

OVERSTOCK.COM, INC
Form 10-Q
November 09, 2018
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2018

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

87-0634302

(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification Number)

799 West Coliseum Way, Midvale, Utah

84047

(Address of principal executive offices)

(Zip Code)

(801) 947-3100

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

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

Large accelerated filer Accelerated filer

Non-accelerated filer Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

Yes No

There were 32,146,065 shares of the Registrant's common stock, par value \$0.0001, outstanding on November 6, 2018.

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OVERSTOCK.COM, INC.

FORM 10-Q

For the quarterly period ended September 30, 2018

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS (UNAUDITED)

Overstock.com, Inc.

Consolidated Balance Sheets (Unaudited)

(in thousands)

	September 30, 2018	December 31, 2017
Assets		
Current assets:		
Cash and cash equivalents	\$ 182,042	\$ 203,215
Restricted cash	1,395	455
Accounts receivable, net	30,552	30,080
Inventories, net	17,308	13,703
Prepays and other current assets	23,863	17,744
Total current assets	255,160	265,197
Fixed assets, net	133,425	129,343
Deferred tax assets, net	135	—
Intangible assets, net	25,140	7,337
Goodwill	22,058	14,698
Equity investments	57,436	13,024
Other long-term assets, net	8,113	4,216
Total assets	\$ 501,467	\$ 433,815
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	\$ 93,277	\$ 85,406
Accrued liabilities	100,753	82,611
Deferred revenue	39,917	46,468
Other current liabilities, net	472	178
Total current liabilities	234,419	214,663
Long-term debt, net	3,069	—
Long-term debt, net - related party	—	39,909
Other long-term liabilities	5,934	7,120
Total liabilities	243,422	261,692
Commitments and contingencies (Note 6)		
Stockholders' equity:		
Preferred stock, \$0.0001 par value authorized shares - 5,000		
Series A, issued and outstanding - 127 and 127	—	—
Series B, issued and outstanding - 555 and 555	—	—
Common stock, \$0.0001 par value		
Authorized shares -100,000		
Issued shares - 35,138 and 30,632		
Outstanding shares - 31,941 and 27,497	3	3
Additional paid-in capital	651,482	494,732
Accumulated deficit	(413,395)	(254,692)
Accumulated other comprehensive loss	(587)	(599)
Treasury stock:		
Shares at cost - 3,197 and 3,135	(66,709)	(63,816)

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Equity attributable to stockholders of Overstock.com, Inc.	170,794	175,628
Equity attributable to noncontrolling interests	87,251	(3,505)
Total equity	258,045	172,123
Total liabilities and stockholders' equity	\$ 501,467	\$ 433,815

See accompanying notes to unaudited consolidated financial statements.

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

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2018	2017	2018	2017
Revenue, net				
Direct	\$15,424	\$19,645	\$46,409	\$64,572
Partner and other	425,156	404,362	1,322,635	1,223,894
Total net revenue	440,580	424,007	1,369,044	1,288,466
Cost of goods sold				
Direct(1)	16,205	19,577	45,649	61,687
Partner and other	337,659	320,755	1,051,067	972,026
Total cost of goods sold	353,864	340,332	1,096,716	1,033,713
Gross profit	86,716	83,675	272,328	254,753
Operating expenses:				
Sales and marketing(1)	55,312	45,153	226,942	126,068
Technology(1)	33,880	28,746	97,597	85,982
General and administrative(1)	45,356	21,651	116,551	66,622
Total operating expenses	134,548	95,550	441,090	278,672
Operating loss	(47,832)	(11,875)	(168,762)	(23,919)
Interest income	383	189	1,547	450
Interest expense	(101)	(713)	(1,370)	(2,139)
Other income (expense), net	(1,848)	5,882	(1,489)	2,751
Loss before income taxes	(49,398)	(6,517)	(170,074)	(22,857)
Benefit from income taxes	(141)	(5,412)	(445)	(7,727)
Consolidated net loss	\$(49,257)	\$(1,105)	\$(169,629)	\$(15,130)
Less: Net loss attributable to noncontrolling interests	(1,334)	(319)	(5,886)	(942)
Net loss attributable to stockholders of Overstock.com, Inc.	\$(47,923)	\$(786)	\$(163,743)	\$(14,188)
Net loss per common share—basic:				
Net loss attributable to common shares—basic	\$(1.55)	\$(0.03)	\$(5.47)	\$(0.55)
Weighted average common shares outstanding—basic	30,279	25,003	29,256	25,024
Net loss per common share—diluted:				
Net loss attributable to common shares—diluted	\$(1.55)	\$(0.03)	\$(5.47)	\$(0.55)
Weighted average common shares outstanding—diluted	30,279	25,003	29,256	25,024

(1) Includes stock-based compensation as follows (Note 9):

Cost of goods sold — direct	\$41	\$46	\$152	\$134
Sales and marketing	277	109	1,465	318
Technology	583	166	1,725	476
General and administrative	1,345	703	8,312	2,081
Total	\$2,246	\$1,024	\$11,654	\$3,009

See accompanying notes to unaudited consolidated financial statements.

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Overstock.com, Inc.

Consolidated Statements of Comprehensive Loss (Unaudited)

(in thousands)

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2018	2017	2018	2017
Consolidated net loss	\$(49,257)	\$(1,105)	\$(169,629)	\$(15,130)
Other comprehensive loss:				
Unrealized gain on cash flow hedges, net of expense for taxes of \$0, \$31, \$0, and \$71	4	52	12	120
Other comprehensive income	4	52	12	120
Comprehensive loss	\$(49,253)	\$(1,053)	\$(169,617)	\$(15,010)
Less: Comprehensive loss attributable to noncontrolling interests	(1,334)	(319)	(5,886)	(942)
Comprehensive loss attributable to stockholders of Overstock.com, Inc.	\$(47,919)	\$(734)	\$(163,731)	\$(14,068)

See accompanying notes to unaudited consolidated financial statements.

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Overstock.com, Inc.

Consolidated Statements of Changes in Stockholders' Equity (Unaudited)

(in thousands)

	Nine months ended September 30, 2018
Equity attributable to stockholders of Overstock.com, Inc.	
Number of common shares issued	
Balance at beginning of period	30,632
Common stock issued upon vesting of restricted stock	226
Common stock issued for asset purchase	147
Exercise of stock warrants	1,250
Common stock sold through ATM offering	2,883
Balance at end of period	35,138
Number of treasury stock shares	
Balance at beginning of period	3,135
Tax withholding upon vesting of restricted stock	62
Balance at end of period	3,197
Total number of outstanding shares	31,941
Common stock	\$3
Number of Series A preferred shares issued and outstanding	127
Number of Series B preferred shares issued and outstanding	555
Preferred stock	\$—
Additional paid-in capital	
Balance at beginning of period	\$494,732
Stock-based compensation to employees and directors	7,614
Common stock issued for asset purchase	4,430
Exercise of stock warrants	50,562
Sale of stock warrants	25
Common stock sold through ATM offering, net of offering costs	94,624
Other	(505)
Balance at end of period	\$651,482
Accumulated deficit	
Balance at beginning of period	\$(254,692)
Cumulative effect of change in accounting principle	5,040
Net loss attributable to stockholders of Overstock.com, Inc.	(163,743)
Balance at end of period	\$(413,395)
Accumulated other comprehensive loss	
Balance at beginning of period	\$(599)

Net other comprehensive income	12
Balance at end of period	\$(587)
Treasury stock	
Balance at beginning of period	\$(63,816)
Tax withholding upon vesting of restricted stock	(2,893)
Balance at end of period	(66,709)
Total equity attributable to stockholders of Overstock.com, Inc.	\$170,794

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Overstock.com, Inc.

Consolidated Statements of Changes in Stockholders' Equity (Unaudited)

(in thousands)

	Nine months ended September 30, 2018
Total equity attributable to stockholders of Overstock.com, Inc.	\$ 170,794
Equity attributable to noncontrolling interests	
Balance at beginning of period	\$(3,505)
Proceeds from security token offering, net of offering costs (Note 2 - Noncontrolling Interest)	82,610
Stock-based compensation to employees and directors	4,040
Tax withholding upon vesting of restricted stock	(1,681)
Net loss attributable to noncontrolling interests	(5,886)
Fair value of noncontrolling interests at acquisition	4,468
Paid in capital for noncontrolling interest	6,700
Other	505
Total equity attributable to noncontrolling interests	\$ 87,251
Total equity	\$ 258,045

See accompanying notes to unaudited consolidated financial statements.

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Overstock.com, Inc.

Consolidated Statements of Cash Flows (Unaudited)

(in thousands)

	Nine months ended September 30,		Twelve months ended September 30,	
	2018	2017	2018	2017
Cash flows from operating activities:				
Consolidated net loss	\$(169,629)	\$(15,130)	\$(266,421)	\$(12,369)
Adjustments to reconcile net loss to net cash used in operating activities:				
Depreciation of fixed assets	19,437	21,895	26,390	29,468
Amortization of intangible assets	3,596	2,839	4,756	3,614
Stock-based compensation to employees and directors	11,654	3,009	12,722	3,795
Deferred income taxes, net	(383)	(8,682)	73,498	(7,651)
Gain on investment in precious metals	—	(1,907)	(64)	(2,108)
Impairment of cryptocurrencies	9,641	—	9,641	—
Gain on sale of cryptocurrencies	(8,412)	(845)	(9,562)	(845)
Impairment of equity securities	511	4,500	1,498	4,500
Early extinguishment costs of long term debts	283	—	2,747	—
Other	741	420	1,197	569
Changes in operating assets and liabilities, net of acquisitions:				
Accounts receivable, net	(73)	3,814	(5,825)	(3,283)
Inventories, net	(1,833)	5,375	(1,974)	2,155
Prepays and other current assets	(4,806)	(5,950)	(1,655)	(680)
Other long-term assets, net	(4,120)	(121)	(6,306)	(551)
Accounts payable	7,143	(35,794)	21,942	(14,370)
Accrued liabilities	18,044	(35,831)	41,564	(10,217)
Deferred revenue	(1,511)	(275)	3,452	248
Other long-term liabilities	(583)	235	(673)	280
Net cash used in operating activities	(120,300)	(62,448)	(93,073)	(7,445)
Cash flows from investing activities:				
Purchases of intangible assets	(9,583)	—	(10,006)	—
Proceeds from sale of precious metals	—	11,603	314	13,213
Investment in precious metals	—	—	—	(1,633)
Disbursement of note receivable	(2,700)	(750)	(2,700)	(1,368)
Investment in equity securities	(43,670)	(4,188)	(44,670)	(4,938)
Acquisitions of businesses, net of cash acquired	(12,912)	—	(12,912)	28
Expenditures for fixed assets, including internal-use software and website development	(20,677)	(20,873)	(23,390)	(33,772)
Other	34	(160)	264	(179)
Net cash used in investing activities	(89,508)	(14,368)	(93,100)	(28,649)
Cash flows from financing activities:				
Payments on capital lease obligations	(372)	—	(455)	—
Payments on interest swap	—	—	(1,535)	—
Proceeds from finance obligations	—	—	—	5,324
Payments on finance obligations	—	(2,436)	(12,880)	(2,988)
Proceeds from long-term debt	—	—	40,000	4,826
Payments on long-term debt	(40,000)	(750)	(85,016)	(750)
Payments of preferred dividends	—	—	(109)	—

