

OVERSTOCK.COM, INC
Form 10-K/A
March 05, 2009

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**
Washington, D.C. 20549

FORM 10-K/A

Amendment No. 1

(Mark
One)

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

For the fiscal year ended December 31, 2008

OR

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

For the transition period from _____ **to** _____
Commission file number 000-49799

OVERSTOCK.COM, INC.

(Exact name of Registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

87-0634302
(I.R.S. Employer
Identification Number)

6350 South 3000 East
Salt Lake City, Utah 84121
(Address of principal executive offices including zip code)

(801) 947-3100
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act: **Common Stock, \$0.0001 par value (title of class)**

Securities registered pursuant to Section 12(g) of the Act: **None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☐ No ☒

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Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ☐ No ☒

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K/A, or any amendment to this Form 10-K/A. ☐

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 "accelerated filer", "large accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ☐	Accelerated filer ☒	Non-accelerated filer ☐ (do not check if a smaller reporting company)	Smaller reporting company ☐
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Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the act). Yes ☐ No ☒

The aggregate market value of voting and non-voting common equity held by non-affiliates of the registrant as of the last business day of the registrant's most recently completed second quarter (June 30, 2008), was approximately \$245.5 million based upon the last sales price reported by NASDAQ. For purposes of this disclosure, shares of Common Stock held by persons who hold more than 5% of the outstanding shares of Common Stock and shares held by officers and directors of the registrant have been excluded in that such persons may be deemed to be affiliates. This determination is not necessarily conclusive.

As of February 23, 2009 there were 22,813,812 shares of the registrant's Common Stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Certain information required by Part III of Form 10-K/A is incorporated by reference to the Registrant's proxy statement for the 2009 Annual Stockholders Meeting, which will be filed with the Securities and Exchange Commission within 120 days after the end of the fiscal year to which this Report relates.

EXPLANATORY NOTE

Overstock.com, Inc. is filing this Amendment No. 1 to its Form 10-K for the fiscal year ended December 31, 2008 (the "Form 10-K"), originally filed with the Securities and Exchange Commission on February 23, 2009, for the purpose of correcting the following typographical errors:

In the table of Quarterly Results of Operations (unaudited), appearing in Item 7, we have corrected "Fulfillment partner revenue" for the quarterly period ended June 30, 2008 to read \$149,004 (in thousands) rather than \$149,044 (in thousands) as originally reported;

In the table of Contractual Obligations appearing in Item 7, we have corrected the "Total contractual cash obligations" for 2009 to total \$17,096 (in thousands) rather than \$17,906 (in thousands) as originally reported;

In the Consolidated Balance Sheets appearing in Item 15, we have corrected "Total liabilities" for 2007 to total \$212,931 (in thousands) rather than \$212,913 (in thousands) as originally reported;

In the Consolidated Statements of Cash Flows appearing in Item 15, we have corrected "Less change in cash and cash equivalents from discontinued operations" for 2006 to be a positive \$1,016 (in thousands) rather than a negative \$(1,016) (in thousands) as originally reported.

In Schedule II, "Valuation and Qualifying Accounts" in Item 15, we have corrected "Deductions" for "Allowance for doubtful accounts" for 2007 to be \$855 (in thousands) rather than \$0 as originally reported and we have corrected "Allowance for sales returns" for 2008 to total \$5,098 (in thousands) rather than \$5,099 (in thousands) as originally reported.

We are also refiling exhibit 10.37, which was inadvertently filed in draft form, as well as updated certifications of our Chief Executive Officer and Chief Financial Officer required by Rules 13a-14(a) and 13a-14(b) under the Securities Exchange Act of 1934.

Except as described above, the information set forth in the Form 10-K/A has not been modified or updated in any way from the information included in the Form 10-K as originally filed.

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K/A 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. These statements include, but are not limited to, statements concerning:

the anticipated benefits and risks of our business relationships;

our ability to attract retail and business customers; our belief that we can attract customers in a cost-efficient manner; the ability of our online marketing campaigns to be a cost-effective method of attracting customers; our belief that we can internally develop cost-effective branding campaigns;

the anticipated benefits and risks associated with our business strategy;

our future operating results;

the anticipated size or trends of the market segments in which we compete and the anticipated competition in those markets;

potential government regulation;

our future capital requirements and our ability to satisfy our capital needs; the potential for additional issuances of our securities;

our future ability to repurchase or retire our publicly traded debt;

our expansion in international markets;

our plans to devote substantial resources to our sales and marketing teams;

our strategy to develop strategic business relationships with additional wholesalers and distributors; our belief that manufacturers will recognize us as an efficient liquidation solution;

our belief that current or future litigation will likely not have a material adverse effect on our business;

the results of upgrades to our infrastructure and the likelihood that additional future upgrades can be implemented without disruption of our business;

our belief that we can meet our published product shipping standards even during periods of relatively high sales activity;

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our belief that we can maintain or improve upon customer service levels that we and our customers consider acceptable;

our belief that our information technology infrastructure can and will support our operations and will not suffer significant downtime;

the potential effects of our facilities consolidation and restructuring program and of the various actions we have taken in connection with that program;

the possibility that we will relocate our corporate offices;

statements about our community site business and its anticipated functionality;

our belief that we can maintain inventory levels at appropriate levels despite the seasonal nature of our business; and

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our belief that we can successfully offer and sell a constantly changing mix of products and services.

Furthermore, 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. In evaluating these statements, you should specifically consider the risks outlined in this Form 10-K/A, including those described in 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.

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PART I

ITEM 1. BUSINESS

The following description of our business contains forward-looking statements relating to future events or our future financial or operating performance that involve risks and uncertainties, as set forth above under "Special Note Regarding Forward-Looking Statements." Our actual results could differ materially from those anticipated in these forward-looking statements as a result of certain factors, including those set forth in Section 1A under the heading "Risk Factors" and elsewhere in this Form 10-K/A.

We are an online closeout retailer offering discount brand name merchandise, including bed-and-bath goods, home décor, kitchenware, watches, jewelry, electronics and computers, sporting goods, apparel, and designer accessories, among other products. We also sell books, magazines, CDs, DVDs, and video games ("BMMG"). We also operate as a section on our Website an online auction site a marketplace for the buying and selling of goods and services as well as the section on our Website for listing cars and real estate for sale.

Our company, based in Salt Lake City, Utah, was founded in 1997, and we launched our first Website through which customers could purchase products 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, limited inventory products to our Website in order to create an atmosphere that encourages customers to visit frequently and purchase products before our inventory sells out. We offer approximately 201,000 products under multiple departments under the Shopping section of our Website, and offer approximately 450,000 additional media products in the Books etc. department on our Website.

Closeout merchandise is typically available in inconsistent quantities and prices and often is only available to consumers after it has been purchased and resold by disparate liquidation wholesalers. We believe that the traditional liquidation market is therefore characterized by fragmented supply and fragmented demand. We utilize the Internet to aggregate this fragmented supply and demand and create a more efficient market for liquidation merchandise. Our objective is to provide a one-stop discount shopping destination for products and services sold through the Internet.

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

Industry Overview

Manufacturers and retailers traditionally hold inventory to buffer against uncertain demand within their normal, "inline" sales channels. Inline sales channels are manufacturers' primary distribution channels, which are characterized by regularly placed orders by established retailers at or near wholesale prices. In recent years, several dynamics have shifted inventory risk from retailers to manufacturers, including:

dominant retailers insist on just-in-time deliveries from manufacturers;

dominant retailers cancel orders mid-production and return unsold merchandise;

style, color or model changes quickly turn inventory into closeout merchandise;

incorrect estimates of consumer demand lead to overproduction; and

changes in a retailer's financial situation or strategy result in cancelled orders.

The disposal of excess, or overstock, inventory represents a substantial burden for many manufacturers, especially those who produce high-quality branded merchandise. Manufacturers seek to avoid liquidating through traditional retail channels where the manufacturer's discounted products may

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be sold alongside other full-price products. This can result in weaker pricing and decreased brand strength, and is known as channel conflict or sales channel pollution. As a result, many manufacturers turn to liquidation wholesalers and discount retailers. These liquidation channels provide manufacturers limited control of distribution and are, we believe, unreliable and expensive to manage when compared with their inline channels.

Despite the challenges manufacturers encountered in the liquidation market, the proliferation of outlet malls, wholesale clubs, and discount chains is evidence of the strong level of consumer demand for discount and closeout merchandise. However, consumers face several difficulties in shopping for this merchandise. For example, many traditional liquidation outlets are in remote locations and have limited shopping hours, which we believe makes shopping burdensome and inconvenient. In addition, in the traditional liquidation outlet there are space constraints limiting the number of products that can be offered at any given time.

We also believe that the market for online liquidation is characterized by a limited number of competitors, some of which use an auction model to price their goods. Furthermore, we believe that many of the online companies that do offer overstock or liquidation merchandise are focused on single product lines.

Lastly, small retailers are under competitive pressure from large national retailers. Small retailers generally do not have purchasing leverage with manufacturers; consequently, they are more likely to pay full wholesale prices and are more likely to receive inferior service. We believe that small retailers generally do not have access to the liquidation market because liquidation wholesalers are most often interested in liquidating large volumes of merchandise, rather than the small quantities appropriate for small, local retailers.

In the fourth quarter 2008, we faced unusual competition from brick and mortar retailers seeking to liquidate inventory directly. The macroeconomic slowdown and discounting by brick and mortar retailers have mixed effects on us. The effects include increased price competition and cautious consumers, but also include opportunities for us to acquire inventory at unusually low prices.

The Overstock Solution

Overstock provides manufacturers with a one-stop liquidation channel to sell both large and small quantities of excess and closeout inventory without disrupting sales through traditional channels. Key advantages for manufacturers liquidating their excess inventory through Overstock include:

Resolution of channel conflict. Channel conflicts arise when a manufacturer's excess inventory is sold through the same channel as their full-priced product offerings. Since excess inventory is usually sold at a discount, sales of the manufacturer's full-priced product offerings may be impacted as a consumer in a retail store may opt for the excess product or become confused by the pricing and model discrepancies. By using Overstock, manufacturers have an alternative and independent channel where they can sell excess inventory without the fear of hindering the sale of their full-priced products.

Single point of distribution. Manufacturers often use multiple liquidation sources to clear their excess inventory. Multiple sources create additional logistics issues that they would rather avoid. By using Overstock, manufacturers have a single source for the distribution of excess inventory.

Improved control of distribution. By using Overstock, manufacturers can monitor what kind of customer, whether individual consumer or small retailer, ultimately purchases their merchandise. In addition, a manufacturer can request that its products be offered in only one of our sales channels in order to avoid sales channel pollution.

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Improved transaction experience. By having a reliable inventory clearing channel, manufacturers are able to more quickly and easily dispense of their excess merchandise, raw materials or production capacity.

Overstock also offers consumers a compelling alternative for bargain shopping. Key advantages for consumers include:

High quality and broad product selection. Much of the merchandise offered on our Website is from well-known, brand-name manufacturers. In the Shopping section of our Website, we currently have approximately 201,000 non-BMMG products and approximately 450,000 BMMG products (books, magazines, CDs, DVDs, and video games) in eight major departments.

Convenient access on a secure site. Our customers are able to access and purchase our products 24 hours a day from the convenience of their computer. We do not sell any personal information about our customer base to third parties.

Responsive customer service and positive shopping experience. Our team of customer service representatives assists customers by telephone, instant online chat and e-mail. Our customer service staff answers approximately 98% of phone calls within 60 seconds, and responds to approximately 93% of e-mail messages within one business day. For our consumer business, we include a return shipment label in our customer's shipment to facilitate product returns and, subject to certain conditions, we allow customers to return most purchased merchandise for a refund. In addition, we continually update and monitor our Website to enhance the shopping experience for our customers.

Our objective is to become the dominant Internet-based closeout solution for holders of brand-name merchandise, allowing them to dispose of that merchandise discreetly and with high recovery values, and to ultimately become a one-stop Internet-based discount shopping destination. We are pursuing this objective through the following key strategies:

Establish strong relationships with manufacturers and distributors. With the growth in the scale of our operations, we believe we are becoming an efficient liquidation channel for manufacturers and distributors. With scale comes the ability to buy in volume, and we believe manufacturers appreciate our ability to liquidate their products without disturbing their traditional channels. Generally, manufacturers do not want their product offerings sold as heavily discounted, closeout products in brick-and-mortar retailers, as is common today. We believe that as manufacturers learn of our capabilities, they will increasingly recognize the attractiveness of Overstock as an efficient liquidation solution.

Optimize inventory management through the use of technology. Our merchandise buyers are supported by proprietary software that provides information on product sales, margins and inventory levels. This technology enables us to make informed decisions and quickly change prices in an effort to maximize sales volume, gross profit and return on inventory capital.

Optimize online marketing initiatives through the use of technology. Our marketing team is supported by technologically advanced software supplied by third party vendors, as well as proprietary software that enhances the level of service provided to our customers and takes advantage of the unique characteristics of online distribution. This software provides us immediate feedback on the effectiveness of various marketing campaigns, allowing us to optimize our online marketing expenditures.

Loyalty programs. We have a frequent buyer's club called Club O. Members of Club O pay an annual fee of \$19.95 and receive a 5% discount on non-BMMG products and free shipping, along with access to a special customer service hotline. Additionally, we partnered with Chase Card Services to launch an Overstock.com Co-Branded Rewards Visa credit card program,

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currently offering our customers a \$30 store credit towards their next Overstock purchase and the opportunity to earn rewards certificates to redeem on our Website.

Our Business

We use the Internet to create a more efficient market for liquidation, closeout and other discount merchandise. We provide consumers and businesses with quick and convenient access to high-quality, brand-name merchandise at discount prices. Our shopping business (sales of product offered through the Shopping section of our Website) includes both a "direct" business and a "fulfillment partner" business (see Item 15 of Part IV, "Financial Statements" Note 23 "Business Segments"). During the years ended December 31, 2006, 2007, and 2008, no single customer accounted for more than 1% of our total revenue.

Unless otherwise indicated or required by the context, the discussion herein of our financial statements, accounting policies and related matters, pertains to the Shopping section of our Website and not necessarily to the Auctions, Cars, Real Estate, or Community sections of our Website.

Direct business

Our direct business includes sales made to individual consumers and businesses, which are fulfilled from our warehouses in Salt Lake City, Utah (see Item 2 of Part I, "Properties"). During the twelve months ended December 31, 2008, we fulfilled approximately 21% of all orders through our warehouses. Our warehouses generally ship between 5,000 and 8,000 orders per day and up to approximately 32,000 orders per day during peak periods, using overlapping daily shifts.

Fulfillment partner business

For our fulfillment partner business, we sell merchandise of other retailers, cataloguers or manufacturers ("fulfillment partners") through our Website. We are considered to be the primary obligor for the majority of these sales transactions and record revenue from the majority of these sales transactions on a gross basis. Our use of the term "partner" or "fulfillment partner" does not mean that we have formed any legal partnerships with any of our fulfillment partners. We currently have approximately 1,200 fulfillment partners which post approximately 196,000 non-BMMG products, as well as most of the BMMG products (found in the Books etc. department) on our Website. Our revenue from sales from both the direct and fulfillment partner businesses is recorded net of returns, coupons and other discounts.

Seasonality

Both direct and fulfillment partner revenues are seasonal, with revenues historically being the highest in the fourth quarter, which ends December 31, reflecting higher consumer holiday spending. We anticipate this will continue in the foreseeable future.

Auctions business

We operate an online auction service as part of our Website. Our auction service allows sellers to list items for sale, buyers to bid on items of interest, and users to browse through listed items online. We record only our listing fees and commissions for items sold as revenue. From time to time, we also sell items returned from our shopping business through our auction service, and for these sales, we record the revenue on a gross basis. Revenue from our auction business is included in the fulfillment partner segment, as it is not significant enough to segregate as a segment.

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Car listing business

We operate an online site for listing cars for sale as a part of our Website. The car listing service allows sellers to list vehicles for sale and allows buyers to review vehicle descriptions, post offers to purchase, and provides the means for purchasers to contact sellers for further information and negotiations on the purchase of an advertised vehicle. Revenue from our car listing business is included in the fulfillment partner segment, as it is not significant enough to segregate as a segment.

Real Estate listing business

We operate an online site for listing real estate for sale as a part of our Website. The real estate listing service allows customers to search active listings across the country. Listing categories include foreclosures, live and on-line auctions, for sale by owner listings, broker/agent listings and numerous aggregated classified ad listings. Revenue from the real estate business is included in the fulfillment partner segment, as it is not significant enough to segregate as a segment.

International business

We began selling products through our website to customers outside the United States in late August 2008. The initial launch included Canada and 33 European countries, including the U.K. and Germany. We do not have operations outside the United States, and are utilizing 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.

Key Relationships

Manufacturer, Supplier and Distribution Relationships

It is difficult to establish closeout buying relationships with manufacturers. Trust and experience gained through past interactions are important. We believe our business model reduces the risk to the manufacturer that its discounted products are sold alongside its full-priced products. Our supplier relationships provide us with recognized, brand-name products. The table below identifies some of the brand names that generate significant revenues in various departments:

Anne Klein	Joseph Abboud	RCA
Bissell	JVC	Samsonite
Blue Ridge Home Fashions	Kodak	Seiko
Broyhill	Movado	Simon & Schuster
Canon	Novica	Sony
Charles David	Panasonic	Steve Madden
Drexel Heritage	Philips	Thomasville
Dyson	Random House	Toshiba
Fuji		Wenger
Hewlett-Packard		
Hoover		
Hunter Fan		

To date, we have not entered into contracts with manufacturers or liquidation wholesalers that guarantee the availability of merchandise for a set duration. Our manufacturer and supplier relationships are based on historical experience with manufacturers and liquidation wholesalers and do not obligate or entitle us to receive merchandise on a long-term or short-term basis. In our direct business, we purchase the products from manufacturers or liquidation wholesalers using standard

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purchase orders. Generally, suppliers do not control the terms under which products are sold through our Website.

Products*Online Products*

Our website is organized into five main sections, namely: Shopping, Auctions, Cars, Real Estate, and Community. The Shopping section is organized into eleven main departments:

Furniture	At Home
Bedding	Clothing & Shoes
Jewelry	Watches
Electronics	Sports
Books, etc.	Worldstock
Other	

Each of these departments has multiple categories that more specifically define the products offered within that department. For example, the "Bedding" department currently has the following product categories:

Memory foam	Mattresses
Sheets	Comforters
Blankets	Down bedding
Duvet covers	Pillows

Each category has several subcategories that further detail the product contained within. For example, under the "Down bedding" category, we have the following subcategories:

Down comforters	Down alternatives
Down pillows	Featherbeds
Down comforter sets	

Individual products can be accessed and viewed from the category or subcategory pages. These specific product pages include detailed product descriptions, color photographs, pricing information and customer reviews.

For 2006, 2007 and 2008, the percentages of gross sales contributed by similar classes of products were as follows:

Product class	2006	2007	2008
Home and garden(1)	42%	44%	50%
Jewelry, watches, clothing and accessories	27%	25%	24%
BMMG(2), electronics and computers	23%	23%	18%
Other	8%	8%	8%
Total	100%	100%	100%

(1)

Home and garden includes home décor, bedding, bath, furniture, house wares, garden, patio and other related products.

(2)

BMMG stands for "Books, Music, Movies and Games."

The number of total products we offer has grown from less than 100 in 1999, to more than 201,000 non-BMMG products and approximately 450,000 BMMG products (books, magazines, CDs, DVDs and

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video games) as of December 31, 2008. As the number of products and product categories change throughout the year, we periodically reorganize our departments and/or categories to better reflect our current product offerings.

Worldstock is our socially-responsible, online marketplace through which artisans in the United States and around the world can sell their products and gain access to a broader market.

Fulfillment Operations

General

When customers place orders on our Website, orders are fulfilled either by a third-party fulfillment partner or directly from our warehouses in Salt Lake City, Utah. We monitor all of these sources for accurate order fulfillment and timely shipment. We currently charge \$2.95 per order for basic ground shipping, but customers can choose from various expedited shipping services at their expense.

Payment Terms

Generally, we require verification of receipt of payment, or authorization from credit card or other payment vendors whose services we offer to our customers (such as Paypal and BillMeLater), before we ship products to consumers or business purchasers. From time to time we grant credit to our business purchasers with normal credit terms (typically 30 days).

Fulfillment for Direct Business

During 2008, we fulfilled approximately 21% of all orders through our leased warehouses in Salt Lake City, Utah (see Item 2 of Part I, "Properties".) Our warehouse staff generally shipped between 5,000 and 8,000 orders per day, and up to 32,000 orders per day during peak periods, using overlapping daily shifts. We also process returns of direct and fulfillment partner merchandise in the Salt Lake City warehouses. Our warehouses store approximately 5,000 non-BMMG products offered on our Website. We operate the Salt Lake City warehouses with an automated warehouse management system that tracks the receipt of inventory, distributes order-fulfillment assignments to warehouse workers and obtains rates for various shipping options to ensure low-cost outbound shipping. Our Website relays orders to the warehouse management system throughout each day, and the warehouse management system in turn confirms to our Website shipment of each order. Customers can track the shipping status of their packages through links we provide on our Website.

Fulfillment Partner Business

During 2008, approximately 79% of our orders were for inventory owned and shipped by third-party fulfillment partners. We currently coordinate approximately 1,200 entities that collect orders through our Website. These third parties perform essentially the same operations as our warehouse: order picking and shipping; however, we handle the majority of the returns for these sales. These third parties relay shipment confirmations to our Website where customers can review shipping and tracking information. All orders through our Website bear Overstock's name on the packing material and shipping documents, including those shipped by our fulfillment partners. We also handle customer service related to all orders placed through our Website.

Sales and Marketing

We use a variety of methods to target our consumer audience, including online campaigns, such as advertising through portals, keywords, search engines, affiliate marketing programs, banners, e-mail and direct mail campaigns, and we are able to monitor and evaluate their results. We seek to identify and eliminate campaigns that do not meet our expectations. We also do brand advertising through television, radio, and print ads. We generally develop these campaigns internally and believe that doing so is cost-effective.

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Customer Service

We are committed to providing superior customer service. We staff our customer service department with dedicated in-house and outsourced professionals who respond to phone, instant online chat and e-mail inquiries on products, ordering, shipping status, and returns. As a result of this commitment, we now rank #2 in customer service rankings among all US retailers, according to rankings published in the 2008 NRF Foundation/American Express Customer Service Survey. Our customer service staff processes approximately 14,000 calls per week and up to approximately 30,000 calls per week during peak periods.

