awards, and historical experience. Actual results may differ substantially from these estimates (see Note 7—Stock-Based Awards).

Loss contingencies

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In the normal course of business, we are involved in legal proceedings and other potential loss contingencies. We accrue a liability for such matters when it is probable that a loss has been incurred and the amount can be reasonably estimated. When only a range of probable loss can be estimated, the most probable amount in the range is accrued. If no amount within this range is a better estimate than any other amount within the range, the minimum amount in the range is accrued. We expense legal fees as incurred.

Restructuring

Restructuring expenses are primarily comprised of lease termination costs. ASC Topic 420, Accounting for Costs Associated with Exit or Disposal Activities, requires that when an entity ceases using a property that is leased under an operating lease before the end of the contractual term, the termination costs should be recognized and measured at fair value when the entity ceases using the facility. Key assumptions in determining the restructuring expenses include the terms that may be negotiated to exit certain contractual obligations (see Note 3—Restructuring Expense).

Income taxes

Our tax provision from income taxes for interim periods is determined using an estimate of our annual effective tax rate, adjusted for discrete items, if any, that are taken into account in the relevant period. Each quarter we update our estimate of the annual effective tax rate, and if our estimated tax rate changes, we make a cumulative adjustment.

At September 30, 2013 and December 31, 2012, we have a full valuation allowance against our deferred tax assets, net of expected reversals of existing deferred tax liabilities, as we believe it is more likely than not that these benefits will not be realized. Significant judgment is required in making this assessment, and it is very difficult to predict when our assessment may conclude that the remaining portion of the deferred tax assets is realizable. To the extent that we remain profitable for the foreseeable future, the full or partial release of the valuation allowance could occur in the near term.

We have tax deductions from stock-based compensation that exceed the stock-based compensation recorded for such instruments. To the extent such excess tax benefits are ultimately realized, they will increase shareholders' equity. We utilize the with-and-without approach in determining if and when such excess tax benefits are realized, and under this approach excess tax benefits related to stock based compensation are the last to be realized.

Earnings per share

Basic earnings per share is computed by dividing net income attributable to common shares by the weighted average number of common shares outstanding during the period. Diluted earnings per share is computed by dividing net income attributable to common shares for the period by the weighted average number of common and potential common shares outstanding during the period. Potential common shares, comprising incremental common shares issuable upon the exercise of stock options and restricted stock awards are included in the calculation of diluted earnings per common share to the extent such shares are dilutive.

The following table sets forth the computation of basic and diluted net income per common share for the periods indicated (in thousands, except per share data):

	Three months ended September 30,		Nine months ended September 30,	
	2013	2012	2013	2012
Net income attributable to common shares	$3,533	$2,693	$14,928	$5,882
Net income per common share—basic:				

Net income attributable to common shares—basic	0.15	0.11	0.63	0.25
Weighted average common shares outstanding—basic	23,766	23,447	23,692	23,382
Effect of dilutive securities:				
Stock options and restricted stock awards	680	307	605	129
Weighted average common shares outstanding—diluted	24,446	23,754	24,297	23,511
Net income attributable to common shares—diluted	$0.14	$0.11	$0.61	$0.25

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The following shares were excluded from the calculation of diluted shares outstanding as their effect would have been anti-dilutive (in thousands):

	Three months ended September 30,		Nine months ended September 30,	
	2013	2012	2013	2012
Stock options and restricted stock units	6	541	38	546

3. RESTRUCTURING EXPENSE

During the fourth quarter of 2006, we began a facilities consolidation and restructuring program designed to reduce the overall expense structure in an effort to improve future operating performance. The facilities consolidation and restructuring program was substantially completed by the end of the second quarter of 2007.

Restructuring liabilities along with charges (credits) to expense and payments associated with the facilities consolidation and restructuring program are as follows (in thousands):

	Balance at 12/31/2012	Accretion Expense	Net Cash Payments	Adjustments	Balance at 9/30/2013
Lease and contract termination costs	$1,197	$55	$(268)	$(471)	$513

There were no lease termination costs reversed during the three months ended September 30, 2013. We reversed $471,000 of lease termination costs during the nine months ended September 30, 2013 primarily due to changes in our restructuring accrual as a result of our reoccupation of a portion of formerly restructured office space. We reversed $45,000 and incurred $53,000 of lease termination costs during the three months and nine months ended September 30, 2012, respectively, due to changes in the estimate of sublease income as a result of our entering into a revised agreement with a sub-lessee and ceasing the use of some of our office facilities.

4. BORROWINGS

U.S. Bank Financing Agreements

On December 26, 2012, we entered into a $3.0 million cash-collateralized line of credit agreement (the “Credit Agreement”) with U.S. Bank National Association (“U.S. Bank”) for the issuance of letters of credit. Advances under the Credit Agreement bear interest at one-month LIBOR plus 1.0%. The Credit Agreement matures on December 31, 2013. Amounts outstanding under the Credit Agreement were zero at September 30, 2013 and December 31, 2012.

Until December 31, 2012, we were party to a Financing Agreement with U.S. Bank (the “Financing Agreement”). In November 2012, we repaid all amounts outstanding under the Financing Agreement. The Financing Agreement expired in accordance with its terms on December 31, 2012. The maximum credit potentially available under the revolving facility was $20 million. Our obligations under the Financing Agreement and all related agreements were secured by all or substantially all of our assets, excluding our interest in certain litigation.

At September 30, 2013 and December 31, 2012, letters of credit totaling $1.8 million and $1.8 million, respectively, were issued on our behalf collateralized by compensating cash balances held at U.S. Bank, which are included in Restricted cash in the accompanying consolidated balance sheets.

U.S. Bank Commercial Purchasing Card Agreement

We have a commercial purchasing card (the “Purchasing Card”) agreement with U.S. Bank. We use the Purchasing Card for business purpose purchasing and must pay it in full each month. At September 30, 2013, $865,000 was outstanding and $4.1 million was available under the Purchasing Card. At December 31, 2012, $3.9 million was outstanding and $1.1 million was available under the Purchasing Card.

Capital leases

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In March 2013, we entered into a capital lease arrangement for $2.6 million of computer equipment that will expire in 2017. We prepaid the entire $2.6 million shortly after entering into the agreement in order to obtain discounted pricing. As such, we have no future payment obligations under capital leases at September 30, 2013.

Fixed assets included assets under capital leases of $4.2 million and $1.7 million and accumulated depreciation related to assets under capital leases of $1.9 million and $1.7 million, at September 30, 2013 and December 31, 2012, respectively. Depreciation expense of assets recorded under capital leases was $161,000 and $1,000, for the three months ended September 30, 2013 and 2012, respectively and $268,000 and $221,000, for the nine months ended September 30, 2013 and 2012, respectively.

5. COMMITMENTS AND CONTINGENCIES

Summary of future minimum lease payments for all operating leases

Minimum future payments under all operating leases as of September 30, 2013, are as follows (in thousands):

Payments due by period	
2013 (remainder)	$2,658
2014	10,403
2015	8,161
2016	4,663
2017	3,922
Thereafter	36,263
	$66,070

Rental expense for operating leases totaled $2.6 million and $2.1 million for the three months ended September 30, 2013 and 2012, respectively and $7.2 million and $6.5 million for the nine months ended September 30, 2013 and 2012, respectively. Estimated sublease income of $29,000 is anticipated to be received in the next 12 months.

On May 13, 2013 we entered into a new operating lease for a warehouse facility that we have leased since September 2008. This lease extends the term of occupancy to August 31, 2026. The minimum future payments due under this new operating lease are included in the summary of future minimum lease payments for all operating leases in the table above.

Legal Proceedings

From time to time, we are involved in litigation concerning consumer protection, employment, intellectual property and other commercial matters related to the conduct and operation of our business and the sale of products on our Website. In connection with such litigation, we may be subject to significant damages. In some instances other parties may have contractual indemnification obligations to us. However, such contractual obligations may prove unenforceable or non-collectible, and in the event we cannot enforce or collect on indemnification obligations, we may bear the full responsibility for damages, fees and costs resulting from such litigation. We may also be subject to penalties and equitable remedies that could force us to alter important business practices. Such litigation could be costly and time consuming and could divert or distract our management and key personnel from our business operations. Due to the uncertainty of litigation and depending on the amount and the timing, an unfavorable resolution of some or all of these matters could materially affect our business, results of operations, financial position, or cash flows.

On February 2, 2007, along with five shareholder plaintiffs, we filed a lawsuit in the Superior Court of California, County of San Francisco against Morgan Stanley & Co. Incorporated, Goldman Sachs & Co., Bear Stearns Companies, Inc., Bank of America Securities LLC, Bank of New York, Citigroup Inc., Credit Suisse (USA) Inc., Deutsche Bank Securities, Inc., Merrill Lynch, Pierce, Fenner & Smith, Inc., and UBS Financial Services, Inc., and later amended the complaint to add Lehman Brothers Holdings Inc. as a defendant. The suit alleged that the defendants, who controlled over 80% of the prime brokerage market, participated in an illegal stock market manipulation scheme and that the defendants had no intention of covering short sell orders with borrowed stock, as they are required to do, causing what are referred to as "fails to deliver" and that the defendants' actions caused and continued to cause dramatic declines in the share price of our stock and that the amount of "fails to deliver" often exceeded our entire supply of outstanding shares. The suit accused the defendants of violations of California securities laws and common law and violations of California's Unfair Business Practices Act. After it filed for bankruptcy on

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September 2008, we elected not to pursue our claims against Lehman Brothers Holdings. On July 23, 2009, the court sustained defendants' demurrer to our amended causes of action for conversion and trespass to chattels. On December 15, 2010, we and the other plaintiffs in the case entered into a settlement agreement with certain of the defendants requiring these defendants to pay in the aggregate $4.5 million to plaintiffs. Other terms of settlement are confidential. At that time, remaining defendants in the suit were Goldman Sachs Group, Inc., Goldman Sachs & Co., Goldman Sachs Execution & Clearing L.P., ("Goldman Defendants") Merrill Lynch, Pierce, Fenner & Smith, Inc., Merrill Lynch Professional Clearing Corporation ("Merrill Lynch Defendants), and Bank of America Securities LLC. On December 15, 2010, we filed a motion to amend our complaint against the Goldman and Merrill Lynch Defendants to add a cause of action based on the New Jersey Racketeer Influenced and Corrupt Organization (RICO) Act. Defendants challenged the RICO claim by demurrer and eventually the court sustained the demurrer. We thereafter entered a settlement agreement with Bank of America Securities LLC, the terms of which are confidential, and have dismissed the action as to that defendant. On August 19, 2011, the remaining defendants filed a motion for summary judgment. On January 10, 2012, the court granted the motion for summary judgment as to all remaining defendants and the judgment has been entered. We have appealed that decision and each side has appealed the trial court's decisions regarding sealing of certain records in the case. The defendants applied to the court for reimbursement from us of their allowable court costs in the collective amount of $2.4 million. We challenged the application, and the court reduced the amount to $689,471, which will be payable only if we do not succeed on our appeal of the summary judgment. The briefing of the appeals on both the records sealing and summary judgment is complete. The Court of Appeal has not set a date for oral argument. The nature of the loss contingencies relating to any court costs ordered against us are described above.

On May 30, 2008, we filed a complaint in New York state court against the New York State Department of Taxation and Finance, its Commissioner, the State of New York and its governor, alleging that a New York state tax law is unconstitutional. The effect of the New York law is to require Internet sellers to collect and remit New York sales taxes on their New York sales even if the seller has no New York tax "nexus" other than with New York based independent contractors who are Internet advertising affiliates. The complaint asks for the court to declare the law unconstitutional and enjoin its application to us. New York filed a motion to dismiss. We responded to the motion and filed a motion for summary judgment, and both motions were heard simultaneously. On January 12, 2009, the court granted New York's motion to dismiss and denied our motion for summary judgment. We appealed the decision, and the New York Appellate Division upheld part of the lower court's ruling rejecting our claims that the law is unconstitutional on its face, but remanded our claims that the law is unconstitutional as applied, for further discovery and proceedings in the lower court. We filed with the New York State Court of Appeals a motion of leave to appeal the portions of the decision upholding the lower court's ruling. On March 15, 2011, the Appellate Division of the New York State Court of Appeals denied our motion for leave to appeal to the New York State Court of Appeals. We determined not to pursue in the trial our claims that the law is unconstitutional as applied and proceeded with an appeal to the New York State Court of Appeals of the Appellate Division's ruling on our claim that the statute is unconstitutional on its face. On March 28, 2013, New York State Court of Appeals denied the appeal. We have petitioned the Supreme Court of the United States for a writ of certiorari. The Supreme Court has not ruled on our petition.

On August 12, 2008, we along with seven other defendants, were sued in the United States District Court for the Northern District of California, by Sean Lane, and seventeen other individuals, on their own behalf and for others similarly in a class action suit, alleging violations of the Electronic Communications Privacy Act, Computer Fraud and Abuse Act, Video Privacy Protection Act, and California's Consumer Legal Remedies Act and Computer Crime Law. The complaint relates to our use of a product known as Facebook Beacon, created and provided to us by Facebook, Inc. Facebook Beacon provided the means for Facebook users to share purchasing data among their Facebook friends. The parties extended by agreement the time for defendants' answer, including our answer, and thereafter, the Plaintiff and Facebook proposed a stipulated settlement to the Court for approval, which would resolve the case without requirement of financial contribution from us. On March 17, 2010, over objections lodged by some parties, the Court entered an order accepting settlement. Various parties appealed and on September 20, 2012, the Federal Appeals Court for the 9th Circuit upheld the settlement. Appealing parties petitioned for a rehearing. On February 26, 2013, the Court denied the petition. The appealing parties have petitioned the Supreme Court of the United States for a writ of certiorari. The Supreme Court has not ruled on the petition. The nature of the loss contingencies relating to claims that have been asserted against us are described above.

On November 14, 2008, we filed suit in Ohio state court against the Ohio Tax Commissioner, the Ohio Attorney General and the Governor of Ohio, alleging the Ohio Commercial Activity Tax is unconstitutional. Enacted in 2005, Ohio's Commercial Activity Tax is based on activities in Ohio that contribute to production or gross income for a company whether or not the company has a physical presence in or nexus within the state. Our complaint asked for a judgment declaring the tax unconstitutional and for an injunction preventing any enforcement of the tax. The defendants moved to dismiss the case. On July 28, 2009, the trial court ruled that there was no justiciable controversy in the case, as we had not yet been assessed a tax, and it granted the defendants' motions to dismiss. In September 2009, we received a letter of determination from the Ohio Department of Taxation noting the Department's determination that we are required to register for remitting of the Commercial

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Activity Tax, and owe $612,784 in taxes, interest, and penalties as of June 30, 2009. The Ohio Department of Taxation issued additional estimated assessments of estimated tax, interest and penalties totaling $170,322 as of September 30, 2013. We have filed protests to challenge the Department's Assessments on constitutional grounds and the matter is currently pending before the Ohio Department of Taxation's Legal Division for administrative review and determination. A hearing on these matters was held November 18, 2011. No administrative ruling has been issued following the hearing. We have reached an agreement in principle with the Ohio Department which would require our payment of a diminished amount of the estimated assessments, a reduction in interest and waiver of penalties. We are in the process of formalizing the agreement.

On March 10, 2009, we were sued in a class action filed in the United States District Court, Eastern District of New York. Cynthia Hines, the nominative plaintiff on behalf of herself and others similarly situated, seeks damages under claims for breach of contract, common law fraud and New York consumer fraud laws. The Plaintiff alleges we failed to properly disclose our returns policy to her and that we improperly imposed a "restocking" charge on her return of a vacuum cleaner. We filed a motion to dismiss based upon assertions that our agreement with our customers requires all such actions to be arbitrated in Salt Lake City, Utah. On December 31, 2010, Hines filed an amended complaint. The amended complaint eliminated common law fraud claims and breach of contract claims and added claims for breach of Utah's consumer protection statute and various other state consumer protection statutes. The amended complaint also asked for an injunction. We filed motions to dismiss and to decertify the class. On August 19, 2013, the court granted our motion and later dismissed the case. The time for filing a notice of appeal has passed, thus concluding the case.