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Proceeds from exercise of stock options	—	654	10	1,473
Proceeds from rights offering, net of offering costs	—	—	—	7,591
Proceeds from issuance and exercise of stock warrants	50,587	—	157,046	—
Proceeds from security token offering, net of offering costs	82,610	3	83,515	3
Proceeds from sale of common stock, net of offering costs	94,624	—	94,624	—
Purchase of treasury stock	—	(10,000)	—	(10,000)
Paid in capital for noncontrolling interest	6,700	—	6,700	—
Payments of taxes withheld upon vesting of restricted stock	(4,574)	(1,104)	(4,699)	(1,207)
Payment of debt issuance costs	—	(251)	(419)	(251)
Net cash provided by (used in) financing activities	189,575	(13,884)	276,782	4,021
Net increase (decrease) in cash, cash equivalents and restricted cash	(20,233)	(90,700)	90,609	(32,073)
Cash, cash equivalents and restricted cash, beginning of period	203,670	183,528	92,828	124,901
Cash, cash equivalents and restricted cash, end of period	\$183,437	\$92,828	\$183,437	\$92,828

Continued on the following page

Overstock.com, Inc.

Consolidated Statements of Cash Flows (Unaudited)

(Continued)

(in thousands)

	Nine months ended		Twelve months ended	
	September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017
Supplemental disclosures of cash flow information:				
Cash paid during the period:				
Interest paid, net of amounts capitalized	\$1,232	\$1,980	\$2,192	\$2,574
Income taxes paid, net of refunds	59	492	54	624
Non-cash investing and financing activities:				
Fixed assets, including internal-use software and website development, costs financed through accounts payable and accrued liabilities	\$731	\$618	\$731	\$618
Equipment acquired under capital lease obligations	—	—	1,421	362
Capitalized interest cost	—	—	—	(12)
Change in fair value of cash flow hedge	—	(180)	(1,558)	(2,619)
Note receivable converted to equity investment	200	869	699	869
Acquisition of assets through stock issuance	4,430	—	4,430	—

See accompanying notes to unaudited consolidated financial statements.

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Overstock.com, Inc.

Notes to Unaudited Consolidated Financial Statements

1. BASIS OF PRESENTATION

Overstock.com, Inc. is an online retailer and advancer of blockchain technology. As used herein, "Overstock," "the Company," "we," "our" and similar terms include Overstock.com, Inc. and its majority-owned subsidiaries, unless the context indicates otherwise.

We have prepared the accompanying unaudited consolidated financial statements pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC") regarding interim financial reporting. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States ("GAAP") have been omitted in accordance with the rules and regulations of the SEC.

These financial statements should be read in conjunction with our audited annual consolidated financial statements and related notes included in our Annual Report on Form 10-K for the year ended December 31, 2017. The accompanying unaudited consolidated financial statements reflect all adjustments, consisting only of normal recurring adjustments, which are, in our opinion, necessary for a fair presentation of results for the interim periods presented. The results of operations for the three and nine months ended September 30, 2018 are not necessarily indicative of the results to be expected for any future period or the full fiscal year.

For purposes of comparability, the presentation of certain immaterial amounts in the prior periods have been conformed with the current period presentation. We retrospectively applied certain accounting standard updates as discussed in Note 2—Accounting Policies, Recently adopted accounting standards.

2. ACCOUNTING POLICIES

Principles of consolidation

The accompanying consolidated financial statements include our accounts and the accounts of our wholly-owned and majority-owned subsidiaries. All intercompany account balances and transactions have been eliminated in consolidation. The financial results of Verify Investor, LLC have been included in our consolidated financial statements from the date of acquisition on February 12, 2018. The financial results of Mac Warehouse, LLC have been included in our consolidated financial statements from the date of acquisition on June 25, 2018.

Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires estimates and assumptions that affect the reported amounts of assets and liabilities, revenues and expenses, and related disclosures of contingent liabilities in our consolidated financial statements and accompanying notes. Estimates are used for, but not limited to, investment valuation, receivables valuation, revenue recognition, sales returns, incentive discount offers, inventory valuation, depreciable lives of fixed assets and internally-developed software, goodwill valuation, intangible asset valuation, equity investment valuation, income taxes, stock-based compensation, performance-based compensation, self-funded health insurance liabilities and contingencies. Although these estimates are based on our best knowledge of current events and actions that we may undertake in the future, actual results may differ materially from these estimates.

Cash equivalents

We classify all highly liquid instruments, including instruments with a remaining maturity of three months or less at the time of purchase, as cash equivalents. Cash equivalents were \$20.1 million and \$25.5 million at September 30, 2018 and December 31, 2017, respectively.

Restricted cash

We consider cash that is legally restricted and cash that is held as compensating balances for credit arrangements and self-funded health insurance as restricted cash.

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Fair value of financial instruments

We account for our assets and liabilities using a hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect our market assumptions. These two types of inputs have created the fair-value hierarchy below. This hierarchy requires us to minimize the use of unobservable inputs and to use observable market data, if available, when determining fair value.

Level 1—Quoted prices for identical instruments in active markets;

Level 2—Quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-derived valuations in which all significant inputs and significant value drivers are observable in active markets; and

Level 3—Valuations derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable.

Under GAAP, certain assets and liabilities are required to be recorded at fair value on a recurring basis. Our assets and liabilities that are adjusted to fair value on a recurring basis are cash equivalents, trading securities, and deferred compensation liabilities, which fair values are determined using quoted market prices from daily exchange traded markets on the closing price as of the balance sheet date and are classified as Level 1. Our other financial instruments, including cash, restricted cash, accounts receivable, accounts payable, accrued liabilities, and debt are carried at cost, which approximates their fair value.

The following tables summarize our assets and liabilities measured at fair value on a recurring basis using the fair value hierarchy as of September 30, 2018 and December 31, 2017 as indicated (in thousands):

p	Fair Value Measurements at September 30, 2018:			
	Total	Level 1	Level 2	Level 3
Assets:				
Cash equivalents - Money market mutual funds	\$ 20,055	\$ 20,055	\$ —	\$ —
Investments in equity securities, at fair value	4,264	4,264	—	—
Trading securities held in a "rabbi trust" (1)	88	88	—	—
Total assets	\$ 24,407	\$ 24,407	\$ —	\$ —
Liabilities:				
Deferred compensation accrual "rabbi trust" (2)	\$ 93	\$ 93	\$ —	\$ —
Total liabilities	\$ 93	\$ 93	\$ —	\$ —
	Fair Value Measurements at December 31, 2017:			
	Total	Level 1	Level 2	Level 3
Assets:				
Cash equivalents - Money market mutual funds	\$ 25,455	\$ 25,455	\$ —	\$ —
Trading securities held in a "rabbi trust" (1)	74	74	—	—
Total assets	\$ 25,529	\$ 25,529	\$ —	\$ —
Liabilities:				
Deferred compensation accrual "rabbi trust" (2)	\$ 92	\$ 92	\$ —	\$ —
Total liabilities	\$ 92	\$ 92	\$ —	\$ —

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

(2)

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

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Accounts receivable, net

Accounts receivable consist primarily of trade amounts due from customers in the United States, uncleared credit card transactions at period end, and carrier rebates. Accounts receivable are recorded at invoiced amounts and do not bear interest. From time to time, we grant credit to some of our business customers on normal credit terms (typically 30 days). We maintain an allowance for doubtful accounts receivable based upon our business customers' financial condition and payment history, and our historical collection experience and expected collectability of accounts receivable. The allowance for doubtful accounts receivable was \$1.9 million and \$1.3 million at September 30, 2018 and December 31, 2017, respectively.

Concentration of credit risk

Three banks held the majority of our cash and cash equivalents at September 30, 2018. Two banks held the majority of our cash and cash equivalents at December 31, 2017. Our cash equivalents primarily consist of money market securities which are uninsured. We do not believe that, as a result of this concentration, we are subject to any unusual financial risk beyond the normal risk associated with commercial banking relationships.

Inventories, net

Inventories, net include merchandise purchased for resale, which are accounted for using a standard costing system which approximates the first-in-first-out ("FIFO") method of accounting, and are valued at the lower of cost and net realizable value. Inventory valuation requires us to make judgments, based on currently available information, about the likely method of disposition, such as through sales to individual customers, returns to product vendors, or liquidations, and expected recoverable values of each disposition category.

Prepays and other current assets

Prepays and other current assets represent expenses paid prior to receipt of the related goods or services, including advertising, license fees, maintenance, packaging, insurance, prepaid inventories, other miscellaneous costs, and cryptocurrency-denominated assets ("cryptocurrencies"). See Cryptocurrencies below.

Cryptocurrencies

Cryptocurrency holdings are included in Prepays and other current assets in our consolidated balance sheets and totaled \$3.1 million and \$1.5 million at September 30, 2018 and December 31, 2017, respectively. Cryptocurrency holdings are recorded at cost less impairment.