The same staff processes approximately 17,000 e-mail messages each week and up to approximately 21,000 e-mail messages per week during peak periods, with a turnaround goal of one business day. We use automated e-mail and phone systems to route traffic to appropriate customer service representatives. The demands on our customer service staff increase significantly during peak periods, including the several weeks before and after the Christmas holiday.

Technology

We use our internally developed Website and a combination of proprietary technologies and commercially available licensed technologies and solutions to support our operations. We use the services of XO Communications, Inc., Qwest Communications International, Inc. and Verizon, Inc. to obtain connectivity to the Internet over multiple Gig-E and OC48 links. We currently store our data on several Oracle databases using Dell and IBM computer hardware connected to multiple large scale Hitachi and EMC storage devices. Currently, we use Dell and IBM servers for our Website, which are connected to the Oracle databases and operate in a multi-processing Linux environment designed to accommodate large volumes of Internet traffic. Currently, our primary computer infrastructure remains at our co-location facility in Salt Lake City. We also have a second data center which we use primarily for backups, redundancy, development, testing, and our corporate systems infrastructure.

Competition

The online liquidation services market is new, rapidly evolving, intensely competitive and has relatively low barriers to entry, as new competitors can launch new websites at relatively low cost. We believe that competition in the online liquidation market is based predominantly on:

price;

product quality and selection;

shopping convenience;

order processing and fulfillment;

customer service; and

company brand recognition.

Our liquidation services compete with other online retailers and traditional liquidation "brokers", some of which may specifically adopt our methods and target our customers. We currently or potentially compete with a variety of companies that can be divided into several broad categories:

liquidation e-tailers such as SmartBargains;

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online general retailers with discount departments such as Amazon.com, Inc., eBay, Inc. and Buy.com, Inc.;

online specialty retailers such as BlueNile and BackCountry; and

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traditional retailers and liquidators such as Ross Stores, Inc., Walmart Stores, Inc., TJX Companies, Inc., Costco Wholesale Corporation, Target Corporation, Best Buy Co., Inc. and Barnes and Noble, Inc., most of which also have an online presence.

As the market for online liquidation grows, we believe that companies involved in online retail, as well as traditional retailers and liquidation brokers, will increase their efforts to develop services that compete with our online services. We also face potential competition from Internet companies not yet focused on the liquidation market, and from retail companies who are currently operating or not yet operating online.

Many of our current and potential competitors have greater brand recognition, longer operating histories, larger customer bases and significantly greater financial, marketing and other resources than we do, and may enter into strategic or commercial relationships with larger, more established and well-financed companies. Some of our competitors could enter into exclusive distribution arrangements with our vendors and deny us access to their products, devote greater resources to marketing and promotional campaigns and devote substantially more resources to their website and systems development than our company. New technologies and the continued enhancement of existing technologies also may increase competitive pressures on our company. We cannot ensure that we will be able to compete successfully against current and future competitors or address increased competitive pressures (see Item 1A "Risk Factors").

Intellectual Property

We regard our domain names and similar intellectual property as critical to our success. We rely on a combination of laws and contractual restrictions with our employees, customers, suppliers, affiliates and others to establish and protect our proprietary rights. Despite these precautions, it may be possible for a third party to copy or otherwise obtain and use our intellectual property without authorization. In addition, we cannot ensure that others will not independently develop similar intellectual property. Although we have registered and are pursuing the registration of our key trademarks in the United States and some internationally, some of our trade names may not be eligible to receive registered trademark protection. In addition, effective trademark protection may not be available or we may not seek protection in every country in which we market or sell our products and services, including in the United States.

Third parties have in the past, and may in the future, recruit our employees who have had access to our proprietary technologies, processes and operations. These recruiting efforts expose us to the risk that such employees and those hiring them will misappropriate and exploit our intellectual property.

Legal and Regulatory Matters

From time to time, we receive claims and become subject to regulatory investigations or actions, consumer protection, employment, intellectual property and other commercial litigation related to the conduct of our business. Such litigation could be costly and time consuming and could divert our management and key personnel from its business operations. The uncertainty of litigation increases these risks. In connection with such litigation, we may be subject to significant damages or equitable remedies relating to the operation of our business and the sale of products on our website. Any such litigation may materially harm our business, prospects, results of operations, financial condition or cash flows. However, we do not currently believe that any of our outstanding litigation will have a material adverse effect on our financial condition.

These and other types of claims could result in increased costs of doing business through legal expenses, adverse judgments or settlements or require us to change our business practices in expensive ways. In addition, litigation could result in interpretations of the law that require us to change our business practices or otherwise increase our costs.

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Additional litigation may be necessary in the future to enforce our intellectual property rights, to protect our trade secrets or to determine the validity and scope of the proprietary rights of others. Any litigation, regardless of outcome or merit, could result in substantial costs and diversion of management and technical resources, any of which could materially harm our business (see Item 1A "Risk Factors").

See the information set forth under Item 15 of Part IV, "Financial Statements" Note 14 "Commitments and Contingencies," subheading "Legal Proceedings," contained in the "Notes to Consolidated Financial Statements" of this Annual Report on Form 10-K/A.

Government Regulation

Our services are subject to federal and state consumer protection laws including laws protecting the privacy of consumer non-public 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, must provide advance notice of any changes to our policies and, with limited exceptions, must give consumers the right to prevent sharing of their non-public personal information with unaffiliated third parties. Furthermore, 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 and could interfere with the conduct of our business.

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. These issues may take years to resolve. In addition, new state tax regulations may subject us to the obligation to collect and remit state and local taxes other than for sales within the state of Utah (where our operations are located), or subject us to additional state and local sales and income taxes. 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 and commercial online services could result in significant additional taxes on our business. These taxes could have an adverse effect on our cash flows and results of operations. Furthermore, there is a possibility that we may be subject to significant fines or other payments for any past failures to comply with these requirements.

Employees

As of December 31, 2008, we had 1,036 full-time employees, including 379 in customer service and fraud prevention, 119 in order fulfillment, 226 in information technology and Website production, 56 in marketing, 150 in merchandising (including auctions, cars, and real estate), 51 in accounting and finance, and 55 in our executive and administrative department. We seasonally augment our workforce with temporary employees during our fourth quarter to handle increased workload in both our warehouse and customer service operations. We have never had a work stoppage, and none of our employees are represented by a labor union. We consider our employee relationships to be positive. Competition for qualified personnel in our industry has historically been intense, particularly for software engineers, computer scientists, and other technical staff.

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The following persons were executive officers of Overstock.com as of February 23, 2009:

Executive Officers	Age	Position
Patrick M. Byrne	46	Chief Executive Officer and Chairman of the Board of Directors
Jonathan E. Johnson III	42	President and Corporate Secretary
Geoffrey R. Atkinson	24	Senior Vice President, Marketing
Stephen J. Chesnut	49	Senior Vice President, Finance
David K. Chidester	37	Senior Vice President, Internal Reporting and Information
Jacob K. Hawkins	33	Senior Vice President, Change Management
Samuel J. Peterson	33	Senior Vice President, Technology
Stormy D. Simon	40	Senior Vice President, Marketing and Customer Care
Stephen P. Tryon	47	Senior Vice President, Logistics and Human Capital Management

Dr. Patrick M. Byrne has served as our Chief Executive Officer (principal executive officer) and as a Director since October 1999, as Chairman of the Board from February 2001 through October 2005, and since July 2006. From September 1997 to May 1999, Dr. Byrne served as President and Chief Executive Officer of Fechheimer Brothers, Inc., a manufacturer and distributor of uniforms. From 1995 until its sale in September 1999, Dr. Byrne was Chairman, President and Chief Executive Officer of Centricut, LLC, a manufacturer and distributor of industrial torch parts. From 1994 to the present, Dr. Byrne has served as a Manager of the Haverford Group, an investment company and an affiliate of Overstock. Dr. Byrne has a Bachelor of Arts degree in Chinese studies from Dartmouth College, a Master's Degree from Cambridge University as a Marshall Scholar, and a Ph.D. in philosophy from Stanford University.

Mr. Jonathan E. Johnson III joined Overstock.com in September 2002 and currently serves as our President. He has served as our General Counsel and as our Vice President, Strategic Projects, and Senior Vice President, Corporate Affairs and Legal. From May 1999 to September 2002, Mr. Johnson held various positions with TenFold Corporation, a software company, including positions as General Counsel, Executive Vice President and Chief Financial Officer. From October 1997 to April 1999, Mr. Johnson practiced law in the Los Angeles offices of Milbank, Tweed, Hadley & McCloy and from September 1994 to September 1997, he practiced law in the Los Angeles offices of Graham & James. From February 1994 to August 1994, Mr. Johnson served as a judicial clerk at the Utah Supreme Court for Justice Leonard H. Russon, and prior to that, from August 1993 to January 1994, Mr. Johnson served as a judicial clerk at the Utah Court of Appeals for Justice Russon. Mr. Johnson holds a Bachelor's Degree in Japanese from Brigham Young University, studied for a year at Osaka University of Foreign Studies in Japan, and received his law degree from the J. Reuben Clark, Jr. Law School at Brigham Young University.

Mr. Geoffrey R. Atkinson currently serves as our Senior Vice President of Marketing. Mr. Atkinson is responsible for the search and email marketing channels as well as the Customer Relationship Management group (the "CRM"). Since joining the Company in 2005, Mr. Atkinson has worked primarily on improving the customer facing search and navigation experience as well as growing the email and search marketing channels. Mr. Atkinson has previously served as Vice President of tactical marketing and Director of web site and email marketing. Before joining Overstock.com, Mr. Atkinson worked in marketing and branding at Smith Sport Optics, a manufacturer of sunglasses and goggles for sports and leisure, in Sun Valley, Idaho. Mr. Atkinson holds a Bachelor of Arts Degree in Sociology from Dartmouth College.

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Mr. Stephen J. Chesnut was appointed Senior Vice President, Finance of the Company, effective January 5, 2009. From August 2007 until he joined the Company, Mr. Chesnut served as Vice President, Strategy/Market Development/Sales for HD Supply, Inc., a privately-held wholesale distribution company based in Atlanta, Georgia. From December 1998 to August 2007, Mr. Chesnut served in a variety of capacities for The Home Depot or its subsidiaries, including Director, Business Development for HD Supply (prior to its sale by Home Depot), Director, Finance and Chief Financial Officer for Home Depot Supply; Director, New Concept Development; and Director, Strategic Planning. Prior to joining The Home Depot, Mr. Chesnut served in a variety of operational, planning and financial positions for Target Stores Inc. from 1986 to 1998. Mr. Chesnut holds a Bachelor's of Science Degree in Accounting and Business Management, from Southern Utah University and a Master of Business Administration Degree, Finance and Strategic Planning, from Brigham Young University.

Mr. David K. Chidester currently serves as our Senior Vice President, Internal Reporting and Information and Assistant Secretary. Mr. Chidester previously served as Senior Vice President, Finance from January 2004 to January 2009, as our Acting Chief Financial Officer from August 2003 to January 2004, and as our Controller from August 1999 to August 2003. Prior to joining Overstock.com, Mr. Chidester was with PricewaterhouseCoopers LLP from December 1995 to August 1999. Mr. Chidester holds a Bachelor of Science Degree in Accounting and a Master's Degree in Business Administration, both from the University of Utah.

Mr. Jacob K. Hawkins currently serves as Senior Vice President, Change Management. Mr. Hawkins has performed various roles across the organization, including business development, marketing, merchandising, technology, and project management. Prior to joining Overstock.com, Mr. Hawkins worked for Professional Marketing International, a business consulting group. Mr. Hawkins holds a Bachelor's Degree in Business Management from Brigham Young University and a Master's Degree of Business Administration with an emphasis in information systems from the University of Utah.

Mr. Samuel J. Peterson currently serves as our Senior Vice President, Technology. Mr. Peterson previously served as the Vice President, Software Development from early 2005, and was appointed as Director, Network and Systems Engineering in 2003.

Ms. Stormy D. Simon currently serves as our Senior Vice President, Marketing and Customer Care. Ms. Simon previously served as our Vice President, BMMG; Travel and Off-Line Advertising; Chief of Staff and as our Director of B2B. Prior to joining Overstock.com in 2001, Ms. Simon worked in the media and travel industries.

Mr. Stephen P. Tryon joined Overstock.com in August 2004, and serves as Senior Vice President, Logistics and Human Capital Management, with primary responsibility for logistics and supervision of the Company's warehouse operations, and most recently, managing the Company's human resources. Prior to joining Overstock.com, Mr. Tryon was the Legislative Assistant to the Chief of Staff of the United States Army. During his 21 years with the Army, his assignments included director of plans for the 10th Mountain Division, Congressional Fellow for United States Senator Max Cleland, Assistant Professor of Philosophy at the United States Military Academy, and commander of a company of paratroopers. Mr. Tryon received a Bachelor's of Science Degree in Applied Sciences from the U.S. Military Academy and a Master's Degree of Arts in Philosophy from Stanford University.

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Name	Age	Position with the Company	Director Since
Allison H. Abraham	45	None	March 2002
Joseph J. Tabacco, Jr.	59	None	June 2007
Patrick M. Byrne	46	Chief Executive Officer	October 1999
Barclay F. Corbus	41	None	March 2007
James V. Joyce	50	Consultant	February 2008

Ms. Allison H. Abraham has served as a Director of Overstock since March 2002 and is currently the President of the Newton School, a non-profit, private school located in Sterling, Virginia. She is Chairwoman of the Audit Committee and a member of the Compensation Committee. Ms. Abraham served as President and as a director of LifeMinders, Inc., an online direct marketing company, from May 2000 until the acquisition of LifeMinders by Cross Media Marketing Corp. in October 2001. Prior to joining LifeMinders, Ms. Abraham served as Chief Operating Officer of iVillage Inc., an online media company, from May 1998 to May 2000. From February 1997 to April 1998, Ms. Abraham was President, Chief Operating Officer and a director of Shoppers Express, an online grocery service, and also served as Vice President of Sales and Marketing for several months prior to her promotion. From 1992 to 1996, Ms. Abraham held several marketing and management positions at Ameritech Corporation. She was employed at American Express Travel Related Services in New York City from 1988 to 1992, focusing on the launch of new products and loyalty programs. Ms. Abraham holds a Bachelor of Arts Degree in Economics from Tufts University and a Master's Degree of Business Administration from the Darden School at the University of Virginia.

Mr. Joseph J. Tabacco, Jr. has served as a Director of Overstock since June 2007. Mr. Tabacco is a member of the Audit Committee and the Compensation Committee. For more than the last five years Mr. Tabacco has served as the managing partner of the San Francisco office of Berman DeValerio (formerly Berman DeValerio Pease Tabacco Burt & Pucillo). A 1974 honors graduate of George Washington University School of Law, Mr. Tabacco litigates antitrust, securities fraud, commercial high tech, and intellectual property matters. Since entering private practice in the early 1980s, Mr. Tabacco has served as trial or lead counsel in numerous antitrust and securities cases and has been involved in all aspects of state and federal litigation. Prior to 1981, Mr. Tabacco served as senior trial attorney for the U.S. Department of Justice, Antitrust Division, and in both the Central District of California and the Southern District of New York. Mr. Tabacco frequently lectures and authors articles on securities and antitrust law issues and is a member of the Advisory Board of the Institute for Consumer Antitrust Studies at Loyola University Chicago School of Law. Mr. Tabacco is also a former teaching fellow of the Attorney General's Advocacy Institute in Washington, D.C., and has served on the faculty of ALI-ABA on programs about U.S.-Canadian business litigation and trial of complex securities cases.

Dr. Patrick M. Byrne has served as our Chief Executive Officer (principal executive officer) and as a Director since October 1999, as Chairman of the Board from February 2001 through October 2005, and since July 2006. From September 1997 to May 1999, Dr. Byrne served as President and Chief Executive Officer of Fechheimer Brothers, Inc., a manufacturer and distributor of uniforms. From 1995 until its sale in September 1999, Dr. Byrne was Chairman, President and Chief Executive Officer of Centricut, LLC, a manufacturer and distributor of industrial torch parts. From 1994 to the present, Dr. Byrne has served as a Manager of the Haverford Group, an investment company and an affiliate of Overstock. Dr. Byrne has a Bachelor of Arts degree in Chinese studies from Dartmouth College, a Master's Degree from Cambridge University as a Marshall Scholar, and a Ph.D. in philosophy from Stanford University.

Mr. Barclay F. Corbus has served as a Director of Overstock since March 2007. He is a member of the Audit Committee and Chairman of the Compensation Committee. Mr. Corbus has served as Senior Vice President of Clean Energy Fuels Corp., a provider of vehicular natural gas, with responsibility for

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strategic development, since September 2007. He served as Co-CEO of WR Hambrecht + Co., an investment banking firm, from July 2004 to September 2007, and prior to that date served in other executive positions with WR Hambrecht + Co. Prior to joining WR Hambrecht + Co in March 1999, Mr. Corbus was in the investment banking group at Donaldson, Lufkin and Jenrette. Mr. Corbus graduated from Dartmouth College with a Bachelor of Arts Degree in Government and has a Master's Degree of Business Administration in Finance from Columbia Business School.

Mr. James V. Joyce has served as a Director of Overstock since February 2008. He is also the chief executive officer of Icent LLC, which is a management consulting company through which Mr. Joyce has provided consulting services to clients, including the Company, for the last five years. Mr. Joyce holds a Bachelor of Arts Degree as well as a Master's Degree in Jurisprudence from the University of Oxford and a Master's Degree of Business Administration from Dartmouth College.

There are no family relationships among any of the current officers and directors of the Company.

Available Information

Our Internet website address is <http://www.overstock.com>. Our Annual Report on Form 10-K/A, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and other filings made pursuant to the Securities Exchange Act of 1934 are available free of charge through our Internet website 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 Annual Report on Form 10-K/A.

ITEM 1A. RISK FACTORS

Please consider the following risk factors carefully. If any one of the following risks were to occur, our business, financial condition, operating results and cash flows could be materially adversely affected, and the market price of our securities could decrease. These are not the only risks we face. In addition, the global economic climate amplifies many of these risks.

Risks Relating to Overstock

General economic factors may adversely affect our financial performance.

General economic conditions may adversely affect our financial performance. In the United States, higher interest rates, higher fuel and other energy costs, weakness in the housing market, inflation, higher levels of unemployment, unavailability of consumer credit, higher consumer debt levels, higher tax rates and other changes in tax laws, overall economic slowdown and other economic factors could adversely affect consumer demand for the products and services we sell, change the mix of products we sell to one 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 factor that can result in an increase in the cost to us of the goods we sell to our customers.

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

We have a history of losses and we may continue to incur operating and net losses for the foreseeable future. We incurred net losses of \$48.0 million and \$12.7 million for the years ended

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December 31, 2007 and 2008. As of December 31, 2008, our accumulated deficit was \$265.0 million. We will need to generate significant revenues to achieve profitability, and we may not be able to do so. Even if we do achieve profitability, we may not be able to sustain or increase profitability on a quarterly or annual basis in the future. If our revenues grow more slowly than we anticipate, or if our operating expenses exceed our expectations, our financial results would be harmed.

We will continue to incur significant operating expenses and capital expenditures to:

enhance our distribution and order fulfillment capabilities;

further improve our order processing systems and capabilities;

develop enhanced technologies and features;

expand our customer service capabilities to better serve our customers' needs;

expand or modify our product offerings;

occupy warehouse and office space;

increase our general and administrative functions to support our operations; and

maintain or increase our sales, branding and marketing activities, including maintaining existing or entering into new online marketing or marketing analytics arrangements, and continuing or increasing our national television and radio advertising and direct mail campaigns.

Because we will incur many of these expenses before we receive any revenues from our efforts, our losses may be greater than the losses we would incur if we developed our business more slowly. Further, we base our expenses in large part on our operating plans and future revenue projections. Many of our expenses are fixed in the short term, and we may not be able to quickly reduce spending if our revenues are lower than we project. Therefore, any significant shortfall in revenues would likely harm our business, prospects, operating results and financial condition. In addition, we may find that these efforts are more expensive than we currently anticipate which would further increase our losses. Also, the timing of these expenses may contribute to fluctuations in our quarterly operating results.

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

Our limited operating history and the rapidly evolving nature of our industry 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, and we are continuing the work to upgrade and further expand these and other components of our infrastructure. We have experienced difficulties with the implementation of various aspects to the upgrades of our infrastructure, and have incurred increased expenses as a result of these difficulties. As a result of these expenditures, our ability to quickly reduce spending if our revenues are lower than we project 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, prospects, operating results and financial condition and cause our results of operation to fall below the expectations of public market analysts and investors.

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

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We expect a disproportionate amount of our sales to occur during our fourth quarter. If we do not stock or restock popular products in sufficient amounts such that we fail to meet customer demand, it could significantly affect our revenue and our future growth. If we liquidate products, we may be required to take significant inventory markdowns or write-offs, which could reduce gross profits. We

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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 these peak periods and delivery and other fulfillment companies and customer service co-sourcers may be unable to meet the seasonal demand.

We depend on our relationships with third party 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 December 31, 2008, we had fulfillment partner relationships with approximately 1,200 third parties whose products we offer for sale on our Website. We depend on our fulfillment partners to provide a large portion of the product selection we offer, as these products accounted for approximately 97% of the non-BMMG products available on our Website. We plan to continue to expand the number of fulfillment partner relationships and the number of products offered for sale by our fulfillment partners on our Website. We do not have any long-term agreements with any of these third parties. Our agreements with third parties are terminable at will by either party immediately upon notice. In general, we agree to offer the third parties' products on our Website and these third parties agree to provide us with information about their products, honor our customer service policies and ship the products directly to the customer. If we do not maintain our existing relationships or build new relationships with third parties on acceptable commercial terms, we may not be able to offer a broad selection of merchandise, and customers may refuse to shop at our Website. In addition, manufacturers may decide not to offer particular products for sale on the Internet. If we are unable to maintain our existing or build new fulfillment partner relationships or if other product manufacturers refuse to allow their products to be sold via the Internet, our business and prospects would suffer severely.

We are dependent on third parties to fulfill a number of our fulfillment, distribution and other retail functions. If such parties are unwilling or unable to continue providing these services, our business could be seriously harmed.