On September 23, 2009, SpeedTrack, Inc. sued us along with 27 other defendants in the United States District Court in the Northern District of California. We are alleged to have infringed a patent covering search and categorization software. We believe that certain third party vendors of products and services sold to us are contractually obligated to indemnify us in this action. On November 11, 2009, the parties stipulated to stay all proceedings in the case until resolution of a reexamination of the patent in question, and also until a previously filed infringement action against Wal-Mart Stores, Inc. and other retailers resulted either in judgment or dismissal. Subsequently, the parties agreed to extend the time for defendants' complaint answer until 21 days following a court order to lift the stay to which the parties stipulated. The United States Patent and Trademark Office resolved the reexamination of the patent in question in favor of SpeedTrack, Inc. The case remains stayed, pending the outcome and appeal of the infringement action against Wal-Mart Stores, Inc. and other retailers. On February 22, 2012, the court in the Wal-Mart Stores case granted Wal-Mart Stores' motion for summary judgment of non-infringement. The court also granted Speedtrack's motion for summary judgment on patent validity. Speedtrack is appealing the ruling. It is not known whether the summary judgments granted in the Wal-Mart Stores case will have an effect on the Speedtrack case in which we are named as one of the defendants. The nature of the loss contingencies relating to claims that have been asserted against us are described above. However no estimate of the loss or range of loss can be made. We intend to vigorously defend this action and pursue our indemnification rights with our vendors.

On September 29, 2010, a trustee in bankruptcy filed against us an adversary proceeding in the matter of In re: Petters Company, Inc., a case filed in United States Bankruptcy Court, in the District of Minnesota. The complaint alleges principal causes of action against us under various Bankruptcy Code sections and the Minnesota Fraudulent Transfer Act, to recover damages for alleged transfers of property from the Petters Company occurring prior to the filing of the case initially as a civil receivership in October 2008. The trustee's complaint alleges such transfers occurred in at least one note transaction whereby we transferred at least $2.3 million and received in return transfers totaling at least $2.5 million. The trustee does not specify a date for the transactions; however we believe that any alleged transaction with the Petters Company would have taken place in excess of seven years from the date of the filing of the adversary proceeding. The case is in its early stages. We filed a motion to dismiss on statute of limitations and other grounds. The court consolidated the issues in our motion with issues raised by motion in similar trustee-filed cases having similar allegations and similar theories of recovery. The court has issued three separate orders containing legal rulings on these consolidated legal issues. We understand that the court will apply these rulings to the specific motions to dismiss, including the motion that we filed, at some point following an upcoming status conference in mid-November. While we expect the application of these rulings will limit the allegations asserted against us, we also expect that the judge will allow portions of the case to proceed to the discovery stage. The nature of the loss contingencies relating to claims that have been asserted against us are described above. However, no estimate of the loss or range of loss can be made. We intend to vigorously defend this action.

On November 17, 2010, we were sued in the Superior Court of California, County of Alameda, by District Attorneys for the California Counties of Alameda, Marin, Monterey, Napa, Santa Clara, Shasta and Sonoma County, and the County of Santa Cruz later joined the suit. These district attorneys seek damages and an injunction under claims for violations of California consumer protection laws, alleging we made untrue or misleading statements concerning our pricing, price reductions, sources of products and shipping charges. The complaint asks for damages in the amount of not less than $15 million. We tried the case in early September 2013 before the judge of the court. Both sides are preparing final written arguments. The nature of the loss contingencies relating to claims that have been asserted against us are described above. We intend to vigorously defend this action.

On September 11, 2011, Droplets, Inc. filed suit against us and eight other defendants in the United States District Court in the Eastern District of Texas for infringement of a patent covering strings of programming code downloaded from a server to a client computer. We have answered the complaint. The case is in its discovery stages. The nature of the loss contingencies relating to claims that have been asserted against us are described above. However, no estimate of the loss or range of loss can be made. We intend to vigorously defend this action and pursue our indemnification rights with our vendors.

On September 13, 2011, Select Retrieval, LLC filed suit against us and 79 other defendants in the United States District Court for the District of Delaware for infringement of a patent covering the hierarchical display of interactive links on a webpage. We filed a motion to dismiss which was denied. The case is in its discovery stages. The nature of the loss contingencies relating to claims that have been asserted against us are described above. However, no estimate of the loss or range of loss can be made. We intend to vigorously defend this action and pursue our indemnification rights, if any, with our vendors.

On November 18, 2011, Smartfit Solutions, LLC filed suit against us and 43 other defendants in the United States District Court for the Eastern District of Texas for infringement of a patent covering certain “methods for presenting exercise protocols to a user and evaluating the effectiveness of the same.” We tendered the defense of this action to an indemnitor which accepted the defense. The indemnitor reached a tentative settlement with the Plaintiff at no cost to us, and the case has now been dismissed.

On January 27, 2012, Pragmatus Telecom, LLC filed suit against us in the United States District Court for the District of Delaware for infringement of two patents covering a system for coordinating data and voice communications via customer contact channel changing system using voice over IP and infringement of one patent for coordinating data and voice communications via customer contact channel changing system. We have answered the complaint. We tendered the defense of the case to an indemnitor. The case against us was stayed July 10, 2012, pending resolution of a declaratory judgment action filed by our indemnitor against Pragmatus. The nature of the loss contingencies relating to claims that have been asserted against us are described above. However, no estimate of the loss or range of loss can be made. We intend to vigorously defend this action and pursue our indemnification rights with our vendors.

On March 1, 2012, H-W Technology, L.C. filed suit against us in the United States District Court in the Northern District of Texas for infringement of a patent entitled “Internet Protocol (IP) Phone with Search and Advertising Capability.” We answered the complaint. On January 28, 2013, we filed a motion for summary judgment for invalidity on two claims of the patent. On September 23, 2013, the court granted the motion. We intend to apply to the court for court-ordered reimbursement of our legal fees and costs expended in our defense.

On May 2, 2012, Execware LLC filed suit against us in the United States District Court for the District of Delaware for infringement of a patent entitled: “Integrated Dialog Box for Rapidly Altering Presentation of Parametric Text Data Objects on a Computer Display.” We have answered the complaint. The case is in its discovery stages. The nature of the loss contingencies relating to claims that have been asserted against us are described above. However, no estimate of the loss or range of loss can be made. We intend to vigorously defend this action and pursue our indemnification rights with our vendors.

On July 16, 2012, Digitech Image Technologies, LLC filed against us and 45 other defendants in the United States District Court for the Central District of California for infringement of a patent covering the imaging technology that facilitates prediction of color and location within digital cameras. We tendered defense of the case to an indemnitor which accepted the defense. Following a ruling in our favor, the case was dismissed and in September 2012, Digitech filed a new complaint in the same court on the same infringement claims. In the new action, our indemnitor continues to defend the case and has filed a motion to stay on our behalf, which the Court granted on April 10, 2013. Subsequently, the court granted a motion for summary judgment on invalidity of the patent and entered judgment for us. Digitech has stated it will appeal the decision. The nature of the loss contingencies relating to claims that have been asserted against us are described above. However, no estimate of the loss or range of loss can be made. We intend to cooperate with our indemnitor and vigorously defend this action.

On July 19, 2012, Data Carriers, LLC filed suit against us in the United States District Court for the District of Delaware for infringement of a patent covering the "autocomplete" features of our website. We believe a third party vendor is contractually obligated to indemnify us in this action. We have answered the complaint. The case is in its discovery stages. The nature of the loss contingencies relating to claims that have been asserted against us are described above. However, no estimate

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of the loss or range of loss can be made. We intend to vigorously defend this action and pursue our indemnification rights with our vendors.

On February 11, 2013, RPost Holdings, Inc., RPost Communications Limited, and RMail Limited, filed suit against us in the United States District Court in Eastern District of Texas for infringement of patents covering products and services that verify the delivery and integrity of email messages. We tendered defense of the case to an indemnitor which accepted the defense. We have answered the complaint. The case is in its early stages. The nature of the loss contingencies relating to claims that have been asserted against us are described above. However, no estimate of the loss or range of loss can be made. We intend to vigorously defend this action and pursue our indemnification rights with our vendors.

On April 23, 2013, Eclipse IP, LLC filed suit against us in the United States District Court in Eastern District of Texas for infringement of patents covering "secure notification messaging systems and methods using authentication indicia." We were served with the complaint on May 10, 2013, and have answered the complaint. The case is in its early stages. The nature of the loss contingencies relating to claims that have been asserted against us are described above. However, no estimate of the loss or range of loss can be made. We intend to vigorously defend this action and pursue our indemnification rights with our vendors.

On August 16, 2013, Online News Link LLC, LLC filed suit against us in the United States District Court in District of Delaware for infringement of patents covering data distribution systems that can make downloading data fast and efficient. We are presently examining whether we are indemnified by any vendor. We were served with the complaint on August 19, 2013. The case is in its early stages. The nature of the loss contingencies relating to claims that have been asserted against us are described above. However, no estimate of the loss or range of loss can be made. We intend to vigorously defend this action and pursue any indemnification rights with our vendors.

On August 22, 2013, Guardian Media Technologies LTD filed suit against us in the United States District Court in the Eastern District of Texas for infringement of patents covering parental control features in DVD players and televisions. The suit relates to a prior lawsuit with Guardian filed in 2008 in which we signed a tolling agreement. We are presently examining whether we are indemnified by any vendor in this subsequent suit. We have not answered the complaint. The nature of the loss contingencies relating to claims that have been asserted against us are described above. However, no estimate of the loss or range of loss can be made. We intend to vigorously defend this action and pursue any indemnification rights with our vendors.

On September 30, 2013, Altaf Nazerali filed suit against us in the Supreme Court of British Columbia for vicarious liability for defamation, liable and slander. The suit relates to alleged representations about Nazerali found on the website www.deepcapture.com. The suit alleges that the representations were made by our Chief Executive Officer, Patrick Byrne, and two other employees. We have not answered the complaint. The nature of the loss contingencies relating to claims that have been asserted against us are described above. However, no estimate of the loss or range of loss can be made.

We establish liabilities when a particular contingency is probable and estimable. At September 30, 2013, we have accrued $2.6 million in light of these probable and estimable liabilities. It is reasonably possible that the actual losses may exceed our accrued liabilities. We have other contingencies which are reasonably possible; however, the reasonably possible exposure to losses cannot currently be estimated.

6. INDEMNIFICATIONS AND GUARANTEES

During our normal course of business, we have made certain indemnities, commitments, and guarantees under which we may be required to make payments in relation to certain transactions. These indemnities include, but are not limited to, indemnities to various lessors in connection with facility leases for certain claims arising from such facility or lease, and indemnities to our directors and officers to the maximum extent permitted under the laws of the State of Delaware. The duration of these indemnities, commitments, and guarantees varies, and in certain cases, is indefinite. In addition, the majority of these indemnities, commitments, and guarantees do not provide for any limitation of the maximum potential future payments we could be obligated to make. As such, we are unable to estimate with any reasonableness our potential exposure under these items. We have not recorded any liability for these indemnities, commitments, and guarantees in the accompanying consolidated balance sheets. We do, however, accrue for losses for any known contingent liability, including those that may arise from indemnification provisions, when future payment is both probable and reasonably estimable.

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7. STOCK-BASED AWARDS

We have equity incentive plans that provide for the grant to employees of stock-based awards, including stock options and restricted stock.

Stock-based compensation expense was as follows (in thousands):

	Three months ended September 30,		Nine months ended September 30,	
	2013	2012	2013	2012
Stock options	$—	$—	$—	$3
Restricted stock awards	809	980	2,377	2,621
Total stock-based compensation expense	$809	$980	$2,377	$2,624

Restricted stock awards

During the three and nine months ended September 30, 2013, the Compensation Committee of the Board of Directors approved grants of 2,500 and 275,000 restricted stock awards, respectively, to our officers, board members and employees. The restricted stock awards vest over three years at 40% at the end of the first year, 30% at the end of the second year and 30% at the end of the third year and are subject to the employee's continuing service to us. At September 30, 2013, there were 714,750 unvested restricted stock awards that remained outstanding.

The cost of restricted stock awards is determined using the fair value of our common stock on the date of the grant, and compensation expense is either recognized on a straight line basis over the three-year vesting schedule or on an accelerated schedule when vesting of restricted stock awards exceeds a straight-line basis. The cumulative amount of compensation expense recognized at any point in time is at least equal to the portion of the grant date fair value of the award that is vested at that date. The weighted average grant date fair value of restricted stock awards granted during the three months and nine months ended September 30, 2013 was $33.44 and $16.12, respectively.

The following table summarizes restricted stock award activity during the nine months ended September 30, 2013 (in thousands):

	Nine months ended September 30, 2013	
	Units	Weighted Average Grant Date Fair Value
Outstanding—beginning of year	1,003	$ 8.81
Granted at fair value	275	16.12
Vested	(334)	10.14
Forfeited	(230)	9.41
Outstanding—end of period	714	$ 10.81

8. BUSINESS SEGMENTS

Segment information has been prepared in accordance with ASC Topic 280 Segment Reporting. Segments were determined based on how we manage the business. There were no inter-segment sales or transfers during the three and nine months ended September 30, 2013 and 2012. We evaluate the performance of our segments and allocate resources to them based primarily on gross profit. The table below summarizes information about reportable segments for the three and nine months ended September 30, 2013 and 2012 (in thousands):

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	Three months ended September 30,			Nine months ended September 30,		
	Direct	Fulfillment partner	Total	Direct	Fulfillment partner	Total
2013						
Revenue, net	$35,681	$265,745	$301,426	$113,873	$792,751	$906,624
Cost of goods sold	30,777	211,499	242,276	99,768	630,931	730,699
Gross profit	$4,904	$54,246	$59,150	$14,105	$161,820	$175,925
Operating expenses			55,692			160,887
Other income, net			166			339
Provision for income taxes			91			449
Net income			$3,533			$14,928
2012						
Revenue, net	$34,215	$221,137	$255,352	$109,048	$648,207	$757,255
Cost of goods sold	30,684	178,126	208,810	99,422	520,614	620,036
Gross profit	$3,531	$43,011	$46,542	$9,626	$127,593	$137,219
Operating expenses			44,767			132,950
Other income, net			1,049			1,795
Provision for income taxes			131			182
Net income			$2,693			$5,882

The direct segment includes revenues, direct costs, and cost allocations associated with sales fulfilled from our warehouses. Costs for this segment include product costs, freight, warehousing and fulfillment costs, credit card fees and customer service costs.

The fulfillment partner segment includes revenues, direct costs and cost allocations associated with sales fulfilled from warehouses maintained by our fulfillment partners. Costs for this segment include product costs, outbound freight and fulfillment costs, credit card fees and customer service costs.

Assets have not been allocated between the segments for our internal management purposes and, as such, they are not presented here.

For the three and nine months ended September 30, 2013 and 2012, 99% of sales revenues were attributable to customers in the United States. At September 30, 2013 and December 31, 2012, all of our fixed assets were located in the United States.

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

Special Note Regarding Forward-Looking Statements

This Quarterly Report on Form 10-Q and the documents incorporated herein by reference contain 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. These statements are therefore entitled to the protection of the safe harbor provisions of these laws. These forward-looking statements involve risks and uncertainties, and relate to future events or our future financial or operating performance. The forward-looking statements include all statements other than statements of historical fact, including, without limitation, all statements regarding:

- the anticipated benefits and risks of our business and plans;
- our ability to attract and retain customers in a cost-efficient manner;
- the effectiveness of our marketing;
- our future operating and financial results;
- the competition we face and will face in our business;
- the effects of government regulation;
- our future capital requirements and our ability to satisfy our capital needs;
- our expectations regarding the adequacy of our liquidity;
- our ability to retire or refinance any debt we may have;
- our plans for international markets, our expectations for our international sales efforts and the anticipated results of international operations;
- our plans for changes to our business;
- our beliefs regarding current or future litigation or regulatory actions;
- our beliefs and expectations regarding existing and future tax laws and related laws and the application of those laws to our business;
- our beliefs regarding the adequacy of our insurance coverage;
- the adequacy of our infrastructure, including our backup facilities, cyber-security and our disaster planning;
- our belief that we can meet our published product shipping standards even during periods of relatively high sales activity;
- our belief that we can maintain or improve upon customer service levels that we and our customers consider acceptable;
- our beliefs regarding the adequacy of our order processing systems and our fulfillment and distribution capabilities;
- our beliefs and expectations regarding the adequacy of our office and warehouse facilities;
- our expectations regarding our car listing service and our community site, and the anticipated functionality and results of operations of them;
- our belief that we and our fulfillment partners will be able to maintain inventory levels at appropriate levels despite the seasonal nature of our business;
- our belief that our sales through other ecommerce marketplace channels will be successful and become an important part of our business; and
- our belief that we can successfully offer and sell a constantly changing mix of products and services.