We recognize impairment on these assets caused by decreases in market value based upon Level 1 inputs. See Fair value of financial instruments above. Such impairment in the value of our cryptocurrencies is recorded in General and administrative expense in our consolidated statements of operations. Impairments on cryptocurrencies were \$150,000 and \$9.6 million for the three and nine months ended September 30, 2018. There was no impairment on cryptocurrencies during the three and nine months ended September 30, 2017.

Gains and losses realized upon sale of cryptocurrencies are also recorded in General and administrative expense in our consolidated statements of operations. We occasionally use our cryptocurrencies to purchase other cryptocurrencies. Gains and losses realized with these non-cash transactions are also recorded in General and administrative expense in our consolidated statements of operations. These non-cash transactions as well as gains (losses) from cryptocurrencies received through our tZERO security token offering are also presented as an adjustment to reconcile Consolidated net loss to Net cash used in operating activities in our consolidated statements of cash flows. Realized gains on sale of

cryptocurrencies were \$64,000 and \$8.4 million for the three and nine months ended September 30, 2018. There were \$3.6 million realized gains or losses on sale of cryptocurrencies during the three and nine months ended September 30, 2017.

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Fixed assets, net

Fixed assets are recorded at cost and stated net of depreciation and amortization. Fixed assets are depreciated using the straight-line method over the estimated useful lives of the related assets or the term of the related capital lease, whichever is shorter, as follows:

	Life (years)
Building	40
Land improvements	20
Building machinery and equipment	15-20
Furniture and equipment	5-7
Computer hardware	3-4
Computer software, including internal-use software and website development	2-4

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

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

During the three months ended September 30, 2018 and 2017, we capitalized \$4.0 million and \$2.2 million, respectively, of costs associated with internal-use software and website development, both developed internally and acquired externally. Amortization of costs for the same periods associated with internal-use software and website development was \$3.4 million and \$3.9 million, respectively. During the nine months ended September 30, 2018 and 2017, we capitalized \$14.7 million and \$8.0 million, respectively, of costs associated with internal-use software and website development, both developed internally and acquired externally. Amortization of costs associated with internal-use software and website development was \$10.0 million and \$12.2 million, respectively.

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

	Three months ended September 30,		Nine months ended September 30,	
	2018	2017	2018	2017
Cost of goods sold - direct	\$85	\$72	\$252	\$230
Technology	5,330	5,940	16,103	18,802
General and administrative	1,038	974	3,082	2,863
Total depreciation, including internal-use software and website development	\$6,453	\$6,986	\$19,437	\$21,895

Total accumulated depreciation of fixed assets was \$202.3 million and \$186.4 million at September 30, 2018 and December 31, 2017, respectively.

Upon sale or retirement of assets, cost and related accumulated depreciation and amortization are removed from the balance sheet and the resulting gain or loss is reflected in our consolidated statements of operations.

Fixed assets included assets under capital leases of \$1.8 million at September 30, 2018 and December 31, 2017. Accumulated depreciation related to assets under capital leases was \$842,000 and \$458,000 at September 30, 2018 and December 31, 2017, respectively.

Depreciation expense of assets recorded under capital leases was \$120,000 and \$1.1 million for the three months ended September 30, 2018 and 2017, respectively, and \$384,000 and \$3.5 million for the nine months ended September 30, 2018 and 2017, respectively.

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Equity investments under ASC 321

At September 30, 2018, we held minority interests (less than 20%) in thirteen privately held entities accounted for under ASC Topic 321, Investments - Equity Securities ("ASC 321"), which are included in Equity investments in our consolidated balance sheets. One of these equity investments, which had a carrying value of \$4.3 million at September 30, 2018, is carried at fair value based on Level 1 inputs. See Fair value of financial instruments above. The remaining equity investments lack readily determinable fair values and therefore the investments are measured at cost minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for the identical or similar equity securities of the same issuer. Dividends received are reported in current earnings. We review our investments individually for impairment by evaluating if events or circumstances have occurred that may indicate the fair value of the investment is less than its carrying value. If such events or circumstances have occurred, we estimate the fair value of the investment and recognize an impairment loss equal to the difference between the fair value of the investment and its carrying value. In such cases, the estimated fair value of the investment is determined using unobservable inputs including assumptions by the investee's management including quantitative information such as lower valuations in recently completed or proposed financings. These inputs are classified as Level 3. Because several of our investees are in the early startup or development stages, these entities are subject to potential changes in cash flows, valuation, and inability to attract new investors which may be necessary for the liquidity needed to support their operations.

The carrying amount of our investments under ASC 321 was approximately \$18.5 million and \$6.5 million at September 30, 2018 and December 31, 2017, respectively. We recognized unrealized losses of \$73,000 and unrealized gains of \$1.8 million on investments carried at fair value during the three and nine months ended September 30, 2018, respectively. We recognized a \$511,000 impairment loss during the three and nine months ended September 30, 2018. We recognized a \$4.5 million impairment loss during the nine months ended September 30, 2017. Impairment loss and any unrealized gains or losses on our investments are recorded in Other income (expense), net on our consolidated statements of operations.

Equity method investments under ASC 323

At September 30, 2018, we held minority interests in nine privately held entities accounted for as equity method investments under ASC Topic 323, Investments - Equity Method and Joint Ventures ("ASC 323"), which are included in Equity investments in our consolidated balance sheets. We can exercise significant influence, but not control, over the investees through either holding more than a 20% voting interest in the entity or through our representation on the entity's board of directors. Based on the nature of our ownership interests, we have variable interests in certain of these entities. However, because we do not have power to direct the investee's activities and we are not the investee's primary beneficiary, we therefore do not consolidate the investee in our financial statements.

The carrying value of our equity method investments exceeded the amount of underlying equity in net assets of the investees and the difference was primarily related to goodwill and the fair value of intangible assets. The difference related to intangible assets is amortized over their estimated useful lives. We record our proportionate share of the net income or loss of the investee and the amortization of the basis difference related to intangible assets in Other income (expense), net in our consolidated statements of operations with corresponding adjustments to the carrying value of the investment.

The carrying amount of our equity method investments was approximately \$39.0 million and \$6.5 million at September 30, 2018 and December 31, 2017, respectively, and the difference between the carrying value and the amount of underlying equity in net assets of each investee was not significant. Our proportionate share of the net income or loss of our equity method investees was approximately \$1.2 million in losses and \$74,000 in losses for the three months ended September 30, 2018 and 2017, respectively, and approximately \$2.5 million in losses and \$74,000

in losses for the nine months ended September 30, 2018 and 2017, respectively.

Noncontrolling interests

Our wholly-owned subsidiary, Medici Ventures, Inc. ("Medici Ventures"), conducts its primary business through its majority-owned subsidiary, tZERO Group, Inc. ("tZERO"), formerly tØ.com, Inc., which includes a financial technology company, two related registered broker dealers, a registered investment advisor, and an accredited investor verification company. tZERO and its consolidated subsidiaries are included in our consolidated financial statements. Intercompany transactions have been eliminated and the amounts of contributions and gains or losses that are attributable to the noncontrolling interests are disclosed in our consolidated financial statements.

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On December 18, 2017, tZERO launched an offering (the "security token offering") of the right to acquire tZERO Preferred Equity Tokens (the "tZERO Security Token") through a Simple Agreement for Future Equity ("SAFE"). The security token offering closed on August 6, 2018. At September 30, 2018, the SAFEs were classified as equity by tZERO. At September 30, 2018, cumulative proceeds, net of withdrawals, from the security token offering totaling \$104.8 million, have been classified as a component of noncontrolling interest within our consolidated financial statements. As of September 30, 2018, tZERO has incurred \$21.3 million of offering costs associated with the security token offering that are classified as a reduction in proceeds within noncontrolling interest of our consolidated financial statements. On October 12, 2018, tZERO issued the tZERO Security Tokens in settlement of the SAFEs. The tZERO Security Tokens are subject to a 90 day trading lock-up period.

During the first quarter of 2018, tZERO purchased 65.8% of ES Capital Advisors, LLC ("ES Capital"), a registered investment advisor under the Investment Advisers Act of 1940, which was accounted for as an asset acquisition. tZERO operates the ES Capital business under the name tZERO Advisors and offers automated investment advisory services under the FinanceHub tab on our Website. tZERO also purchased 81.0% of Verify Investor, LLC, an accredited investor verification company. This transaction is described further in Note 3—Acquisitions, Goodwill, and Acquired Intangible Assets. These entities are included in our consolidated financial statements.

Medici Land Governance Inc., a Delaware public benefit corporation ("MLG"), was recently formed by Medici Ventures with our President and Chief Executive Officer, Dr. Patrick M. Byrne ("Dr. Byrne"). Pursuant to the Subscription Agreements dated September 21, 2018, Medici Ventures contributed certain of its assets, including intellectual property relating to technologies regarding land governance and property rights, to MLG in exchange for 510,000 shares of MLG common stock and at the same time Dr. Byrne personally contributed \$6.7 million in cash to MLG in exchange for 390,000 shares of MLG common stock. As a result of the transactions described above, Medici Ventures holds approximately 57% of the outstanding capital stock of MLG, and Dr. Byrne, holds approximately 43% of the outstanding capital stock of MLG.

Leases

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

Treasury stock

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

Goodwill

Goodwill represents the excess of the purchase price paid over the fair value of the net assets acquired in business combinations. Goodwill is not amortized but is tested for impairment at least annually. When evaluating whether goodwill is impaired, we make a qualitative assessment to determine if it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If the qualitative assessment determines that it is more likely than not that its fair value is less than its carrying amount, we compare the fair value of the reporting unit to which the goodwill is assigned to its carrying amount. If the carrying amount exceeds its fair value, then the amount of the impairment loss must be measured. The impairment loss, if any, is calculated by comparing the implied fair value of

the goodwill to its carrying amount. In calculating the implied fair value of goodwill, the fair value of the reporting unit is allocated to the other assets and liabilities within the reporting unit based on estimated fair value. The excess of the fair value of a reporting unit over the amount allocated to its other assets and liabilities is the implied fair value of goodwill. An impairment loss is recognized when the carrying amount of goodwill exceeds its implied fair value.