In our fulfillment partner business, although we handle returned merchandise, we rely on third parties to conduct a number of other traditional retail operations with respect to their respective products that we offer for sale on our Website, including maintaining inventory, preparing merchandise for shipment to individual customers and timely distribution of purchased merchandise. We have no effective means 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 third parties' products, we are unable to fulfill these traditional retail operations ourselves. Our customers could become dissatisfied and cancel their orders or decline to make future purchases if these third parties are unable to deliver products on a timely basis. If our customers become dissatisfied with the services provided by these third parties, our reputation and the Overstock.com brand could suffer.

We rely on our relationships with manufacturers, retailers and other suppliers to obtain sufficient quantities of quality merchandise on acceptable terms. If we fail to maintain our supplier relationships on acceptable terms, our sales and profitability could suffer.

To date, we have not entered into contracts with manufacturers or liquidation wholesalers that guarantee the availability of merchandise for a set duration. Our contracts or arrangements with suppliers do not provide for the continuation of particular pricing practices and may be terminated by

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either party at any time. Our current suppliers may not continue to sell their excess inventory to us on current terms or at all and we may not be able to establish new supply relationships. For example, it is difficult for us to maintain high levels of product quality and selection because none of the manufacturers, suppliers and liquidation wholesalers from whom we purchase products on a purchase order by purchase order basis have a continuing obligation to provide us with merchandise at historical levels or at all. In most cases, our relationships with our suppliers do not restrict the suppliers from selling their respective excess inventory to other traditional or online merchandise liquidators, which could in turn limit the selection of products available on our Website. If we are unable to develop and maintain relationships with suppliers that will allow us to obtain sufficient quantities of merchandise on acceptable commercial terms, such inability could harm our business, prospects, results of operation and financial condition.

We depend upon third-party delivery services to deliver our 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 multiple third parties for the shipment of our products. We cannot be sure that these relationships will continue on terms favorable to us, if at all. Unexpected increases in shipping costs or delivery times, particularly during the holiday season, could harm our business, prospects, financial condition and results of operations. If our relationships with these third parties are terminated or impaired or if these third parties are unable to deliver products for us, whether through labor shortage, slow down or stoppage, deteriorating financial or business condition, responses to terrorist attacks 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 can prevent any carriers from performing their 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 favorable to us, or at all. Changing carriers would likely have a negative effect on our business, prospects, operating results and financial condition. Potential adverse consequences include:

reduced visibility of order status and package tracking;

delays in order processing and product delivery;

increased cost of delivery, resulting in reduced gross profit percentages; and

reduced shipment quality, which may result in damaged products and customer dissatisfaction.

A significant number of merchandise returns could harm our business, financial condition and results of operations.

We allow our customers to return products. If merchandise returns are significant, our business, prospects, financial condition and results of operations could be harmed. 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.

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 specific 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 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, prospects, results of operations and financial condition.

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We face risks relating to our inventory.

We directly purchase some of the merchandise that we sell on our Website. We assume the inventory damage, theft and obsolescence risks, as well as price erosion risks for products that we purchase directly. These risks are especially significant because some of the merchandise we sell on our Website is characterized by rapid technological change, obsolescence and price erosion (for example, computer hardware, software and consumer electronics) and because we sometimes make large purchases of particular types of inventory. In addition, we often do not receive warranties on the merchandise we purchase. We accept returns of products sold through our fulfillment partners and we have the risk of reselling the returned products.

In the recent past we have recorded charges for obsolete inventory and have had to sell certain merchandise at a discount or loss. It is impossible to determine with certainty whether an item will sell for more than the price we pay for it. To the extent that we rely on purchased inventory, our success will depend on our ability to liquidate 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 the shrinkage resulting from theft, loss and misrecording of inventory. If we are unsuccessful in any of these areas, we may be forced to sell our inventory at a discount or loss.

We purchase inventory from foreign markets and pay for inventory with U.S. dollars. If the dollar weakens with respect to foreign currencies, foreign vendors may require us to pay higher prices for products, which could negatively affect our gross profit percentage.

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

If we do not successfully optimize and operate our warehouse and customer service operations, it could significantly limit our ability to meet customer demand. 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 be unable to adequately staff our fulfillment and customer service centers. In addition, we rely on a limited number of companies to deliver inventory to us and to ship orders to our customers. If we are not able to negotiate acceptable terms with these companies, or they experience performance problems or other difficulties, it could negatively impact our operating results and customer experience.

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, including Patrick M. Byrne, our Chief Executive Officer. Our performance also depends on our ability to retain and motivate other officers and key employees. The loss of the services of any of our executive officers or other key employees for any unforeseen reason, including without limitation, illness or call to military service, could harm our business, prospects, financial condition and results of operations. 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, and we cannot assure you that we will be able to successfully attract, assimilate or retain sufficiently qualified personnel. Our failure to retain and attract the necessary technical, managerial, editorial, merchandising, marketing and customer service personnel could harm our revenues, business, prospects, financial condition and results of operations.

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We have an evolving business model.

Our business model has evolved and continues to do so. In the past 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.

We may be unable to manage expansion into new business areas which could harm our business operations and reputation.

Our long-term strategic plan involves expansion of our operations to offer additional types of products and services. We cannot assure you that our efforts to expand our business in this manner will succeed. Our failure to succeed in these markets or businesses or in other product or service offerings may harm our business, prospects, financial condition and results of operation. We cannot assure you that we will be able to expand our operations in a cost-effective or timely manner or that our efforts to expand will be successful. Furthermore, any new business or website we launch that is not favorably received by consumers could damage our reputation or the Overstock.com brand. We may expand the number of categories of products we carry on our Website and these and any other expansions of our operations would also require significant additional expenses and development and would strain our management, financial and operational resources. The lack of market acceptance of such efforts or our inability to generate satisfactory revenues from such expanded services or products to offset their cost could harm our business, prospects, financial condition and results of operations.

We are expanding our international business, causing our business to become increasingly susceptible to numerous international business risks and challenges that could affect our profitability.

We have begun selling 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; and

unexpected changes in international regulatory requirements, taxes and tariffs, and geopolitical events such as war and terrorist attacks.

To the extent we generate international sales and transactions in the future, any negative impact on our international operations could negatively impact our business. In particular, gains and losses on the conversion of foreign payments into United States 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.

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In order to obtain future revenue growth and achieve 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. If we are unable to develop or maintain these relationships on acceptable terms, our ability to attract new customers and our financial condition could be harmed. If the underlying technology's development evolves in a manner that is no longer beneficial to us our financial condition could be harmed. 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. Accordingly, if these relationships or agreements that we may enter into in the future fail to produce the sales that we anticipate, our results of operations will be adversely affected. We cannot assure you that we will be able to increase our revenues, if at all, in a cost-effective manner. 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.

Further, many of the parties with which we may have online-advertising arrangements could provide advertising services for other online or traditional retailers and merchandise liquidators. As a result, these parties may be reluctant to enter into or maintain relationships with us. Failure to achieve sufficient traffic or generate sufficient revenue from purchases originating from third parties may result in termination of these relationships by these third parties. Without these relationships, our revenues, business, prospects, financial condition and results of operations could suffer.

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

The online liquidation services 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. Our consumer Website currently competes with:

liquidation e-tailers such as SmartBargains;

online retailers with discount departments such as Amazon.com, Inc., eBay, Inc. and Buy.com, Inc.; and

online specialty retailers such as BlueNile and BackCountry; and

traditional retailers and liquidators such as Ross Stores, Inc., Walmart Stores, Inc., TJX Companies, Inc., Costco Wholesale Corporation, Target Corporation, Best Buy Co., Inc., and Barnes and Noble, Inc., most of which also have an online presence.

Our Website competes with liquidation "brokers" and retailers and online marketplaces such as eBay, Inc.

We expect the online liquidation services market to become even more competitive as traditional liquidators and online retailers continue to develop services that compete with our services. In addition, manufacturers and retailers may decide to create their own Website to sell their own excess inventory and the excess inventory of third parties. Competitive pressures created by any one of our competitors, or by our competitors collectively, could harm our business, prospects, financial condition and results of operations.

Further, as a strategic response to changes in the competitive environment, we may from time to time make certain pricing, service or marketing decisions or acquisitions that could harm our business,

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prospects, financial condition and results of operations. 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 Ltd., Ross Stores, Inc., respectively. We have recently entered the online auctions and car listing businesses in which we compete with large established businesses including eBay, Inc. and AutoTrader.com, Inc.

Many of our current and potential competitors described above have longer operating histories, larger customer bases, greater brand recognition and significantly greater financial, marketing and other resources than we do. In addition, online retailers and liquidation e-tailers may be acquired by, receive investments from or enter into other commercial relationships with larger, well-established and well-financed companies. Some of our competitors may be able to secure merchandise from manufacturers on more favorable terms, devote greater resources to marketing and promotional campaigns, adopt more aggressive pricing or inventory availability policies and devote substantially more resources to Website and systems development than we do. Increased competition may result in reduced operating margins, loss of market share and a diminished brand franchise. We cannot provide assurance that we will be able to compete successfully against current and future competitors.

Our operating results depend on our Website, network infrastructure and transaction-processing systems. Capacity constraints or system failures would harm our business, prospects, results of operations and financial condition.

Any system interruptions that result in the unavailability of our Website or reduced performance of our transaction systems would reduce our transaction volume and the attractiveness of the services that we provide to suppliers and third parties and would harm our business, prospects, operating results and financial condition.

We use internally developed systems for our Website and certain aspects of transaction processing, including customer profiling and order verifications. We have experienced periodic systems interruptions due to server failure and power failure, which we believe will continue to occur from time to time. If the volume of traffic on our Website or the number of purchases made by customers substantially increases, we will need to further expand and upgrade our technology, transaction processing systems and network infrastructure. We have experienced and expect to 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 unanticipated system disruptions, slower response times, and degradation in levels of customer service, impaired quality and delays in reporting accurate financial information.

Our transaction processing systems and network infrastructure may be unable to accommodate increases in traffic in the future. We may be unable to project accurately the rate or timing of traffic increases or successfully upgrade our systems and infrastructure to accommodate future traffic levels on our Website. In addition, we may be unable to upgrade and expand our transaction processing systems in an effective and timely manner or to integrate any newly developed or purchased functionality with our existing systems. For example, in the third quarter 2005 we experienced difficulties with our implementation of infrastructure upgrades, which resulted in our inability to upload new products to our Website for a period of approximately five weeks. Any such difficulties with our transaction processing systems or other difficulties upgrading, expanding or integrating various aspects of our systems may cause unanticipated system disruptions, slower response times, and degradation in levels of customer service, additional expense, impaired quality and speed of order fulfillment or delays in reporting accurate financial information.

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If the facility where substantially all of our computer and communications hardware is located fails, our business, results of operations and financial condition will 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 near our corporate headquarters in Salt Lake City. Although we have designed our back-up system in an effort to avoid or 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, acts of war, break-ins, earthquake and similar events. Our disaster recovery plan may be inadequate, and our business interruption insurance may be insufficient to compensate us for losses that may occur. Despite the implementation of network security measures, our servers are vulnerable to computer viruses, physical or electronic break-ins and similar disruptions, 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, prospects, financial condition and results of operations.

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 and take appropriate steps to enforce our intellectual property rights. In addition, our competitors could, without violating our proprietary rights, develop technologies that are as good as or better than our technology.

Our failure to protect our software and other proprietary intellectual property rights or to develop 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, results of operations and financial condition.

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

Other parties also 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, whether or 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.

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

To remain competitive, we must continue to enhance and improve the functionality and features of our e-commerce businesses. We may face material delays in introducing new services, products and

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enhancements. If this happens, our customers may forgo the use of our Website and use those of our competitors. The Internet and the online commerce industry are rapidly changing. If competitors introduce new products and services using new technologies or if new industry standards and practices emerge, our existing 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, prospects, financial condition and results of operations.

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 negatively affect our business.

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

As we begin to sell products internationally, 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.

Our business and reputation may be harmed by the listing 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 certain items listed 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 listing 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. In the future, we may implement measures 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 revenues, business, prospects, financial condition and results of operations.

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.

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Negative publicity generated as a result of the foregoing could damage our reputation, harm our business and diminish the value of our brand name.

Our Rocker Partners, L.P. litigation may have an adverse effect on our business and financial condition.

In August 2005, we filed an unfair business practice lawsuit against Gradient Analytics, Rocker Partners, LP and others, alleging that the defendants have conspired to denigrate Overstock's business for personal profit. In October 2005, we filed an amended complaint alleging additional causes of action and articulating in greater detail the allegations against the defendants. In November 2007, Copper River Partners, L.P. (formerly known as Rocker Partners, LP) filed a cross-complaint against us and some of our current and former directors. Though the cross-claims against other current and former directors were dismissed, the cross claims against us and Dr. Byrne remain. Dr. Patrick Byrne has appeared on nationally syndicated television programs and elsewhere to discuss the litigation. The use of management's time and attention and the Company's resources in connection with the litigation and related matters may reduce the time and attention management is able to spend on or give to other aspects of our business, which may have adverse effects on other aspects of our business. In addition, the use of the Company's resources in connection with the litigation and related matters may reduce the resources we are able to spend on or give to 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 pursuing the litigation, our business, prospects, financial condition and results of operation may suffer. We have settled, and dismissed, our claims against and by Gradient. If we are unsuccessful in defeating the remaining cross-claims, we may incur damages which may not be covered by existing insurance or may not be within policy limits which could adversely impact our financial condition.

Our Prime Broker litigation may have an adverse effect on our business and financial condition.

In February 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. In September 2007, we filed an amended complaint adding Lehman Brothers, Inc. as an additional defendant and articulating in greater detail the allegations against the defendants. 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 pursuing the litigation, our business, prospects, financial condition and results of operation may suffer. Further, the bankruptcy filing by Lehman Brothers may adversely affect our ability to collect any judgment we may obtain against Lehman.

We may be liable if third parties misappropriate our customers' personal information.

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

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affect our business. In addition, the Federal Trade Commission and state agencies have been investigating various Internet companies regarding their use of personal information. We could incur additional expenses if new regulations regarding the use of personal information are introduced or if government agencies investigate our privacy practices.

We rely on encryption and authentication technology licensed from third parties to provide the security and authentication necessary to effect secure transmission of confidential information such as customer credit card numbers. We cannot provide assurance that advances in computer capabilities, new discoveries in the field of cryptography or other events or developments will not result in a compromise or breach of the algorithms that we use to protect customer transaction data. If any such compromise of our security were to occur, it could harm our reputation, business, prospects, financial condition and results of operations. A party who is able to circumvent our security measures could misappropriate proprietary information or cause interruptions in our operations. We may be required to expend significant capital and other resources to protect against such security breaches or to alleviate problems caused by such breaches. We cannot assure you that our security measures will prevent security breaches or that failure to prevent such security breaches will not harm our business, prospects, financial condition and results of operations.

We may be subject to product liability claims that could be costly and time consuming.

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 could bring claims against us as the manufacturer and/or retailer of the product. Our insurance coverage may not be adequate to cover every claim that could be asserted. If a successful claim were brought against us in excess of our insurance coverage, it could adversely affect our business. Even unsuccessful claims could result in the expenditure of funds and management time and could have a negative impact on our business.

We have significant indebtedness.

As a result of the sale of our 3.75% Convertible Senior Notes (the "Senior Notes") in November 2004, we incurred \$120.0 million of indebtedness, due December 1, 2011. Under the repurchase program approved by our Board of Directors in 2005, we retired \$33.0 million and \$10.0 million of the Senior Notes in June and November 2005, and \$9.5 million during the quarter ended September 30, 2008. As of December 31, 2008, \$67.5 million of the Senior Notes remained outstanding. On February 17, 2009, our Board of Directors approved a debt repurchase program that authorizes us to utilize up to \$20.0 million to repurchase a portion of its 3.75% Senior Notes. Under this repurchase program, we retired \$4.9 million of the Senior Notes for \$3.0 million in cash. As a result of the Senior Notes retirements, we expect to recognize a gain of \$1.9 million, net of the associated unamortized discount of \$63,000 (see Item 15 of Part IV, "Financial Statements" Note 17 "Stock and Debt Repurchase Program"). The degree to which we are leveraged could materially and adversely affect our ability to obtain additional financing for working capital, acquisitions or other purposes and could make us more vulnerable to industry downturns and competitive pressures. Our ability to meet our debt service obligations is dependent upon our future performance, which will be subject to financial, business and other factors affecting our operations, many of which are beyond our control. If we fail to comply with our debt covenants, we will be in default.

We may be unable to generate sufficient cash flow to satisfy our debt service obligations.

Our ability to generate cash flow from operations to make interest payments on our debt obligations will depend on our future performance, which will be affected by a range of economic, competitive and business factors. We cannot control many of these factors, including general economic conditions and the health of the internet retail industry. If our operations do not generate sufficient

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cash flow from operations to satisfy our debt service obligations, we may need to borrow additional funds to make these payments or undertake alternative financing plans, such as refinancing or restructuring our debt, or reducing or delaying capital investments and acquisitions. Additional funds or alternative financing may not be available to us on acceptable terms, or at all. Our inability to generate sufficient cash flow from operations or obtain additional funds or alternative financing on acceptable terms could have a material adverse effect on our business, prospects, financial condition and results of operations.

We may have difficulty during the current economic turmoil.

In the current volatile credit market, there is risk that any lenders, even those with strong balance sheets and sound lending practices, could fail or refuse to honor their legal commitments and obligations under existing credit commitments, including but not limited to: extending credit up to the maximum permitted by a credit facility, allowing access to additional credit features and otherwise accessing capital and/or honoring loan commitments. Our lender on our credit facility is Wells Fargo. If our lender fails to honor its legal commitments under our credit facility, it could be difficult in this environment to replace our credit facility on similar terms.

We believe that continued turmoil in the financial markets may lead to general economic weakness, which could have a negative impact on our business. Due to the recent economic developments seen nationally that have adversely impacted the retail industry, liquidation wholesalers and discount retailers have also been under competitive pressure from large national retailers seeking either to liquidate inventory as they go out of business or steeply discounting inventory to mitigate losses as of the end of the year. This resulting margin pressure is anticipated to not be sustainable as brick-and-mortar stores clear out excess inventory in their supplies chains and adjust their business model for the changes in the economy.

Our suppliers, fulfillment partners or key third party vendors of necessary services and technical systems may encounter difficulty with credit or liquidity in their own businesses, which may adversely affect ours.

Risks Relating to our Auctions Site Business

Our auctions business is a new business.

Our auctions business began operation in September 2004. The online auctions business is a relatively new business for us, and we cannot ensure that our expansion into the online auctions business will succeed. Our entry into the online auctions business will require us to devote substantial financial, technical, managerial and other resources to the business. It will also expose us to additional risks, including legal and regulatory risks, and it will require us to compete with established businesses having substantially greater experience in the online auctions business and substantially greater resources than we have.

Our auctions business may be subject to a variety of regulatory requirements.

Many states and other jurisdictions, including Utah, where our company is located, have regulations governing the conduct of traditional "auctions" and the liability of traditional "auctioneers" in conducting auctions. Although the vast majority of these regulations clearly contemplated only traditional auctions, not online auctions, the potential application of these types of regulations to online auction sites is not clear. We are aware that several states and some foreign jurisdictions have attempted to impose such regulations on other companies operating online auction sites or on the users of those sites. In addition, certain states have laws or regulations that do expressly apply to online auction site services. Although we do not expect these laws to have a significant effect on our auction site business, we will incur costs in complying with these laws, and we may from time to time be

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required to make changes in our business that may increase our costs, reduce our revenues, cause us to prohibit the listing of certain items in certain locations, or make other changes that may adversely affect our auctions business.

Current and future laws could affect our auctions business.

Like our shopping site business, our auction site business is subject to the same laws and regulations that apply to other companies conducting business on and off the Internet. In addition, our auction site business may be affected by other laws and regulations, such as those that expressly apply to online auction site services. Further, because of the wide range of items that users of our auctions service may choose to list on the site, a variety of additional laws and regulations may apply to transactions between users of our site, such as those requiring a license to sell or purchase certain items or mandating particular disclosures in connection with an offer or sale of an item. At least one state recently proposed legislation that sought to prohibit the sale of certain items through internet auction without similar application of the law to traditional retail establishments, online or printed classified advertising publications, or other types of sales list services. To the extent that such current or future laws or regulations prevent or inhibit users from selling items on our auction site, or to the extent these laws discriminate against internet auctions or apply in a discriminatory fashion, they could harm our business.

Our business may be harmed if our auctions business is used for unlawful transactions.

The law regarding the potential liability of an online auction service for the activities of its users is not clear. We prohibit the listing of numerous categories of items in an effort to reduce the possibility that users of our auction site will engage in an unlawful transaction. However, we cannot assure that users of the site will comply with all laws and regulations applicable to them and their transactions, and we may be subject to allegations of civil or criminal liability for any unlawful activities conducted by them. Any costs we incur as a result of any such allegations, as a result of actual or alleged unlawful transactions utilizing our site, or in our efforts to prevent any such transactions, may harm our business. In addition, any negative publicity we receive regarding any such transactions or allegations may damage our reputation, our ability to attract new customers to our main shopping site, and the Overstock.com brand name generally.

Fraudulent activities using our auctions business and disputes between users of our auctions business may harm our business.

We are aware that other companies operating online auction services have periodically received complaints from users alleging that they have not received the purchase price or the goods they expected to receive and that, in some cases, users have been arrested and convicted for engaging in fraudulent activities using those companies' auction sites. We may receive similar complaints. We do not have the ability to require users of our services to fulfill their obligations to make payments or to deliver items. We are aware that other companies periodically receive complaints from buyers about the quality of the items they purchase, requests for reimbursement of amounts paid, and communications threatening or commencing legal actions against them. We may receive similar complaints, requests and communications in connection with our auctions business.

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We are subject to risks associated with information transmitted through our auctions service.

The law relating to the liability of online services companies for information carried on or disseminated through their services is currently unsettled. Claims could be made against online services companies under both U.S. and foreign law for defamation, libel, invasion of privacy, negligence, copyright or trademark infringement, or other theories based on the nature and content of the materials disseminated through their services. We are aware that private lawsuits seeking to impose liability under a number of these theories have been brought against other companies operating auction sites. In addition, domestic and foreign legislation has been proposed that would prohibit or impose liability for the transmission over the Internet of certain types of information. Our auctions service permits users to make comments regarding other users. Although all such comments are generated by users and not by us, we are aware that claims of defamation or other injury have been made against other companies operating auction services in the past and could be made in the future against us for comments made by users. Recent court decisions have narrowed the scope of the immunity provided to Internet service providers like us under the Communications Decency Act. This trend, if continued, may increase our potential liability to third parties for the user-provided content on our site.