Further, in some cases, you can identify forward-looking statements by terminology such as may, will, could, should, expect, plan, intend, anticipate, believe, estimate, predict, potential or continue, the negative of such terms or other comparable terminology. These statements are only predictions. Actual events or results may differ materially from those contemplated by forward-looking statements for a variety of reasons, including among others:

- changes in U.S. and global economic conditions and consumer spending;
- world events;
- the rate of growth of the Internet and online commerce, and the occurrence of any event that would discourage or prevent consumers from shopping online;

- any failure to maintain our existing relationships or build new relationships with fulfillment partners on acceptable terms;
- any difficulties we may encounter maintaining optimal levels of product quality and selection or in attracting sufficient consumer interest in our product offerings;
- modifications we may make to our business model from time to time, including aspects relating to our product mix and the mix of direct/fulfillment partner sourcing of the products we offer;
- the mix of products purchased by our customers;
- problems with cyber security or data breaches or the costs of preventing or responding to any such problems;

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- problems with or affecting our credit card processors, including cyber-attacks, Internet or other infrastructure or communications impairment or other events that could interrupt the normal operation of the credit card processors;
- problems with the facility where substantially all of our computer and communications hardware is located or other problems that result in the unavailability of our Website or reduced performance of our transaction systems;
- difficulties we may have in responding to technological changes;
- problems with fraudulent purchases;
- problems we may encounter as a result of counterfeit items or the listing or sale of pirated, counterfeit or illegal items by third parties;
- difficulties we may have financing our operations or expansion with either internally generated funds or external sources of financing;
- the extent to which we owe income taxes or are required to collect sales taxes or to modify our business model in order to avoid being required to collect sales taxes;
- competition;
- difficulties with the management of our growth;
- fluctuations in our operating results;
- our efforts to expand internationally;
- the outcomes of legal proceedings, investigations and claims;
- our inability to optimize our warehouse operations;
- risks of inventory management and seasonality; and
- the other risks described in our public filings.

In evaluating all forward-looking statements, you should specifically consider the risks outlined above and in this Form 10-Q in Part II, Item 1A under the caption "Risk Factors." These factors may cause our actual results to differ materially from those contemplated by any forward-looking statement. Except as otherwise required by law, we expressly disclaim any obligation to release publicly any update or revisions to any forward-looking statements to reflect any changes in our expectations or any change in events, conditions or circumstances on which any of our forward-looking statements are based. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements or other events.

These forward-looking statements speak only as of the date of this report and, except as required by law, we undertake no obligation to update forward-looking statements to reflect events or circumstances occurring after the date of this report.

Available Information

Our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and other reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 are available free of charge through the Investors Relations section of our main website www.overstock.com as soon as reasonably practicable after we electronically file such material with, or furnish it to, the Securities and Exchange Commission. Our Internet Website and the information contained therein or connected thereto are not a part of or incorporated into this Quarterly Report on Form 10-Q.

Overview

We are an online retailer offering discount brand name, non-brand name and closeout merchandise, including furniture, home décor, bedding and bath, housewares, jewelry and watches, apparel and designer accessories, electronics and computers, and sporting goods, among other products. We sell hundreds of thousands of best seller and current run books, magazines, CDs, DVDs and video games ("BMMG"). We sell these products and services through our Internet websites located at www.overstock.com, www.o.co and www.o.biz ("Website"). Although our three websites are located at different domain addresses, the technology and equipment and processes supporting the

Website and the process of order fulfillment described herein are the same for all three websites.

Our company, based in Salt Lake City, Utah, was founded in 1997. We launched our initial website in March 1999. Our Website offers our customers an opportunity to shop for bargains conveniently, while offering our suppliers an alternative inventory liquidation or sales channel. We continually add new, and sometimes limited, inventory to our Website in order to create an atmosphere that encourages customers to visit frequently and purchase products before our inventory sells out. We sell products primarily in the United States, with a small amount of products (up to approximately 1% of our total net revenue) sold internationally.

As used herein, “Overstock,” “Overstock.com,”, “O.co,” “we,” “our” and similar terms include Overstock.com, Inc. and its subsidiaries, unless the context indicates otherwise.

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Executive Commentary

This executive commentary is intended to provide investors with a view of our business through the eyes of our management. As an executive commentary, it necessarily focuses on selected aspects of our business. This executive commentary is intended as a supplement to, but not a substitute for, the more detailed discussion of our business included elsewhere herein. Investors are cautioned to read our entire “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” as well as our interim and audited financial statements, and the discussion of our business and risk factors and other information included elsewhere or incorporated in this report. This executive commentary includes forward-looking statements, and investors are cautioned to read the “Special Note Regarding Forward-Looking Statements” at the beginning of Item 2, “Management’s Discussion and Analysis of Financial Condition and Results of Operations.”

Net income was $3.5 million in Q3 2013 compared to $2.7 million in Q3 2012. The $840,000 year-over-year improvement in net income resulted primarily from revenue growth of 18% and a 140 basis point improvement in gross margin (together, resulting in a $12.6 million increase in gross profit). This increase in gross profit was partially offset by a $10.9 million increase in operating expenses.

Revenues in Q3 2013 increased 18% compared to Q3 2012. The growth in revenue was primarily due to a 16% increase in average order size, from $147 to $170, coupled with a 2% increase in orders. The increase in average order size is largely due to a sales mix shift into the higher margin home and garden category.

Gross profit increased 27% compared to Q3 2012 primarily as a result of that revenue growth and a shift in product sales mix into higher margin home and garden products.

Sales and marketing expenses as a percentage of revenue increased from 5.8% to 7.5% during Q3 2013 as compared to the same period in 2012, primarily due to increased expenditures in the sponsored search marketing channel due to a higher proportion of our revenue coming through that channel.

During Q3 2013, Google, Inc. ("Google") tested and later implemented changes to its search engine algorithms, which reduced our ranking in certain Google search results, and slowed our revenue growth in the natural search channel. While we worked on adapting to Google's changes, we emphasized other marketing channels, such as sponsored search, which generated higher revenue growth but with higher marketing expenses as a percentage of revenue than is the case for natural search.

As a result, we had a 16% increase in Contribution (see “Non-GAAP Financial Measures” below for a reconciliation of Contribution to Gross Profit) compared to Q3 2012. Contribution margin was 12.2% for Q3 2013, and 12.4% for Q3 2012.

Technology expense in Q3 2013 increased $1.2 million compared to Q3 2012, primarily due to an increase in staff-related costs.

General and administrative expense in Q3 2013 increased $2.1 million compared to Q3 2012, primarily due to increased legal fees.

Legal fees increased during Q3 2013 due to increased activity on legal matters, including our defense of a case brought by district attorneys in eight California counties. We completed preparation for, and the bench trial of, this case during Q3 2013. We do not expect a verdict in this case for several months.

The balance of our Management's Discussion and Analysis of Financial Condition and Results of Operations provides further information about the matters discussed above and other important matters affecting our business.

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Results of Operations

The following table sets forth our results of operations expressed as a percentage of total net revenue:

	Three months ended September 30,		Nine months ended September 30,	
	2013	2012	2013	2012
	(as a percentage of total net revenue)		(as a percentage of total net revenue)	
Revenue, net				
Direct	11.8 %	13.4 %	12.6 %	14.4 %
Fulfillment partner	88.2	86.6	87.4	85.6
Total net revenue	100.0	100.0	100.0	100.0
Cost of goods sold				
Direct	10.2	12.0	11.0	13.1
Fulfillment partner	70.2	69.8	69.6	68.8
Total cost of goods sold	80.4	81.8	80.6	81.9
Gross profit	19.6	18.2	19.4	18.1
Operating expenses:				
Sales and marketing	7.5	5.8	6.7	5.7
Technology	5.7	6.3	5.9	6.2
General and administrative	5.3	5.4	5.3	5.7
Restructuring	—	—	(0.1)	—
Total operating expenses	18.5	17.5	17.7	17.6
Operating income	1.1	0.7	1.7	0.5
Interest income	—	—	—	—
Interest expense	—	(0.1)	—	(0.1)
Other income, net	0.1	0.5	—	0.3
Net income before income taxes	1.2	1.1	1.7	0.8
Provision for income taxes	—	0.1	—	—
Net income	1.2 %	1.1 %	1.6 %	0.8 %

Comparisons of Three Months Ended September 30, 2013 to Three Months Ended September 30, 2012, and Nine Months Ended September 30, 2013 to Nine Months Ended September 30, 2012.

Revenue

The following table reflects our net revenues for the three and nine months ended September 30, 2013 and 2012 (in thousands):

	Three months ended September 30,				Nine months ended September 30,			
	2013	2012	$ Change	% Change	2013	2012	$ Change	% Change
Revenue, net								
Direct	$35,681	$34,215	$1,466	4.3 %	$113,873	$109,048	$4,825	4.4 %
Fulfillment partner	265,745	221,137	44,608	20.2 %	792,751	648,207	144,544	22.3 %
Total revenue, net	$301,426	$255,352	$46,074	18.0 %	$906,624	$757,255	$149,369	19.7 %

The primary reason for increased total net revenue for the three and nine months ended September 30, 2013 was a 16% increase in average order size from $147 to $170, coupled with a 2% increase in orders, and a 20% increase in average order size from $136 to $163, respectively.

The primary reason for increased direct revenue for the three and nine months ended September 30, 2013 was a continued shift in sales mix into our home and garden products, partially offset by a decrease in sales of clothing and shoes due

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to a shift from a direct inventory-based model to a fulfillment partner-based model to reduce exposure from seasonal inventory and markdowns.

The primary reason for the increase in fulfillment partner revenue for the three and nine months ended September 30, 2013 was an increase in sales of home and garden products.

The shift of business from direct to fulfillment partner (or vice versa) is an economic decision based on the economics of each particular product offering at the time and we generally do not have particular goals for an "appropriate" mix or percentage for the size of either. We believe that the mix of the business between direct and fulfillment partner is consistent with our strategic objectives for our business model in the current economic environment and we do not currently foresee any material shifts in mix.

We continue to seek increased participation in our Club O loyalty program as we have seen revenue, average order size and gross profit from customers with paid Club O memberships grow faster than from other customers. For additional information regarding our Club O loyalty program see Item 1 of Part I, "Financial Statements (Unaudited)" —Note 2 —"Accounting Policies" under the section "Club O loyalty program."

International sales were less than 1% of total net revenues for the three and nine months ended September 30, 2013 and 2012.

Change in estimate of average transit times (days)

Revenue related to merchandise sales is recognized upon delivery to our customers. As we ship high volumes of packages through multiple carriers, it is not practical for us to track the actual delivery date of each shipment. Therefore, we use estimates to determine which shipments are delivered and, therefore, recognized as revenue at the end of the period. Our delivery date estimates are based on average shipping transit times. We review and update our estimates on a quarterly basis based on our actual transit time experience. However, actual shipping times may differ from our estimates.

The following table shows the effect that hypothetical changes in the estimate of average shipping transit times would have had on the reported amount of revenue and net income for the three months ended September 30, 2013 (in thousands):

	Three Months Ended September 30, 2013	
Change in the Estimate of Average Transit Times (Days)	Increase (Decrease) Revenue	Increase (Decrease) Net Income
2	$(9,652)	$(1,601)
1	$(4,072)	$(642)
As reported	As reported	As reported
-1	$2,858	$541
-2	$5,758	$1,039

See "Executive Commentary" above for additional discussion regarding revenue.

Gross profit and gross margin

Our overall gross margins fluctuate based on our sales volume mix between our direct business and fulfillment partner business; changes in vendor and / or customer pricing, including competitive pricing; inventory management decisions within the direct business; sales coupons and promotions; product mix of sales; and operational and fulfillment costs.

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The following table reflects our net revenues, cost of goods sold and gross profit for the three and nine months ended September 30, 2013 and 2012 (in thousands):

	Three months ended September 30,				Nine months ended September 30,			
	2013	2012	$ Change	% Change	2013	2012	$ Change	% Change
Revenue, net								
Direct	$35,681	$34,215	$1,466	4.3 %	$113,873	$109,048	$4,825	4.4 %
Fulfillment partner	265,745	221,137	44,608	20.2 %	792,751	648,207	144,544	22.3 %
Total net revenues	$301,426	$255,352	$46,074	18.0 %	$906,624	$757,255	$149,369	19.7 %
Cost of goods sold								
Direct	$30,777	$30,684	$93	0.3 %	$99,768	$99,422	$346	0.3 %
Fulfillment partner	211,499	178,126	33,373	18.7 %	630,931	520,614	110,317	21.2 %
Total cost of goods sold	$242,276	$208,810	$33,466	16.0 %	$730,699	$620,036	$110,663	17.8 %
Gross Profit								
Direct	$4,904	$3,531	$1,373	38.9 %	$14,105	$9,626	$4,479	46.5 %
Fulfillment partner	54,246	43,011	11,235	26.1 %	161,820	127,593	34,227	26.8 %
Total gross profit	$59,150	$46,542	$12,608	27.1 %	$175,925	$137,219	$38,706	28.2 %

Gross margins for the past seven quarterly periods and fiscal year ending 2012 were:

	Q1 2012	Q2 2012	Q3 2012	Q4 2012	FY 2012	Q1 2013	Q2 2013	Q3 2013
Direct	8.0 %	8.3 %	10.3 %	11.5 %	9.6 %	11.4 %	12.2 %	13.7 %
Fulfillment Partner	20.0 %	19.6 %	19.4 %	18.9 %	19.4 %	20.0 %	20.8 %	20.4 %
Combined	18.1 %	18.0 %	18.2 %	17.9 %	18.1 %	18.9 %	19.7 %	19.6 %

The increase in direct gross margin for the three months ended September 30, 2013 when compared to the same period in 2012 is primarily due to a shift in sales mix into higher margin home and garden products, reduced returns, and lower customer service costs.

The increase in direct gross margin for the nine months ended September 30, 2013 when compared to the same period in 2012 is primarily due to a shift in sales mix into higher margin home and garden products and lower warehousing costs, partially offset by higher freight costs.

The increase in fulfillment partner gross margin for the three months ended September 30, 2013 is primarily due to a shift in sales mix into higher margin home and garden products.

The increase in fulfillment partner gross margin for the nine months ended September 30, 2013 is primarily due to a shift in sales mix into higher margin home and garden products, partially offset by higher freight costs.

Cost of goods sold includes stock-based compensation expense of $37,000 and $74,000 for the three months ended September 30, 2013 and 2012, respectively and $117,000 and $200,000 for the nine months ended September 30, 2013 and 2012, respectively.

See "Executive Commentary" above for additional discussion.

Fulfillment costs

Fulfillment costs include all warehousing costs, including fixed overhead and variable handling costs (excluding packaging costs), as well as credit card fees and customer service costs, all of which we include as costs in calculating gross margin. We believe that some companies in our industry, including some of our competitors, account for fulfillment costs

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within operating expenses, and therefore exclude fulfillment costs from gross margin. As a result, our gross margin may not be directly comparable to others in our industry.

The following table has been included to provide investors additional information regarding our classification of fulfillment costs, gross profit and margin, thus enabling investors to better compare our gross margin with others in our industry (in thousands):

	Three months ended September 30,				Nine months ended September 30,			
	2013		2012		2013		2012	
Total revenue, net	$301,426	100%	$255,352	100%	$906,624	100%	$757,255	100%
Cost of goods sold								
Product costs and other cost of goods sold	228,963	76%	196,522	77%	690,563	76%	582,436	77%
Fulfillment and related costs	13,313	4%	12,288	5%	40,136	4%	37,600	5%
Total cost of goods sold	242,276	80%	208,810	82%	730,699	81%	620,036	82%
Gross profit	$59,150	20%	$46,542	18%	$175,925	19%	$137,219	18%

Fulfillment costs as a percentage of sales may vary due to several factors, such as our ability to manage costs at our warehouses, significant changes in the number of units received and fulfilled, the extent to which we use third party fulfillment services and warehouses, and our ability to effectively manage customer service costs and credit card fees. Fulfillment and related costs remained relatively flat during the three and nine months ended September 30, 2013 as compared to the same periods in 2012.

See “Gross profit” above for additional discussion.