We test for impairment of goodwill annually or when we deem that a triggering event has occurred. There were no impairments to goodwill recorded during the nine months ended September 30, 2018 and 2017.

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For nine months ended September 30, 2018, we recognized \$7.4 million in goodwill related to a business acquisition as described in Note 3—Acquisitions, Goodwill, and Acquired Intangible Assets. The change in goodwill relates to a non-reportable segment, included in Other as described in Note 10—Business Segments.

Intangible assets other than goodwill

We capitalize and amortize intangible assets other than goodwill over their estimated useful lives unless such lives are indefinite. Intangible assets other than goodwill acquired separately from third-parties are capitalized at cost while such assets acquired as part of a business combination are capitalized at their acquisition-date fair value. Indefinite lived intangible assets include intellectual property and investment advisor licenses purchased in connection with our tZERO Advisors and Medici Ventures' portfolio company in the blockchain property titling businesses. Certain licenses are subject to annual renewal terms with immaterial fees which are expensed as incurred. Indefinite-lived intangible assets are tested for impairment annually or more frequently when events or circumstances indicate that the carrying value more likely than not exceeds its fair value. In addition, we routinely evaluate the remaining useful life of intangible assets not being amortized to determine whether events or circumstances continue to support an indefinite useful life, including any legal, regulatory, contractual, competitive, economic, or other factors that may limit their useful lives. Definite lived intangible assets are amortized using the straight-line method of amortization over their useful lives, with the exception of certain intangibles (such as acquired technology, customer relationships, and trade names) which are amortized using an accelerated method of amortization based on cash flows. Definite lived intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that their carrying amount may not be recoverable as described below under Impairment of long-lived assets.

Intangible assets, net consist of the following (in thousands):

	September 30, 2018	December 31, 2017
Intangible assets subject to amortization, gross (1)	\$ 28,347	\$ 17,779
Less: accumulated amortization of intangible assets subject to amortization	(14,040)	(10,442)
Intangible assets subject to amortization, net	14,307	7,337
Intangible assets not subject to amortization	10,833	—
Total intangible assets, net	\$ 25,140	\$ 7,337

(1) — At September 30, 2018, the weighted average remaining useful life for intangible assets subject to amortization, excluding fully amortized intangible assets, was 5.69 years.

Amortization of intangible assets other than goodwill is classified within the corresponding operating expense categories in our consolidated statements of operations as follows (in thousands):

	Three months ended September 30, 2018		Nine months ended September 30, 2017	
Technology	\$885	\$905	\$2,534	\$2,715
Sales and marketing	119	22	442	62
General and administrative	542	21	620	62
Total amortization	\$1,546	\$948	\$3,596	\$2,839

Estimated amortization expense for the next five years is: \$1.3 million for the remainder of 2018, \$4.7 million in 2019, \$2.2 million in 2020, \$1.8 million in 2021, \$892,000 in 2022, and \$3.5 million thereafter.

Impairment of long-lived assets

We review property and equipment and other long-lived assets, including amortizable intangible assets other than goodwill, for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset group may not be recoverable. Recoverability is measured by comparison of the assets' carrying amount to future undiscounted net cash flows the asset group is expected to generate. Cash flow forecasts are based on trends of historical performance and management's estimate of future performance, giving consideration to existing and anticipated competitive and economic

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conditions. If such asset group is considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds their fair values. There were no impairments to long-lived assets recorded during the nine months ended September 30, 2018 and 2017.

Other long-term assets, net

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

Revenue recognition

We derive our revenue primarily from retail merchandise sales on our Website. We also earn revenue from advertising on our Website and from other sources. We have organized our operations into two principal reporting segments based on the primary source of revenue: (i) direct revenue and (ii) partner and other revenue. Net revenue from contracts with customers is further disaggregated by Retail and Other net revenue as disclosed in Note 10—Business Segments.

On January 1, 2018, we adopted ASU 2014-09, Revenue from Contracts with Customers (Topic 606). See Recently adopted accounting standards, below. Under Topic 606, revenue is recognized when control of the product passes to the customer or the service is provided and is recognized in an amount that reflects the expected consideration to be received in exchange for such goods or services. Shipping and handling is considered a fulfillment activity and fees charged to customers are included in net revenue upon completion of our performance obligation. We present revenue net of sales taxes, discounts, and expected refunds. We record an allowance for returns based on current period revenues and historical returns experience. We analyze actual historical returns, current economic trends and changes in order volume and acceptance of our products when evaluating the adequacy of the sales returns allowance in any accounting period.

Generally, we require authorization from credit card or other payment vendors whose services we offer to our customers (such as PayPal), or verification of receipt of payment, 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). For sales in our partner business, we generally receive payments from our customers before our payments to our suppliers are due.

We evaluate the criteria outlined in ASC 606-10-55, Principal versus Agent Considerations, in determining whether it is appropriate to record the gross amount of merchandise sales and related costs or the net amount earned as commissions. When we are the principal in a transaction and control the specific good or service before it is transferred to the customer, revenue is recorded gross; otherwise, revenue is recorded on a net basis. Currently, the majority of both direct revenue and partner revenue is recorded on a gross basis.

Revenue related to merchandise sales is recognized upon transfer of control to our customers which generally occurs upon delivery of the product to our customers. As such, customer orders are recorded as deferred revenue prior to delivery of products or services ordered. As we ship high volumes of packages through multiple carriers, it is not practical for us to track the actual delivery date of each shipment. Therefore, we use estimates to determine which shipments are delivered and, therefore, recognized as revenue at the end of the period. Our delivery date estimates are based on average shipping transit times, which are calculated using the following factors: (i) the type of shipping carrier (as carriers have different in-transit times); (ii) the fulfillment source (either our warehouses, those warehouses we control, or those of our 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.

During the nine months ended September 30, 2018, we recognized \$37.8 million of net revenue included in Deferred revenue at December 31, 2017.

The allowance for returns was \$12.4 million and \$17.4 million at September 30, 2018 and December 31, 2017, respectively.

We evaluate the revenue recognition criteria above for our broker dealer subsidiaries and we recognize revenue based on the gross amount of consideration that we expect to receive on securities transactions (commission revenue) on a trade date basis.

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Direct revenue

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

Partner and other revenue

Partner and other revenue is derived primarily from merchandise sales of inventory sourced through our partners which are generally shipped directly to our consumers and businesses. Through contractual terms with our partners, we have the ability to control the promised goods or services and as a result record the majority of our partner revenue on a gross basis. Partner and other revenue comes from merchandise sales that occur primarily through our Website, but may also occur through offline and other channels, including through our broker dealer subsidiaries in our Other segment.

Club O loyalty program

We have a customer loyalty program called Club O Gold for which we sell annual memberships. For Club O Gold memberships, we record membership fees as deferred revenue, and we recognize revenue ratably over the membership period. The Club O Gold loyalty program allows members to earn Club O Reward dollars for qualifying purchases made on our Website. We also have a co-branded credit card program which provides Club O Gold members additional reward dollars for purchases made on our Website, and from other merchants.

Earned Club O Reward dollars may be redeemed on future purchases made through our Website. We recognize revenue for Club O Reward dollars when customers redeem such rewards as part of a purchase on our Website. We account for these transactions as multiple element arrangements and allocate the transaction price to separated performance obligations using their relative fair values. We include the fair value of reward dollars earned in deferred revenue at the time the reward dollars are earned. Club O Reward dollars expire 90 days after the customer's Club O Gold membership expires. We recognize estimated reward dollar breakage, to which we expected to be entitled, over the expected redemption period in proportion to actual redemptions by customers. Upon adoption of Topic 606, Revenue Contracts with Customers, on January 1, 2018, we began classifying the breakage income related to Club O Reward dollars and gift cards as a component of revenue in our consolidated statements of operations rather than as a component of Other income (expense), net. Breakage included in revenue was \$1.3 million and \$4.2 million for the three and nine months ended September 30, 2018. We also recognized a cumulative adjustment that reduced Accumulated deficit by approximately \$5.0 million upon adoption related to the unredeemed portion of our gift cards and loyalty program rewards.

Our total deferred revenue related to the outstanding Club O Reward dollars was \$6.6 million and \$8.7 million at September 30, 2018 and December 31, 2017, respectively. The timing of revenue recognition of these reward dollars is driven by actual customer activities, such as redemptions and expirations.

Advertising Revenue

Advertising revenues is derived primarily from sponsored links and display advertisements that are placed on our Website, distributed via email, or sent out as direct mailers. Advertising revenue is recognized in net revenue when the advertising services are rendered. Advertising revenues were less than 2% of total net revenues for all periods presented.

Cost of goods sold

Cost of goods sold includes product costs, warehousing costs, outbound shipping costs, handling and fulfillment costs, customer service costs and credit card fees, and is recorded in the same period in which related revenues have been recorded.

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Cost of goods sold, including product cost and other costs and fulfillment and related costs are as follows (in thousands):

	Three months ended				Nine months ended			
	September 30,		September 30,		September 30,		September 30,	
	2018	2017	2018	2017	2018	2017	2018	2017
Total revenue, net	\$440,580	100 %	\$424,007	100 %	\$1,369,044	100 %	\$1,288,466	100 %
Cost of goods sold								
Product costs and other cost of goods sold	334,156	76 %	321,678	76 %	1,039,518	76 %	977,827	76 %
Fulfillment and related costs	19,708	4 %	18,654	4 %	57,198	4 %	55,886	4 %
Total cost of goods sold	353,864	80 %	340,332	80 %	1,096,716	80 %	1,033,713	80 %
Gross profit	\$86,716	20 %	\$83,675	20 %	\$272,328	20 %	\$254,753	20 %

Advertising expense

We expense the costs of producing advertisements the first time the advertising takes place and expense the cost of communicating advertising in the period during which the advertising space or airtime is used. Internet advertising expenses are recognized as incurred based on the terms of the individual agreements, which are generally: 1) a commission for traffic driven to our Website that generates a sale or 2) a referral fee based on the number of clicks on keywords or links to our Website generated during a given period. Advertising expense is included in Sales and marketing expenses and totaled \$49.7 million and \$41.2 million during the three months ended September 30, 2018 and 2017, respectively. For the nine months ended September 30, 2018 and 2017, advertising expenses totaled \$207.5 million and \$114.6 million, respectively. Prepaid advertising (included in Prepaids and other current assets in the accompanying consolidated balance sheets) was \$1.2 million and \$987,000 at September 30, 2018 and December 31, 2017, respectively.