Difficulties or negative publicity associated with our auctions business could affect our main shopping site business.

Any significant operational or other difficulties we encounter with our auctions business could damage our reputation, our ability to attract new customers to our main shopping site, and the Overstock.com brand name generally. Negative publicity resulting from actual or alleged fraudulent or deceptive conduct by users of our auctions business could also damage our reputation, our ability to attract new customers to our main shopping site, and the Overstock.com brand name generally.

Risks Relating to our Cars Site and Real Estate Businesses

Our cars site and real estate businesses are new businesses.

Our car listing site and real estate listing businesses began operation in December 2006 and August 2008, respectively. The listing sites are listing services for automobile and real estate sellers. The online car listing service and real estate listing service are relatively new businesses for us. We cannot ensure that our expansion into these businesses will succeed. Our entry into these businesses will require us to devote substantial financial, technical, managerial and other resources to this car listing and real estate listing sites. It will also expose us to additional risks, including legal and regulatory risks, and it will require us to compete with established businesses having substantially greater experience in the online car listing and real estate listing service businesses and substantially greater resources than we have.

Our car listing and real estate listing businesses may be subject to a variety of regulatory requirements.

Many states and other jurisdictions, including Utah, where we are located, have regulations governing the conduct of car sellers and real estate agents and public advertisement for car and real estate sales. Generally, these regulations govern the conduct of those sellers advertising their automobiles for sale and real estate listing 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." The application of these regulations to online car listing service and real estate listing providers is not clear. Although we do not expect these laws to have a significant effect on our listing businesses, we will incur costs in researching and complying with these laws, and we may from time to time be required to make changes in our businesses that may increase our costs, reduce our revenues, cause us to prohibit certain listing or

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advertising practices, or make other changes that may adversely affect our car and real estate listing businesses.

Current and future laws could affect our car and real estate listing businesses.

Like our shopping business, our car and real estate listing services are subject to the same laws and regulations that apply to other companies conducting business on and off the Internet. In addition, our car and real estate listing services may be affected by other laws and regulations, such as those that expressly apply to advertising automobiles and real estate for sale. To the extent that such current or future laws or regulations prevent users from selling items on our car and real estate listing sites, they could harm our business.

Our business may be harmed if our car and real estate listing sites are used for unlawful transactions.

The law regarding the potential liability of an online listing service for automobile sales and real estate is not clear. The platform of the listing service will be accessible to those subscribers who will have the ability to feature their cars and real estate listings for sale and will supply the text descriptions of the vehicles, including the general condition of the vehicle and property and other important information. We will have no ability beforehand to know if the information sellers provide is correct. While our site terms and conditions of usage will prohibit unlawful acts, we cannot rule out the possibility that users of our car and real estate listing sites will engage in unlawful transactions, or fail to comply with all laws and regulations applicable to them and their transactions. We may be subject to allegations of civil or criminal liability for any unlawful activities conducted by such users. Any costs we incur as a result of any such allegations, as a result of actual or alleged unlawful transactions utilizing our site, or in our efforts to prevent any such transactions, may harm our business. In addition, any negative publicity we receive regarding any such transactions or allegations may damage our reputation, our ability to attract new customers to our main shopping site, and the Overstock.com brand name generally.

Fraudulent activities using our car and real estate listing sites and disputes between users of our car and real estate listing sites may harm our business.

We are aware that other companies operating online car and real estate listing services have periodically received complaints from users alleging improprieties in connection with listings and occasionally these complaints may result in regulatory action. With any online listing service there is the possibility that sellers may attempt to employ "bait and switch" techniques, attracting consumers with advertisements of low cost, good condition vehicles in hopes of switching buyer interest to another less favorable vehicle or different property once a potential purchaser responds. Additionally, sellers may attempt to sell vehicles and real estate without accurate descriptions of the condition of the vehicles or real estate. We do not have the ability to require users of our services to fulfill their obligations to make accurate disclosures or comply with consumer laws prohibiting "bait and switch" or other prohibited seller tactics. We are aware that other companies providing similar services periodically receive complaints about the quality of the vehicles or real estate they purchase, requesting reimbursement of amounts they have paid, threatening or commencing legal actions against the listing service for damages. We may receive similar complaints, requests and communications, and encounter similar legal actions in connection with our cars and real estate listing businesses, which may harm our business or reputation among consumers.

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Risks Relating to our Community Site Business

Our community site business is a new business

Our Community site began operation in February 2006 with the introduction of Omuse, an Overstock supported, collaborative writing platform. Omuse allows Community site users to read about and or write "guides" about a universe of subjects in which they may have a particular expertise or interest. The Community site when fully deployed will also have services intended to establish user forum participation, provide customers access to recent news about Overstock and allow users the opportunity to participate in forum reading and writing, to create weblogs or post comments to the weblogs or "blogs" of other site users, or in our Omuse collaborative writing platform. Presently Omuse is the only operating platform on the Community site. We cannot ensure that our expansion into this business will succeed. It is a business which allows persons to contribute content within certain guidelines and subject to terms and conditions. We cannot always be in a position to assure that our community users are abiding by these terms and conditions, or be in a position to interdict or remove inappropriate or infringing material. Our entry into this business will require us to devote substantial financial, technical, managerial and other resources to this site. It is uncertain whether we will benefit financially from the Community site. The Community site will also expose us to additional risks, including legal and regulatory risks, including, but not limited to, legal actions for possible intellectual property infringement, and claims for libel. Additionally, our entry into the Community site service will require us to compete with established businesses having substantially greater experience in the Community site service business and which have substantially greater resources than we have.

Risks Relating to the Internet Industry

Our success is tied to the continued use of the Internet and the adequacy of the Internet infrastructure.

Our future revenues and profits, if any, substantially depend upon the continued widespread use of the Internet as an effective medium of business and communication. Factors which could reduce the widespread use of the Internet include:

actual or perceived lack of security of information or privacy protection;

possible disruptions, computer viruses or other damage to the Internet servers or to users' computers;

significant increases in the costs of transportation of goods; and

governmental regulation.

Customers may be unwilling to use the Internet to purchase goods.

Our long-term future depends heavily upon the general public's willingness to use the Internet as a means to purchase goods. E-commerce remains a relatively new concept and large numbers of customers may not begin or continue to use the Internet to purchase goods. The demand for and acceptance of products sold over the Internet are highly uncertain and most e-commerce businesses have a short track record. If consumers are unwilling to use the Internet to conduct business, our business may not develop profitably.

The security risks or perception of risks of e-commerce may discourage customers from purchasing goods from us.

In order for the e-commerce market to develop successfully, we and other market participants must be able to transmit confidential information securely over public networks. Third parties may have the technology or know-how to breach the security of customer transaction data. Any breach could

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cause customers to lose confidence in the security of our Website and choose not to purchase from our Website. If someone is able to circumvent our security measures, he or she could destroy or steal valuable information or disrupt our operations. Concerns about the security and privacy of transactions over the Internet could inhibit the growth of the Internet and e-commerce. Our security measures may not effectively prohibit others from obtaining improper access to our information. Third parties may target our customers directly with fraudulent identity theft schemes designed to appear as legitimate communications from us. Any security breach or fraud perpetrated on our customers could expose us to increased costs and to risks of loss, litigation and liability and could seriously disrupt our operations.

Credit card fraud could adversely affect our business.

We routinely receive orders placed with fraudulent credit card data. We do not carry insurance against the risk of credit card fraud, so the failure to adequately control fraudulent credit card transactions could reduce our net revenues and our gross profit percentage. We have implemented technology to help us detect 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 though 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, results of operation or financial condition.

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, our business could be harmed.

We do not currently collect sales or other similar taxes for physical shipments of goods into states other than Utah. 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 we have no physical presence in those jurisdictions. The future location of our fulfillment centers and customer service center networks, or any other operation of the company, establishing a physical presence in states where we are not now present, may result in additional sales and other tax obligations. We challenged the constitutionality of a New York state law which requires internet retailers 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 trial court dismissed our challenge and we are appealing the dismissal. As a result of the enactment of the New York law, we terminated our relationship with New York based advertizing affiliates. Several other states currently have legislative proposals similar to New York's tax law, and if such laws are evaluated and constitutionally upheld, we may have to elect to discontinue in those states valuable marketing through the use of affiliates based in those states, or begin in those states the collection of the taxes. In either event, our business could be harmed and our business could be adversely affected 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 in compliance with these or any other state law.

Existing or future government regulation could harm our business.

We are subject to the same federal, state and local laws as other companies conducting business on the Internet. Today there are relatively few laws specifically directed towards conducting business on the Internet. However, due to the increasing popularity and use of the Internet, many laws and regulations relating to the Internet are being debated at the state and federal levels. These laws and regulations could cover issues such as user privacy, freedom of expression, pricing, fraud, quality of products and services, taxation, advertising, intellectual property rights and information security. Applicability to the Internet of existing laws governing issues such as property ownership, copyrights

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and other intellectual property issues, taxation, libel, obscenity and personal privacy could also harm our business. For example, United States and foreign laws regulate our ability to use customer information and to develop, buy and sell mailing lists. The vast majority of these laws were adopted prior to the advent of the Internet and do not contemplate or address the unique issues raised thereby. Those laws that do reference the Internet are only beginning to be interpreted by the courts and their applicability and reach are therefore uncertain. Additionally, laws governing the permissible contents of products may adversely affect us. Recently the United States Congress passed the Consumer Product Safety Improvement Act ("CPSIA"), which created more stringent safety requirements for children's products and any products containing lead paint sold within the United States. The CPSIA, not only regulates the future manufacture of items such as cribs, pacifiers, toys and children's jewelry, but applies to existing inventories and may cause us to incur losses for any non-compliant items in our inventory, or which we may have sold subsequent to the effective dates of the legislation, through regulatory or civil actions against us. These current and future laws and regulations could harm our business, results of operation and financial condition.

Laws or regulations relating to privacy and data protection may adversely affect the growth of our Internet business or our marketing efforts.

We are subject to increasing regulation at the federal, state and international levels relating to privacy and the use of personal user information. For example, we are subject to various telemarketing laws that regulate the manner in which we may solicit future suppliers and customers. Such regulations, along with increased governmental or private enforcement, may increase the cost of growing our business. In addition, many jurisdictions have laws that limit the uses of personal user information gathered online or offline or require companies to establish privacy policies. The Federal Trade Commission has adopted regulations regarding the collection and use of personal identifying information obtained from children under 13. Proposed legislation in this country and existing laws in foreign countries require companies to establish procedures to notify users of privacy and security policies, obtain consent from users for collection and use of personal information, and/or provide users with the ability to access, correct and delete personal information stored by us. Additional legislation regarding data security and privacy has been proposed in Congress. These data protection regulations may restrict our ability to collect demographic and personal information from users, which could be costly or harm our marketing efforts, and could require us to implement new and potentially costly processes, procedures and/or protective measures.

Risks Relating to the Securities Markets and Ownership of Our Securities

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

Our common stock has been publicly traded only since May 30, 2002. The market price of our common stock has been subject to significant fluctuations since the date of our initial public offering. These fluctuations could continue. It is possible that in some 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. Some of the factors that could affect the market price of our securities are as follows:

changes in securities analysts' recommendations or estimates of our financial performance or publication of research reports by analysts;

changes in market valuations of similar companies;

announcements by us or our competitors of significant contracts, acquisitions, commercial relationships, joint ventures or capital commitments;

general market conditions;

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actual or anticipated fluctuations in our operating results;

intellectual property or litigation developments;

changes in our management team;

economic factors unrelated to our performance; and

our issuance of additional shares of stock or other securities.

In addition, the securities markets have experienced significant price and trading volume fluctuations. These broad market fluctuations may adversely affect the trading price of our securities. In the past, following periods of volatility in the market price of a public company's securities, securities class action litigation has often been instituted against that company. Such litigation could result in substantial cost and a diversion of management's attention and resources.

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

Our future revenues and operating results are likely 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;

our inability to retain existing customers or encourage repeat purchases;

the extent to which our existing and future marketing agreements 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;

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

offering new lines of products;

our ability to attract users to our auctions, car listing and real estate sites; and

our inability to replace the loss of significant customers.

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

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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.

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 will be 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 have filed an unfair business practice lawsuit against, Rucker Partners, L.P. and others, alleging that the defendants have conspired to denigrate Overstock's business for personal profit, as well as an amended complaint alleging additional causes of action and articulating in greater detail the allegations against the defendants. We have also 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. In September 2007, we filed an amended complaint adding Lehman Brothers Holdings Inc. as an additional defendant and articulating in greater detail the allegations against the defendants. We believe that the defendants in both of these lawsuits have 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

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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 may suffer, 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.

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, we have consistently appeared on the Regulation SHO threshold list and, while we do not currently appear on the Regulation SHO threshold list, we have 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-K/A and in any reports we file with the SEC after we file this Form 10-K/A, 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-K/A 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 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

Corporate office space

In July 2005, we leased approximately 154,000 rentable square feet in the Old Mill Corporate Center III in Salt Lake City, Utah for a term of ten years.

Logistics and warehouse space

We currently lease 795,000 square feet of warehouse facilities in Utah under operating leases which expire in August 2012 and August 2015.

On April, 8, 2008, we entered into a lease agreement with Natomas Meadows, LLC (the "Natomas Lease"). The Natomas Lease is for a 686,865 square foot warehouse facility in Salt Lake City, Utah (the "New Warehouse"). The Natomas Lease provides that we will lease the New Warehouse in stages: on October 15, 2008, we leased the initial 232,900 square feet of the New Warehouse; on February 1, 2009, we leased a total of 435,400 square feet; and, on September 1, 2009, we will lease the remainder, for a total of 686,865 square feet. The Natomas Lease term is seven years, and specifies rent, exclusive of common area maintenance fees, at a variable rate over the course of the staged lease term, ranging from \$0.3300 per square foot for the first stage, to \$0.3950 per square foot for the last year of the Natomas Lease term. Including the space now leased in the New Warehouse, we currently have warehouse operations in two facilities in Salt Lake City. The Natomas Lease anticipates that we may construct a corporate office facility within the New Warehouse. We constructed a 40,000 square foot customer service facility in the New Warehouse and commenced use of the facility on November 3, 2008.

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Co-location data center

In December 2006, we entered into a Data Center Agreement (the "OM I Agreement") to lease 3,999 square feet of space at Old Mill Corporate Center I for an IT data center to allow us to consolidate other IT data center facilities.

We believe that all the above listed facilities will be sufficient for our needs for at least the next twelve months, subject to seasonal requirements for additional warehouse space during the fourth quarter.

ITEM 3. LEGAL PROCEEDINGS

The information set forth under Item 15 of Part IV, "Financial Statements" Note 14 "Commitments and Contingencies," subheading "Legal Proceedings," contained in the "Notes to Consolidated Financial Statements" of this Annual Report on Form 10-K/A is incorporated by reference in answer to this Item.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to a vote of security holders during the fourth quarter of 2008.

Table of Contents**PART II****ITEM 5. MARKET FOR THE REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES***Market Information*

Our common stock is traded on the NASDAQ Global Market under the symbol "OSTK." Prior to May 30, 2002, there was no public market for our common stock. The following table sets forth, for the periods indicated, the high and low sales prices per share for our common stock as reported by NASDAQ.

	Common Stock Price	
	High	Low
Year Ended December 31, 2007		
First Quarter	19.72	14.05
Second Quarter	19.98	15.80
Third Quarter	28.99	17.22
Fourth Quarter	39.39	14.75
Year Ended December 31, 2008		
First Quarter	15.68	8.61
Second Quarter	28.50	11.50
Third Quarter	29.59	13.64
Fourth Quarter	20.13	6.34

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STOCK PERFORMANCE GRAPH

The following graph shows a comparison of cumulative total stockholder return, calculated on a dividend reinvested basis, from the market closing price on December 31, 2003 through December 31, 2008 for Overstock.com, Inc., Hemscott's (formerly Media General's) Nasdaq U.S. Index and Hemscott's Internet Software and Services Index. The graph assumes that \$100 was invested in Overstock's common stock and the above indices at the closing prices on December 31. Historic stock price performance is not necessarily indicative of future stock price performance.

**COMPARISON OF CUMULATIVE TOTAL RETURN
AMONG OVERSTOCK.COM, INC.,
NASDAQ MARKET INDEX-U.S. AND HEMSCOTT GROUP INDEX**

ASSUMES \$100 INVESTED ON DEC. 31, 2003
ASSUMES DIVIDEND REINVESTED
FISCAL YEAR ENDING DEC. 31, 2008

Holders

As of February 23, 2009, there were 183 holders of record of our common stock. Because many of our shares of common stock are held by brokers and other institutions on behalf of shareholders, we are unable to estimate the total number of shareholders represented by these record holders.

Dividends

We have never declared or paid any cash dividends on our common stock. We currently intend to retain any earnings for future growth and do not anticipate paying any cash dividends in the foreseeable future. Any future determination to pay dividends will be at the discretion of our board of directors and will depend on our results of operations, financial conditions, contractual and legal restrictions and other factors the board deems relevant. Our Loan and Security Agreement with Wells Fargo Retail Finance, LLC as amended and restated on January 6, 2009, prohibits us from paying dividends without the consent of the lender.

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None.

Issuer Purchases of Equity Securities

In January 2008, the Board of Directors approved a repurchase program under which we were authorized to repurchase up to \$20.0 million of our common stock and/or Convertible Senior Notes due 2011 through December 31, 2009. Under this repurchase program, we repurchased approximately 1.2 million shares of our common stock in open market transactions for \$13.4 million during the year ended December 31, 2008. The Company had fully utilized the authorized this \$20.0 million repurchase program as of December 31, 2008.

We have a 401(k) defined contribution plan which permits participating employees to defer up to a maximum of 25% of their compensation, subject to limitations established by the Internal Revenue Code. Employees who have completed a half-year of service and are 21 years of age or older are qualified to participate in the plan. We match 50% of the first 6% of each participant's contributions to the plan. Participant contributions are immediately vested. Company contributions vest based on the participant's years of service at 20% per year over five years. Our matching contribution totaled \$389,000, \$494,000 and \$570,000 during the years ended December 31, 2006, 2007 and 2008, respectively. Beginning in 2006 and through January of 2008, our matching contribution was paid using common stock issued from treasury. In addition, for 2006 and 2007, the board of directors approved discretionary contributions of 2% of salary to all employees eligible to participate in the plan totaling \$409,000 and \$408,000, respectively. The contributions in 2006 and 2007 were settled with shares of our common stock in the following year. No discretionary contributions were approved or paid for 2008.

Stock based Compensation

Stock Options

Our board of directors adopted the Amended and Restated 1999 Stock Option Plan, the 2002 Stock Option Plan and the 2005 Equity Incentive Plan (collectively, the "Plans"), in May 1999, April 2002 and April 2005, respectively. Under these Plans, the Board of Directors may issue incentive stock options to our employees and directors and non-qualified stock options to our consultants, as well as other types of awards under the 2005 Equity Incentive Plan. Options granted under these Plans generally expire at the end of either five or ten years and vest in accordance with a vesting schedule determined by our Board of Directors, usually over four years from the grant date. As of the initial public offering, the Amended and Restated 1999 Stock Option Plan was terminated. Subsequent awards will be made under the 2005 Equity Incentive Plan. As of December 31, 2008, 1.2 million shares of stock based awards were available for future grants under the 2005 Equity Incentive Plan.

The following is a summary of stock option activity (amounts in thousands, except per share data):

	2006		2007		2008	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Outstanding beginning of year	1,299	\$ 18.09	1,011	\$ 18.97	1,161	\$ 20.48
Granted at fair value	183	22.47	762	18.14	11	14.14
Exercised	(276)	9.19	(354)	8.81	(112)	12.96
Canceled/forfeited	(195)	30.17	(258)	23.65	(86)	20.45
Outstanding end of year	1,011	18.97	1,161	20.48	974	21.27
Options exercisable at year-end	679	\$ 15.74	408	\$ 22.36	609	\$ 23.18

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Restricted Stock Units Activity

During the year ended December 31, 2008, 491,000 restricted stock units were granted. The cost of restricted stock units is determined using the fair value of our common stock on the date of the grant and compensation expense is recognized in accordance with the vesting schedule. The weighted average grant date fair value of restricted stock units granted during the year ended December 31, 2008 was \$12.64.

The following is a summary of restricted stock unit activity (amounts in thousands, except per share data):

	Units	2008 Grant Date Fair Value
Outstanding beginning of year		\$
Granted at fair value	491	12.64
Vested		
Canceled/forfeited	(42)	12.13
Outstanding end of year	449	12.69

Restricted stock units vested at year-end

Restricted stock units vest over three years at 25% at the end of the first year, 25% at the end of the second year and 50% at the end of the third year. During the years ended December 31, 2006, 2007 and 2008, the Company recorded stock based compensation related to restricted stock units of \$0, \$0 and \$896,000.

At December 31, 2008, 449,000 restricted stock units were outstanding. No restricted stock units had been vested as of December 31, 2008. On January 13, 2009, 337,000 restricted stock units were granted.