Operating expenses

Sales and marketing expenses

We advertise through a number of targeted online marketing channels, such as sponsored search, affiliate marketing, portal advertising, e-mail campaigns, and other initiatives. We also use nationwide television, print and radio advertising campaigns to promote sales.

The following table reflects our sales and marketing expenses for the three and nine months ended September 30, 2013 and 2012 (in thousands):

	Three months ended September 30,				Nine months ended September 30,			
	2013	2012	$ Change	% Change	2013	2012	$ Change	% Change
Sales and marketing expenses	$22,463	$14,899	$7,564	50.8 %	$60,376	$42,886	$17,490	40.8 %
Sales and marketing expenses as a percent of net revenues	7.5 %	5.8 %			6.7 %	5.7 %		

Sales and marketing expenses as a percentage of revenue increased from 5.8% to 7.5% and 5.7% to 6.7% for the three and nine months ended September 30, 2013, respectively, as compared to the same periods in 2012, primarily due to increased expenditures in the sponsored search marketing channel due to a higher proportion of our revenue coming through that channel.

During the three months ended September 30, 2013, Google, Inc. ("Google") tested and later implemented changes to its search engine algorithms, which reduced our ranking in certain Google search results, and slowed our revenue growth in the natural search channel. While we worked on adapting to Google's changes, we emphasized other marketing channels, such as sponsored search, which generated higher revenue growth but with higher marketing expenses as a percentage of revenue than is the case for natural search.

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Sales and marketing expenses include stock-based compensation expense of $44,000 and $108,000 for the three months ended September 30, 2013 and 2012, respectively and $123,000 and $260,000 for the nine months ended September 30, 2013 and 2012, respectively.

Costs associated with our discounted shipping and other promotions, such as coupons, are not included in marketing expense. Rather, they are accounted for as a reduction of revenue and therefore affect sales and gross margin. We consider discounted shipping and other promotions, such as our new policy of free shipping on orders over $50 introduced in early January 2013, as an effective marketing tool, and intend to continue to offer them as we deem appropriate as part of our overall marketing plan.

Technology expenses

We seek to invest efficiently in technology, including web services, customer support solutions and website search, and in expansion of new and existing product categories, and in investments in technology to enhance the customer experience, improve our process efficiency and support our logistics infrastructure.

The following table reflects our technology expenses for the three and nine months ended September 30, 2013 and 2012 (in thousands):

	Three months ended September 30,				Nine months ended September 30,			
	2013	2012	$ Change	% Change	2013	2012	$ Change	% Change
Technology expenses	$17,259	$16,085	$1,174	7.3 %	$53,339	$46,845	$6,494	13.9 %
Technology expenses as a percent of net revenues	5.7 %	6.3 %			5.9 %	6.2 %		

The $1.2 million and $6.5 million increases for the three and nine months ended September 30, 2013, respectively, are primarily due to an increase in staff related costs.

Technology expenses include stock-based compensation expense of $33,000 and $218,000 for the three months ended September 30, 2013 and 2012, respectively and $235,000 and $585,000 for the nine months ended September 30, 2013 and 2012, respectively.

General and administrative expenses

The following table reflects our general and administrative expenses for the three and nine months ended September 30, 2013 and 2012 (in thousands):

	Three months ended September 30,				Nine months ended September 30,			
	2013	2012	$ Change	% Change	2013	2012	$ Change	% Change
General and administrative expenses	$15,970	$13,828	$2,142	15.5 %	$47,643	$43,166	$4,477	10.4 %
General and administrative expenses as a percent of net revenues	5.3 %	5.4 %			5.3 %	5.7 %		

The $2.1 million and $4.5 million increases in general and administrative expenses (“G&A”) for the three and nine months ended September 30, 2013, respectively, are primarily due to increases in legal fees and staff-related costs.

Legal fees increased during the three and nine months ended September 30, 2013 due to increased activity on legal matters, including our defense of a case brought by district attorneys in eight California counties. We completed preparation for, and the bench trial of, this case during the three months ended September 30, 2013. We do not expect a verdict in this case for several months.

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G&A expenses include stock-based compensation expense of approximately $695,000 and $580,000 for the three months ended September 30, 2013 and 2012, respectively, and $1.9 million and $1.6 million for the nine months ended September 30, 2013 and 2012, respectively.

Restructuring

There were no restructuring expenses or reversals during the three months ended September 30, 2013. During the nine months ended September 30, 2013 we reversed $471,000 of lease termination costs primarily due to changes in our restructuring accrual as a result of our reoccupation of a portion of formerly restructured office space. We reversed $45,000 and incurred $53,000 of lease termination costs during the three and nine months ended September 30, 2012, respectively, due to changes in the estimate of sublease income as a result of our entering into a new sublease agreement and ceasing the use of some of our office facilities.

Depreciation expense

Depreciation expense is classified within the corresponding operating expense categories on the consolidated statements of operations as follows (in thousands):

	Three months ended September 30,		Nine months ended September 30,	
	2013	2012	2013	2012
Cost of goods sold - direct	$87	$123	$292	$350
Technology	2,937	3,371	9,595	10,570
General and administrative	283	345	946	1,015
Total depreciation and amortization, including internal-use software and website development	$3,307	$3,839	$10,833	$11,935

Non-operating income (expense)

Interest income

Interest income is primarily derived from the investment of our cash in cash equivalents and short-term investments. Interest income for the three months ended September 30, 2013 and 2012 totaled $34,000 and $30,000, respectively and $100,000 and $86,000 for the nine months ended September 30, 2013 and 2012, respectively.

Interest expense

Interest expense is primarily related to interest incurred on line of credit and our capital leases. Interest expense for the three months ended September 30, 2013 and 2012 totaled $33,000 and $194,000, respectively and $121,000 and $655,000 for the nine months ended September 30, 2013 and 2012, respectively. The decrease is primarily due to our repayment of the $17.0 million in advances under the U.S. Bank Financing Agreement in November 2012.

Other income, net

Other income, net for the three months ended September 30, 2013 decreased to $165,000 from $1.2 million in 2012 primarily due to a decrease in Club O rewards breakage. Other income, net for the nine months ended September 30, 2013 decreased to $360,000 from $2.4 million in 2012 primarily due to a decrease in Club O rewards and gift card breakage and from losses on precious metals.

Income taxes

Our provision for income taxes is for federal alternative minimum tax, state taxes and certain income tax uncertainties, including interest and penalties. Our provision for income taxes for the three and nine months ended September 30, 2013 was $91,000 and $449,000, respectively. Our provision for income taxes for the three and nine months ended September 30, 2012 was $131,000 and $182,000, respectively. At September 30, 2013 and December 31, 2012 we had federal net operating loss carry forwards of approximately $154.0 million and $174.1 million, respectively, and state net operating loss carry forwards of

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approximately $137.5 million and $151.6 million, respectively, which may be used to offset future taxable income. Our net operating loss carry forwards will begin to expire in 2019.

At September 30, 2013 and December 31, 2012, we have a full valuation allowance against our deferred tax assets, net of expected reversals of existing deferred tax liabilities, as we believe it is more likely than not that these benefits will not be realized. Significant judgment is required in making this assessment, and it is very difficult to predict when our assessment may conclude that the remaining portion of the deferred tax assets is realizable. To the extent that we remain profitable for the foreseeable future, the full or partial release of the valuation allowance could occur in the near term.

In September 2013, the U.S. Department of the Treasury and the Internal Revenue Service released final regulations relating to guidance on applying tax rules to amounts paid to acquire, produce or improve tangible personal property as well as rules for materials and supplies. We are evaluating the future impact of the final regulations to our tax provision.

Seasonality

Based upon our historical experience, revenue typically increases during the fourth quarter because of the holiday retail season. The actual quarterly results for each quarter could differ materially depending upon consumer preferences, availability of product and competition, among other risks and uncertainties. Accordingly, there can be no assurances that seasonal variations will not materially affect our results of operations in the future.

The following table reflects our total net revenues for each of the quarters in 2013, 2012 and 2011 (in thousands):

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
2013	$311,994	$293,204	$301,426	N/A
2012	$262,367	$239,536	$255,352	$342,034
2011	$265,470	$234,992	$239,738	$314,077

Liquidity and Capital Resources

Current sources of liquidity

While we believe that the cash and cash equivalents currently on hand and expected cash flows from future operations will be sufficient to continue operations for at least the next twelve months; we may require additional financing. Although we may attempt to obtain additional financing, there can be no assurance that we will be able to do so. There can be no assurance that if additional financing is necessary it will be available, or, if available, that such financing can be obtained on satisfactory terms. Our failure to generate sufficient revenues or profits or to obtain additional financing or raise additional capital could have a material adverse effect on our operations and on our ability to achieve our intended business objectives. Any projections of future cash needs and cash flows are subject to substantial uncertainty.

Our principal sources of liquidity are cash flows generated from operations, and our existing cash and cash equivalents. At September 30, 2013, our only available credit facility was a $3.0 million facility solely to support letters of credit. At September 30, 2013, we had cash and cash equivalents of $84.9 million.

Cash flow information is as follows (in thousands):

	Nine months ended September 30,	Twelve months ended September 30,

	2013	2012	2013	2012
Cash provided by (used in):				
Operating activities	$13,784	$(13,337)	$55,266	$28,626
Investing activities	(19,783)	(10,428)	(23,119)	(12,863)
Financing activities	(2,686)	(751)	(19,754)	(22,432)

Free Cash Flow

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"Free Cash Flow" (a non-GAAP measure) for the nine months ended September 30, 2013 and 2012, was $(186,000) and $(23.9) million, respectively and $39.4 million and $15.7 million for the twelve months ended September 30, 2013 and 2012, respectively. See "Non-GAAP Financial Measures" below for a reconciliation of Free Cash Flow to net cash provided by (used in) operating activities.

Cash flows from operating activities

For the nine months ended September 30, 2013 and 2012, our operating activities resulted in a net cash inflow of $13.8 million and a net cash outflow of $13.3 million, respectively.

Cash received from customers generally corresponds to our net revenues as our customers primarily use credit cards to buy from us causing our receivables from these sales transactions to settle quickly. We have payment terms with our fulfillment partners that generally extend beyond the amount of time necessary to collect proceeds from our customers. As a result, following our typically seasonally strong fourth quarter sales, at December 31 of each year, our cash, cash equivalents and accounts payable balances normally reach their highest level (other than as a result of cash flows provided by or used in investing and financing activities). However, our accounts payable balance normally declines during the first three months following year-end, which normally results in a decline in our cash and cash equivalents balances from the year-end balance. The seasonality of our business causes payables and accruals to grow significantly in the fourth quarter, and then decrease in the first quarter when they are typically paid.

The $13.8 million of net cash provided by operating activities during the nine months ended September 30, 2013 was primarily from net income of $14.9 million, non-cash depreciation and amortization expense of 10.8 million, a reduction in accounts receivable of $4.6 million and reduction in inventory of $3.7 million, partially offset by a decrease in deferred revenue of $8.6 million, payments of accounts payable of $7.8 million, and a decrease in prepaids of $3.0 million.

The $13.3 million of net cash used in operating activities during the nine months ended September 30, 2012 was primarily for payments of accounts payable of $27.0 million following the holiday season, and a decrease in accrued liabilities of $7.5 million, partially offset by non-cash depreciation, amortization and stock compensation expense of $14.6 million and net income of $5.9 million.

Cash flows from investing activities

Cash provided by investing activities primarily corresponds with purchases, sales, and maturities of marketable securities, investments in precious metals and cash expenditures for fixed assets, including internal-use software and website development costs. For the nine months ended September 30, 2013, investing activities resulted in net cash outflows of $19.8 million, primarily from expenditures for fixed assets of $14.0 million and investments in precious metals of $6.0 million. For the nine months ended September 30, 2012 investing activities resulted in net cash outflows of $10.4 million, resulting primarily from expenditures for fixed assets.

Cash flows from financing activities

For the nine months ended September 30, 2013 and 2012, financing activities resulted in net cash outflows of $2.7 million and $751,000, respectively.

The $2.7 million used in financing activities during the nine months ended September 30, 2013 resulted primarily from $2.6 million for prepayment of capital leases for computer equipment and $1.4 million for the purchase of shares of our common stock withheld for minimum tax withholdings upon the vesting of a portion of certain restricted stock award grants, partially offset by $1.5 million in proceeds for the exercise of stock options.

The $751,000 used in financing activities during the nine months ended September 30, 2012 resulted primarily from $464,000 for the purchase of shares of our common stock withheld for minimum tax withholdings upon the vesting of a portion of certain restricted stock award grants.

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Contractual Obligations and Commitments

The following table summarizes our contractual obligations as of September 30, 2013 and the effect such obligations and commitments are expected to have on our liquidity and cash flow in future periods (in thousands):

	Payments Due by Period						
Contractual Obligations	Remainder of 2013	2014	2015	2016	2017	Thereafter	Total
Operating leases	$2,658	$10,403	$8,161	$4,663	$3,922	$36,263	$66,070
Naming rights	—	1,311	1,351	1,391	—	—	4,053
Purchase obligations	13,716	211	—	—	—	—	13,927
Other	100	2,774	107	—	—	—	2,981
Total contractual cash obligations	$16,474	$14,699	$9,619	$6,054	$3,922	$36,263	$87,031

	Amounts of Commitment Expiration Per Period						
Other Commercial Commitments	2013	2014	2015	2016	2017	Thereafter	Total
Letters of credit	$1,780	$—	$—	$—	$—	$—	$1,780

Operating Leases

From time to time we enter into operating leases for facilities and equipment for use in our operations. On May 13, 2013 we entered into a new operating lease for a warehouse facility that we have leased since September 2008. This lease extends the term of occupancy to August 31, 2026. The minimum future payments due under this new operating lease are included in the summary of future minimum lease payments for all operating leases in the table above.

Naming Rights

During 2011, we entered into a six-year agreement with the Oakland-Alameda County Coliseum Authority (“OACCA”) for the right to name Oakland Alameda County Coliseum (now known as “O.co Coliseum”). Amounts represent annual payments due OACCA for the naming rights. We have the right to terminate this agreement at our sole option, subject to payment of a termination fee.

Purchase obligations

The amount of purchase obligations shown above is based on assumptions regarding the legal enforceability against us of inventory purchase orders we had outstanding at September 30, 2013. Under different assumptions regarding our rights to cancel our purchase orders or different assumptions regarding the enforceability of the purchase orders under applicable law, the amount of purchase obligations shown in the table above would be less.

Other

From time to time we enter into long-term contractual agreements for marketing, technology, or other services.

Tax Contingencies

Our contractual obligations presented above exclude unrecognized tax contingencies, including interest and penalties, of $386,000 for which we cannot make a reasonably reliable estimate of the amount and period of payment.

Borrowings

U.S. Bank Financing Agreement

In November 2012, we repaid all amounts outstanding under our Financing Agreement with U.S. Bank National Association ("U.S. Bank"). The Financing Agreement expired in accordance with its terms on December 31, 2012; and we

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entered into a $3.0 million cash-collateralized line of credit agreement (the “Credit Agreement”) with U.S. Bank for the issuance of letters of credit. Advances under the Credit Agreement bear interest at one-month LIBOR plus 1.0%. The Credit Agreement matures on December 31, 2013. There were no amounts outstanding on the Credit Agreement at September 30, 2013 and December 31, 2012.

As of December 31, 2012, no amounts were outstanding under the Financing Agreement. As of September 30, 2013 and December 31, 2012, letters of credit totaling $1.8 million and $1.8 million, respectively, were issued on our behalf collateralized by compensating cash balances held at U.S. Bank, which are included in Restricted cash in the accompanying consolidated balance sheets.

U.S. Bank Commercial Purchasing Card Agreement

We have a commercial purchasing card (the “Purchasing Card”) agreement with U.S. Bank. We use the Purchasing Card for business purpose purchasing and must pay it in full each month. At September 30, 2013, $865,000 was outstanding and $4.1 million was available under the Purchasing Card. At December 31, 2012, $3.9 million was outstanding and $1.1 million was available under the Purchasing Card.

Capital leases

In March 2013, we entered into a capital lease arrangement for $2.6 million of computer equipment that will expire in 2017. We prepaid the entire $2.6 million shortly after entering into the agreement in order to obtain discounted pricing. As such, we have no future payment obligations under capital leases at September 30, 2013.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that would be material to investors.

Critical Accounting Policies and Estimates

The preparation of our financial statements requires that we make estimates and judgments. We base these on historical experience and on other assumptions that we believe to be reasonable. Our critical accounting policies are discussed in Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations” section of our Annual Report on Form 10-K for the year ended December 31, 2012. There have been no material changes to the critical accounting policies previously disclosed in that report.