Stock-based compensation

We measure compensation expense for all outstanding unvested share-based awards at fair value on the date of grant and recognize compensation expense over the service period for awards at the greater of a straight-line basis or on an accelerated schedule when vesting of the share-based awards exceeds a straight-line basis. When an award is forfeited prior to the vesting date, we recognize an adjustment for the previously recognized expense in the period of the forfeiture. See Note 9—Stock-Based Awards.

Self-funded health insurance

We have a partially self-funded health insurance plan for our employees. We maintain a stop-loss insurance policy through an insurance company that limits our losses both on a per employee basis and an aggregate basis. Although we intend to maintain this plan indefinitely, we may terminate, modify, suspend, or discontinue this plan at any time and for any reason.

We are responsible for estimating our liability for unpaid costs of insured events that have occurred, which includes known cases on a case-by-case basis, and also for events that have occurred, but have not yet been reported. The accrued liability related to the self-funded health insurance plan was \$1.5 million and \$1.0 million at September 30, 2018 and December 31, 2017, respectively, and is included in Accrued liabilities in the accompanying consolidated balance sheets. Actual claims may differ from the amount accrued and any difference could be significant.

Loss contingencies

In the normal course of business, we are involved in legal proceedings and other potential loss contingencies. We accrue a liability for such matters when it is probable that a loss has been incurred and the amount can be reasonably estimated. When only a range of probable loss can be estimated, the most probable amount in the range is accrued. If no amount within this range is a better estimate than any other amount within the range, the minimum amount in the range is accrued. We expense legal fees as incurred (see Note 6—Commitments and Contingencies).

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Income taxes

Our income tax provision for interim periods is determined using an estimate of our annual effective tax rate adjusted for discrete items, if any, for relevant interim periods. We update our estimate of the annual effective tax rate each quarter and make cumulative adjustments if our estimated annual effective tax rate changes.

Our quarterly tax provision and our quarterly estimate of our annual effective tax rate are subject to significant variations due to several factors including variability in predicting our pre-tax and taxable income and the mix of jurisdictions to which those items relate, relative changes in expenses or losses for which tax benefits are not recognized, how we do business, fluctuations in our stock price, and changes in law, regulations, and administrative practices. Our effective tax rate can be volatile based on the amount of pre-tax income. For example, the impact of discrete items on our effective tax rate is greater when pre-tax income is lower.

Each quarter we assess the recoverability of our deferred tax assets under ASC Topic 740. We assess the available positive and negative evidence to estimate whether we will generate sufficient future taxable income to use our existing deferred tax assets. We have limited carryback ability and do not have significant taxable temporary differences to recover our existing deferred tax assets, therefore we must rely on future taxable income, including tax planning strategies, to support their realizability. We have established a valuation allowance for our deferred tax assets not supported by carryback ability or taxable temporary differences, primarily due to uncertainty regarding our future taxable income. We have considered, among other things, the cumulative loss incurred over the three-year period ended September 30, 2018 as a significant piece of objective negative evidence. We intend to continue maintaining a valuation allowance on our net deferred tax assets until there is sufficient evidence to support the reversal of all or some portion of these allowances. The amount of the deferred tax asset considered realizable could be adjusted if objective negative evidence in the form of cumulative losses is no longer present and additional weight may be given to subjective evidence such as long-term projections for growth. We will continue to monitor the need for a valuation allowance against our remaining deferred tax assets on a quarterly basis.

Tax laws and regulations themselves are subject to change as a result of changes in fiscal policy, changes in legislation, the evolution of regulations, and court rulings. On December 22, 2017, the President signed into law Public Law No. 115-97, commonly referred to as the Tax Cuts and Jobs Act ("TCJA"), following its passage by the United States Congress. The TCJA made significant changes to U.S. federal income tax laws, mostly effective for tax years beginning after December 31, 2017. Among many other changes, the new law lowers the corporate tax rate from 35% to 21% for tax years beginning in 2018, transitions U.S. international taxation from a worldwide tax system to a territorial system, and includes a one-time transition tax on the mandatory deemed repatriation of cumulative foreign earnings as of December 31, 2017. Staff Accounting Bulletin No. 118 ("SAB 118") was issued to address the application of US GAAP in situations when a registrant does not have the necessary information available, prepared, or analyzed (including computations) in reasonable detail to complete the accounting for certain income tax effects of the TCJA. As noted at year-end, however, we were able to reasonably estimate certain effects and, therefore, recorded adjustments associated with the remeasurement of certain deferred tax assets and liabilities and the mandatory deemed repatriation of cumulative foreign earnings.

Our accounting for the following elements of the TCJA is complete. The expense related to the remeasurement of certain deferred tax assets and liabilities, based on the rates at which they are expected to reverse in the future, was \$25.2 million. The expense related to the one-time transition tax on the mandatory deemed repatriation of cumulative foreign earnings was \$47,000. We did not make any measurement-period adjustments related to these items during the quarter because there were no significant changes to our provisional amounts, and therefore, there is no impact to our effective tax rate due to measurement-period adjustments.

The TCJA includes a provision to tax global intangible low-taxed income ("GILTI") of foreign subsidiaries beginning in 2018. Under GAAP, we can make an accounting policy election to either treat taxes due on the GILTI inclusion as a current period expense, or factor such amounts into our measurement of deferred taxes. We will elect to treat any potential GILTI inclusions as a period cost as we are not projecting any material impact from GILTI inclusions and any deferred taxes related to any inclusion would be immaterial.

The TCJA included a mandatory deemed repatriation of cumulative foreign earnings for the year ended December 31, 2017, for which we accrued U.S. tax expense. However, we would still need to accrue and pay various other taxes on this amount if repatriated, which we have not provided for because we intend to indefinitely reinvest these earnings outside the U.S. We have begun expansion of operations outside of the U.S. and have plans for additional expansion for which we have incurred

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and will continue to incur capital requirements. We have considered ongoing capital requirements of the parent company in the U.S.

We are subject to taxation in the United States and several state and foreign jurisdictions. Tax years beginning in 2013 are subject to examination by taxing authorities, although net operating loss and credit carryforwards from all years are subject to examinations and adjustments for at least three years following the year in which the attributes are used. We are under audit by the Ireland Revenue Agency for the calendar year 2016. We expect the audit to continue during 2018.

Net loss per share

In 2016, we issued shares of our Blockchain Voting Series A Preferred Stock and our Voting Series B Preferred Stock (collectively the "preferred shares"). These shares are considered participating securities, and as a result, net loss per share is calculated using the two-class method. Under this method, we give effect to preferred dividends and then allocate remaining net loss attributable to our stockholders to both common shares and participating securities (based on the percentages outstanding) in determining net loss per common share.

Basic net loss per common share is computed by dividing net loss attributable to common shares (after allocating between common shares and participating securities) by the weighted average number of common shares outstanding during the period.

Diluted net loss per share is computed by dividing net loss attributable to common shares (after allocating between common shares and participating securities) by the weighted average number of common and potential common shares outstanding during the period (after allocating total dilutive shares between our common shares outstanding and our preferred shares outstanding). Potential common shares, comprising incremental common shares issuable upon the exercise of stock options, warrants, and restricted stock awards are included in the calculation of diluted net loss per common share to the extent such shares are dilutive. Net loss attributable to common shares is adjusted for options and restricted stock awards issued by our subsidiaries when the effect of our subsidiary's diluted earnings per share is dilutive.

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

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2018	2017	2018	2017
Net loss attributable to stockholders of Overstock.com, Inc.	\$(47,923)	\$(786)	\$(163,743)	\$(14,188)
Less: Preferred stock dividends - declared and accumulated	27	27	80	80
Undistributed loss	(47,950)	(813)	(163,823)	(14,268)
Less: Undistributed loss allocated to participating securities	(1,055)	(22)	(3,728)	(386)
Net loss attributable to common shares	\$(46,895)	\$(791)	\$(160,095)	\$(13,882)
Net loss per common share—basic:				
Net loss attributable to common shares—basic	\$(1.55)	\$(0.03)	\$(5.47)	\$(0.55)
Weighted average common shares outstanding—basic	30,279	25,003	29,256	25,024
Effect of dilutive securities:				
Stock options and restricted stock awards	—	—	—	—
Weighted average common shares outstanding—diluted	30,279	25,003	29,256	25,024
Net loss attributable to common shares—diluted	\$(1.55)	\$(0.03)	\$(5.47)	\$(0.55)

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

	Three months ended September 30, 2018		Nine months ended September 30, 2017	
Stock options and restricted stock units	498	192	578	165
Common shares issuable under stock warrant	—	—	28	—

Warrants

On November 8, 2017, we issued warrants to purchase up to a combined aggregate of 3,722,188 shares of our common stock to two purchasers in privately negotiated transactions, for an aggregate purchase price of \$6.5 million, net of issuance costs. The exercise price for the warrants was \$40.45 per share of common stock. On December 29, 2017, one of the warrant holders exercised its warrant in full and purchased a total of 2,472,188 shares of common stock for \$100.0 million. On January 17, 2018, the other warrant holder exercised its warrant in full and purchased 1,250,000 shares of common stock for \$50.6 million.

Recently adopted accounting standards

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606), which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. We adopted the new standard on January 1, 2018 with a cumulative adjustment that reduced Accumulated deficit by approximately \$5.0 million as opposed to retrospectively adjusting prior periods. The adjustment primarily relates to the unredeemed portion of our gift cards and loyalty program rewards, which we will recognize over the expected redemption period, rather than waiting until the likelihood of redemption becomes remote or the rewards expire. We have also updated revenue disclosures in the notes to our financial statements as required under the new standard.