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	Year ended December 31,				
	2004	2005	2006(1)	2007	2008
	(in thousands, except per share data)				
Consolidated Statement of Operations Data:					
Revenue					
Direct revenue	\$ 212,264	\$ 323,136	\$ 301,509	\$ 197,088	\$ 174,203
Fulfillment partner revenue	278,357	471,839	478,628	568,814	660,164
Total revenue	490,621	794,975	780,137	765,902	834,367
Cost of goods sold					
Direct	183,653	280,647	284,774	168,008	154,501
Fulfillment partner	240,530	397,855	405,559	473,344	536,957
Total cost of goods sold	424,183	678,502	690,333	641,352	691,458
Gross profit	66,438	116,473	89,804	124,550	142,909
Operating expenses:					
Sales and marketing	40,559	77,155	70,897	55,458	57,634
Technology	8,509	27,901	65,158	59,453	57,815
General and administrative	22,024	33,043	46,837	41,976	38,373
Restructuring(2)			5,674	12,283	
Total operating expenses	71,092	138,099	188,566	169,170	153,822
Operating loss	(4,654)	(21,626)	(98,762)	(44,620)	(10,913)
Interest income, net	1,064	(161)	3,566	4,788	3,163
Interest expense	(775)	(5,582)	(4,765)	(4,188)	(3,462)
Other income (expense), net	(49)	4,728	81	(92)	(1,446)
Loss from continuing operations	(4,414)	(22,641)	(99,880)	(44,112)	(12,658)
Loss from discontinued operations		(2,571)	(6,882)	(3,924)	
Net loss	(4,414)	(25,212)	(106,762)	(48,036)	(12,658)
Deemed dividend related to redeemable common stock	(188)	(185)	(99)		
Net loss attributable to common shares	\$ (4,602)	\$ (25,397)	\$ (106,861)	\$ (48,036)	\$ (12,658)
Net loss per common share basic and diluted					
Loss from continuing operations	\$ (0.26)	\$ (1.17)	\$ (4.91)	\$ (1.86)	\$ (0.55)
Loss from discontinued operations	\$	\$ (0.13)	\$ (0.34)	\$ (0.17)	\$
Net loss per common share basic and diluted	\$ (0.26)	\$ (1.30)	\$ (5.25)	\$ (2.03)	\$ (0.55)
Weighted average common shares outstanding basic and diluted	17,846	19,429	20,332	23,704	22,901

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	As of December 31,				
	2004	2005	2006(3)	2007(3)	2008
	(in thousands)				
Balance Sheet Data:					
Cash and cash equivalents	\$ 198,678	\$ 55,875	\$ 126,965	\$ 101,394	\$ 100,577
Marketable securities	88,802	55,799		46,000	8,989
Working capital	267,640	79,561	59,475	62,621	39,679
Total assets	381,600	335,953	264,453	231,143	172,445
Total indebtedness	117,589	84,676	84,336	82,453	69,130
Redeemable common stock	3,166	3,205			
Stockholders' equity (deficit)	169,504	89,148	56,367	18,212	(2,985)

- (1) Effective January 1, 2006, we adopted SFAS 123(R) and recognized stock-based compensation of \$4.1 million, \$4.5 million, and \$3.3 million during the years ended December 31, 2006, 2007 and 2008, respectively.
- (2) During the fourth quarter of 2006, we commenced implementation of a facilities consolidation and restructuring program designed to reduce the overall expense structure in an effort to improve future operating performance (see Item 15 of Part IV, "Financial Statements" Note 3 "Restructuring Expense").
- (3) As part of the program to reduce our expense structure and sell non-core businesses, we decided during the fourth quarter of 2006 to sell our travel subsidiary ("OTravel"). As a result, OTravel's operations have been classified as a discontinued operation and therefore are not included in the results of continuing operations. The loss from discontinued operations for OTravel was \$6.9 million for the year ended December 31, 2006 (including a goodwill impairment charge of \$4.5 million) and \$3.9 million for the year ended December 31, 2007 (including a goodwill impairment charge of \$3.8 million see Item 15 of Part IV, "Financial Statements" Note 4 "Acquisition and Subsequent Discontinued Operations").

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ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This Annual Report on Form 10-K/A includes forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. All statements other than statements of historical fact, including statements regarding guidance, industry prospects or future results of operations or financial position, made in this Annual Report on Form 10-K/A are forward-looking. We use words such as anticipates, believes, expects, future, intends, and similar expressions to identify forward-looking statements. Forward-looking statements reflect management's current expectations and are inherently uncertain. Actual results could differ materially for a variety of reasons, including, among others, changes in global economic conditions and consumer spending, world events, the rate of growth of the Internet and online commerce, the amount that Overstock.com invests in new business opportunities and the timing of those investments, the mix of products sold to customers, the mix of net sales derived from products as compared with services, the extent to which we owe income taxes, competition, management of growth, potential fluctuations in operating results, international growth and expansion, fluctuations in foreign exchange rates, the outcomes of legal proceedings and claims, fulfillment center optimization, risks of inventory management, seasonality, the degree to which the Company enters into, maintains, and develops commercial agreements, acquisitions, and strategic transactions, payments risks, and risks of fulfillment throughput and productivity. In addition, the current global economic climate amplifies many of these risks. These risks and uncertainties, as well as other risks and uncertainties that could cause our actual results to differ significantly from management's expectations, are described in greater detail in Item 1A of Part I, "Risk Factors."

Overview

We are an online "closeout" retailer offering discount brand name merchandise, including bed-and-bath goods, home décor, kitchenware, watches, jewelry, electronics and computers, sporting goods, apparel, and designer accessories, among other products. We also sell books, magazines, CDs, DVDs and video games ("BMMG"). We also operate as part of our Website an online auctions business a marketplace for the buying and selling of goods and services as well as online sites for listing cars and real estate for sale.

We are based in Salt Lake City, Utah, and were founded in 1997. We launched our first Website through which customers could purchase products in March 1999. Our Website offers our customers an opportunity to shop for bargains conveniently, while offering our suppliers an alternative inventory liquidation distribution channel. We continually add new, limited inventory products to our Website in order to create an atmosphere that encourages customers to visit frequently and purchase products before our inventory sells out. We offer approximately 201,000 products under multiple departments under the shopping tab on our Website, and offer approximately 450,000 media products in the Books etc. department on our Website.

Closeout merchandise is typically available in inconsistent quantities and often is only available to consumers after it has been purchased and resold by disparate liquidation wholesalers. We believe that the traditional liquidation market is therefore characterized by fragmented supply and fragmented demand. We utilize the Internet to aggregate both supply and demand and create a more efficient market for liquidation merchandise. Our objective is to provide a one-stop destination for discount shopping for products and services sold through the Internet.

In the fourth quarter 2008, we faced unusual competition from brick and mortar retailers seeking to liquidate inventory directly. The macroeconomic slowdown and discounting by brick and mortar retailers have mixed effects on us. The effects include increased price competition and cautious consumers, but also include opportunities for us to acquire inventory at unusually low prices.

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Our Business

We use the Internet to create a more efficient market for liquidation, closeout and other discount merchandise. We provide consumers and businesses with quick and convenient access to high-quality, brand-name merchandise at discount prices. Our shopping business (sales of product offered through the Shopping section of our Website) includes both a "direct" business and a "fulfillment partner" business (see Item 15 of Part IV, "Financial Statements" Note 23 "Business Segments"). Products from our direct segment and fulfillment partner segments (including products from various industry verticals, such as florist supplies, restaurant supplies, and office supplies) are also available in bulk to both consumers and businesses through the Wholesale product category on our Website. During the years ended December 31, 2006, 2007, and 2008, no single customer accounted for more than 1% of our total revenue.

Direct business

Our direct business includes sales made to individual consumers and businesses, which are fulfilled from our warehouses in Salt Lake City, Utah (see Item 2 of Part I, "Properties"). During the years ended December 31, 2007 and 2008, we fulfilled approximately 25% and 21%, respectively, of all orders through our warehouses. Our warehouses generally ship between 5,000 and 8,000 orders per day and up to approximately 32,000 orders per day during peak periods, using overlapping daily shifts.

Fulfillment partner business

For our fulfillment partner business, we sell merchandise of other retailers, cataloguers or manufacturers ("fulfillment partners") through our Website. We are considered to be the primary obligor for the majority of these sales transactions and we record revenue from the majority of these sales transactions on a gross basis. Our use of the term "partner" or "fulfillment partner" does not mean that we have formed any legal partnerships with any of our fulfillment partners. We currently have fulfillment partner relationships with approximately 1,200 third parties which post approximately 196,000 non-BMMG products, as well as most of the BMMG products, on our Website.

Our revenue from sales on our shopping site from both the direct and fulfillment partner businesses is recorded net of returns, coupons and other discounts.

Both direct and fulfillment partner revenues are seasonal, with revenues historically being the highest in the fourth quarter, reflecting higher consumer holiday spending. We anticipate this will continue in the foreseeable future.

Unless otherwise indicated or required by the context, the discussion herein of our financial statements, accounting policies and related matters, pertains to the Shopping section of our Website and not necessarily to the Auctions, Cars, Real Estate or Community sections of our Website.

Auctions business

We operate an online auction service as part of our Website. Our auction tab allows sellers to list items for sale, buyers to bid on items of interest, and users to browse through listed items online. We record only our listing fees and commissions for items sold as revenue. From time to time, we also sell items returned from our shopping site on our auction site, and for these sales, we record the revenue on a gross basis. Revenue from our auction business is included in the fulfillment partner segment, as it is not significant enough to segregate as its own segment.

Car listing business

We operate an online site for listing cars for sale as a part of our Website. The car listing service allows sellers to list vehicles for sale and allows buyers to review vehicle descriptions, post offers to

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purchase, and provides the means for purchasers to contact sellers for further information and negotiations on the purchase of an advertised vehicle. Revenue from our car listing business is included in the fulfillment partner segment, as it is not significant enough to segregate as its own segment.

Real Estate listing business

We operate an online site for listing real estate for sale as a part of our Website. The real estate listing service allows customers to search active listings across the country. Listing categories include foreclosures, live and on-line auctions, for sale by owner listings, broker/agent listings and numerous aggregated classified ad listings. Advertising revenue from the real estate business is included in the fulfillment partner segment, as it is not significant enough to segregate as its own segment.

International business

We began selling products through our website to customers outside the United States in late August 2008. The initial launch included Canada and 33 European countries, including the U.K. and Germany. We do not have operations outside the United States, and are utilizing 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.

Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with generally accepted accounting principles of the United States ("GAAP") requires estimates and assumptions that affect the reported amounts of assets and liabilities, revenues and expenses, and related disclosures of contingent assets and liabilities in the consolidated financial statements and accompanying notes. The Securities and Exchange Commission ("SEC") has defined a company's critical accounting policies as the ones that are most important to the portrayal of the company's financial condition and results of operations, and which require the company to make its most difficult and subjective judgments, often as a result of the need to make estimates of matters that are inherently uncertain. Based on this definition, we have identified the critical accounting policies and judgments addressed below. We also have other key accounting policies, which involve the use of estimates, judgments, and assumptions that are significant to understanding our results. For additional information, see Item 15 of Part IV, "Financial Statements" Note 2 "Summary of Significant Accounting Policies." Although we believe that our estimates, assumptions, and judgments are reasonable, they are based upon information presently available. Actual results may differ significantly from these estimates under different assumptions, judgments, or conditions. Our critical accounting policies are as follows:

revenue recognition;

estimating valuation allowances and accrued liabilities (specifically, the reserve for returns, the allowance for doubtful accounts and the reserve for 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; and

stock-based compensation and performance share plan.

Revenue recognition

We derive our revenue primarily from two sources: direct revenue and fulfillment partner revenue, including listing fees and commissions collected from products being listed and sold through the

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Auctions tab of our Website as well as advertisement revenue derived from our cars listing business. The Company has organized its operations into two principal segments based on the primary source of revenue: Direct revenue and Fulfillment partner revenue (see Item 15 of Part IV, "Financial Statements" Note 23 "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 shipping carrier (as carriers differ in transit times); (ii) the fulfillment source (either our warehouses or those of our fulfillment partners); (iii) the 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. 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 loss for the year ended December 31, 2008 (in thousands):

Change in the Estimate of Average Transit Times (Days)	Year ended December 31, 2008	
	Effect on Revenue	Effect on Net Income
-2	\$ 7,633	\$ 1,264
-1	\$ 3,949	\$ 652
As reported	As reported	As reported
1	\$ (959)	\$ (142)
2	\$ (1,634)	\$ (259)

We evaluate the criteria outlined in EITF Issue No. 99-19, *Reporting Revenue Gross as a Principal Versus Net as an Agent*, 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 periodically provide incentive offers to our customers to encourage purchases. Such offers include discount offers, such as percentage discounts off current purchases and other similar offers, which, when used by our customers, are treated as a reduction to the purchase price of the related transaction.

Direct revenue

Direct revenue consists of sales of merchandise to both individual consumers and businesses that are fulfilled directly from our leased warehouses (see Item 2 of Part I, "Properties"). Direct sales occur primarily through our Website, but may also occur through other offline channels.

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Fulfillment partner revenue

Fulfillment partner revenue consists of merchandise sold through our Website and shipped by third parties directly to consumers and other businesses from warehouses maintained by our fulfillment partners.

During September 2004, we added an online auction service to our Website. The Auctions business allows sellers to list items for sale, buyers to bid on items of interest, and users to browse through listed items online. With limited exceptions, we are not considered the seller of the items sold on the auction site and have no control over the pricing of those items. Therefore, for these sales, only the listing fees for items listed and commissions for items sold are recorded as revenue during the period items are listed or items are sold. Revenue from the auctions business has been included in the fulfillment partner segment, as it is not large enough to separate out as its own segment at this early stage of the business.

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, post offers to purchase, and provides the means for purchasers to contact sellers for further information and negotiations on the purchase of an advertised vehicle. Revenue from the cars listing business is not large enough to separate as a segment, and therefore has been included within the fulfillment partner segment.

We operate an online site for listing real estate for sale as a part of our Website. The real estate listing service allows customers to search active listings across the country. Listing categories include foreclosures, live and on-line auctions, for sale by owner listings, broker/agent listings and numerous aggregated classified ad listings. Revenue from the real estate listing business is not large enough to separate as a segment, and therefore has been included within the fulfillment partner segment.

International business

We began selling products through our website to customers outside the United States in August 2008. The initial launch included Canada and 33 European countries, including the U.K. and Germany. We do not have operations outside the United States, and are utilizing 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.

Cost of goods sold

Cost of goods sold consists of the cost of the product, as well as inbound and outbound freight, warehousing and fulfillment costs (including payroll and related expenses and stock-based compensation), credit card fees and customer service costs.

Operating expenses

Sales and marketing expenses consist primarily of advertising, public relations and promotional expenditures, as well as payroll and related expenses, including stock-based compensation, for personnel engaged in marketing and selling activities.

Advertising expense is the largest component of our sales and marketing expenses and is primarily attributable to expenditures related to online marketing activities and offline radio and television advertising. Our advertising expenses totaled approximately \$68.1 million, \$51.0 million and \$52.8 million for the years ended December 31, 2006, 2007 and 2008, respectively, representing 96%, 92% and 92% of sales and marketing expenses for those respective periods.

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Technology expenses consist of wages and benefits, including stock-based compensation, for technology personnel, rent, utilities, connectivity charges, as well as support and maintenance and depreciation and amortization related to software and computer equipment.

General and administrative expenses consist of wages and benefits, including stock-based compensation, for executive, legal, accounting, merchandising and administrative personnel, rent and utilities, travel and entertainment, depreciation and amortization of intangible assets and other general corporate expenses.

Business Restructuring

During 2006, we began a facilities consolidation and restructuring program which continued through 2007 designed to reduce our overall expense structure in an effort to improve future operating performance. If we determine to move our corporate headquarters we expect to incur future restructuring expenses. (see Item 15 of Part IV, "Financial Statements" Note 3 "Restructuring Expense").

Deferred revenue

Payment is generally required by credit card at the point of sale. Amounts owed or received prior to delivery of products or services provided are recorded as deferred revenue. Amounts received in advance for Club O membership fees are recorded as deferred revenue and recognized ratably over the membership period. In addition, we sell gift cards and record related deferred revenue at the time of the sale. Revenue from a gift card is recognized when a customer redeems it. If a gift card is not redeemed, we recognize revenue when the likelihood of its redemption becomes remote.

Reserve for returns

Total revenue is recorded net of estimated returns. We maintain a reserve for returns based on current period revenues and historical returns experience. Management analyzes historical returns, current economic trends and changes in customer demand and acceptance of our products when evaluating the adequacy of the sales returns reserve and other allowances in any accounting period. The reserve for returns was \$6.9 million and \$5.1 million at December 31, 2007 and 2008, respectively.

Allowance for doubtful accounts

From time to time, we grant credit to certain of our business customers on normal credit terms (typically 30 days). We perform ongoing credit evaluations of our customers' financial condition and maintain an allowance for doubtful accounts receivable based upon our historical collection experience and expected collectability of all accounts receivable. We maintained an allowance for doubtful accounts receivable of \$2.5 million and \$1.6 million as of December 31, 2007 and 2008, respectively.

Reserve for obsolete and damaged inventory

We write down our inventory for estimated obsolescence or damage equal to the difference between the cost of inventory and the estimated 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 reserve represents the new cost basis of such products. Reversal of these reserves is recognized only when the related inventory has been sold or scrapped. At December 31, 2007, our inventory balance was \$25.6 million (including \$3.1 million of inventory in-transit related to sales shipped but not yet delivered), net of allowance for obsolescence or damaged inventory of \$1.8 million. At December 31, 2008, our inventory balance was \$17.7 million (including

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\$2.8 million of inventory in-transit related to sales shipped but not yet delivered), net of allowance for obsolescence or damaged inventory of \$2.1 million.

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. As required by Statement of Position 98-1, *Accounting for the Costs of Computer Software Developed or Obtained for Internal Use*, 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 years ended December 31, 2007 and 2008, we capitalized \$2.0 million and \$9.0 million, respectively, of costs associated with internal-use software and website development, both internally developed and acquired externally. Amortization of previously capitalized amounts totaled \$13.5 million and \$11.6 million for those respective periods.

Accounting for income taxes

Significant management judgment is required in determining our provision for income taxes, our deferred tax assets and liabilities and any valuation allowance recorded against our net deferred tax assets. As of December 31, 2007 and 2008, we have recorded a full valuation allowance of \$86.0 million and \$86.9 million, respectively, against our net deferred tax asset balance due to uncertainties related to our deferred tax assets as a result of our history of operating losses. The valuation allowance is based on our estimates of taxable income by jurisdiction in which we operate and the period over which our deferred tax assets will be recoverable. In the event that actual results differ from these estimates or we adjust these estimates in future periods, we may need to change the valuation allowance, which could materially impact our financial position and results of operations.

In July 2006, the Financial Accounting Standards Board ("FASB") issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes - an Interpretation of FASB Statement No. 109* ("FIN 48"). FIN 48 prescribes a comprehensive model for how a company should recognize, measure, present, and disclose in its financial statements uncertain tax positions that it has taken or expects to take on a tax return.

We adopted the provisions of FIN 48 on January 1, 2007. As a result of a full valuation allowance there was no effect on our financial condition or results of operations as a result of implementing FIN 48. We are subject to audit by the IRS and various states for periods since inception. Our policy is that we recognize interest and penalties accrued on any unrecognized tax positions as a component of income tax expense. As of the date of adoption of FIN 48, we did not have any accrued interest or penalties associated with unrecognized tax positions, nor was any interest expense recognized during the year ended December 31, 2008.

We have recorded no provision or benefit for federal and state income taxes as we have incurred net operating losses since inception. We have provided a full valuation allowance on the net deferred tax assets, consisting primarily of net operating loss carry-forwards, because of uncertainty regarding their realizability.

Valuation of long-lived and intangible assets and goodwill

Under Statement of Financial Accounting Standard ("SFAS") No. 142, *Goodwill and Other Intangible Assets*, ("SFAS 142"), goodwill is not amortized, but must be tested for impairment at least annually. Other long-lived assets must also be evaluated for impairment when management believes that an asset has experienced a decline in value that is other than temporary. Future adverse changes in

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market conditions or poor operating results of underlying investments could result in losses or an inability to recover the carrying value of the asset that may not be reflected in an asset's current carrying value, thereby possibly requiring an impairment charge in the future. Goodwill totaled \$2.8 million as of December 31, 2007 and 2008.

In conjunction with the decision to sell OTravel, our travel subsidiary, we performed an evaluation of its goodwill, pursuant to SFAS 144, *Accounting for the Impairment Long-Lived Assets*, ("SFAS 144") and SFAS 142 and determined that goodwill was subject to an impairment loss of approximately \$4.5 million and \$3.8 million during the years ended December 31, 2006 and 2007 (see Item 15 of Part IV, "Financial Statements" Note 4 "Acquisition and Subsequent Discontinued Operations"). These have been recorded as a component of the loss from discontinued operations. There were no impairments to goodwill recorded during the year ended December 31, 2008.

Stock-based compensation

As of January 1, 2006, we adopted SFAS 123(R) *Share Based Payment* ("SFAS 123(R)"), which requires us to measure compensation cost for all outstanding unvested share-based awards at fair value and recognize compensation over the service period for awards expected to vest. The estimation of stock awards that will ultimately vest requires judgment, and to the extent actual results differ from our 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, employee class, and historical experience. Actual results may differ substantially from these estimates. We use the Black-Scholes-Merton ("BSM") valuation model to estimate the value of stock options granted to employees. Several of the primary estimates used in measuring stock-based compensation are as follows:

Expected Volatility: The fair value of stock options were valued using a volatility factor based on our historical stock prices.

Expected Term: For 2005 and 2006 option grants, the expected term represents the period that our stock options are expected to be outstanding and was determined based on historical experience of similar awards, giving consideration to the contractual terms and vesting provisions of the stock-based awards. For 2007 and 2008 option grants, we elected to use the "simplified method" as discussed in Staff Accounting Bulletin ("SAB") No. 107, *Share Based Payment* ("SAB No. 107") to develop an estimate of expected term. In December 2007, the SEC issued SAB No. 110, *Certain Assumptions Used in Valuation Methods Expected Term* ("SAB No. 110"). According to SAB No. 110, under certain circumstances the SEC staff will continue to accept the use of the simplified method as discussed in SAB No. 107, in developing an estimate of expected term of "plain vanilla" share options in accordance with SFAS No. 123(R), beyond December 31, 2007. We adopted SAB No. 110 effective January 1, 2008 and will continue to use the simplified method in developing the expected term used for our valuation of stock-based compensation.

Expected Dividend: We have not paid any dividends and do not anticipate paying dividends in the foreseeable future.

Risk-Free Interest Rate: We base the risk-free interest rate used on the implied yield currently available on U.S. Treasury zero-coupon issues with remaining term equivalent to the expected term of the options.

Estimated Pre-vesting Forfeitures: When estimating forfeitures, we consider voluntary and involuntary termination behavior.

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Performance Share Plan

In January 2006, the Board of Directors and Compensation Committee adopted the Overstock.com Performance Share Plan (the "Plan") and approved grants to executive officers and certain employees of the Company. The Plan provided for a three-year period for the measurement of the Company's attainment of the performance goal described in the form of grant.