Non-GAAP Financial Measures

Regulation G, Conditions for Use of Non-GAAP Financial Measures, and other SEC regulations regulate the disclosure of certain non-GAAP financial information.

Contribution and Contribution Margin

Contribution (a non-GAAP financial measure) (which we reconcile to “Gross profit” in our consolidated statements of income and comprehensive income) consists of gross profit less sales and marketing expense and reflects an additional way of viewing our results. Contribution Margin is Contribution as a percentage of revenues. When viewed together with our GAAP results, we believe Contribution and Contribution Margin provide management and users of the financial statements information about our ability to cover our operating costs, such as technology and general and administrative expenses. Contribution and Contribution Margin are used in addition to and in conjunction with results presented in accordance with GAAP and should not be relied upon to the exclusion of GAAP financial measures. You should review our financial statements and publicly-filed reports in their entirety and not rely on any single financial measure. The material limitation associated with the use of Contribution is that it is an incomplete measure of profitability as it does not include all operating expenses or non-operating income and expenses. Management compensates for these limitations when using this measure by looking at other GAAP measures, such as operating income and net income.

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For further details on Contribution and Contribution Margin, see the calculation of these non-GAAP financial measures below (in thousands):

	Three months ended September 30,				Nine months ended September 30,			
	2013		2012		2013		2012	
Total net revenue	$301,426	100%	$255,352	100%	$906,624	100%	$757,255	100%
Cost of goods sold	242,276	80.4%	208,810	81.8%	730,699	80.6%	620,036	81.9%
Gross profit	59,150	19.6%	46,542	18.2%	175,925	19.4%	137,219	18.1%
Less: Sales and marketing expense	22,463	7.5%	14,899	5.8%	60,376	6.7%	42,886	5.7%
Contribution and contribution margin	$36,687	12.2%	$31,643	12.4%	$115,549	12.7%	$94,333	12.5%

Free Cash Flow

Free cash flow (a non-GAAP financial measure) reflects an additional way of viewing our cash flows and liquidity that, when viewed with our GAAP results, provides a more complete understanding of factors and trends affecting our cash flows and liquidity. Free cash flow, which we reconcile to “Net cash provided by (used in) operating activities”, is cash flows from operations reduced by “Expenditures for fixed assets, including internal-use software and website development.” We believe that cash flows from operating activities is an important measure, since it includes both the cash impact of the continuing operations of the business and changes in the balance sheet that impact cash. However, we believe free cash flow is a useful measure to evaluate our business since purchases of fixed assets are a necessary component of ongoing operations and free cash flow measures the amount of cash we have available for mandatory debt service and financing obligations, changes in our capital structure, and future investments after we have paid all of our operating expenses. Therefore, we believe it is important to view free cash flow as a complement to our entire consolidated statements of cash flows as calculated below (in thousands):

	Nine months ended September 30,		Twelve months ended September 30,	
	2013	2012	2013	2012
Net cash provided by (used in) operating activities	$13,784	$(13,337)	$55,266	$28,626
Expenditures for fixed assets, including internal-use software and website development	(13,970)	(10,563)	(15,896)	(12,960)
Free cash flow	$(186)	$(23,900)	$39,370	$15,666

Government Regulation

Our services are subject to federal and state consumer protection laws including laws protecting the privacy of consumer information and regulations prohibiting unfair and deceptive trade practices. In particular, under federal and state financial privacy laws and regulations, we must provide notice to consumers of our policies on sharing non-public information with third parties, advance notice of any changes to our policies and, with limited exceptions, we must give consumers the right to prevent sharing of their non-public personal information with unaffiliated third parties. Further, the growth and demand for online commerce could result in more stringent consumer protection laws that impose additional compliance burdens on online companies. These consumer protection laws could result in substantial compliance costs.

New disclosure and reporting requirements, established under existing or new state or federal laws, such as rules regarding requirements to identify the origin and existence of certain “conflict minerals” or regarding the disclosure of abusive labor practices in portions of our supply chain, could increase the cost of doing business, adversely affecting our results of operations.

In many states, there is currently great uncertainty whether or how existing laws governing issues such as property ownership, sales and other taxes, libel and personal privacy apply to the Internet and commercial online services. In addition, new state tax regulations in states where we do not now collect state and local taxes may subject us to the obligation to collect and remit state and local taxes, or subject us to additional state and local sales and income taxes, or to requirements intended to assist states with their tax collection efforts. New legislation or regulation, the application of laws and regulations from jurisdictions whose laws do not currently apply to our business or the application of existing laws and regulations to the Internet

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and commercial online services could result in significant additional taxes on our business. These taxes or tax collection obligations could have an adverse effect on our cash flows and results of operations. Further, there is a possibility that we may be subject to significant fines or other payments for any past failures to comply with these requirements.

Factors that May Affect Future Results

Any investment in our securities involves a high degree of risk. Investors should consider carefully the risks and uncertainties described in this Form 10-Q, and all other information in this Form 10-Q and in our other filings with the SEC including those we file after we file this Form 10-Q, before deciding whether to purchase or hold our securities.

Additional risks and uncertainties not currently known to us or that we currently deem immaterial may also become important factors that may harm our business. The occurrence of any of the risks described under “Risk Factors” in our most recent Annual Report on Form 10-K or herein could harm our business. The trading price of our securities could decline due to any of these risks and uncertainties, and investors may lose part or all of their investment.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We do not use derivative financial instruments in our investment portfolio, except, prior to January 1, 2013, for an interest rate cap agreement on our line of credit (which expired December 31, 2012), and we have no foreign exchange contracts. Our financial instruments consist of cash and cash equivalents, trade accounts and contracts receivable, accounts payable and long-term obligations. We consider investments in highly-liquid instruments with a remaining maturity of 90 days or less at the date of purchase to be cash equivalents.

Our exposure to market risk for changes in interest rates relates primarily to our short-term investments and short-term obligations; thus, fluctuations in interest rates would not have a material impact on the fair value of these securities. However, the fair values of our investments may be subject to fluctuations due to volatility of the stock market in general, investment-specific circumstances, and changes in general economic conditions.

At September 30, 2013, we had $84.9 million in cash and cash equivalents. Hypothetically, an increase or decrease in interest rates of one hundred basis points would have an estimated impact of $849,000 on our earnings or loss, or the fair market value or cash flows of these instruments.

At September 30, 2013, we had assets consisting of precious metals totaling $8.6 million. Hypothetically, an increase or decrease in the market value of one hundred basis points would have an estimated impact of $86,000 on our earnings or loss, or the recorded value or cash flows of these instruments. Earnings resulting from increases in the market value of precious metals would be limited to losses incurred in the same fiscal year.

At September 30, 2013, letters of credit totaling $1.8 million were outstanding under our credit facilities. Hypothetically, an increase or decrease in interest rates of one hundred basis points would have an estimated impact of $18,000 on our earnings or loss, or the cash flows of these instruments, if the letters of credit were fully drawn.

ITEM 4. CONTROLS AND PROCEDURES

We maintain disclosure controls and procedures, as such term is defined in Rule 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934 (the “Exchange Act”). The term disclosure controls and procedures means controls and other procedures of an issuer that are designed to ensure that information required to be disclosed by the issuer in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Commission’s rules and forms.

Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the Exchange Act is accumulated and communicated to the issuer’s management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

Evaluation of Disclosure Controls and Procedures

We carried out an evaluation required by the Exchange Act under the supervision and with the participation of our principal executive officer and principal financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rule 13a-15(e) of the 1934 Act, as of the end of the period covered by this report. Based

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on this evaluation, our principal executive officer and principal financial officer concluded that our disclosure controls and procedures were effective to provide reasonable assurance that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and to provide reasonable assurance that such information is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

During the most recent fiscal quarter, there has not occurred any change in our internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Our disclosure controls and procedures are designed to provide reasonable assurance of achieving their objectives as specified above. Management does not expect, however, that our disclosure controls and procedures will prevent or detect all error and fraud. Any control system, no matter how well designed and operated, is based upon certain assumptions and can provide only reasonable, not absolute, assurance that its objectives will be met. Further, no evaluation of controls can provide absolute assurance that misstatements due to error or fraud will not occur or that all control issues and instances of fraud, if any, within the Company have been detected.

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PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The information set forth under Item 1 of Part I, “Financial Statements “—Note 5—“Commitments and Contingencies,” subheading “Legal Proceedings,” contained in the “Notes to Consolidated Financial Statements” of this Quarterly Report on Form 10-Q is incorporated by reference in answer to this Item.

ITEM 1A. RISK FACTORS

Please consider the following risk factors carefully. If any of the following risks were to occur, it could have a material adverse effect on our business, prospects, financial condition and results of operations, and the market price of our securities could decrease significantly. Statements below to the effect that an event could harm our business (or similar statements) mean that the event could have a material adverse effect on our business, prospects, financial condition and results of operations. These are not the only risks we face.

We have a history of significant losses. If we do not maintain profitability, our financial condition and our stock price could suffer.

We have a history of losses and we may incur operating and net losses in the foreseeable future. At September 30, 2013, our accumulated deficit was $232.2 million. We need to generate significant revenues to maintain profitability, and we may not be able to do so. Although we had net income of $14.9 million for the nine months ended September 30, 2013 and $14.7 million in 2012, we incurred a net loss of $19.4 million in 2011. We may be unable to maintain profitability in the future. If our revenues grow more slowly than we anticipate or decline, or if our expenses exceed our expectations, our financial results would be harmed and our business, prospects, financial condition and results of operations could fall below the expectations of public market analysts and investors.

We are an e-commerce business and we depend on the continued use of the Internet and the adequacy of the Internet infrastructure.

Our business depends upon the widespread use of the Internet and e-commerce. Factors which could reduce the widespread use of the Internet for e-commerce include:

- actual or perceived lack of security of information or privacy protection;
- cyber-attacks or other disruptions or damage to the Internet or to users’ computers;
- significant increases in the costs of transportation of goods; and
- taxation and governmental regulation.

We depend on our relationships with independent fulfillment partners for a large portion of the products that we offer for sale on our Website. If we fail to maintain these relationships, our business will suffer.

At September 30, 2013, we had relationships with approximately 2,300 independent fulfillment partners whose products we offer for sale on our Website. Sales through our fulfillment partners accounted for 88% of our net revenues for the three and nine months ended September 30, 2013, respectively. If we do not maintain our existing relationships or build new relationships with fulfillment partners on acceptable commercial terms, we may not be able to maintain a broad selection of merchandise, and our business and prospects would suffer severely. Our agreements with fulfillment partners are generally terminable at will by either party upon short notice.

We depend on our fulfillment partners to perform certain services regarding the products that we offer.

In general, we agree to offer the fulfillment partners' products on our Website and these fulfillment partners agree to conduct a number of other traditional retail operations with respect to their respective products, including maintaining inventory, preparing merchandise for shipment to individual customers and delivering purchased merchandise on a timely basis. We may be unable to ensure that these third parties will continue to perform these services to our satisfaction or on commercially reasonable terms. In addition, because we do not take possession of these fulfillment parties' products (other than on the return of such products), we are generally unable to fulfill these traditional retail operations ourselves. If our customers become dissatisfied with the services provided by these third parties, our business and reputation and the Overstock.com brand could suffer.

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Risks associated with the suppliers from whom our products are sourced and the safety of those products could adversely affect our financial performance.

Global sourcing of many of the products we sell is an important aspect of our business. We depend on our ability to access products from qualified suppliers in a timely and efficient manner. Political and economic instability, the financial stability of suppliers, suppliers' ability to meet our standards, labor problems experienced by our suppliers, the availability of raw materials, merchandise quality issues, currency exchange rates, transport availability and cost, transport security, inflation, and other factors relating to the suppliers and the countries in which they are located are beyond our control. Further, our customers count on us to provide them with safe products. Concerns regarding the safety of products that we source from our suppliers and then sell could cause shoppers to avoid purchasing certain products from us, or to seek alternative sources of supply for all of their needs, even if the basis for the concern is outside of our control. Any lost confidence on the part of our customers would be difficult and costly to reestablish. As such, any issue regarding the safety of any items we sell, regardless of the cause, could adversely affect our financial performance. Further, we sell products manufactured for us by third parties, some of which may be defective. If any product that we sell were to cause physical injury or injury to property, the injured party or parties might bring claims against us as the manufacturer and/or retailer of the product. Our insurance coverage may not be adequate to cover claims that could be asserted. Even unsuccessful claims could result in the expenditure of funds and management time and could have a negative impact on our business.

Manufacturers may refuse to sell to us or through our site.

We rely upon our fulfillment partners and other suppliers for the product offerings sold on our website and other products and services we use to run our business. Our ability to retain or attract new fulfillment partners and other suppliers may depend in part on our financial performance. Poor financial performance could result in suppliers choosing to limit or suspend doing business with us or require us to prepay for our purchases. Further, some manufacturers are unwilling to offer products for sale on the Internet or on sites like ours. Our inability to source and offer popular products could be a significant problem for us.

Our business depends on our Website, network infrastructure and transaction-processing systems.

As an e-commerce company, we are completely dependent on our infrastructure. Any system interruption that results in the unavailability of our Website or reduced performance of our transaction systems could substantially reduce our ability to conduct our business. We use internally and externally developed systems for our Website and our transaction processing systems, including personalization databases used for internal analytics, recommendations and order verifications. We have experienced periodic systems interruptions due to server failure and power failure in the past, which we expect will continue to occur from time to time. We have also experienced and may continue to experience temporary capacity constraints due to sharply increased traffic during sales or other promotions and during the holiday shopping season. Capacity constraints can cause system disruptions, slower response times, delayed page presentation, degradation in levels of customer service and other problems. In the past we have also experienced difficulties with our infrastructure upgrades. Any future difficulties with our transaction processing systems or difficulties upgrading, expanding or integrating aspects of our systems may cause system disruptions, slower response times, and degradation in levels of customer service, additional expense, impaired quality and speed of order fulfillment or other problems.

If the facility where substantially all of our computer and communications hardware is located fails, our business, prospects, financial condition and results of operations could be harmed.

If the facility where substantially all of our computer and communications hardware is located fails, or if we suffer an interruption or degradation of services at the facility for any reason, our business could be harmed. Our success, and in particular, our ability to successfully receive and fulfill orders and provide high-quality customer service, largely depends on the efficient and uninterrupted operation of our computer and communications systems. Substantially all of our computer and communications hardware is located at a single co-location facility in Salt Lake City, Utah, with a partially redundant back-up system located less than six miles from the co-location facility. In the event of an earthquake or major local disaster, or any other cause of interruption of service, both our primary and back-up sites could be adversely affected. Although we have designed our back-up system in an effort to minimize service interruptions in the event of a failure of our main facility, our systems and operations are vulnerable to damage or interruption from fire, flood, power loss, telecommunications failure, terrorist attacks, cyber-attacks, acts of war, break-ins, earthquake and similar events. In the event of a failure of our primary facility, the failover to our back-up facility would take at least several hours, during which time our Website would be completely shut down. Our back-up facility is designed to support sales at a level slightly above our average daily sales, but is not adequate to support sales at a high level. The back-up facility may not process effectively during time of higher traffic to our Website and may process transactions more slowly and may not support all of the functionality of our primary site. These limitations could have an adverse effect on our conversion rate and sales. Our disaster recovery plan may be inadequate, and we do not carry business interruption insurance sufficient to compensate us for the losses that could occur. Despite our implementation of network security measures, our servers are vulnerable to computer viruses, physical or electronic break-ins and similar disruptions, the occurrence of any of which could lead to interruptions, delays, loss of critical data or the inability to accept and fulfill customer orders. The occurrence of any of the foregoing risks could harm our business.

We depend upon third-party delivery services to deliver products to our customers on a timely and consistent basis. Deterioration in our relationship with any one of these third parties could decrease our ability to track shipments, cause shipment delays, and increase our shipping costs and the number of damaged products.