The implementation did not impact our gross and net recognition for our revenue transactions. In addition, we continue to recognize revenue related to merchandise sales upon delivery to our customers. However, we now present breakage on our Club O Rewards and gift cards in Partner and other revenue in our consolidated statement of operations rather as a component of Other expense, net.

In January 2016, the FASB issued ASU 2016-01, Financial Instruments-Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities, which requires equity investments previously recognized under the cost method to be measured at cost minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for the identical or similar investment of the same issuer. We adopted the changes under the new standard on January 1, 2018 on a prospective basis. The implementation of ASU 2016-01 did not have a material impact on our consolidated financial statements and related disclosures.

In November 2016, the FASB issued ASU 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash, which requires amounts generally described as restricted cash be included with cash and cash equivalents when reconciling beginning-of-period and end-of-period total amounts shown in the statement of cash flows. We adopted the new standard on January 1, 2018 retrospectively to each period presented in the statement of cash flows. The implementation of ASU 2016-18 did not have a material impact on our consolidated financial statements and related disclosures.

In January 2017, the FASB issued ASU 2017-01, Business Combinations (Topic 805): Clarifying the Definition of a Business, which provides guidance to assist entities with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. We adopted the changes under the new standard on January 1, 2018 on a prospective basis. The implementation of ASU 2017-01 did not have a material impact on our consolidated financial statements and related disclosures.

Recently issued accounting standards

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842), which, among other things, requires lessees to recognize most leases on their balance sheets related to the rights and obligations created by those leases. The new standard also requires new disclosures to help financial statement users better understand the amount, timing, and uncertainty of cash flows

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arising from leases. The new standard becomes effective for us on January 1, 2019, with early adoption permitted. We plan to adopt this ASU beginning on January 1, 2019. The amendments in this update should be applied under a modified retrospective approach. We are evaluating the effect that ASU 2016-02 will have on our consolidated financial statements and related disclosures.

In June 2018, the FASB issued ASU 2018- 07, Compensation-Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting; which aligns the measurement and classification guidance for share-based payments to nonemployees with the guidance for share-based payments to employees, with certain exceptions. Under the guidance, the measurement of equity-classified nonemployee awards will be fixed at the grant date. The new standard becomes effective for us on January 1, 2019, with early adoption permitted. We plan to adopt this ASU beginning on January 1, 2019. We do not expect the adoption to have a material impact on our consolidated financial statements and related disclosures.

3. ACQUISITIONS, GOODWILL, AND ACQUIRED INTANGIBLE ASSETS

Verify Investor, LLC

On February 12, 2018, tZERO acquired 81% of the total equity interests of Verify Investor, LLC, an accredited investor verification company, for a total purchase price of \$12.0 million in cash. With the acquisition of the majority interest in Verify Investor, LLC, tZERO plans to integrate the software and technology of Verify Investor, LLC with the Token Trading System that tZERO plans to develop and deploy. We estimated the fair value of the acquired assets based on Level 3 inputs, which were unobservable (see Note 2—Accounting Policies, Fair value of financial instruments). These inputs included our estimate of future revenues, operating margins, discount rates, royalty rates and assumptions about the relative competitive environment.

The fair values of the assets acquired and liabilities assumed at the acquisition date are as follows (in thousands):

Purchase Price	Fair Value
Cash paid, net of cash acquired	\$11,769
Allocation	
Intangible assets	\$7,400
Goodwill	7,360
Other assets acquired	3
Other liabilities assumed	(179)
Total net assets, net of cash acquired	14,584
Less: noncontrolling interest	(2,815)
Total net assets attributable to tZERO, net of cash acquired	\$11,769

The following table details the identifiable intangible assets acquired at their fair value and estimated useful lives as of September 30, 2018 (amounts in thousands):

Intangible Assets	Fair Value	Estimated Useful Life (in years)
Technology and developed software	\$6,300	10
Trade name	700	10
Customer relationships	400	0.5
Total acquired intangible assets at the acquisition date	7,400	
Less: accumulated amortization of acquired intangible assets	904	
Total acquired intangible assets, net	\$8,304	

The expense for amortizing intangible assets acquired in connection with this acquisition was \$302,000 and \$904,000 for the three and nine months ended September 30, 2018, respectively.

Acquired intangible assets primarily include technology, trade name, and customer relationships. As described above, we determined the fair value of these assets using an income approach method to determine the present value of expected future

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cash flows for each identifiable intangible asset. This method was based on discount rates which incorporate a risk premium to take into account the risks inherent in those expected cash flows. The expected cash flows were estimated based on the company's historical operating results.

The acquired assets, liabilities, and associated operating results were consolidated into our financial statements at the acquisition dates, or the dates on which we obtained control of the acquired assets or interests.

Mac Warehouse, LLC

On June 25, 2018, we acquired 100% of the total equity interests of Mac Warehouse, LLC, an electronics retailer of refurbished Apple products, for a total purchase price of \$1.2 million in cash. With the acquisition of Mac Warehouse, LLC, we plan to integrate the inventory and business processes of Mac Warehouse, LLC in our direct retail business. We estimated the fair value of the acquired assets based on Level 3 inputs, which were unobservable (see Note 2—Accounting Policies, Fair value of financial instruments). These inputs included our estimate of future revenues, operating margins, discount rates, royalty rates and assumptions about the relative competitive environment.

Determination and allocation of the purchase price to net tangible and intangible assets is based upon preliminary estimates. These preliminary estimates and assumptions could change significantly during the measurement period as we finalize the valuations of the net tangible and intangible assets acquired and liabilities assumed. Any change could result in variances between our future financial results and the amounts recognized in the financial information presented below, including variances in fair values recorded, as well as expenses associated with these items.

The preliminary estimated fair values of the assets acquired and liabilities assumed at the acquisition date are as follows (in thousands):

Purchase Price	Fair Value
Cash paid, net of cash acquired	\$1,143
Allocation	
Accounts receivable, net	\$399
Inventories, net	1,772
Prepays and other current assets	29
Fixed assets	154
Intangible assets	2,763
Accounts payable	(682)
Accrued liabilities	(223)
Long-term debt, net	(3,069)
Total net assets, net of cash acquired	\$1,143

Acquired intangible assets primarily include trade name and customer relationships which have an estimated useful life of 18 months.

The acquired assets, liabilities, and associated operating results were consolidated into our financial statements at the acquisition dates, or the dates on which we obtained control of the acquired assets or interests.

The following unaudited pro forma financial information presents our results as if the current year acquisitions of Mac Warehouse, LLC had occurred at the beginning of 2017 (amounts in thousands):

Three months ended		Nine months ended	
September 30,		September 30,	
2018	2017	2018	2017

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Total revenue	\$440,580	\$428,309	\$1,373,228	\$1,300,365
Consolidated net loss	\$(49,257)	\$(778)	\$(171,673)	\$(14,472)

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The unaudited pro forma financial information is not intended to represent or be indicative of our consolidated results of operations that would have been reported had the acquisition been completed during the periods indicated, nor should it be taken as indicative of our future consolidated results of operations.

4. ACCRUED LIABILITIES

Accrued liabilities consist of the following (in thousands):

	September 30, 2018	December 31, 2017
Sales and other taxes payable	\$ 20,254	\$ 2,363
Accounts payable accruals	16,393	16,614
Accrued compensation and other related costs	16,200	10,716
Accrued marketing expenses	13,446	25,959
Allowance for returns	12,448	17,391
Accrued loss contingencies	10,304	608
Accrued freight	6,754	5,040
Other accrued expenses	4,954	3,920
Total accrued liabilities	\$ 100,753	\$ 82,611

5. BORROWINGS

High Bench Senior Credit Agreement

On June 25, 2018, we became party to a senior credit agreement, as amended, with High Bench-Mac Warehouse-Senior Debt, LLC ("High Bench Loan"), in connection with our acquisition of Mac Warehouse, LLC. Under the amended agreement, the loan carries an annual interest rate of 11.0% and a default rate of 18.0%. The High Bench Loan is subject to monthly interest only payments with the remaining principal amount and any then unpaid interest due and payable on April 18, 2020. The High Bench Loan is subject to mandatory prepayment under certain circumstances, and is prepayable at our election at any time without penalty or premium. There are no financial covenants associated the High Bench Loan. At September 30, 2018, our outstanding balance on the High Bench Loan was \$3.1 million.

Letters of credit

At September 30, 2018 and December 31, 2017, letters of credit totaling \$280,000 and \$355,000, respectively, were issued on our behalf collateralized by compensating cash balances held at a bank, which are included in Restricted cash in our consolidated balance sheets.

Commercial purchasing card agreement

We have a commercial purchasing card (the "Purchasing Card") agreement. We use the Purchasing Card for business purpose purchasing and must pay it in full each month. At September 30, 2018, \$107,000 was outstanding and \$893,000 was available under the Purchasing Card. At December 31, 2017, \$822,000 was outstanding and \$4.2 million was available under the Purchasing Card.

Capital lease

During the year ended December 31, 2017, we entered into a capital lease arrangement of computer equipment for \$1.4 million. The arrangement will expire in 2020. At September 30, 2018, the outstanding balance under the capital lease was \$1.0 million and is included in Other current liabilities, net and Other long-term liabilities on our consolidated balance sheets. Future payment obligations, including interest, under the capital lease are \$124,000, \$496,000 and \$413,000 for the rest of 2018, 2019 and 2020, respectively.

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6. COMMITMENTS AND CONTINGENCIES

Summary of future minimum lease payments for all operating leases

Minimum future payments under all operating leases as of September 30, 2018, are as follows (in thousands):

Payments due by period

2018 (Remainder)	\$ 1,757
2019	7,446
2020	5,648
2021	6,038
2022	6,156
Thereafter	17,515
	\$44,560

Rental expense for operating leases totaled \$1.9 million and \$2.1 million for the three months ended September 30, 2018 and 2017, respectively, and \$5.3 million and \$7.0 million for the nine months ended September 30, 2018 and 2017, respectively.