The performance goal was measured by growth in economic value, as defined in the Plan. The amount of payments due to participants under the Plan was a function of the then current market price of a share of the Company's common stock, multiplied by a percentage dependent on the extent to which the performance goal was attained, which was between 0% and 200%. If the growth in economic value was 10% compounded annually or less, the percentage would be 0%. If the growth in economic value was 25% compounded annually, the percentage would be 100%. If the growth in economic value was 40% compounded annually or more, the percentage would be 200%. If the percentage growth was between these percentages, the payment percentage would be determined on the basis of straight line interpolation. Amounts payable under the Plan were subject to Board discretion. Amounts payable under the Plan were originally payable in cash. During interim and annual periods prior to the third quarter of 2007, we recorded compensation expense based upon the period-end stock price and estimates regarding the ultimate growth in economic value that was expected to occur. These estimates included assumed future growth rates in revenues, gross profit percentages and other factors. If we were to use different assumptions, the estimated compensation charges could be significantly different.

An amendment to the Plan to allow the Company to make payments in the form of common stock was approved by the shareholders on May 15, 2007. In the third quarter of 2007, we determined the fair value of the awards on the amendment date and determined to make the payments in the form of common stock, rather than cash. Therefore, we reclassified awards under the Plan from their current status as liability awards to equity awards in accordance with SFAS No. 123(R).

Over the remaining six months of 2007, we reduced the estimated compensation expense under the plan by approximately \$550,000, based on changes in its estimate of growth in economic value over the remaining twelve months of the plan. As of December 31, 2007, the cumulative expense related to the performance share awards was \$1.0 million.

During the year ended December 31, 2008, we reversed the cumulative \$1.0 million in total compensation expense under the Plan as the Board determined no payments would be made under the plan. The plan expired on December 31, 2008.

Restricted Stock Units

During the year ended December 31, 2008, 491,000 restricted stock units were granted. The restricted stock units vest over three years at 25% at the end of the first year, 25% at the end of the second year and 50% at the end of the third year and are subject to the employee's continuing service to the Company. At December 31, 2008, there were 449,000 restricted stock units that remained outstanding.

The cost of restricted stock units is determined using the fair value of the Company's shares of common stock on the date of the grant and compensation expense is recognized in accordance with the vesting schedule. The weighted average grant date fair value of restricted stock units granted during the year ended December 31, 2008 was \$12.64.

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Recent Accounting Pronouncements.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* ("SFAS No. 159"). Under SFAS No. 159, companies may elect to measure certain financial instruments and certain other items at fair value. The standard requires that unrealized gains and losses on items for which the fair value option has been elected be reported in earnings. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. We adopted SFAS No. 159 on January 1, 2008; however, we did not elect to apply the fair value option to any financial instruments or other items upon adoption of SFAS No. 159 during the year ended December 31, 2008. Therefore, the adoption of SFAS No. 159 did not impact our consolidated financial position, results of operations or cash flows.

In December 2007, the FASB issued SFAS No. 141 (R), *Business Combinations* ("SFAS No. 141 (R)"), and SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements* ("SFAS No. 160"). SFAS No. 141 (R) requires an acquirer to measure the identifiable assets acquired, the liabilities assumed and any noncontrolling interest in the acquired entity at their fair values on the acquisition date, with goodwill being the excess value over the net identifiable assets acquired. SFAS No. 160 clarifies that a noncontrolling interest in a subsidiary should be reported as equity in the consolidated financial statements. The calculation of earnings per share will continue to be based on income amounts attributable to the parent. SFAS No. 141 (R) and SFAS No. 160 are effective for financial statements issued for fiscal years beginning after December 15, 2008. Early adoption is prohibited. We do not expect the adoption of SFAS No. 141 (R) or SFAS No. 160 will have a material impact on our financial position and results of operations or cash flows.

In March 2008, the FASB issued SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities - an amendment of FASB Statement No. 133* ("SFAS No. 161"). SFAS No. 161 requires enhanced disclosures about a company's derivative and hedging activities, in particular: 1) how and why derivative instruments are utilized; 2) how derivative instruments and related hedged items are accounted for under SFAS No. 133 and its related interpretations; and 3) how derivative instruments and related hedged items affect a company's financial position, financial performance and cash flows. SFAS No. 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008, with early adoption encouraged. We have no derivative instruments. Therefore, we do not expect the adoption of SFAS No. 161 to impact our financial position and results of operations or cash flows.

In April 2008, the FASB issued FSP No. 142-3, *Determination of the Useful Life of Intangible Assets* ("FSP No. 142-3"). FSP No. 142-3 amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under FASB Statement No. 142, *Goodwill and Other Intangible Assets*. FSP No. 142-3 is effective for financial statements issued for fiscal years beginning after December 15, 2008. Early adoption is prohibited. We do not expect the adoption of FSP No. 142-3 will have a material impact on our consolidated financial statements.

In May 2008, the FASB issued SFAS No. 162, *The Hierarchy of Generally Accepted Accounting Principles* ("SFAS No. 162"). The current GAAP hierarchy was established by the American Institute of Certified Public Accountants, and faced criticism because it was directed to auditors rather than entities. The issuance of this statement corrects this and makes some other hierarchy changes. This statement is effective 60 days following the Securities and Exchange Commission's approval of the Public Company Accounting Oversight Board amendments to AU Section 411, *The Meaning of Present Fairly in Conformity with Generally Accepted Accounting Principles*. The adoption of SFAS No. 162 did not result in a change to our consolidated financial statements.

In May 2008, the FASB issued FASB Staff Position ("FSP") APB 14-1, *Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)* ("FSP

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APB 14-1"), which clarifies the accounting for convertible debt instruments that may be settled in cash upon conversion, including partial cash settlement. FSP APB 14-1 specifies that an issuer of such instruments should separately account for the liability and equity components of the instruments in a manner that reflect the issuer's non-convertible debt borrowing rate when interest costs are recognized in subsequent periods. FSP APB 14-1 is effective for financial statements issued for fiscal years beginning after December 15, 2008 and interim periods within those fiscal years. We anticipate that the adoption of FSP APB 14-1 will not have a material impact on our consolidated financial statements.

We periodically review new accounting standards that are issued from time to time. Although some of these accounting standards may be applicable to us, we have not identified any other new standards that we believe merit further discussion and we expect that none would have a significant impact on our consolidated financial statements.

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 in this report. This executive commentary includes forward-looking statements, and investors are cautioned to read the "Special Note Regarding Forward-Looking Statements" included elsewhere in this report.

Commentary Revenue. We experienced strong revenue growth in the first three quarters of 2008. As of September 30, 2008, year-to-date revenue growth was 23% compared to a decrease of 2% for the same prior year period. However, our business experienced a significant slowdown in Q4 as consumers pulled back on discretionary spending over worries of a weakening economy. As a result, total revenue increased 9% for the fiscal year 2008 to \$834.4 million from \$765.9 million for the fiscal year 2007 notwithstanding a decrease of 13% in Q4 2008 revenue to \$255.9 million from \$294.5 million in Q4 2007.

The fulfillment partner business continued to be the primary driver of growth throughout 2008. We believe this is due to our initiative to considerably increase the number of non-media products we offer on our website. At the end of 2008, we had approximately 201,000 non-media SKUs on site compared to 63,000 at the end of last year, a 219% increase. The fulfillment partner business accounted for 79% of total revenue during 2008 and 81% during Q4, and it grew 16% for the full year, despite decreasing 9% in Q4 2008. Going forward, our plan is to continue to add products to existing and new categories from new and existing partners. We ended 2008 with 1,200 fulfillment partners, up from 730 a year ago.

Our direct business, unlike the fulfillment partner business, continued to contract in 2008 and revenues were down 12% from last year. As part of our initiative to add partner products to our website, some suppliers have transitioned into fulfillment partners, eliminating the need for us to purchase their inventory, and as a result, we have experienced a shift from direct to fulfillment partner business.

Commentary Gross Profit and Gross Profit Percentage. Higher revenues and better purchasing contributed to 15% growth in gross profit dollars in 2008. Gross profit rose to \$142.9 million, while gross profit percentage expanded 80 basis points to 17.1%, a historical best for the Company. Gross profit contracted in the fourth quarter by 6% due to lower revenues, but gross profit percentage expanded to 17.0% from 15.7%. This was partly due to a decision we made to be less promotional around the holiday season.

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In addition, during Q4 2008, we reduced Cost of Goods Sold by \$1.8 million for billing recoveries from partners who were underbilled earlier in the year for certain fees and charges that they were contractually obligated to pay. When the underbilling was originally discovered, we determined that the recovery of such amounts was not assured, and that consequently the potential recoveries constituted a gain contingency. Accordingly, we determined that the appropriate accounting treatment for the potential recoveries was to record their benefit only when such amounts became realizable (i.e., an agreement had been reached with the partner and the partner had the wherewithal to pay). We are currently reviewing our policies and procedures surrounding partner supplier cost updates and partner billing processes to ensure that the amounts contractually negotiated are billed in a complete and timely manner. We may have further billing recoveries from our partners in the future that we will seek to recover. We will recognize such recoveries in the manner described above. This accounted for 60 basis points of the 130 basis point improvement from Q4 2007. Gross profit percentages for each of the quarters and fiscal years during 2007 and 2008 were:

	Q1 2007	Q2 2007	Q3 2007	Q4 2007	FY 2007	Q1 2008	Q2 2008	Q3 2008	Q4 2008	FY 2008
Direct	11.7%	16.5%	15.3%	15.4%	14.8%	13.4%	12.5%	10.4%	8.7%	11.3%
Fulfillment Partner	16.6%	18.0%	17.7%	15.8%	16.8%	17.9%	19.0%	18.7%	19.0%	18.7%
Combined	15.2%	17.6%	17.1%	15.7%	16.3%	16.7%	17.6%	17.2%	17.0%	17.1%

Fulfillment partner gross profit benefited throughout the year from a mix shift of higher-margin sales away from the direct business and into the fulfillment partner business, and a continued shift away from our low margin BMMG business, which accounted for 5% of gross sales for 2008, down from 8% a year ago. Fulfillment partner gross profit expanded by 29% to \$123.2 million or 18.7% of revenue, a 190 basis point improvement.

In addition to the sales mix shift away from the direct business and lower revenues, higher product and freight costs negatively impacted direct gross profit, which declined 32% compared to 2007. Direct gross profit percentage fell by approximately 350 basis points to 11.3% despite a 40 basis point reduction in fulfillment costs.

Commentary Marketing. While revenues increased by 9% this year our sales and marketing expense increased only 4% to \$57.6 million during fiscal 2008, and marketing efficiency (marketing as a percentage of revenue) improved to 6.9% from 7.2% in 2007. In Q4 2007, we invested heavily in television, radio and print advertising to both strengthen our brand and enhance future revenue growth. We continued to invest in our brand throughout 2008, but with a more consistent, disciplined approach. Because our branding spend was minimal in the first three quarters of 2007, sales and marketing expenses rose sharply through the first three quarters of 2008 compared to 2007. In Q4 2008, we reduced the level of marketing to \$16.4 million or 6.4% of total revenue compared to \$27.4 million or 9.3% of total revenue in Q4 2007.

Commentary Contribution and Contribution Percentage. With higher gross profit and more efficient marketing, contribution (gross profit dollars less sales and marketing expense) increased 23% to \$85.3 million in 2008. Contribution as a percentage of revenue was 9.0% and 10.2% in 2007 and 2008, respectively. Contribution increased by 43% in Q4 to \$27.2 million, an \$8.2 million improvement

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due primarily to lower marketing costs. The following table represents our calculation of contribution (in thousands):

	Three months ended December 31,		Twelve months ended December 31,	
	2007	2008	2007	2008
Total revenue	\$ 294,516	\$ 255,862	\$ 765,902	\$ 834,367
Cost of goods sold	248,134	212,252	641,352	691,458
Gross profit	46,382	43,610	124,550	142,909
Less: Sales and marketing expense	27,377	16,437	55,458	57,634
Contribution	\$ 19,005	\$ 27,173	\$ 69,092	\$ 85,275
Contribution percentage	6.5%	10.6%	9.0%	10.2%

Commentary Technology and G&A costs. Our combined technology and G&A costs were down 5% to \$96.2 million for fiscal 2008. Technology costs fell 3% to \$57.8 million from \$59.5 million in 2007 as we offset falling depreciation expense with IT development and related staff in 2008.

G&A costs decreased 9.0% to \$38.4 million for the year 2008 from \$42.0 million or \$3.6 million. The primary reduction in G&A expenses year over year is primarily due to a \$4.1 million decrease in bonuses accrued in 2008 (including our decision to not pay senior executives and company-wide profit sharing bonuses). In addition, the performance goal described in the Performance Share Plan (the "Plan") was not attained as of the end of the year ended 2008 and \$1.0 million in total compensation expense accrued under the Plan was reversed. This year over year decrease was offset in part by an increase of approximately \$1.5 million related to consulting costs and professional fees. Technology/G&A costs have been falling over the last few years; we expect that trend will reverse in 2009 as we invest in development and corporate staff and projects.

Commentary Operating loss. Overall, our operating expenses, including sales and marketing, technology/G&A and restructuring were down 9% for 2008 and down 29% for Q4 2008 compared to the previous year. Our resulting operating loss for 2008 was \$10.9 million, a 76% improvement from \$44.6 million in 2007. For the three months ended December 31, 2008, our operating profit was \$5.7 million, \$12.5 million better than the \$6.8 million operating loss during the same period last year. The 2007 operating loss includes \$12.3 million of restructuring costs (\$6.1 million in Q1 2007 and \$6.2 million in Q2 2007). We did not incur any restructuring costs in 2008.

Commentary Other income (expense), net. For the year ended 2008, other expense was \$1.4 million and included a \$2.8 million gain on the retirement of \$9.5 million of 3.75% Senior Notes, a \$3.9 million loss on settlement of notes receivable and a \$300,000 other-than-temporary impairment of marketable securities.

Commentary Adjusted EBITDA (non-GAAP). Adjusted EBITDA (a non-GAAP financial measure) for fiscal 2008 was \$15.1 million, \$25.5 million better than the \$(10.5) million in 2007. For the fourth quarter of 2008, Adjusted EBITDA was \$9.9 million, a \$10.4 million improvement from (\$415,000) in Q4 2007. In 2008, capital expenditures were \$18.7 million, while depreciation expense was \$22.7 million. We believe that a discussion of Adjusted EBITDA at this stage of our business is useful to investors, as Adjusted EBITDA is a reasonable measure of actual cash used or cash generated by the continuing operations of our business. See "Non-GAAP Financial Measures" below for a reconciliation of Adjusted EBITDA to net income (loss).

Commentary Balance Sheet Items. We ended the year with \$109.6 million in cash, cash equivalents and marketable securities, compared to \$147.4 million at the end of 2007. Working capital

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decreased to \$39.7 million from \$62.6 million. The difference is largely the result of \$20 million of stock repurchases and debt retirement and \$18.7 million of capital expenditures.

We ended the year with \$17.7 million of inventory (including inventory in-transit of \$2.8 million), a decrease from the \$25.6 million of inventory (including inventory in-transit of \$3.1 million) we had at the end of 2007. We were able to turn our inventory more frequently due to more efficient inventory management and maintaining a more attractive product selection.

Commentary Cash Flows (non-GAAP). For the year ended December 31, 2008, we generated \$2.0 million in cash inflows from operations compared to cash inflows of \$10.0 million during 2007. "Free Cash Flow" (a non-GAAP financial measure) for the three months ended December 31, 2007 and 2008 totaled \$55.3 million and \$39.4 million, respectively. For the years ended December 31, 2007 and 2008, free cash flow was \$7.3 million and \$(16.7) million. See "Non-GAAP Financial Measures" below for a reconciliation of Free Cash Flow to net cash provided by operating activities.

Commentary Debt Repurchase Program. At December 31, 2008, \$67.5 million of our 3.75% Senior Convertible Notes due 2011 were outstanding. On February 17, 2009 our Board authorized us to spend up to \$20.0 million to repurchase Senior Notes. To date we have spent \$3.0 million under the new debt repurchase program.

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.

[Table of Contents](#)**Results of Operations**

The following table sets forth our results of operations expressed as a percentage of total revenue for 2006, 2007 and 2008:

	Years ended December 31,		
	2006	2007	2008
	(as a percentage of total revenue)		
Revenue			
Direct revenue	38.6%	25.7%	20.9%
Fulfillment partner revenue	61.4	74.3	79.1
Total revenue	100.0	100.0	100.0
Cost of goods sold			
Direct	36.5	21.9	18.5
Fulfillment partner	52.0	61.8	64.4
Total cost of goods sold	88.5	83.7	82.9
Gross profit	11.5	16.3	17.1
Operating expenses:			
Sales and marketing	9.1	7.2	6.9
Technology	8.4	7.8	6.9
General and administrative	6.0	5.5	4.6
Restructuring	0.7	1.6	0.0
Total operating expenses	24.2	22.1	18.4
Operating loss	(12.7)	(5.8)	(1.3)
Interest income, net	0.5	0.6	0.4
Interest expense	(0.6)	(0.6)	(0.4)
Other (expense) income, net	0.0	(0.0)	(0.2)
Loss from continuing operations	(12.8)%	(5.8)%	(1.5)%

Comparison of Years Ended December 31, 2007 and 2008**Revenue**

Total revenue increased 9% to \$834.4 million for the year ended December 31, 2008, from \$765.9 million in 2007. During the three months ended December 31, 2007 and 2008, total revenue was \$294.5 million and \$255.9 million, respectively, a 13% decrease. Direct revenue decreased 12% from \$197.1 million in 2007 to \$174.2 million in 2008. In the fourth quarters, direct revenue decreased 28%, from \$67.2 million in 2007 to \$48.4 million in 2008. Fulfillment partner revenue increased 16% during fiscal 2008, but decreased 9% during the fourth quarter. For the year ended December 31, 2008, fulfillment partner revenue was \$660.2 million compared to \$568.8 million in 2007. For the three months ended December 31, 2008, fulfillment partner revenue was \$207.4 million compared to \$227.3 million in 2007.

Gross profit and gross profit percentage

Generally, our overall gross profit percentages fluctuate based on several factors, including our product mix of sales; sales volumes mix within our direct business and fulfillment partners business; changes in vendor and / or customer pricing, including competitive pricing and inventory management decisions within the direct business; warehouse management costs; customer service costs; and our

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discounted shipping offers. Discounted shipping offers reduce shipping revenue, and therefore reduce our gross profit percentage on retail sales.

Gross profit percentage for the twelve months ended December 31, 2008 increased 80 basis points, from 16.3% in 2007 to 17.1% in 2008. Gross profit for the years ended December 31, 2007 and 2008 amounted to \$124.6 million and \$142.9 million, respectively, a 15% increase. For the three months ended December 31, 2008, gross profit percentage increased 130 basis points, from 15.7% in 2007 to 17.0% in 2008, and gross profit decreased 6% from \$46.4 million in Q4 2007 to \$43.6 million in Q4 2008. Gross profit percentages for the quarters and fiscal years during 2007 and 2008 were:

Q1 2007	Q2 2007	Q3 2007	Q4 2007	FY 2007	Q1 2008	Q2 2008	Q3 2008	Q4 2008	FY 2008
15.2%	17.6%	17.1%	15.7%	16.3%	16.7%	17.6%	17.2%	17.0%	17.1%

Cost of goods sold includes stock-based compensation related to the adoption of SFAS 123(R) of \$460,000 and \$181,000 for the years ended December 31, 2007 and 2008, respectively.

Direct Gross Profit and Gross Profit Percentage Gross profit for our direct business declined 32% from \$29.1 million during the year ended December 31, 2007 to \$19.7 million for the same period in 2008. Gross profit for our direct business as a percentage of direct revenue decreased from 14.8% in 2007 to 11.3% in 2008. For the three-month periods ended December 31, 2007 and 2008, gross profit for our direct business totaled \$10.4 million and \$4.2 million, respectively, a 59% decrease. Gross profit percentage for our direct business for those three-month periods decreased from 15.4% in 2007 to 8.7% in 2008.

Gross profit percentage for our direct business decreased along with a decrease in direct revenue of 12% for fiscal 2008, decreasing 28% for the fourth quarter of 2008 compared to the respective periods in 2007. While fulfillment costs continue to improve, these benefits are more than offset by our fixed warehouse cost being amortized over a smaller direct revenue base.

Fulfillment Partner Gross Profit and Gross Profit Percentage Our fulfillment partner business generated gross profit of \$95.5 million and \$123.2 million for the years ended December 31, 2007 and 2008, respectively, a 29% improvement. Gross profit percentage for the fulfillment partner business also increased from 16.8% in 2007 to 18.7% in 2008 for those respective periods. The increase in gross profit dollars for our fulfillment partner business is the result of the 16% increase in fulfillment partner revenue combined with increased gross profit percentage.

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 profit percentage. We believe that some companies in our industry, including some of our competitors, account for fulfillment costs within operating expenses, and therefore exclude fulfillment costs from gross profit percentage. As a result, our gross profit percentage may not be directly comparable to others in our industry.

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

	Years ended December 31,			
	2007		2008	
Total revenue	\$ 765,902	100%	\$ 834,367	100%
Cost of goods sold				
Product costs and other cost of goods sold	594,276	78%	644,212	77%
Fulfillment costs	47,076	6%	47,246	6%
Total cost of goods sold	641,352	84%	691,458	83%
Gross profit	\$ 124,550	16%	\$ 142,909	17%

As displayed in the above table, fulfillment costs during the years ended December 31, 2007 and 2008 were \$47.1 million and \$47.2 million, representing 6% of total revenue for those respective periods. 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 utilize third party fulfillment services and warehouses, and our ability to effectively manage customer service costs and credit card fees.

Operating expenses

Sales and marketing. Sales and marketing expenses totaled \$55.5 million and \$57.6 million for the years ended December 31, 2007 and 2008, representing 7% of total revenue for those respective periods. Comparing 2007 and 2008, sales and marketing expenses increased 4% from 2007 to 2008. We direct customers to our Website primarily 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 nation-wide television, print and radio advertising campaigns to promote sales. Sales and marketing expenses also include stock-based compensation related to the adoption of SFAS 123(R) in 2006 of \$336,000 and \$313,000 for the years ended December 31, 2007 and 2008, respectively.

Costs associated with our discounted shipping promotions are not included in marketing expense. Rather they are accounted for as a reduction of revenue and therefore affect sales growth and gross profit percentage. We consider discounted shipping promotions 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 efficiently invest in our technology, including web services, customer support, search, and expansion of new and existing product categories, as well as technology infrastructure to continue to enhance the customer experience, improve our process efficiency and support our web services infrastructure.