We rely upon third party delivery providers for the shipment of products to customers. We cannot be sure that these relationships will continue on terms we find acceptable, or at all. Increases in shipping costs or delivery times, particularly during the holiday season, could harm our business. If our relationships with these third parties are terminated or impaired or if these third parties are unable to deliver products for us, whether as a result of labor shortage, slow down or stoppage, deteriorating financial or business condition, terrorist attacks, cyber-attacks, Internet or other infrastructure or communications impairment, natural disasters, or for any other reason, we would be required to use alternative carriers for the shipment of products to our customers. In addition, conditions such as adverse weather or natural disasters can prevent any carrier from performing its delivery services, which can have an adverse effect on our customers' satisfaction with us. In any of these circumstances, we may be unable to engage alternative carriers on a timely basis, upon terms we find acceptable, or at all. Changing carriers, or absence of carrier availability, could have a material adverse effect on our business.

We depend upon our credit card processors and payment card associations.

Our customers primarily use credit cards to buy from us. We are dependent upon our credit card processors to process the sales transactions and remit the proceeds to us. The credit card processors have the right to withhold funds otherwise payable to us to establish or increase a reserve based on their assessment of the inherent risks of credit card processing and their assessment of the risks of processing our customers' credit cards at any time, and have done so from time to time in the past. We are also subject to payment card associations' 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 our customers, process electronic funds transfers, or facilitate other types of online payments. In addition, events affecting our credit card processors, including cyber-attacks, Internet or other infrastructure or communications impairment or other events that could interrupt the normal operation of the credit card processors, could have a material adverse effect on our business.

We rely upon paid and natural search engines like Google, Bing, and Yahoo! to rank our product offerings. Our financial results may suffer if search engines change their ranking algorithms and our product offerings are ranked lower, and we may at times be subject to ranking penalties if search engines believe we are not in compliance with their guidelines.

We rely on paid and natural search engines to attract consumer interest in our product offerings. Potential and existing customers use search engines provided by search engine companies, including, but not limited to, Google, Bing, and Yahoo!, which use algorithms and other devices to provide users a natural ranked listing of relevant Internet sites matching a user's search criteria and specifications. Generally, Internet sites ranked higher in the paid and natural search results attract the largest visitor share among similar Internet sites, and often benefit from increased sales. Natural search engine algorithms use information available throughout the Internet, including information available on our site. If search engine companies change their natural search engine algorithms, and our ranking in natural searches is adversely affected by those changes, our financial results may suffer from reduced revenues and from increased marketing expenses from seeking to replace such lost revenues from other sources.

Rules and guidelines of these natural search engine companies govern our participation on their sites and how we share relevant Internet information that may be considered or incorporated into the algorithms used by these sites. If these rules and guidelines change, or if we fail to present, or improperly present, our site information for use by natural search engine companies, or if any of these natural search engine companies determine that we have violated their rules or guidelines, as Google did in February 2011 through April 2011, or if others improperly present our site information to these search engine companies, we may fail to achieve an optimum ranking in natural search engine listing results, or we may be penalized in a way that could harm our business.

In addition, large marketplace websites and sites which aggregate marketplace sellers with a large product selection are becoming increasingly popular, and we may not be able to place our products on these sites to take advantage of their internal search platforms. Our inability to place products on or access these sites may have a material adverse effect on our business.

We are subject to cyber security risks and may incur increasing costs in an effort to minimize those risks and to respond to cyber incidents.

Our business is entirely dependent on the secure operation of our website and systems as well as the operation of the Internet generally. Our business involves the storage and transmission of users' proprietary information, and security breaches could expose us to a risk of loss or misuse of this information, litigation, and potential liability. A number of large Internet companies have suffered security breaches, some of which have involved intentional attacks. From time to time we and many other Internet businesses also experience denial of service attacks wherein attackers attempt to block customers' access to our Website. If we are unable to avert a denial of service attack for any significant period, we could sustain substantial revenue loss from lost sales and customer dissatisfaction. We may not have the resources or technical sophistication to anticipate or prevent rapidly evolving types of cyber-attacks. Cyber-attacks may target us, our customers, our suppliers, banks, credit card processors, delivery services, e-commerce in general or the communication infrastructure on which we depend. If an actual or perceived attack or breach of our security occurs, customer and/or supplier perception of the effectiveness of our security measures could be harmed and we could lose customers, suppliers or both. Actual or anticipated attacks and risks may cause us to incur increasing costs, including costs to deploy additional personnel and protection technologies, train employees, and engage third party experts and consultants.

A person who is able to circumvent our security measures might be able to misappropriate our or our users' proprietary information, cause interruption in our operations, damage our computers or those of our users, or otherwise damage our reputation and business. Any compromise of our security could result in a violation of applicable privacy and other laws, significant legal and financial exposure, damage to our reputation, and a loss of confidence in our security measures, which could harm our business.

Most of our customers use credit cards to pay for their purchases. We rely on encryption and authentication technology licensed from third parties to provide the security and authentication to effectively secure transmission of confidential information, including customer payment card numbers. We cannot provide assurance that our technology can prevent breaches of the systems that we use to protect customer data. Data breaches can also occur as a result of non-technical issues.

Under payment card rules and our contracts with our card processors, if there is a breach of payment card information that we store, we could be liable to the payment card issuing banks for their cost of issuing new cards and related expenses. In addition, if we fail to follow payment card industry security standards, even if there is no compromise of customer information, we could incur significant fines or lose our ability to give customers the option of using payment cards to fund their payments or pay their fees. If we were unable to accept payment cards, our business would be seriously damaged.

Our servers and the servers of our suppliers may also be vulnerable to computer viruses, physical or electronic break-ins, and similar disruptions, including denial-of-service attacks. We may need to expend significant resources to protect against attacks or security breaches or to address problems caused by attacks or breaches. Any attack or breach incident involving us or persons with whom we have commercial relationships, that results in the unauthorized release of our users' personal information, could damage our reputation and expose us to a risk of loss or litigation and possible liability.

Third parties have demonstrated that they can breach the security of customer transaction data of large sophisticated Internet retailers, government organizations and others. Any breach, whether it affects us directly or not, could cause our customers to lose confidence in the security of our site or the use of the Internet and e-commerce in general. If third parties are able to penetrate our network security or otherwise misappropriate our customers' personal information or credit card information, or if we give third parties improper access to our customers' personal information or credit card information, we could be subject to liability. This liability could include claims for unauthorized purchases with credit card information, impersonation or other similar fraud claims or damages for alleged violations of state or federal laws governing security protocols for the safekeeping of customers' personal or credit card information. This liability could also include claims for other misuses of personal information, including unauthorized marketing purposes. These claims could result in litigation. Liability for misappropriation of this information could adversely affect our business.

Credit card fraud and our response to it could adversely affect our business.

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We routinely receive orders placed with fraudulent credit card data. We do not carry insurance against the risk of credit card fraud, so our failure to adequately control fraudulent credit card transactions could reduce our net revenues and our gross profit. We have implemented technology to help us detect and reject the fraudulent use of credit card information. However, we may in the future suffer losses as a result of orders placed with fraudulent credit card data even if the associated financial institution approved payment of the orders. Under current credit card practices, we may be liable for fraudulent credit card transactions because we do not obtain a cardholder's signature. If we are unable to detect or control credit card fraud, our liability for these transactions could harm our business, prospects, financial condition and results of operation. Further, to the extent that our efforts to prevent fraudulent orders result in our inadvertent refusal to fill legitimate orders, we would lose the benefit of legitimate potential sales and risk the alienation of legitimate customers.

Cyber-attacks affecting our suppliers, delivery services or other service providers could adversely affect us.

We depend on our fulfillment partners to provide a large portion of the product selection we offer and on vendors for the products we purchase and offer in our direct business. We also depend on delivery services to deliver products, and on other service providers, including suppliers of services which support Website operations, including payment systems, customer service support, and communications. Cyber-attacks affecting our delivery services or any of our most significant suppliers or affecting a significant number of our suppliers of products or services could have a material adverse effect on our business. The adverse effects could include our inability to source product or fulfill orders, our customers' or suppliers' inability to contact us or access our Website or call centers or chat lines, or the compromise of our customers' confidential data.

Natural disasters and geo-political events could adversely affect our business.

Natural disasters, including hurricanes, cyclones, typhoons, tropical storms, floods, earthquakes and tsunamis, weather conditions, including winter storms, droughts and tornados, whether as a result of climate change or otherwise, and geo-political events, including civil unrest or terrorist attacks, that affect us or our delivery services, suppliers, credit card processors or other service providers could adversely affect our business.

Our insurance coverage and indemnity rights may not adequately protect us against loss.

Although we maintain liability and other types of insurance, including but not limited to, property, workers compensation, general liability, product liability, and security and privacy breach insurance, we cannot be certain that the types, coverage, or the amounts of coverage we maintain will be adequate for losses actually incurred, or that the insurance will continue to be available to us on economically reasonable terms. Similarly, although we are indemnified by most of our suppliers and vendors for product liability for products they supply us, and we have indemnification agreements with software and hardware suppliers for losses we might incur as a result of the use of the technology products they supply, we are not indemnified by all our suppliers, nor can we be certain that our indemnification rights are enforceable or adequate to cover actual losses we may incur as a result of the sale or use of products our indemnitors provide to us. Actual losses for which we are not insured or indemnified, or which exceed our insurance coverage or the capacity of our indemnitors, could harm our business, prospects, financial condition and results of operations.

We may not be able to compete successfully against existing or future competitors.

The online retail market is rapidly evolving and intensely competitive. Barriers to entry are minimal, and current and new competitors can launch new websites at a relatively low cost. We currently compete with numerous competitors, including:

- liquidation e-tailers such as SmartBargains;
- online retailers with discount departments such as Amazon.com, Inc., eBay, Inc. and Rakuten.com, Inc. (formerly Buy.com, Inc.);
- private sale sites such as Rue La La and Gilt Groupe;
- online specialty retailers such as Bluefly, Inc., Blue Nile, Inc. and Zappos.com.; and
- traditional general merchandise and specialty retailers and liquidators such as Ross Stores, Inc., T.J. Maxx, Wal-Mart Stores, Inc., Costco Wholesale Corporation, J.C. Penny Company, Inc., Sears Holding Corporation, Target Corporation, Best Buy Co., Inc., Home Depot, Inc. and Barnes and Noble, Inc., all of which also have an online presence.

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We expect the online retail market to become even more competitive as traditional liquidators and online retailers continue to develop and improve services that compete with our services. In addition, more traditional manufacturers and retailers may continue to add or improve their e-commerce offerings. Traditional or online retailers may create proprietary, store-based distribution and returns channels. Competitive pressures, including the introduction of same-day delivery capabilities, from any of our competitors, many of whom have longer operating histories, larger customer bases, greater brand recognition and significantly greater financial, marketing and other resources than we do, could harm our business.

Further, as a strategic response to changes in the competitive environment, we may from time to time make competitive pricing, service, marketing or other decisions that could harm our business. For example, to the extent that we enter new lines of businesses such as third-party logistics, or discount brick and mortar retail, we would be competing with large established businesses such as APL Logistics and Ross Stores, Inc. In the past we have entered the online auctions, car listing and real estate listing businesses in which we compete or competed with large established businesses including eBay, Inc., AutoTrader.com, Inc. and Realtor.com. We no longer offer online auctions services or real estate listing services.

If one or more states successfully assert that we should collect sales or other taxes on the sale of our merchandise or the merchandise of third parties that we offer for sale on our Website, or that we should pay commercial activity taxes, our business could be harmed.

We do not currently collect sales or other similar taxes for physical shipments of goods into states where we have no duty to do so under federal court decisions construing applicable constitutional law. One or more local, state or foreign jurisdictions may seek to impose sales tax collection obligations on us because we are engaged in online commerce, even though to do so would be contrary to existing court decisions. The future location of our fulfillment or customer service centers networks, or any other operation, service contracts with third parties located in another state, channel distribution arrangements or other agreements with third party sellers, or any act that may be deemed by a state to have established a physical presence in states where we are not now present, may result in additional sales and other tax obligations. New York and other states have passed so-called “Internet affiliate advertising” statutes, which require a remote seller, with no physical presence in the state, to collect state sales tax if the remote seller contracted for advertising services with an Internet advertiser in that state. In New York and states passing similar laws, we have terminated our use of locally based Internet advertisers. Several other states currently have similar tax proposals under consideration. In a case that went up on appeal, an Illinois state court struck down on constitutional grounds a similar Illinois statute, and the Illinois Supreme Court has upheld that decision. If such laws survive constitutional challenge, we may elect to discontinue in those states valuable marketing through the use of affiliates based in those states, or may begin to collect taxes in those states. In either event, our business could be harmed. Further, our business could be harmed if one or more states or any foreign country successfully asserts that we should collect sales or other taxes on the sale of our merchandise.

The United States Senate passed the Marketplace Fairness Act (“MFA”) which if also passed by the United States House of Representatives and not vetoed, would permit states which comply with the requirements of the MFA to force remote sellers like us to collect taxes in states where we have no physical presence. We oppose MFA in its current form and if it becomes law our business could be harmed.

Other states have enacted forms of economic taxes to which we may be subject. In September 2009, we received a letter of determination from the Ohio Department of Taxation noting the Department’s determination that we are required to register for remitting of the Commercial Activity Tax, and that we owed $612,784 in taxes, interest, and penalties as of June 30, 2009. The Ohio Department of Taxation issued additional estimated assessments of estimated tax, interest and penalties totaling $170,322 as of September 30, 2013. We filed protests to challenge the Department’s

Assessments on constitutional grounds and the matter is currently pending before the Ohio Department of Taxation's Legal Division for administrative review and determination. The Division held a hearing on these matters November 18, 2011, but has not yet issued a ruling. Recently we reached an agreement in principle with the Ohio Department which would require our payment of a diminished amount of the estimated assessments, a reduction in interest and waiver of penalties. We are in the process of formalizing the agreement. If other states enact and commence enforcement of similar commercial activity tax laws, these could harm our business.

Several other states have enacted laws requiring remote vendors to notify resident purchasers in those states of their obligation to pay a use tax on their purchases and, in some instances, to report untaxed purchases to the state tax authorities. In Colorado, a federal court on constitutional grounds granted a preliminary injunction against the state's enforcement its tax-notice and reporting law. Colorado appealed, and the injunction was overturned on jurisdictional grounds. The case is in the process of being dismissed and the plaintiff in that action will likely re-file the case in state court. Other states have enacted similar legislation and more states may enact these laws. Such laws could harm our business by imposing unreasonable notice burdens upon us, by interposing burdensome transaction notices that negatively affect conversion, or by discouraging customer purchases by requiring detailed purchase reporting.

Economic pressure on states could harm our business.

The current economic climate has resulted in a sharp decline in state revenues, and states have projected large state budget shortfalls in the years ahead. These shortfalls require state legislatures and agencies to examine the means to increase state revenues. States may increase sales and use tax rates, create new tax laws covering previously untaxed activities, or increase existing license fees or create new fees all of which may directly or indirectly harm our business. Similarly, administrative agencies may apply more rigorous enforcement efforts or take inflexible positions respecting the laws they administer, especially if the laws permit the imposition of monetary penalties and fines which either the state or the administrative agency may use to balance their budgets. To the extent that states pass additional revenue measures, or significantly increase their enforcement efforts, these activities could directly or indirectly harm our business.

If we do not respond to rapid technological changes, our services could become obsolete and we could lose customers.

The Internet and the online commerce industry are changing rapidly. To remain competitive, we must continue to enhance and improve the functionality and features of our e-commerce businesses. If we fail to do so, we may lose customers. If competitors introduce new products or services using new technologies or if new industry standards and practices emerge, our Website and our proprietary technology and systems may become obsolete. Our failure to respond to technological change or to adequately maintain, upgrade and develop our computer network and the systems used to process customers' orders and payments could harm our business.

We have an evolving business model.

Our business model has evolved in the past and continues to do so. In prior years we have added additional types of services and product offerings and in some cases we have modified or discontinued those offerings. We may continue to try to offer additional types of products or services, and we cannot offer any assurance that any of them will be successful. From time to time we have also modified aspects of our business model relating to our product mix and the mix of direct/fulfillment partner sourcing of the products we offer. We may continue to modify this aspect of our business as well as other significant aspects of our business. We cannot offer any assurance that these or any other modifications will be successful or will not result in harm to the business. The additions and modifications to our business have increased the complexity of our business and placed significant strain on our management, personnel, operations, systems, technical performance, financial resources, and internal financial control and reporting functions. Future additions to or modifications of our business are likely to have similar effects. We may not be able to manage growth effectively, which could damage our reputation, limit our growth and negatively affect our operating results. Further, any new business or website we launch that is not favorably received by consumers could damage our reputation or the Overstock.com brand.