Legal proceedings and contingencies

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

On September 23, 2009, SpeedTrack, Inc. sued us along with 27 other defendants in the United States District Court in the Northern District of California. We are alleged to have infringed a patent covering search and categorization software. We believe that certain third-party vendors of products and services sold to us are contractually obligated to indemnify us, and we have tendered defense of the case to an indemnitor who accepted the defense. On April 21, 2016, the court entered an order partially dismissing the claims against us. On May 4, 2016, the plaintiff filed an amended complaint, and we filed our answer. No estimate of the possible loss or range of loss can be made. We intend to vigorously defend this action and pursue our indemnification rights with our vendors.

On February 11, 2013, RPost Holdings, Inc., RPost Communications Limited, and RMail Limited, filed suit against us in the United States District Court in the Eastern District of Texas for infringement of patents covering products and services that verify the delivery and integrity of email messages. We tendered defense of the case to an indemnitor who accepted the defense. No estimate of the possible loss or range of loss can be made. We intend to vigorously defend this action and pursue our indemnification rights with our vendors.

On September 20, 2018, a jury returned a verdict against us in our Delaware unclaimed property case, which is expected to result in a judgment against us in the amount of approximately \$7.3 million (for certain unredeemed gift card balances, treble damages, and penalties) plus attorneys' fees and costs. Our estimated liability for these amounts has been included in Accrued liabilities as of September 30, 2018 and the expense associate with these litigation charges are included in general and administrative expense in our consolidated statement of operations for the three and nine months ended September 30, 2018. William French ("French") and the State of Delaware ("Delaware") sued us, along with numerous other defendants, in the Superior Court of the State of Delaware for alleged violations of Delaware's unclaimed property laws. French and Delaware alleged that we knowingly refused to fulfill obligations under Delaware's Abandoned Property Law by failing to report and deliver unclaimed gift card funds to the State of Delaware, and knowingly made, used or caused to be made or used, false

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statements and records to conceal, avoid or decrease an obligation to pay or transmit money to Delaware in violation of the Delaware False Claims and Reporting Act. We intend to file an appeal once the judgment has been entered by the court.

On June 21, 2018, the U.S. Supreme Court issued an opinion in our South Dakota sales tax case and ruled against us. The State of South Dakota sued us along with three other defendants in the Sixth Judicial Circuit Court of South Dakota alleging that U.S. constitutional law should be revised to permit South Dakota to require out-of-state e-commerce websites to collect and remit sales tax in South Dakota in accordance with South Dakota's sales tax statute. Under the U.S. Supreme Court's ruling, the longstanding *Quill Corp v. North Dakota* sales tax case was overruled, and states may now require remote sellers to collect sales tax under certain circumstances. We began collecting sales tax in all 45 states that have sales tax. Pursuant to South Dakota's statute, we are not required to pay sales tax retroactively. The U.S. Supreme Court's opinion vacated and remanded the case back to the South Dakota Supreme Court for further proceedings.

On July 7, 2017, the State of Wyoming sued us along with five other defendants in the Second Judicial District Court of Wyoming. Wyoming alleged that U.S. constitutional law should be revised to permit Wyoming to require out-of-state e-commerce retailers to collect and remit sales tax in Wyoming in accordance with Wyoming's sales tax statute. After the U.S. Supreme Court's ruling in our South Dakota case listed above, we began collecting sales tax in Wyoming. Wyoming's statute does not require us to pay sales tax retroactively. The Wyoming case has not yet been dismissed.

On August 28, 2017, the State of Indiana sued us along with one other defendant in the Superior Court of Indiana, Marion County. Indiana alleged that U.S. constitutional law should be revised to permit Indiana to require out-of-state e-commerce retailers to collect and remit sales tax in Indiana in accordance with Indiana's sales tax statute. After the U.S. Supreme Court's ruling in our South Dakota case listed above, we began collecting sales tax in Indiana. Indiana's statute does not require us to pay sales tax retroactively. The Indiana case was dismissed August 16, 2018.

In February 2018, the Division of Enforcement of the SEC informed tZERO and subsequently informed us that it is conducting an investigation and requested that we and tZERO voluntarily provide certain information and documents related to tZERO and the tZERO security token offering in connection with its investigation. We are cooperating fully with the SEC in connection with its investigation.

tZERO's broker-dealer subsidiaries are, and any broker-dealer subsidiaries that it acquires or forms in the future will be, subject to extensive regulatory requirements under federal and state laws and regulations and self-regulatory organization ("SRO") rules. Each of SpeedRoute and PRO Securities is registered with the SEC as a broker-dealer under the Exchange Act and in the states in which it conducts securities business and is a member of FINRA and other SROs (as applicable). In addition, PRO Securities owns and operates the PRO Securities ATS, which is registered with the SEC as an alternative trading system. Each of SpeedRoute and PRO Securities is subject to regulation, examination and disciplinary action by the SEC, FINRA and state securities regulators, as well as other governmental authorities and SROs with which it is registered or licensed or of which it is a member. On February 22, 2018, the SEC's New York Regional Office notified PRO Securities that it is conducting an examination of PRO Securities, and on March 6, 2018 the SEC's Boston Regional Office notified tZERO Advisors that it is conducting an examination of tZERO Advisors. These examinations remain open.

As a result of tZERO's projects seeking to apply distributed ledger technologies to the capital markets, tZERO's subsidiaries have been, and remain involved in, ongoing discussions with regulatory authorities. While certain of the discussions have been relatively informal, tZERO's broker-dealer subsidiaries have also received and responded to several written inquiries from FINRA relating to such projects. While tZERO considers these continuing inquiries to be ordinary course in light of the non-traditional nature of tZERO's distributed ledger projects, any failure by tZERO's

broker-dealer subsidiaries to satisfy their regulatory authorities that they are in compliance with all applicable rules and regulations could have a material adverse effect on tZERO and on us.

In addition, in December 2017, SpeedRoute received a letter from FINRA stating that the Department of Enforcement at FINRA has received a referral from the staff of FINRA's Department of Market Regulation relating to rules applicable to supervision and required supervisory procedures for review of certain potential trading activity, such as pre-arranged trades or wash trades. In addition, SpeedRoute continues to have discussions with FINRA about several matters, including a matter related to potential violations of FINRA rules relating to Order Audit Trail System reporting and trading practice matters, and has received document requests from FINRA in connection with certain ongoing matters. SpeedRoute has received and responded to inquiries from FINRA and the SEC. In an unrelated matter, SpeedRoute and PRO Securities have been named in a FINRA investigatory matter in which FINRA has conducted on the record interviews of certain senior officers of SpeedRoute and PRO Securities, who are also senior officers of tZERO.

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On March 29, 2018, a purported securities class action lawsuit was filed against us and two of our executives in the United States District Court in the Central District of Utah, alleging violations of the Securities Exchange Act of 1934 ("Exchange Act"). On April 6, 2018, a substantially similar lawsuit was filed in the same court also naming the Company, and two of our executives as defendants, bringing the same claims under the Exchange Act, and seeking substantially similar relief. On June 20, 2018, the Court consolidated the two cases and appointed a lead plaintiff in the case. On August 7, 2018, the plaintiffs voluntarily dismissed the lawsuit without prejudice.

We have recognized liabilities for contingencies deemed probable and estimable totaling \$10.3 million and \$608,000 at September 30, 2018 and December 31, 2017, which are included in Accrued liabilities in our consolidated balance sheets. It is reasonably possible that the actual losses may exceed our accrued liabilities.

7. INDEMNIFICATIONS AND GUARANTEES

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

8. STOCKHOLDERS' EQUITY

Common Stock

Each share of common stock has the right to one vote. The holders of common stock are also entitled to receive dividends declared by the Board of Directors out of funds legally available, subject to prior rights of holders of all classes of stock outstanding having priority rights as to dividends. No dividends have ever been declared or paid on our common stock.

Preferred Stock

Each share of Series A Preferred and each share of Series B Preferred (collectively the "preferred shares") is intended to have voting and dividend rights similar to those of one share of common stock. Preferred shares rank senior to common stock with respect to dividends. Holders of the preferred shares will be entitled to an annual cash dividend of \$0.16 per share, in preference to any dividend payment to the holders of the common stock, out of funds of the Company legally available for payment of dividends and subject to declaration by our Board of Directors. Holders of the preferred shares are also entitled to participate in any cash dividends we pay to the holders of the common stock and are also entitled to participate in non-cash dividends we pay to holders of the common stock, subject to potentially different treatment if we effect a stock dividend, stock split or combination of the common stock. There are no arrearages in cumulative preferred dividends. We declared and paid a cash dividend of \$0.16 per share on our preferred stock during 2017.

Neither the Series A Preferred or Series B Preferred is convertible into or exchangeable for shares of our common stock or any other entity; however, at our sole discretion, we may convert the Series A Preferred shares into Series B Preferred shares at any time on a one-to-one basis. Until the third anniversary of the original issuance date, we may redeem, at our discretion, both the Series A and Series B Preferred shares for an amount equal to the highest of the following: (1) the subscription price plus any accrued but unpaid dividends, (2) 105% of the average trading price of our common stock during a five-trading-day period and (3) 105% of the average trading price of the series of preferred shares during the same five-day-trading period. In the event of any liquidation, any amount available for distribution to stockholders after payment of all liabilities will be distributed proportionately, with each share of Series A Preferred and each share of Series B Preferred being treated as though it were a share of our common stock.

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JonesTrading Sales Agreement

In August 2018, we entered into a sales agreement with JonesTrading Institutional Services LLC ("JonesTrading"), under which we conducted "at the market" public offerings of our common stock during the quarter ended September 30, 2018 and may conduct additional "at the market" public offerings of our common stock from time to time. Under the sales agreement, JonesTrading, acting as our agent, may offer our common stock in the market on a daily basis or otherwise as we request from time to time. We have no obligation to sell additional shares under the sales agreement, but expect to do so from time to time. We will pay JonesTrading up to a 2.0% sales commission on all sales. The sales agreement contemplates sales of up to \$150 million of our common stock over a period of up to three years. As of September 30, 2018, we had sold 2,883,344 shares of our common stock pursuant to the sales agreement and have received \$94.6 million in proceeds, net of \$2.6 million of offering costs, including commissions paid to JonesTrading. The average price per share of stock sold pursuant to the sales agreement during the quarter ended September 30, 2018, excluding offering costs, was \$33.71.