Technology expenses totaled \$59.5 million and \$57.8 million for the years ended December 31, 2007 and 2008, respectively (7.8% and 6.9% of revenue for 2007 and 2008). From 2007 to 2008, technology expenses decreased 3% primarily due to decreased depreciation expense. Technology expenses also included stock-based compensation related to the adoption of SFAS 123(R) in 2006 of \$764,000 and \$792,000 for the years ended December 31, 2007 and 2008, respectively.

General and administrative expenses. General and administrative ("G&A") expenses totaled \$42.0 million and \$38.4 million for the years ended December 31, 2007 and 2008, respectively, representing approximately 5.5% and 4.6% of total revenue, respectfully. G&A costs decreased 9.0% to \$38.4 million for the year 2008 from \$42.0 million or \$3.6 million. The primary reduction in G&A expenses year over year is primarily due to a \$4.1 million decrease in bonuses accrued in 2008

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(including our decision to not pay senior executives and company-wide profit sharing bonuses). In addition, the performance goal described in the Performance Share Plan (the "Plan") was not attained as of the end of the year ended 2008 and \$1.0 million in total compensation expense accrued under the Plan was reversed. This year over year decrease was offset in part by an increase of approximately \$1.5 million related to consulting costs and professional fees.

We incurred stock-based compensation related to the adoption of SFAS 123(R) in 2006 within general and administrative expenses of approximately \$3.0 million and \$2.0 million for the years ended December 31, 2007 and 2008, respectively.

A large portion of our technology and general and administrative expenses are non-cash expenses. These non-cash expenses (which include depreciation and amortization and stock-based compensation) for the year ended December 31, 2008 were \$26.0 million, compared to similar non-cash expense of \$34.2 million during 2007. We estimate that that these non-cash expenses for 2009 will be approximately \$18-\$20 million.

Overall, our total operating expenses decreased 9% during fiscal 2008 compared to the previous year, while total revenues increased 9% and gross profit increased 15%.

Restructuring expenses. During the fourth quarter of 2006, we commenced a facilities consolidation and restructuring program designed to reduce our 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. There were no restructuring expenses recorded during the third and fourth quarters of 2007 or for any period in 2008. If we determine to move our corporate headquarters we expect to incur future restructuring expenses. (see Item 15 of Part IV, "Financial Statements" Note 3 "Restructuring Expense").

During fiscal year 2006, we recorded \$5.7 million of restructuring charges, of which \$4.6 million related to costs to terminate a co-location data center lease. Other costs included in the restructuring charge related to \$638,000 of accelerated amortization of leasehold improvements in our current office facilities that we are attempting to sublease, and \$450,000 of costs to return these office facilities to their original condition as required by the lease agreement.

During fiscal year 2007, we recorded \$12.3 million of restructuring charges, of which \$9.9 million related to the termination of a logistics services agreement, termination and settlement of a lease related to vacated warehouse facilities in Indiana, and abandonment and marketing for sub-lease office and data center space in our current corporate office facilities. We also recorded an additional \$2.2 million of restructuring charges related to accelerated depreciation of leasehold improvements located in the abandoned office and co-location data center space and \$200,000 of other miscellaneous restructuring charges. We had no restructuring charges in 2008.

Non-operating income (expense)

Interest income and interest expense. Interest income is primarily derived from the investment of our cash in short-term investments. Comparing 2007 and 2008, the decrease in interest income is due to a decrease in total cash and interest rates in 2008.

Interest expense is largely related to interest incurred on our convertible notes and our credit lines. Interest expense for the years ended December 31, 2007 and 2008 totaled \$4.2 million and \$3.5 million, respectively.

Other income (expense). Other income (expense) for the year ended December 31, 2007 was net expense of \$(92,000). For the year ended December 31, 2008, other income (expense) was net expense of \$(1.4) million. This included a \$2.8 million gain, net of amortization of debt discount of \$142,000 on the retirement of \$9.5 million of the 3.75% Senior Notes (see Item 15 of Part IV, "Financial

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Statements" Note 17 "Stock and Debt Repurchase Program"), a \$3.9 million loss on the settlement of notes receivable (see Item 15 of Part IV, "Financial Statements" Note 4 "Acquisition and Subsequent Discontinued Operations") and a \$300,000 other-than-temporary impairment of marketable securities.

On January 14, 2008, the Company's Board of Directors authorized a repurchase program that allowed the Company to purchase up to \$20.0 million of its common stock and / or its 3.75% Senior Convertible Notes due 2011 ("Senior Notes") through December 31, 2009. During the year ended 2008, we retired \$9.5 million of the Senior Notes for \$6.6 million in cash and recognized a gain of \$2.8 million, net of amortization of debt discount of \$142,000.

Sale of discontinued operations

We determined during the fourth quarter of 2006 to sell our travel subsidiary ("OTravel"). As a result, OTravel's operations were classified as a discontinued operation and therefore are not included in the results of continuing operations. The loss from discontinued operations for OTravel was \$6.9 million and \$3.9 million for the years ended December 31, 2006 and 2007, respectively.

In conjunction with the discontinuance of OTravel, we performed an evaluation of the goodwill associated with the reporting unit pursuant to SFAS 142 and SFAS 144 and determined that goodwill of approximately \$4.5 million was impaired as of December 31, 2006 based on a non-binding letter of intent from a third party to purchase this business. On April 25, 2007, we completed the sale of OTravel for cash proceeds of \$9.9 million, net of cash transferred, and \$6.0 million of notes. Based on the estimated fair value of the discounted cash flows of the net proceeds from the sale, we recorded an additional goodwill impairment of \$3.8 million in 2007. (see Item 15 of Part IV, "Financial Statements" Note 4 "Acquisition and Subsequent Discontinued Operations").

On January 21, 2009, we entered into a Note Purchase Agreement to sell both the senior and junior promissory notes to Castles Travel, Inc for \$1.3 million in cash and recognized a loss on the settlement of these notes and interest receivable of approximately \$3.9 million which was recorded as of December 31, 2008 (see Item 15 of Part IV, "Financial Statements" Note 4 "Acquisition and Subsequent Discontinued Operations").

Income taxes

For the year ended December 31, 2007 and 2008, we incurred net operating losses, and consequently paid insignificant amounts of federal, state and foreign income taxes. As of December 31, 2007 and 2008, we had net operating loss carry-forwards of approximately \$164.2 million and \$171.8 million, respectively, which may be used to offset future taxable income. An additional \$21.9 million of net operating losses are limited under Internal Revenue Code Section 382 to \$799,000 a year. These net operating loss carry-forwards will begin to expire in 2018.

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

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our results of operations in the future. The following table reflects our total revenues for each of the quarters since 2005 (in thousands):

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
2008	\$ 202,814	\$ 188,836	\$ 186,855	\$ 255,862
2007	162,156	149,171	160,059	294,516
2006	179,783	159,717	158,230	282,407
2005	165,028	153,519	166,396	310,033

Comparison of Years Ended December 31, 2006 and 2007**Revenue**

Total revenue decreased 2% to \$765.9 million for the year ended December 31, 2007, from \$780.1 million in 2006. During the three months ended December 31, 2006 and 2007, total revenue was \$282.4 million and \$294.5 million, respectively, a 4% increase. Direct revenue decreased 35% from \$301.5 million in 2006 to \$197.1 million in 2007, and comparing the fourth quarters, direct revenue decreased 29%, from \$94.4 million in 2006 to \$67.2 million in 2007. On the other hand, fulfillment partner revenue experienced 19% growth during fiscal 2007 and 21% growth during the fourth quarter. For the year ended December 31, 2007, fulfillment partner revenue was \$568.8 million compared to \$478.6 million in 2006. For the three months ended December 31, 2007, fulfillment partner revenue was \$227.3 million versus \$188.0 million in 2006.

Gross Profit Percentage

Generally, our overall gross profit percentages fluctuate based on several factors, including our product mix of sales; sales volumes mix by our direct business and fulfillment partners businesses; changes in vendor and / or customer pricing, including competitive pricing and inventory management decisions within the direct business; warehouse management costs; customer service costs; and our discounted shipping offers. Discounted shipping offers reduce shipping revenue, and therefore reduce our gross profit percentage on retail sales.

Gross profit percentage for the twelve months ended December 31, 2007 increased 480 basis points, from 11.5% in 2006 to 16.3% in 2007. Gross profit for the years ended December 31, 2006 and 2007 amounted to \$89.8 million and \$124.6 million, respectively, a 39% increase. For the three-month period ended December 31, 2007, gross profit percentage increased 730 basis points, from 8.4% in 2006 to 15.7% in 2007, and gross profit increased 95% from \$23.8 million in 2006 to \$46.4 million in 2007. Gross profit percentages for the quarters and fiscal years during 2006 and 2007 were:

Q1 2006	Q2 2006	Q3 2006	Q4 2006	FY 2006	Q1 2007	Q2 2007	Q3 2007	Q4 2007	FY 2007
12.8%	13.5%	13.6%	8.4%	11.5%	15.2%	17.6%	17.1%	15.7%	16.3%

Cost of goods sold includes stock-based compensation related to the adoption of SFAS 123(R) of \$412,000 and \$460,000 for the years ended December 31, 2006 and 2007, respectively.

Direct Gross Profit and Gross Profit Percentage Gross profit for our direct business grew 74% from \$16.7 million during the year ended December 31, 2006 to \$29.1 million for the same period in 2007. Gross profit for our direct business as a percentage of direct revenue increased from 5.6% in 2006 to 14.8% in 2007. For the three-month periods ended December 31, 2006 and 2007, gross profit for our direct business totaled \$(4.3) million and \$10.4 million, respectively, a 342% increase. Gross profit percentage for our direct business for those three-month periods increased from -4.5% in 2006 to 15.4% in 2007. Gross profit percentage for our direct business expanded despite direct revenue decreasing 35% for fiscal 2007 and decreasing 29% for the fourth quarter of 2007 compared to the respective periods in 2006. This was primarily due to a significant reduction in direct inventory.

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However, gross profit percentages have increased at the same time, since the remaining inventory in general turns faster and has higher profitability. Gross profit percentages have also improved from the reduction of fulfillment costs (defined as warehousing costs, credit card fees and customer service costs see further discussion in the following section entitled "Fulfillment Costs") to 6.1% of sales in 2007 compared to 7.8% in 2006, a 170 basis point improvement.

Fulfillment Partner Gross Profit and Gross Profit Percentage Our fulfillment partner business generated gross profit of \$73.1 million and \$95.5 million for the years ended December 31, 2006 and 2007, respectively, a 31% improvement. Gross profit percentage for the fulfillment partner business also increased from 15.3% in 2006 to 16.8% in 2007 for those respective periods. The increase in gross profit dollars for our fulfillment partner business is the result of the 19% increase in fulfillment partner revenue combined with increased gross profit percentage. The increase in partner gross profit percentage is the result of better product pricing and improvements in partner fulfillment costs, particularly the cost of customer service.

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 profit percentage. We believe that some companies in our industry, including some of our competitors, account for fulfillment costs within operating expenses, and therefore exclude fulfillment costs from gross profit percentage. As a result, our gross profit percentage 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 and gross profit percentage, thus enabling investors to better compare our gross profit percentage with others in our industry (in thousands):

	Years ended December 31,			
	2006		2007	
Total revenue	\$780,137	100%	\$765,902	100%
Cost of goods sold				
Product costs and other cost of goods sold	629,477	81%	594,276	78%
Fulfillment costs	60,856	7%	47,076	6%
Total cost of goods sold	690,333	88%	641,352	84%
Gross profit	\$ 89,804	12%	\$ 124,550	16%

As displayed in the above table, fulfillment costs during the years ended December 31, 2006 and 2007 were \$60.9 million and \$47.1 million, representing 7% and 6% of total revenue for those respective periods. 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 utilize third party fulfillment services and warehouses, and our ability to effectively manage customer service costs and credit card fees.

Operating expenses

Sales and marketing. Sales and marketing expenses totaled \$70.9 million and \$55.5 million for the years ended December 31, 2006 and 2007, representing 9% and 7% of total revenue for those respective periods. Comparing 2006 and 2007, sales and marketing expenses decreased 22% from 2006 to 2007. We direct customers to our Website primarily through a number of targeted online marketing channels, such as sponsored search, affiliate marketing, portal advertising, e-mail campaigns, and other initiatives. We also utilize channels such as nation-wide television, print and radio advertising campaigns. Sales and marketing expenses also include stock-based compensation related to the adoption of SFAS 123(R) in 2006 of \$301,000 and \$336,000 for the years ended December 31, 2006 and 2007, respectively.

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Costs associated with our discounted shipping promotions are not included in marketing expense. Rather they are accounted for as a reduction of revenue and therefore affect sales growth and gross profit. We consider discounted shipping promotions 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. Technology expenses totaled \$65.2 million and \$59.5 million for the years ended December 31, 2006 and 2007, respectively (8% of revenue in both years). From 2006 to 2007, technology expenses decreased 9% primarily due to decreased depreciation expense. Technology expenses also included stock-based compensation related to the adoption of SFAS 123(R) in 2006 of \$684,000 and \$764,000 for the years ended December 31, 2006 and 2007, respectively.

General and administrative expenses. General and administrative ("G&A") expenses totaled \$46.8 million and \$42.0 million for the years ended December 31, 2006 and 2007, respectively, representing approximately 6% of total revenue for both years. Comparing fiscal years 2006 and 2007, general and administrative expenses decreased 10%. The decrease in G&A expenses relates to decreases in corporate facilities costs, payroll-related expenses, professional fees, merchandising, legal and finance costs as we have made reductions to our corporate office space and headcount.

We incurred stock-based compensation related to the adoption of SFAS 123(R) in 2006 within general and administrative expenses of approximately \$2.7 million and \$3.0 million for the years ended December 31, 2006 and 2007, respectively.

A large portion of our technology and general and administrative expenses are non-cash expenses. These non-cash expenses (which include depreciation and amortization and stock-based compensation and excludes non-cash restructuring costs) for the year ended December 31, 2007 were \$34.2 million, compared to similar non-cash expense of \$37.3 million during 2006. We estimate that that these non-cash expenses for 2008 will be approximately \$28-\$30 million.

Overall, our total operating expenses decreased 10% during fiscal 2007 compared to the previous year, while total revenues decreased 2% and gross profit increased 39%.

Restructuring expenses. During the fourth quarter of 2006, we commenced a facilities consolidation and restructuring program designed to reduce our 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. There were no restructuring expenses recorded during the third and fourth quarters of 2007 (see Item 15 of Part IV, "Financial Statements" Note 3 "Restructuring Expense").

During fiscal year 2006, we recorded \$5.7 million of restructuring charges, of which \$4.6 million related to costs to terminate a co-location data center lease. Other costs included in the restructuring charge related to \$638,000 of accelerated amortization of leasehold improvements in our current office facilities that we are attempting to sublease, and \$450,000 of costs to return these office facilities to their original condition as required by the lease agreement.

During fiscal year 2007, we recorded \$12.3 million of restructuring charges, of which \$9.9 million related to the termination of a logistics services agreement, termination and settlement of a lease related to vacated warehouse facilities in Indiana, and abandonment and marketing for sub-lease office and data center space in our current corporate office facilities. We also recorded an additional \$2.2 million of restructuring charges related to accelerated depreciation of leasehold improvements located in the abandoned office and co-location data center space and \$200,000 of other miscellaneous restructuring charges.

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Non-operating income (expense)

Interest income, interest expense and other income (expense). Interest income is derived from the investment of our cash in short-term investments. Over the last two years, interest income totaled \$3.6 million and \$4.8 million for the years ended December 31, 2006 and 2007, respectively. Comparing 2006 and 2007, the increase in interest income is due to an increase in total cash and interest rates in 2007, and from interest income earned from our notes receivable related to the sale of our OTravel business which occurred in the second quarter of 2007 (see Item 15 of Part IV, "Financial Statements" Note 4 "Acquisition and Subsequent Discontinued Operations"). During Q2 of 2006, we recorded \$1.9 million of interest income related to the sale of Foreign Notes (see Item 15 of Part IV, "Financial Statements" Note 5 "Marketable Securities").

Interest expense is largely related to interest incurred on our convertible notes, capital leases and our credit lines. Interest expense for the years ended December 31, 2006 and 2007 totaled \$4.8 million and \$4.2 million, respectively. The decrease from 2006 to 2007 is due primarily to the fact that we had \$20 million of borrowings outstanding on our inventory line of credit in the first quarter of 2006, and no borrowings outstanding during the same period in 2007.

Other income (expense) for the year ended December 31, 2006 was income of \$81,000 and net expense of \$92,000 in 2007.

Discontinued operations

We determined during the fourth quarter of 2006 to sell our travel subsidiary ("OTravel"). As a result, OTravel's operations were classified as a discontinued operation and therefore are not included in the results of continuing operations. The loss from discontinued operations for OTravel was \$6.9 million and \$3.9 million for the years ended December 31, 2006 and 2007, respectively.

In conjunction with the discontinuance of OTravel, we performed an evaluation of the goodwill associated with the reporting unit pursuant to SFAS 142 and SFAS 144 and determined that goodwill of approximately \$4.5 million was impaired as of December 31, 2006 based on a non-binding letter of intent from a third party to purchase this business. On April 25, 2007, we completed the sale of OTravel for cash proceeds of \$9.9 million, net of cash transferred, and \$6.0 million of notes. Based on the estimated fair value of the discounted cash flows of the net proceeds from the sale, we recorded an additional goodwill impairment of \$3.8 million. There was no additional impairment of goodwill during the year ended December 31, 2007 (see Item 15 of Part IV, "Financial Statements" Note 4 "Acquisition and Subsequent Discontinued Operations").

On January 21, 2009, we entered into a Note Purchase Agreement to sale both the senior and junior promissory notes to Castles Travel, Inc for \$1.3 million in cash and recognized a loss on the settlement of these notes and interest receivable of approximately \$3.9 million (see Item 15 of Part IV, "Financial Statements" Note 4 "Acquisition and Subsequent Discontinued Operations").

Income taxes

For the year ended December 31, 2006 and 2007, we incurred net operating losses, and consequently paid insignificant amounts of federal, state and foreign income taxes. As of December 31, 2006 and 2007, we had net operating loss carry-forwards of approximately \$145.2 million and \$164.2 million, respectively, which may be used to offset future taxable income. An additional \$21.9 million of net operating losses are limited under Internal Revenue Code Section 382 to \$799,000 a year. These net operating loss carry-forwards will begin to expire in 2018.

Table of Contents**Liquidity and Capital Resources****Historical sources of liquidity**

Prior to the second quarter of 2002, we financed our activities primarily through a series of private sales of equity securities, warrants to purchase our common stock and promissory notes. During the second quarter of 2002, we completed our initial public offering pursuant to which we received approximately \$26.1 million in cash, net of underwriting discounts, commissions, and other related expenses. Additionally, we completed follow-on offerings in February 2003, May 2004 and November 2004, pursuant to which we received approximately \$24.0 million, \$37.9 million and \$75.2 million, respectively, in cash, net of underwriting discounts, commissions, and other related expenses. In November 2004, we also received \$116.2 million in proceeds from the issuance of our convertible senior notes in a transaction event exempt from registration under the Securities Act. During 2006, we received \$64.4 million from two stock offerings in May and December.

Current sources of liquidity

While we believe that the cash and marketable securities currently on hand, amounts available under our credit facility 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. However, 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. Failure to generate sufficient revenues, profits or to raise additional capital could have a material adverse effect on our ability to continue as a going concern and 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, cash equivalents, and sale or maturity of marketable securities. At December 31, 2008, our cash and cash equivalents balance was \$100.6 million and we had \$9.0 million in marketable securities, for a total of \$109.6 million of cash, cash equivalents and marketable securities.

Cash flow information is as follows:

	Year Ended December 31,		
	2006	2007	2008
	(in thousands)		
Cash provided by (used in):			
Operating activities	\$(26,293)	\$ 9,977	\$ 1,960
Investing activities	33,367	(33,514)	19,550
Financing activities	63,983	(2,031)	(22,327)

Free Cash Flow. "Free Cash Flow" (a non-GAAP measure) for the years ended December 31, 2007 and 2008, was \$7.3 million and \$(16.7) million. See "Non-GAAP Financial Measures" below for a reconciliation of Free Cash Flow to net cash provided by operating activities.

Cash provided by (used in) operating activities. For the years ended December 31, 2007 and 2008, our operating activities resulted in net cash inflows of \$10.0 million and net cash inflows of \$2.0 million, respectively.

Cash received from customers generally corresponds to our net sales 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 seasonally strong fourth quarter sales, at December 31 of each year, our cash, cash equivalents, marketable securities and accounts payable balances typically reach their highest level (other than as a result of cash flows

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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, cash equivalents, and marketable securities 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 paid.

The primary operating use of cash and cash equivalents during the year ended December 31, 2008 was to fund our net losses of \$12.7 million (which includes \$27.3 million of net non-cash activity, including \$3.9 million related to the loss on settlement of notes receivable (see Item 15 of Part IV, "Financial Statements" Note 4 "Acquisition and Subsequent Discontinued Operations") and \$2.8 million related to the gain from early extinguishment of debt (see Item 15 of Part IV, "Financial Statements" Note 17 "Stock and Debt Repurchase Program"), as well as changes in prepaid expenses, other long term assets, accounts payable, accrued liabilities, deferred revenue and other long-term liabilities of \$2.1 million, \$516,000, \$8.2 million, \$12.3 million, \$3.9 million and \$462,000, respectively. This was offset by the cash provided from changes in accounts receivable, inventories, net, and prepaid inventory of \$4.8 million, \$7.9 million and \$2.2 million, respectively.

In late December 2008, our credit card processor began withholding approximately 1% of our daily credit card remittances as a reserve. They have indicated that they expect to continue such withholding until the reserve reaches a total of \$3.5 million. The reserve was \$125,000 at December 31, 2008 and is included in Accounts Receivable in the Consolidated Balance Sheets.

The primary operating use of cash and cash equivalents during the year ended December 31, 2007 was to fund our net losses of \$48.0 million (which includes \$50.4 million of loss from discontinued operations and other net non-cash activity), as well as changes in inventories, prepaid inventory, prepaid expenses, accrued liabilities, deferred revenue and other long-term liabilities of \$1.8 million, \$1.3 million, \$99,000, \$5.9 million, \$255,000 and \$193,000, respectively. This was offset by the cash provided from changes in accounts receivable, other long-term assets and accounts payable of \$4.8 million, \$471,000 and \$11.8 million, respectively.