We are attempting to expand our international business, which may cause our business to become increasingly susceptible to numerous international business risks and challenges that could affect our profitability.

We sell products in international markets, and in the future we may expand into these markets more aggressively. International sales and transactions are subject to inherent risks and challenges that could adversely affect our profitability, including:

- the need to develop new supplier and manufacturer relationships;

- the need to comply with additional U.S. and foreign laws and regulations to the extent applicable, including but not limited to, restrictions on advertising practices, regulations governing online services, restrictions on importation of specified or proscribed items, importation quotas, consumer protection laws, enforcement of intellectual property rights, laws dealing with consumer and data protection, privacy, encryption, and restrictions on pricing or discounts;

- changes in international laws, regulatory requirements, taxes and tariffs; and

- geopolitical events, such as war and terrorist attacks.

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To the extent we generate international sales transactions in the future, any negative impact on our international operations could negatively impact our business. To date, most of our international sales have been denominated in U.S. dollars, and we have not had significant foreign currency risk on those sales. However, in the future, gains and losses on the conversion of foreign payments into U. S. dollars may contribute to fluctuations in our results of operations and fluctuating exchange rates could cause reduced gross revenues and/or gross profit percentages from non-dollar-denominated international sales. Additionally, penalties for non-compliance with laws applicable to international business and trade, such as the U.S. Foreign Corrupt Practices Act, could negatively impact our business.

Our foreign brand domain name may cause confusion.

In July 2010, we undertook an effort to associate our brand globally with the domain address: www.O.co. We did this in part because in many foreign markets the word “Overstock” lacked a good foreign cognate. Following a period of testing for the O.co brand and domain address, we returned to the Overstock.com name as our primary brand domestically because domestic consumer acceptance did not occur as quickly as we had hoped. While we have returned domestically to the Overstock.com brand and principal domain address, there is no assurance that the use of Overstock.com or O.co will gain acceptance or have success in foreign markets.

We may incur substantial indebtedness.

At September 30, 2013, we had no indebtedness for borrowed money, and our only credit facility was a $3 million facility for the issuance of letters of credit. Although we have reduced our indebtedness substantially over the last several years, in the future we may again incur substantial indebtedness. Any such indebtedness would increase our business risks, including our vulnerability to industry downturns and competitive pressures. Further, financing may not be available to us on acceptable terms, or at all.

Existing or future government regulation could harm our business.

We are subject to regulation at the federal, state and international levels, including regulation relating to privacy, security, retention, transfer and use of personal user information and telemarketing laws. Increasing regulation, along with increased governmental or private enforcement, may increase the cost of our business. Compliance with existing and new privacy and security laws may be difficult and costly and may further restrict our ability to collect demographic and personal information from users, which could harm our marketing efforts, and could require us to implement new and potentially costly processes, procedures and/or protective measures. The expansion of these and other laws, both in terms of their number and their applicability to the Internet could also harm our business. Many laws, adopted prior to the advent of the Internet, do not contemplate or address the unique issues raised thereby. Consequently, courts or regulators may apply these laws to Internet commerce in ways that may present difficult or impossible compliance challenges. Many of those laws that do reference the Internet are still being interpreted by the courts and their applicability and reach are therefore uncertain. Moreover, Internet advances and innovations may result in new questions about the applicability and reach of these laws. Additionally, laws governing the permissible contents of products may adversely affect us, and we are subject to federal and state consumer laws, including those governing advertising, product labeling, product content requirements and product safety, and mandated website disclosures about programs to eliminate abusive labor practices in our supply chain. The laws not only apply to future manufacture of consumer product, but also apply to existing inventories and may cause us to incur losses for any non-compliant items in our inventory, or which we may have sold which may subject us to regulatory or civil actions. Some of the products we sell or manufacture may, under statutory or common law, from time to time expose us to claims related to personal injury, death, environmental or property damage and may from time to time require product recalls or other actions which may not be covered, in whole or in part, by our liability insurance. These current and future laws and regulations could harm our business, prospects, financial condition and results of operation.

General economic factors may adversely affect our financial performance.

General economic conditions may adversely affect our financial performance. In the United States, changes in interest rates, changes in fuel and other energy costs, weakness in the housing market, inflation or deflation or expectations of either inflation or deflation, higher levels of unemployment, unavailability or limitations of consumer credit, higher consumer debt levels or efforts by consumers to reduce debt levels, higher tax rates and other changes in tax laws, overall economic slowdown, changes in consumer desires affecting demand for the products and services we sell and other economic factors could adversely affect consumer demand for the products and services we sell, change the mix of products we sell to a mix with a lower average gross margin and result in slower inventory turnover and greater markdowns on inventory. Higher interest rates, transportation costs, inflation, higher costs of labor, insurance and healthcare, foreign exchange rates fluctuations, higher tax rates and other changes in tax laws, changes in other laws and regulations and other economic factors in the United States can increase our cost of sales and operating, selling, general and administrative expenses, and otherwise adversely affect our operations and operating results. These factors affect not only our operations, but also the operations of suppliers from whom we purchase goods, a condition that can result in an increase in the cost to us of the goods and services we sell.

Decreases in discretionary consumer spending may have an adverse effect on us.

A substantial portion of the products and services we offer are products or services that consumers may view as discretionary items rather than necessities. As a result, our results of operations are sensitive to changes in macro-economic conditions that impact consumer spending, including discretionary spending. Difficult macro-economic conditions, particularly high levels of unemployment, also impact our customers' ability to obtain consumer credit. Other factors, including consumer confidence, employment levels, interest rates, tax rates, consumer debt levels, and fuel and energy costs could reduce consumer spending or change consumer purchasing habits. Slowdowns in the U.S. or global economy, or an uncertain economic outlook, could materially adversely affect consumer spending habits and our operating results.

We may need to implement additional finance and accounting systems, procedures and controls as we grow our business and organization and to satisfy new reporting requirements.

We are required to comply with a variety of reporting, accounting and other rules and regulations. Compliance with existing requirements is expensive. Further requirements may increase our costs and require additional management time and resources. We may need to implement additional finance and accounting systems, procedures and controls to satisfy our reporting requirements. If our internal control over financial reporting is determined to be ineffective, such failure could cause investors to lose confidence in our reported financial information, negatively affect the market price of our common stock, subject us to regulatory investigations and penalties, and adversely impact our business and financial condition.

Changes in accounting standards and subjective assumptions, estimates and judgments by management related to complex accounting matters could significantly affect our financial results.

Generally accepted accounting principles and related accounting pronouncements, implementation guidelines and interpretations with regard to a wide range of matters that are relevant to our business, including but not limited to revenue recognition, estimating valuation allowances and accrued liabilities (including allowances for returns, credit card chargebacks, doubtful accounts and obsolete and damaged inventory), internal use software and website development (acquired and developed internally), accounting for income taxes, valuation of long-lived and intangible assets and goodwill, stock-based compensation and loss contingencies, are highly complex and involve many subjective assumptions, estimates and judgments by our management. Changes in these rules or their interpretation or changes in underlying assumptions, estimates or judgments by our management could significantly change our reported or expected financial performance.

We face risks relating to our inventory.

In our direct business, we sell merchandise that we have purchased and hold in inventory. 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, rapid technological change, obsolescence and price erosion and because we sometimes make large purchases of particular types of inventory. Subject to our returns policies, we accept returns of products sold through our fulfillment partners and we have the risk of reselling the returned products. In the past we have recorded charges for obsolete inventory and have had to sell certain merchandise at a discount or loss. To the extent that we rely on purchased 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. Further, we purchase some of our inventory from foreign suppliers and pay for inventory with U.S. dollars. If the dollar weakens with respect to foreign currencies, foreign suppliers may require us to pay higher prices for products, which could negatively affect our profit margins.

If we do not successfully optimize and operate our warehouse and customer service operations, our business could be harmed.

We have expanded, contracted and otherwise modified our warehouse and customer service operations from time to time in the past, and expect that we will continue to do so. If we do not successfully optimize and operate our warehouse and customer service operations, it could significantly limit our ability to meet customer demand, customer shipping or return time expectations, or result in excessive costs and expenses for the size of our business. Because it is difficult to predict demand, we may not manage our facilities in an optimal way, which may result in excess or insufficient inventory or warehousing capacity. We may also fail to staff our fulfillment and customer service centers at optimal levels. Our failure to do so could negatively impact our operating results and customer experience.

Our cash, cash equivalents, investments in precious metals and short-term investments are subject to a risk of loss based upon the solvency of the financial institutions in which they are maintained.

We maintain the majority of our cash, cash equivalents and short-term investments in accounts with a small number of major financial institutions within the United States, in the form of demand deposits, money market accounts, time deposits, U.S. Treasury Bills and other short-term investments. Our deposits in these institutions generally exceed the amounts of insurance provided, and some deposits may not be covered by insurance at all. We keep our precious metals in a third party facility that we believe to be secure. If any of these institutions were to become insolvent, we could lose some, or all, of such deposits, which would have a material adverse effect on our financial condition.

We may be adversely affected by fluctuations in precious metal prices.

At September 30, 2013 our investments in precious metals was $8.6 million. Our financial results may be adversely affected by declines in the price of precious metals. The prices of precious metals may fluctuate widely and are affected by numerous factors beyond our control such as interest rates, exchange rates, inflation or deflation, fluctuation in the value of the United States dollar and foreign currencies, global and regional supply and demand, and the political and economic conditions of mineral producing countries throughout the world.

If we fail to accurately forecast our expenses and revenues, our business, prospects, financial condition and results of operations may suffer and the price of our securities may decline.

The rapidly evolving nature of our industry and the constantly evolving nature of our business, make forecasting operating results difficult. Since 2005, we have completed several large, complex and expensive infrastructure upgrades in order to increase our ability to handle larger volumes of sales and to develop or increase our ability to perform a variety of analytical procedures relating to our business. We are continuing to upgrade and further expand these and other components of our infrastructure. In the past, we have experienced difficulties with upgrades of our infrastructure, and have incurred increased expenses as a result of these difficulties. As a result of these expenditures on our infrastructure, our ability to reduce spending is limited. Therefore, any significant shortfall in the revenues for which we have built and are continuing to build our infrastructure would likely harm our business.

The seasonality of our business places increased strain on our operations.

A disproportionate amount of our sales normally occur during our fourth quarter. If we do not stock or are otherwise unable to source products sufficient to meet customer demand, our business would be adversely affected. If we liquidate products, as we have in the past, we may be required to take significant inventory markdowns or write-offs, which could reduce gross profits. We may experience an increase in our net shipping cost due to complimentary upgrades, split-shipments, and additional long-zone shipments necessary to ensure timely delivery for the holiday season. If too many customers access our Website within a short period of time due to increased holiday demand, we may experience system interruptions that make our Website unavailable or prevent us from efficiently fulfilling orders, which may reduce the volume of goods we sell and the attractiveness of our products and services. In addition, we may be unable to adequately staff our fulfillment and customer service centers during peak periods, and delivery services and other fulfillment companies and customer service providers may be unable to meet the seasonal demand.

Significant merchandise returns could harm our business.

We allow our customers to return products, subject to our returns policies. If merchandise returns are significant, our business, prospects, financial condition and results of operations could be harmed. Further, we modify our policies relating to returns from time to time and any policies intended to reduce the number of product returns may result in customer dissatisfaction and fewer repeat customers.

Our pricing strategy may not meet customers' price expectations or result in net income.

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Demand for our products is generally highly sensitive to price. Our pricing strategies have had, and may continue to have, a significant impact on our net sales and net income. We often offer discounted prices, and free or discounted shipping as a means of attracting customers and encouraging repeat purchases. Such offers and discounts reduce our margins. In addition, our competitors' pricing and marketing strategies are beyond our control and can significantly impact the results of our pricing strategies. If we fail to meet our customers' price expectations, or if we are unable to compete effectively with our competitors when they engage in aggressive pricing strategies or other competitive activities, our business would suffer.

If the products that we offer on our Website do not reflect our customers' tastes and preferences, our sales and profit margins would decrease.

Our success depends in part on our ability to offer products that reflect consumers' tastes and preferences. Consumers' tastes are subject to frequent, significant and sometimes unpredictable changes. Because some of the products that we sell consist of manufacturers' and retailers' excess inventory, we have limited control over some of the products that we are able to offer for sale. If our merchandise fails to satisfy customers' tastes or respond to changes in customer preferences, our sales could suffer and we could be required to mark down unsold inventory, as we have in the past, which would depress our profit margins. In addition, any failure to offer products in line with customers' preferences could allow our competitors to gain market share. This could have an adverse effect on our business.

The loss of key personnel or any inability to attract and retain additional personnel could affect our ability to successfully grow our business.

Our performance is substantially dependent on the continued services and on the performance of our senior management and other key personnel. Our performance also depends on our ability to retain and motivate our officers and key employees. The loss of the services of any of our executive officers or other key employees for any reason could harm our business. Occasionally, members of senior management or key employees may find it necessary to take a leave of absence due to medical or other causes. On February 12, 2013 we announced that our Chief Executive Officer and Chairman of the Board, Dr. Patrick M. Byrne, was taking a personal leave of absence for medical reasons. On April, 15, 2013, we announced that Dr. Patrick M. Byrne had resumed his duties as Chief Executive Officer. Leaves of absence for temporary or extended periods may harm our business. We do not have employment agreements with any of our key personnel and we do not maintain "key person" life insurance policies. Our future success also depends on our ability to identify, attract, hire, train, retain and motivate other highly-skilled technical, managerial, editorial, merchandising, marketing and customer service personnel. Competition for such personnel is intense. Our failure to retain and attract the necessary technical, managerial, editorial, merchandising, marketing, and customer service personnel could harm our business.

In order to obtain future revenue growth and sustain profitability, we will have to attract and retain customers on cost-effective terms.

Our success depends on our ability to attract and retain customers on cost-effective terms. We have relationships with online services, search engines, affiliate marketing websites, directories and other website and e-commerce businesses to provide content, advertising banners and other links that direct customers to our Website. We rely on these relationships as significant sources of traffic to our Website and to generate new customers. In the past we have terminated affiliate marketing websites as a result of efforts by certain states to require us to collect sales taxes based on the presence of those third party Internet advertising affiliates in those states, and we are likely to do so again in the future if necessary. If we are unable to develop or maintain these relationships on acceptable terms, our ability to attract new customers and our financial condition would suffer. In addition, certain of our online marketing agreements may require us to pay upfront fees and make other payments prior to the realization of the sales, if any, associated with those payments. Current or future relationships or agreements may fail to produce the sales that we anticipate. We periodically conduct national television and radio branding and advertising campaigns. Such campaigns are expensive and may not result in the cost-effective acquisition of customers.

We may be unable to protect our proprietary technology or keep up with that of our competitors.

Our success depends to a significant degree upon the protection of our software and other proprietary intellectual property rights. We may be unable to deter misappropriation of our proprietary information, detect unauthorized use or take appropriate steps to enforce our intellectual property rights. In addition, our competitors may now have or may in the future develop technologies that are as good as or better than our technology without violating our proprietary rights. Our failure to protect our software and other proprietary intellectual property rights or to utilize technologies that are as good as our competitors' could put us at a disadvantage to our competitors. In addition, the failure of the third parties whose products we offer for sale on our Website to protect their intellectual property rights, including their domain names, could impair our operations. These failures could harm our business.

We may not be able to obtain trademark protection for our marks, which could impede our efforts to build brand identity.

We have filed trademark applications with the Patent and Trademark Office seeking registration of certain service marks and trademarks. There can be no assurance that our applications will be successful or that we will be able to secure significant protection for our service marks or trademarks in the United States or elsewhere as we expand internationally. Our competitors or others could adopt product or service marks similar to our marks, or try to prevent us from using our marks, thereby impeding our ability to build brand identity and possibly leading to customer confusion. Any claim by another party against us or customer confusion related to our trademarks, or our failure to obtain trademark registration, could harm our business.

We may not be able to enforce protection of our intellectual property rights under the laws of other countries.

We sell products internationally and consequently we are subject to risks of doing business internationally as related to our intellectual property, including:

· legal uncertainty regarding liability for the listings and other content provided by our users, including uncertainty as a result of less Internet-friendly legal systems, unique local laws, and lack of clear precedent or applicable law; and

· differing intellectual property laws, which may provide insufficient protection for our intellectual property.

We may be accused of infringing intellectual property rights of third parties.

Other parties have claimed and may claim that we infringe their intellectual property rights. We have been and are subject to, and expect to continue to be subject to, legal claims of alleged infringement of the intellectual property rights of third parties. The ready availability of damages, royalties and the potential for injunctive relief has increased the defense litigation costs of patent infringement claims, especially those asserted by third parties whose sole or primary business is to assert such claims. Such claims, even if not meritorious, may result in significant expenditure of financial and managerial resources, and the payment of damages or settlement amounts. Additionally, we may become subject to injunctions prohibiting us from using software or business processes we currently use or may need to use in the future, or requiring us to obtain licenses from third parties when such licenses may not be available on financially feasible terms or terms acceptable to us or at all. In addition, we may not be able to obtain on favorable terms, or at all, licenses or other rights with respect to intellectual property we do not own in providing e-commerce services to other businesses and individuals under commercial agreements.

Our business and reputation may be harmed by the offering or sale of pirated, counterfeit or illegal items by third parties, and by intellectual property litigation.

We have received in the past, and we anticipate we will receive in the future, communications alleging that items offered or sold through our Website infringe third-party copyrights, trademarks and trade names or other intellectual property rights or that we have otherwise infringed third parties' past, current or future intellectual property rights. We may be unable to prevent third parties from offering and selling unlawful goods, and we may be subject to allegations of civil or criminal liability for unlawful activities carried out by third parties through our Website. We may implement measures in an effort to protect against these potential liabilities that could require us to spend substantial resources and/or to reduce revenues by discontinuing certain service offerings. Any costs incurred as a result of liability or asserted liability relating to the sale of unlawful goods or the unlawful sale of goods could harm our business. Resolving litigation or claims regarding patents or other intellectual property, whether meritorious or not, could be costly, time-consuming, cause service delays, divert our management and key personnel from our business operations, require expensive or unwanted changes in our methods of doing business or require us to enter into costly royalty or licensing agreements, if available. As a result, these claims could harm our business. Negative publicity generated as a result of the foregoing could damage our reputation, harm our business and diminish the value of our brand name.

Use of social media may adversely impact our reputation.

There has been a marked increase in use of social media platforms and similar devices, including weblogs (blogs), social media websites, and other forms of Internet-based communications which allow individual access to a broad audience of consumers and other interested persons. Consumers value readily available information concerning retailers, manufacturers, and their goods and services and often act on such information without further investigation, authentication and without regard to its accuracy. The availability of information on social media platforms and devices is virtually immediate as is its impact. Social media platforms and devices immediately publish the content their subscribers and participants post, often without filters or checks on accuracy of the content posted. The opportunity for dissemination of information, including inaccurate information, is virtually limitless. Information concerning or affecting us may be posted on such platforms and devices at any time. Information posted may be inaccurate and adverse to us, and it may harm our business. The harm may be immediate without affording us an opportunity for redress or correction. Such platforms also could be used for the dissemination of trade secret information or compromise of other valuable company assets, any of which could harm our business.

Our car listing service may be subject to a variety of regulatory requirements and risks.

Many states and other jurisdictions, including Utah, where we are located, have regulations governing the conduct of car sellers and public advertisement for car sales. Generally, these regulations govern the conduct of those sellers advertising their automobiles for sale and are not directly applicable to those providing the medium through which the advertisement is made available to the public. Sellers are often subject to regulations in the nature of “truth in advertising laws.” We have no ability to know whether the information sellers provide is correct. While our site terms and conditions of usage prohibit unlawful acts, we cannot assure that sellers will comply with all laws and regulations applicable to them and their transactions. The application of these regulations to online car listing service providers is not clear. Although we do not expect these laws to have a significant effect on our listing service, we will incur costs in complying with these laws, and we may from time to time be required to make changes in our service that may increase our costs, reduce our revenues, cause us to prohibit certain listing or advertising practices, or make other changes that may adversely affect our car listing service. Further, like our shopping business, our car listing service is subject to most of the same laws and regulations that apply to other companies conducting business on and off the Internet. To the extent that current or future laws or regulations prevent users from selling items on our car listing site, they could harm our business. In addition, any negative publicity we receive regarding any allegations of unlawful or deceptive conduct may damage our reputation, our ability to attract new customers to our main shopping site, and the Overstock.com brand name generally.

We are involved in substantial litigation.

From time to time we receive claims of and become subject to consumer protection, employment, intellectual property and other commercial litigation related to the conduct and operation of our business and the sale of products on our Website. In connection with such litigation, we may be subject to significant damages or equitable remedies. In addition, we have in the past been, are now, and in the future may be, involved in substantial litigation in which we are the plaintiff, including litigation regarding the constitutionality of certain state tax laws, and the prime broker litigation described below. Any of such litigation, whether as plaintiff or defendant, could be costly and time consuming and could divert management and key personnel from our regular business operations. We do not currently believe that any of our outstanding litigation will have a material adverse effect on our business, prospects, financial condition or results of operations. However, due to the uncertainty of litigation and depending on the amount and the timing, an unfavorable resolution of some or all of these matters could materially affect our business, prospects, financial condition and results of operations.

California District Attorneys have sued us for alleged violations of California law.

In April 2008, we received a letter from the Office of the District Attorney of Marin County, California, stating that the District Attorneys of Marin and four other counties in Northern California had begun an investigation into the way we advertise products for sale. In November 2010, District Attorneys for the California Counties of Alameda, Marin, Monterey, Napa, Santa Clara, Shasta and Sonoma filed a lawsuit seeking damages and an injunction, alleging violations of California consumer protection laws, alleging we made untrue or misleading statements concerning our pricing, price reductions, sources of products and shipping charges. The complaint asked for damages in the amount of not less than $15 million. We disputed the allegations and tried the case to the Judge of the court in September 2013. Both the District Attorneys and our legal counsel are briefing final arguments. We do not expect a verdict in the case for several months. We intend to continue to defend ourselves vigorously. However, an unfavorable resolution of this matter could materially affect our business, prospects, financial condition and results of operations.

Our prime broker litigation may have an adverse effect on our business and financial condition.

We remain involved in substantial litigation against Goldman Sachs Group, Inc., Goldman Sachs & Co., Goldman Sachs Execution & Clearing L.P., Merrill Lynch, Pierce, Fenner & Smith, Inc., and Merrill Lynch Professional Clearing

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Corporation, and the use of management's time and attention in connection with the litigation and related matters may reduce the time management is able to spend on other aspects of our business, which may have adverse effects on other aspects of our business. To the extent that any such adverse effects exceed any benefits we may realize from the litigation, it could harm our business, prospects, financial condition and results of operation.

Public statements we or our chairman of the board of directors, Patrick M. Byrne, have made or may make in the future may antagonize regulatory officials or others.

We and our chairman of the board of directors, Patrick M. Byrne, have from time to time made public statements regarding our or his beliefs about matters of public interest, including statements regarding naked short selling and regulatory capture. Some of those public statements have been critical of the Securities and Exchange Commission and other regulatory agencies. These public statements may have consequences for us, whether as a result of increased regulatory scrutiny or otherwise.

The price of our securities may be volatile and you may lose all or a part of your investment.

The market price of our common stock historically has been subject to significant fluctuations. These fluctuations could continue. It is possible that in future periods our results of operations may be below the expectations of public market analysts and investors. If this occurs, the market price of our securities may decline.

Our quarterly operating results are volatile and may adversely affect the market price of our securities.

Our future revenues and operating results have varied in the past and may continue to vary significantly from quarter to quarter due to a number of factors, many of which are outside our control, and any of which could harm our business. As a result, we believe that quarterly comparisons of our operating results are not necessarily meaningful and that you should not rely on the results of one quarter as an indication of our future performance. In addition to the other risk factors described in this report, additional factors that have caused and/or could cause our quarterly operating results to fluctuate and in turn affect the market price of our securities include:

- increases in the cost of advertising and changes in our sales and marketing expenditures;

- our inability to retain existing customers or encourage repeat purchases;

- the extent to which our existing and future marketing campaigns are successful;

- price competition that results in lower profit margins or losses;

- the amount and timing of operating costs and capital expenditures relating to the expansion of our business operations and infrastructure;

- the amount and timing of our purchases of inventory;

- our inability to manage distribution operations or provide adequate levels of customer service;

- increases in the cost of fuel and transportation;

- our ability to successfully integrate operations and technologies from acquisitions or other business combinations;

· our efforts to offer new lines of products and services; and

· our ability to attract users to our shopping and other sites.

Our operating results may fluctuate depending on the season, and such fluctuations may affect the market price of our securities.

We have experienced and expect to continue to experience fluctuations in our operating results because of seasonal fluctuations in traditional retail patterns. Sales in the retail and wholesale industry tend to be significantly higher in the fourth calendar quarter of each year than in the preceding three quarters due primarily to increased shopping activity during the holiday season. However, there can be no assurance that our sales in the fourth quarter will exceed those of the preceding quarters or, if the fourth quarter sales do exceed those of the preceding quarters, that we will be able to manage the increased sales effectively. Further, we generally increase our inventories substantially in anticipation of holiday season shopping activity, which has a negative effect on our cash flow. Securities analysts and investors may inaccurately estimate the effects of seasonality on our results of operations in one or more future quarters and, consequently, our operating results may fall below expectations, causing the market price of our securities to decline.

Sales by our significant stockholders could have an adverse effect on the market price of our stock.

Several of our stockholders own significant portions of our common stock. If one or more of stockholders were to sell all or a portion of their holdings of our common stock, the market price of our common stock could be negatively impacted. The effect of such sales, or of significant portions of our stock being offered or made available for sale, could result in strong downward pressure on our stock price. Investors should be aware that they could experience significant short-term volatility in our stock if such stockholders decide to sell all or a portion of their holdings of our common stock at once or within a short period of time. In addition, the transfer of ownership of 50% or more of our outstanding shares within a three year period could adversely affect our ability to use our net operating losses to offset future taxable net income.

We do not intend to pay dividends on our common stock and you may lose the entire amount of your investment in our common stock.

We have never declared or paid any cash dividends on our common stock and do not intend to pay dividends on our common stock for the foreseeable future. We intend to invest our future earnings, if any, to fund our growth. Therefore, you will not receive any funds without selling your shares. We cannot assure that you will receive a positive return on your investment when you sell your shares or that you will not lose the entire amount of your investment.

Our Amended and Restated Certificate of Incorporation, Amended and Restated Bylaws and the Delaware General Corporation Law contain anti-takeover provisions which could discourage or prevent a takeover, even if an acquisition would be beneficial to our stockholders.

Several provisions of our Amended and Restated Certificate of Incorporation and Amended and Restated Bylaws could discourage potential acquisition proposals and could delay or prevent a change in control of our company even if that change in control would be beneficial to our stockholders. For example, only one-third of our board of directors is elected at each of our annual meetings of stockholders, which will make it more difficult for a potential acquirer to change the management of our company, even after acquiring a majority of the shares of our common stock. These provisions, which cannot be amended without the approval of two-thirds of our stockholders, could diminish the opportunities for a stockholder to participate in tender offers, including tender offers at a price above the then current market value of our common stock. In addition, our board of directors, without further stockholder approval, may issue preferred stock, with such terms as the board of directors may determine, that could have the effect of delaying or preventing a change in control of our company. The issuance of preferred stock could also adversely affect the voting powers of the holders of common stock, including the loss of voting control to others. We are also afforded the protections of Section 203 of the Delaware General Corporation Law, which could delay or prevent a change in control of our company or could impede a merger, consolidation, takeover or other business combination involving our company or discourage a potential acquirer from making a tender offer or otherwise attempting to obtain control of our company.

The price of our stock may be vulnerable to manipulation.

We filed an unfair business practice lawsuit against Morgan Stanley & Co. Incorporated, Goldman Sachs & Co., Bear Stearns Companies, Inc., Bank of America Securities LLC, Bank of New York, Citigroup Inc., Credit Suisse (USA) Inc., Deutsche Bank Securities, Inc., Merrill Lynch, Pierce, Fenner & Smith, Inc., and UBS Financial Services, Inc., and settled the case with respect to all defendants except Goldman Sachs Group, Inc., Goldman Sachs & Co., Goldman Sachs Execution & Clearing L.P.; Merrill Lynch, Pierce, Fenner & Smith, Inc., and Merrill Lynch Professional Clearing Corporation. In January 2012, the trial court granted the remaining defendants’ motion for summary judgment. We have appealed the ruling.

We believe these remaining defendants engaged in unlawful actions and have caused substantial harm to Overstock, and that certain of the defendants have made efforts to drive the market price of Overstock’s common stock down. To the extent that the defendants or other persons engage in any such actions or take any other actions to interfere with or destroy or harm Overstock’s existing and/or prospective business relationships with its suppliers, bankers, customers, lenders, investors, prospective investors or others, our business, prospects, financial condition and results of operation could be harmed, and the price of our common stock may be more volatile than it might otherwise be and/or may trade at prices below those that might prevail in the absence of any such efforts. The practice of "abusive naked short selling" continues to place our stock at risk for manipulative attacks by large investment pools and prime brokers.

Abusive naked short selling is the practice by which short sellers place large short sell orders for shares without first borrowing the shares to be sold, or without having first adequately located such shares and arranged for a firm contract to borrow such shares prior to the delivery date set to close the sale. While selling broker dealers are by rule required to deliver shares to close a transaction by a certain date, and while purchasing broker-dealers are obligated by rule to purchase the sold quantity of shares when they are not delivered to close the sale, these rules are often ignored. Abusive naked short selling has a depressive effect on share prices when it is allowed to persist because the economic effect of abusive naked short selling is the oversupply of counterfeit stock to the market. We believe the regulations designed to address this abusive practice are both inadequately structured and inadequately enforced. Consequently, we believe that without the enactment of adequate regulations and the enforcement necessary to curb these abuses, the manipulations achieved through abusive naked short selling are likely to continue. We believe that our stock has been subject to these abusive practices by those attempting to manipulate its price downward. To the extent that our stock is subject to these practices in the future, our stock may be more volatile than it might otherwise be and/or may trade at prices below those that might prevail in the absence of such abuses.

In the past, our stock has consistently been on the Regulation SHO threshold list.

Regulation SHO requires the stock exchanges to publish daily a list of companies whose stock has failures-to-deliver above a certain threshold. It also requires mandatory close-outs for open fail-to-deliver positions in threshold securities persisting for over 13 days, with the aim that no security would appear on the threshold for any extended period. Despite that aim, our common stock has frequently appeared on the Regulation SHO threshold list for extended and continuous periods and, while we do not currently appear on the Regulation SHO threshold list, in the past our stock has been on the list for more trading days than any other company.

Any investment in our securities involves a high degree of risk. Investors should consider carefully the risks and uncertainties described above, and all other information in this Form 10-Q and in any reports we file with the SEC after we file this Form 10-Q, before deciding whether to purchase or hold our securities. Additional risks and uncertainties not currently known to us or that we currently deem immaterial may also become important factors that may harm our business. The occurrence of any of the risks described in this Form 10-Q could harm our business. The trading price of our securities could decline due to any of these risks and uncertainties, and investors may lose part or all of their investment.

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

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

None.

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ITEM 6. EXHIBITS

(a) Exhibits

3.1	Amended and Restated Bylaws of Overstock.com, Inc., as amended through October 23, 2013 (incorporated by reference to exhibit 3.1 to our Report on Form 8-K filed on October 24, 2013 (File No. 000-49799).
31.1	Exhibit 31.1 Certification of Chief Executive Officer
31.2	Exhibit 31.2 Certification of Chief Financial Officer
32.1	Exhibit 32.1 Section 1350 Certification of Chief Executive Officer
32.2	Exhibit 32.2 Section 1350 Certification of Chief Financial Officer
101	The following financial information from our Quarterly Report on Form 10-Q for the third quarter of 2013, filed with the SEC on October 24, 2013, formatted in Extensible Business Reporting Language ("XBRL"): (i) the Consolidated Balance Sheets, (ii) Consolidated Statements of Income and Comprehensive Income (iii) Consolidated Statements of Cash Flows, (iv) Consolidated Statements of Stockholders' Equity, and (v) Notes to Consolidated Financial Statements.(1)

(1) Pursuant to Rule 406T of Regulation S-T, these interactive data files are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933 or Section 18 of the Securities Act of 1934 and otherwise are not subject to liability under these sections.

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SIGNATURE

Pursuant to the requirements 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.

Date: October 24, 2013	OVERSTOCK.COM, INC.
	/s/ ROBERT P. HUGHES Robert P. Hughes Senior Vice President, Finance and Risk Management