Cash provided by (used in) investing activities. Cash provided by (used in) investing activities corresponds with purchases, sales, and maturities of marketable securities, cash purchases of fixed assets, including internal-use software and website development costs. Investing activities resulted in cash outflows of \$33.5 million and cash inflows of \$19.6 million for the years ended December 31, 2007 and 2008, respectively. The \$19.6 million provided by investing activities during fiscal 2008 resulted from the net cash outflows for expenditures of fixed assets of \$18.7 million, offset by payments received from purchases, sales and maturities of marketable securities of \$36.7 million and a note receivable of \$1.5 million related to the sale of the Company's interest in a variable interest entity (see Item 15 of Part IV, "Financial Statements" Note 25 "Deconsolidation of Variable Interest Entity.")

The \$33.5 million used in investing activities during fiscal 2007 resulted from the net cash outflows from purchases, sales and maturities of marketable securities of \$46.0 million and expenditures of fixed assets of \$2.6 million, offset by payments received from a note receivable of \$5.2 million and the net proceeds from the sale of OTravel of \$9.9 million.

Cash provided by (used in) financing activities. Financing activities resulted in cash outflows of \$2.0 million and cash outflows of \$22.3 million for the years ended December 31, 2007 and 2008, respectively. The net cash used in financing activities in 2008 was primarily due to payments for capital leases, paydown of long term debt, and treasury stock purchases of \$3.8 million, \$6.6 million, and \$13.4 million, respectively (see Item 15 of Part IV, "Financial Statements" Note 17 "Stock and Debt Repurchase Program."), offset by \$1.5 million received from the exercise of stock options. The net cash used in financing activities in 2007 was primarily due to payments for capital leases of \$5.3 million offset by \$3.2 million received from the exercise of stock options.

Table of Contents**Stock and Debt Repurchase Program**

On January 14, 2008, our Board of Directors authorized a repurchase program that allowed us to purchase up to \$20.0 million of our common stock and / or our 3.75% Senior Convertible Notes due 2011 ("Senior Notes") through December 31, 2009. Under this repurchase program, we repurchased approximately 1.2 million shares of our common stock in open market purchases for \$13.4 million during the year ended December 31, 2008.

In addition, during the third quarter of 2008, we retired \$9.5 million of the Senior Notes for \$6.6 million in cash. As a result of the Senior Notes retirements, we recognized a gain of \$2.8 million, net of the associated unamortized discount of \$142,000. As of December 31, 2008, \$67.5 million of Senior Notes remain outstanding. We had fully utilized the authorized \$20.0 million repurchase program as of December 31, 2008.

On February 17, 2009, our Board of Directors approved a debt repurchase program that authorizes us to utilize up to \$20.0 million to repurchase a portion of our 3.75% Senior Notes. Under this repurchase program, we have retired \$4.9 million of the Senior Notes for \$3.0 million in cash. As a result of the Senior Notes retirements, we expect to recognize a gain of \$1.9 million, net of the associated unamortized discount of \$63,000 (see Item 15 of Part IV, "Financial Statements" Note 17 "Stock and Debt Repurchase Program").

Shelf Registration

In April 2005, we filed a registration statement with the Securities and Exchange Commission using a "shelf" registration or continuous offering process. On May 1, 2006, we issued approximately 1,042,000 shares of common stock for net proceeds of approximately \$25.0 million. Additionally, on December 12, 2006, we issued approximately 2,734,000 shares for net proceeds of approximately \$39.4 million. We did not issue any shares of common stock under the shelf registration statement during fiscal years 2007 and 2008. During 2008 we filed a new shelf registration statement with the Securities and Exchange Commission, which was declared effective on December 5, 2008. The new shelf registration statement registers offerings of our securities in an aggregate amount of up to \$500.0 million.

Contractual Obligations and Commitments

The following table summarizes our contractual obligations as of December 31, 2008 and the effect such obligations and commitments are expected to have on our liquidity and cash flow in future periods (in thousands):

Contractual Obligations	2009	2010	Payments Due by Period				Total
			2011	2012	2013	Thereafter	
Long-term debt arrangements	\$	\$	\$67,500	\$	\$	\$	\$ 67,500
Interest on convertible senior notes	2,530	2,530	2,319				7,379
Operating leases	8,060	8,652	8,989	8,868	8,325	15,036	57,930
Purchase obligations	6,506	700	508				7,714
Total contractual cash obligations	\$17,096	\$11,882	\$79,316	\$8,868	\$8,325	\$ 15,036	\$140,523

Other Commercial Commitments	Amounts of Commitment Expiration Per Period						
	2008	2009	2010	2011	2012	Thereafter	Total
Letters of credit	\$ 2,200	\$	\$	\$	\$	\$	\$ 2,200
Total commercial commitments	\$ 2,200	\$	\$	\$	\$	\$	\$ 2,200

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Purchase Obligations. The amount of purchase obligations shown above is based on assumptions regarding the legal enforceability against us of purchase orders we had outstanding at December 31, 2008. 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.

Long-Term Debt Arrangements and Interest. In November 2004, we completed an offering of \$120.0 million of 3.75% Convertible Senior Notes (the "Senior Notes"). Proceeds to us were \$116.2 million, net of \$3.8 million of initial purchaser's discount and debt issuance costs. The discount and debt issuance costs are being amortized using the straight-line method which approximates the interest method. We recorded amortization of discount and debt issuance costs related to this offering totaling \$620,000, \$417,000 and \$344,000 during the years ended December 31, 2006, 2007 and 2008, respectively. Interest on the Senior Notes is payable semi-annually on June 1 and December 1 of each year. The Senior Notes mature on December 1, 2011 and are unsecured and rank equally in right of payment with all existing and future unsecured, unsubordinated debt and senior in right of payment to any existing and future subordinated indebtedness.

The Senior Notes are convertible at any time prior to maturity into our common stock at the option of the note holders at a conversion price of \$76.23 per share or, approximately 885,000 shares in aggregate (subject to adjustment in certain events, including stock splits, dividends and other distributions and certain repurchases of our stock, as well as certain fundamental changes in the ownership of us). Beginning December 1, 2009, we have the right to redeem the Senior Notes, in whole or in part, for cash at 100% of the principal amount plus accrued and unpaid interest. Upon the occurrence of a fundamental change (including the acquisition of a majority interest in us, certain changes in our board of directors or the termination of trading of our stock) meeting certain conditions, holders of the Senior Notes may require us to repurchase for cash all or part of their notes at 100% of the principal amount plus accrued and unpaid interest.

The indenture governing the Senior Notes requires us to comply with certain affirmative covenants, including making principal and interest payments when due, maintaining our corporate existence and properties, and paying taxes and other claims in a timely manner. Wilmington Trust Company currently serves as Trustee under the indenture.

Under the repurchase program discussed above, we retired \$9.5 million of the Senior Notes during the quarter ended September 30, 2008 for \$6.6 million in cash, resulting in a gain of \$2.8 million on early extinguishment of debt, net of \$142,000 of associated unamortized discount. As of December 31, 2008, \$67.5 million of the Senior Notes remained outstanding.

Operating Leases

Computer equipment operating leases. We have two operating leases for certain computer equipment that expire in the first and fourth quarters of 2010. It is expected that such leases will be renewed by exercising purchase options or replaced by leases of other computer equipment.

Corporate office space. In July 2005, we leased approximately 154,000 rentable square feet in the Old Mill Corporate Center III in Salt Lake City, Utah for a term of ten years. The total lease obligation over the remaining term of this lease is \$30.4 million, of which approximately \$4.0 million is payable in the next twelve months. \$8.0 million of the total lease obligation is offset by estimated sublease payments related to restructuring, of which \$1.0 million is anticipated to be received in the next twelve months (see Item 15 of Part IV, "Financial Statements" Note 3 "Restructuring Expense").

Logistics and warehouse space. We currently lease 795,000 square feet for warehouse facilities in Utah under operating leases which expire in August 2012 and August 2015.

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On April, 8, 2008, we entered into a lease agreement with Natomas Meadows, LLC (the "Natomas Lease"). The Natomas Lease is for a 686,865 square foot warehouse facility in Salt Lake City, Utah (the "New Warehouse"). The Natomas Lease provides that we will lease the New Warehouse in stages: on October 15, 2008, we leased the initial 232,900 square feet of the New Warehouse; on February 1, 2009, we leased a total of 435,400 square feet; and, on September 1, 2009, we will lease the remainder, for a total of 686,865 square feet. The Natomas Lease term is seven years, and specifies rent, exclusive of common area maintenance fees, at a variable rate over the course of the staged lease term, ranging from \$0.3300 per square foot for the first stage, to \$0.3950 per square foot for the last year of the Natomas Lease term. Including the space now leased in the New Warehouse, we currently have warehouse operations in two facilities in Salt Lake City. The Natomas Lease anticipates that we may construct a corporate office facility within the New Warehouse. We constructed a 40,000 square foot customer service facility in the New Warehouse and commenced use of the facility on November 3, 2008.

Co-location data center. We lease approximately 4,000 square feet of space at Old Mill Corporate Center I for an IT data center. The lease expires in May 1, 2017.

Borrowings

Wells Fargo Credit Agreement. We have a credit agreement (as amended to date, the "Credit Agreement") with Wells Fargo Bank, National Association ("Wells Fargo"). The Credit Agreement provides a revolving line of credit to us of up to \$30.0 million which we use primarily to obtain letters of credit to support inventory purchases. Interest on borrowings is payable monthly and accrued at either (i) 1.0% above LIBOR in effect on the first day of an applicable fixed rate term, or (ii) at a fluctuating rate per annum determined by the bank to be one half a percent (0.50%) above daily LIBOR in effect on each business day a change in daily LIBOR is announced by the bank. The Credit Agreement expires on January 1, 2010, and requires us to comply with certain covenants, including restrictions on mergers, business combinations or transfer of assets.

Borrowings and outstanding letters of credit under the Credit Agreement are required to be completely collateralized by cash balances held at Wells Fargo Bank, N.A., and therefore the facility does not provide additional liquidity to us.

At December 31, 2008, no amounts were outstanding under the Credit Agreement, and letters of credit totaling \$2.2 million were issued on our behalf.

Wells Fargo Retail Finance Agreement. On January 6, 2009 we entered into an Amended and Restated Loan and Security Agreement dated January 6, 2009 (the "WFRF Agreement") with Wells Fargo Retail Finance, LLC ("WFRF"). The WFRF Agreement replaces our Loan and Security Agreement dated December 12, 2005 with WFRF.

The WFRF Agreement provides for advances to us and for the issuance of letters of credit for our account of up to an aggregate maximum of \$35.0 million. The amount actually available to us may be less and may vary from time to time, depending on, among other factors, the amount of its eligible inventory and receivables. Our obligations under the WFRF Agreement and all related agreements are collateralized by all or substantially all of our and our subsidiaries' assets. Our obligations under the WFRF Agreement are cross-collateralized with our obligation under our \$30.0 million credit facility with Wells Fargo Bank, N.A. The WFRF Agreement contains standard default provisions and expires on January 5, 2011. The conditions to our use of the facility include a 45-day advance notice requirement.

Advances under the WFRF Agreement bear interest at either (a) the rate announced, from time to time, within Wells Fargo Bank, N.A. at its principal office in San Francisco as its "prime rate" or (b) a rate based on LIBOR plus a varying percentage between 1.25% and 1.75%; however, the annual

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interest rate on advances under the Agreement will be at least 3.50%. The Agreement includes affirmative covenants as well as negative covenants that prohibit a variety of actions without the lender's approval, including covenants that limit our ability to (a) incur or guarantee debt, (b) create liens, (c) enter into any merger, recapitalization or similar transaction or purchase all or substantially all of the assets or stock of another person, (d) sell assets, (e) change our name or the name of any of our subsidiaries, (f) make certain changes to our business, (g) optionally prepay, acquire or refinance indebtedness, (h) consign inventory, (i) pay dividends on, or purchase, acquire or redeem shares of, our capital stock, (j) change method of accounting, (k) make investments, (l) enter into transactions with affiliates, or (m) store any of our inventory or equipment with third parties.

At December 31, 2008, no amounts were outstanding under the WFRF Agreement or under our prior loan agreement with WFRF.

Wells Fargo Commercial Purchasing Card Agreement. We have a commercial purchasing card agreement (the "Purchasing Card") with Wells Fargo Bank, National Association ("Wells Fargo"). We use the Purchasing Card for business purpose purchasing and must pay it in full each month. Outstanding amounts under the Purchasing Card are collateralized by cash balances held at Wells Fargo Bank, N.A, and therefore the facility does not provide additional liquidity to us. At December 31, 2008, \$436,000 was outstanding and \$564,000 was available under the Purchasing Card.

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.

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.

Adjusted EBITDA. Our measure of Adjusted EBITDA (a non-GAAP financial measure) (which we reconcile to "Net income (loss)" in our statement of operations) consists of earnings before interest, taxes, depreciation, amortization, stock-based compensation, other income (expense) and discontinued operations. Adjusted EBITDA is 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. Adjusted EBITDA reflects an additional way of viewing our results that, when viewed with our GAAP results, provides a more complete understanding of factors and trends affecting our results. You should review our financial statements and publicly-filed reports in their entirety and not rely on any single financial measure. Our discussion above and below (i) explains why management believes that presentation of Adjusted EBITDA provides useful information to investors regarding our financial condition and results of continuing operations, (ii) to the extent material, discloses the additional purposes, if any, for which management uses this non-GAAP measure, and (iii) provides a

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reconciliation of this measure to our net income (loss). For further details on Adjusted EBITDA, see the reconciliation of this non-GAAP measure to our GAAP net income (loss) below (in thousands):

	Three months ended December 31,		Twelve months ended December 31,	
	2007	2008	2007	2008
Net income (loss)	\$ (6,470)	\$ 1,014	\$ (48,036)	\$ (12,658)
Add back amounts for computation of Adjusted EBITDA:				
Depreciation and amortization, including internal-use software and website development, and other amortization	6,670	4,703	29,495	22,667
Stock-based compensation expense to employees and directors	1,136	780	4,522	4,022
Stock-based compensation to consultants for services	(91)	78	189	259
Stock-based compensation related to performance share plan	(900)	(1,300)	(550)	(1,000)
Treasury stock issued from treasury for 401(k) matching contribution	(434)		494	19
Interest (income) expense, net	(326)	371	(600)	299
Other income (expense), net		4,297	92	1,446
Loss from discontinued operations			3,924	
Adjusted EBITDA	\$ (415)	\$ 9,943	\$ (10,470)	\$ 15,054

We believe that discussing Adjusted EBITDA at this stage of our business is useful to us and investors, as Adjusted EBITDA is a reasonable measure of actual cash used or cash generated by the continuing operations of our business.

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. Free cash flow, which we reconcile to "Net cash provided by (used in) operating activities", is cash flow from operations reduced by "Expenditures for fixed assets, including internal-use software and website development." Although we believe that cash flow from operating activities is an important measure, 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. Therefore, we believe it is important to view free cash flow as a complement to our entire consolidated statements of cash flows.

	Three months ended December 31,		Twelve months ended December 31,	
(in thousands)	2007	2008	2007	2008
Net cash provided by operating activities	\$55,734	\$42,830	\$ 9,977	\$ 1,960
Expenditures for fixed assets, including internal-use software and website development	(411)	(3,432)	(2,643)	(18,690)
Free cash flow	\$55,323	\$39,398	\$ 7,334	\$ (16,730)

Table of Contents**Quarterly Results of Operations (unaudited)**

The following tables set forth our unaudited quarterly results of operations for the eight most recent quarters for the period ended December 31, 2008, as well as such data expressed as a percentage of our total revenue for the periods presented. The information in the table below should be read in conjunction with the Consolidated Financial Statements and the Notes thereto included elsewhere in this Form 10-K/A. We have prepared this information on the same basis as the Consolidated Financial Statements and the information includes all adjustments, consisting only of normal recurring adjustments, that we consider necessary for a fair statement of our financial position and operating results for the quarters presented. Our quarterly operating results have varied substantially in the past and may vary substantially in the future. You should not draw any conclusions about our future results from the results of operations for any particular quarter.

	Three Months Ended							
	Mar. 31, 2007	June 30, 2007	Sept. 30, 2007	Dec. 31, 2007	Mar. 31, 2008	June 30, 2008	Sept. 30, 2008	Dec. 31, 2008
(in thousands, except per share data)								
Consolidated Statement of Operations Data:								
Revenue								
Direct revenue	\$ 46,990	\$ 43,658	\$ 39,270	\$ 67,170	\$ 51,764	\$ 39,832	\$ 34,176	\$ 48,431
Fulfillment partner revenue	115,166	105,513	120,789	227,346	151,050	149,004	152,679	207,431
Total revenue	162,156	149,171	160,059	294,516	202,814	188,836	186,855	255,862
Cost of goods sold								
Direct	41,469	36,456	33,268	56,815	44,803	34,871	30,633	44,194
Fulfillment partner	96,077	86,523	99,425	191,319	124,040	120,756	124,103	168,058
Total cost of goods sold	137,546	122,979	132,693	248,134	168,843	155,627	154,736	212,252
Gross profit	24,610	26,192	27,366	46,382	33,971	33,209	32,119	43,610
Operating expenses:								
Sales and marketing	11,284	7,962	8,835	27,377	15,019	14,244	11,934	16,437
Technology	14,973	15,237	14,576	14,667	14,516	15,311	14,119	13,869
General and administrative	10,689	10,429	9,724	11,134	9,563	10,867	10,321	7,622
Restructuring	6,089	6,194						
Total operating expenses	43,035	39,822	33,135	53,178	39,098	40,422	36,374	37,928
Operating income/(loss)	(18,425)	(13,630)	(5,769)	(6,796)	(5,127)	(7,213)	(4,255)	5,682
Interest income, net	990	1,078	1,291	1,429	1,304	740	664	455
Interest expense	(1,029)	(1,027)	(1,029)	(1,103)	(901)	(888)	(847)	(826)
Other income (expense), net			(92)			2	2,849	(4,297)
Income /(loss) from continuing operations	(18,464)	(13,579)	(5,599)	(6,470)	(4,724)	(7,359)	(1,589)	1,014
Discontinued operations:								
Loss from discontinued operations	(3,624)	(300)						
Net income/(loss) attributable to common shares	\$ (22,088)	\$ (13,879)	\$ (5,599)	\$ (6,470)	\$ (4,724)	\$ (7,359)	\$ (1,589)	\$ 1,014

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	Three Months Ended							
	Mar. 31, 2007	June 30, 2007	Sept. 30, 2007	Dec. 31, 2007	Mar. 31, 2008	June 30, 2008	Sept. 30, 2008	Dec. 31, 2008
(in thousands, except per share data)								
Net income/(loss) per common share basic								
Income /(loss) from continuing operations	\$ (0.78)	\$ (0.57)	\$ (0.23)	\$ (0.27)	\$ (0.20)	\$ (0.32)	\$ (0.07)	\$ 0.04
Loss from discontinued operations	\$ (0.16)	\$ (0.01)	\$	\$	\$	\$	\$	\$
Net income /(loss) per share basic	\$ (0.94)	\$ (0.58)	\$ (0.23)	\$ (0.27)	\$ (0.20)	\$ (0.32)	\$ (0.07)	\$ 0.04
Weighted average common shares outstanding basic	23,594	23,689	23,726	23,807	23,345	22,750	22,768	22,745
Net income /(loss) per common share diluted								
Income /(loss) from continuing operations	\$ (0.78)	\$ (0.57)	\$ (0.23)	\$ (0.27)	\$ (0.20)	\$ (0.32)	\$ (0.07)	\$ 0.04
Loss from discontinued operations	\$ (0.16)	\$ (0.01)	\$	\$	\$	\$	\$	\$
Net income /(loss) per share diluted	\$ (0.94)	\$ (0.58)	\$ (0.23)	\$ (0.27)	\$ (0.20)	\$ (0.32)	\$ (0.07)	\$ 0.04
Weighted average common shares outstanding diluted	23,594	23,689	23,726	23,807	23,345	22,750	22,768	22,827

	Three Months Ended							
	Mar. 31, 2007	June 30, 2007	Sept. 30, 2007	Dec. 31, 2007	Mar. 31, 2008	June 30, 2008	Sept. 30, 2008	Dec. 31, 2008
Additional Operating Data(1):								
Gross bookings (in thousands)(2)	\$ 174,740	\$ 164,646	\$ 176,410	\$ 336,340	\$ 219,754	\$ 206,151	\$ 204,656	\$ 285,648
Number of orders(3)	1,481,000	1,288,000	1,457,000	2,973,000	1,773,000	1,574,000	1,570,000	2,509,000
Number of new B2C customers(4)	473,000	394,000	486,000	1,104,000	596,000	516,000	547,000	930,000
Average customer acquisition cost(5)	\$ 24.58	\$ 20.20	\$ 18.17	\$ 24.98	\$ 25.21	\$ 27.61	\$ 21.82	\$ 17.67

- (1) The additional operating data sets forth certain operating data relating to our business for the eight most recent quarters for the period ended December 31, 2008. While we believe that the information in the table above facilitates an understanding of our business and results of operations for the periods presented, such information is not in accordance with generally accepted accounting principles and should be read in conjunction with the quarterly results of operations data set forth above.
- (2) Gross bookings exclude bookings related to the auctions, cars and real estate businesses (shopping business only). We believe that gross bookings is a metric widely used in our industry and by making this metric available to investors, we believe investors are able to compare our performance against others in our industry.
- (3) Number of orders represents the number of individual orders for merchandise through our Website excluding Business to Business ("B2B") orders.
- (4)

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Number of new Business to Consumers ("B2C") customers represents the number of valid new customer accounts. To establish a valid customer account, a person must provide us with the following information and purchase merchandise on our B2C Website: a unique e-mail address; a unique password; and a verified credit card account number.

(5)

Average customer acquisition cost represents total shopping sales and marketing expense divided by the number of new shopping customers for the period presented (excluding both new customers and marketing costs for the

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auctions, real estate, and cars business). We believe that investors may use the average customer acquisition cost metric to determine how efficiently we are able to acquire new customers.

Three Months Ended					
Mar. 31, 2007	June 30, 2007	Sept. 30, 2007	Dec. 31, 2007	Mar. 31, 2008	June 30, 2008