JonesTrading Standby Equity Agreement

In August 2018 we also entered into a standby equity underwriting agreement with JonesTrading. We did not sell any shares under the standby equity underwriting agreement, and the agreement terminated in accordance with its terms during the quarter ended September 30, 2018. Under the standby underwriting agreement, we had the right, but no obligation, to sell up to \$50 million of our common stock to JonesTrading, as underwriter, for sale to the public in a firm commitment public offering. We paid a 1% commitment fee to JonesTrading for entering into the underwriting agreement.

GSR Agreements

As previously announced, in August 2018, Overstock signed a Token Purchase Agreement with GSR Capital Ltd., a Cayman Islands exempted company ("GSR"), and a term sheet contemplating a sale of Overstock common stock to GSR. Concurrently, tZERO signed a term sheet contemplating a sale of tZERO common stock to GSR.

The Token Purchase Agreement sets forth the terms on which GSR agreed to purchase, for \$30 million, on May 6, 2019 or such other date as may be agreed by the parties, security tokens at a price of \$6.67 per security token. These security tokens were issued by tZERO to Overstock in satisfaction of \$30 million of tZERO's indebtedness to Overstock. We may be required to obtain additional tokens in order to fulfill our obligations under the agreement. The agreement states that the obligations of GSR to complete the transaction described will be subject to conditions, some of which are unidentified.

Overstock, tZERO and GSR are currently negotiating definitive agreements for GSR's purchase of Overstock common stock and tZERO common stock. Although we continue to negotiate the terms, GSR has proposed purchasing fewer shares and at a lower price per share than those described in the Overstock term sheet. We believe that if a definitive agreement is reached regarding the purchase of tZERO shares, the terms, including the post money valuation of tZERO, may be less favorable than those described in the tZERO term sheet. Both the Overstock and tZERO term sheets constitute binding agreements for the parties to negotiate in good faith the terms of the transaction documents; however, the obligation to negotiate in good faith terminates on December 15, 2018, if any of the closing conditions, one of which is the negotiation, execution and delivery of mutually acceptable transaction documents, have not been satisfied. While we expect to complete these transactions, there can be no assurance that Overstock, tZERO or GSR will enter into definitive agreements regarding either of the proposed transactions.

9. STOCK-BASED AWARDS

We have equity incentive plans that provide for the grant to employees and board members of stock-based awards, including stock options and restricted stock. Stock-based compensation expense was as follows (in thousands):

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2018	2017	2018	2017
Overstock restricted stock awards	\$1,779	\$1,015	\$6,863	\$3,000
Medici Ventures stock options	138	9	273	9
tZERO equity awards	329	—	4,518	—
Total stock-based compensation expense	\$2,246	\$1,024	\$11,654	\$3,009

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Overstock restricted stock awards

The Overstock.com, Inc. Amended and Restated 2005 Equity Incentive Plan provides for the grant of restricted stock units and other types of equity awards of the Company. The restricted stock awards generally vest over three years at 33.3% at the end of the first year, 33.3% at the end of the second year and 33.3% at the end of the third year; subject to the recipient's continuing service to us.

The following table summarizes restricted stock award activity during the nine months ended September 30, 2018 (in thousands):

	Nine months ended September 30, 2018	Weighted Average Grant Date Fair Value
Outstanding—beginning of year	540	\$ 17.05
Granted at fair value	360	68.85
Vested	(226)	17.29
Forfeited	(109)	43.63
Outstanding—end of period	565	\$ 44.82

Medici Ventures stock options

The Medici Ventures, Inc. 2017 Stock Option Plan provides for the grant of options to employees and directors of and consultants to Medici Ventures to acquire up to 10% of the authorized shares of Medici Ventures' common stock. During the nine months ended September 30, 2018, Medici Ventures granted 19,700 stock options with a cumulative grant date fair value of \$1.7 million which vest over a three year period. During the year ended December 31, 2017, Medici Ventures granted 74,750 stock options to certain Medici Ventures and Overstock employees with a cumulative grant date fair value of \$91,000 which will be expensed on a straight-line basis over the vesting period of three years.

tZERO equity awards

The tZERO.com 2017 Equity Incentive Plan provides for grant of options to employees and directors of and consultants to tZERO to acquire up to 5% of the authorized shares of tZERO's common stock. In January 2018, tZERO granted stock awards under the equity incentive plan for an aggregate of approximately 1.0% of tZERO's common stock all of which vested on January 23, 2018. In January 2018, tZERO recognized \$4.0 million in compensation expense associated with these awards, which was the entire estimated fair value at the grant date. Accordingly, there is no expense to be recognized in future periods related to these awards. As a result of these vested awards, our indirect ownership interest in tZERO was reduced from 81% to approximately 80%. During the nine months ended September 30, 2018, tZERO granted awards to acquire 382 shares of its stock with a cumulative grant date fair value of \$3.1 million which will be expensed on a straight-line basis over the vesting period of two to three years. No awards were issued during the year ended December 31, 2017.

10. BUSINESS SEGMENTS

Segment information has been prepared in accordance with ASC Topic 280 Segment Reporting. We determined our segments based on how we manage our business, which, in our view, consists primarily of our Retail and Medici businesses. Our Retail business consists of our Direct and Partner reportable segments. We use gross profit as the measure to determine our reportable segments because there is not discrete financial information available below gross profit for our Direct and Partner segments. As a result, our Medici business is not significant as compared to our Direct and Partner segments and is included in Other. Our Other segment consists of Medici Ventures and its subsidiaries, including tZERO. Although our Direct and Partner segments both relate to our Retail business, we do not combine these segments because they have dissimilar economic characteristics, such as gross profit margins. We do not allocate assets between our segments for our internal management purposes, and as such, they are not presented here. There were no significant inter-segment sales or transfers during the three and nine months ended September 30, 2018 and 2017.

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The following table summarizes information about reportable segments for three and nine months ended September 30, 2018 and 2017 (in thousands):

	Three months ended September 30,				
	Direct	Partner	Retail Total	Other	Total
2018					
Revenue, net	\$ 15,424	\$ 420,351	\$ 435,775	\$ 4,805	\$ 440,580
Cost of goods sold	16,205	334,446	350,651	3,213	353,864
Gross profit	\$(781)	\$ 85,905	\$ 85,124	\$ 1,592	\$ 86,716
Operating expenses			124,571	9,977	134,548
Interest and other expense, net (1)			(515)	(1,051)	(1,566)
Pre-tax loss			(39,962)	(9,436)	(49,398)
Provision for (benefit from) income taxes			(155)	14	(141)
Net loss (2)			\$(39,807)	\$(9,450)	\$(49,257)
2017					
Revenue, net	\$ 19,645	\$ 400,419	\$ 420,064	\$ 3,943	\$ 424,007
Cost of goods sold	19,577	318,121	337,698	2,634	340,332
Gross profit	\$ 68	\$ 82,298	\$ 82,366	\$ 1,309	\$ 83,675
Operating expenses			90,592	4,958	95,550
Interest and other income (expense), net (1)			5,375	(17)	5,358
Pre-tax loss			(2,851)	(3,666)	(6,517)
Benefit from income taxes			(3,993)	(1,419)	(5,412)
Net income (loss) (2)			\$ 1,142	\$(2,247)	\$(1,105)
	Nine months ended September 30,				
	Direct	Partner	Retail Total	Other	Total
2018					
Revenue, net	\$ 46,409	\$ 1,307,045	\$ 1,353,454	\$ 15,590	\$ 1,369,044
Cost of goods sold	45,649	1,039,834	1,085,483	11,233	1,096,716
Gross profit	\$ 760	\$ 267,211	\$ 267,971	\$ 4,357	\$ 272,328
Operating expenses			399,540	41,550	441,090
Interest and other income (expense), net (1)			654	(1,966)	(1,312)
Pre-tax loss			(130,915)	(39,159)	(170,074)
Benefit from income taxes			(283)	(162)	(445)
Net loss (2)			\$(130,632)	\$(38,997)	\$(169,629)
2017					
Revenue, net	\$ 64,572	\$ 1,211,536	\$ 1,276,108	\$ 12,358	\$ 1,288,466
Cost of goods sold	61,687	963,310	1,024,997	8,716	1,033,713
Gross profit	\$ 2,885	\$ 248,226	\$ 251,111	\$ 3,642	\$ 254,753
Operating expenses			264,455	14,217	278,672
Interest and other income (expense), net (1)			5,490	(4,428)	1,062
Pre-tax loss			(7,854)	(15,003)	(22,857)
Benefit from income taxes			(3,280)	(4,447)	(7,727)
Net loss (2)			\$(4,574)	\$(10,556)	\$(15,130)

(1) — Excludes intercompany transactions eliminated in consolidation, which consist primarily of service fees and interest. The net amounts of these intercompany transactions were \$539,000 and \$403,000 for the three months

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ended September 30, 2018 and 2017, respectively, and \$3.0 million and \$1.1 million for the nine months ended September 30, 2018 and 2017, respectively.

(2) — Net income (loss) presented for segment reporting purposes is before any adjustments attributable to noncontrolling interests.

Our Direct segment includes revenues, direct costs, and cost allocations associated with sales of inventory we own. Costs for this segment include product costs, freight, warehousing and fulfillment costs, credit card fees and customer service costs.

Our Partner segment includes revenues, direct costs and cost allocations associated with sales of inventory owned by our partners. Costs for this segment include product costs, outbound freight and fulfillment costs, credit card fees and customer service costs.

For the three and nine months ended September 30, 2018 and 2017, substantially all of our sales revenues were attributable to customers in the United States. At September 30, 2018 and December 31, 2017, substantially all our fixed assets were located in the United States.

11. BROKER DEALERS

As part of our Medici blockchain and fintech technology initiatives, we hold a controlling interest in each of two broker dealers, SpeedRoute LLC ("SpeedRoute") and Pro Securities LLC ("Pro Securities"), which we acquired in January 2016.

SpeedRoute is an electronic, agency-only FINRA-registered broker dealer that provides connectivity for its customers to U.S. equity exchanges as well as off-exchange sources of liquidity such as dark pools. All of SpeedRoute's customers are registered broker dealers. SpeedRoute does not hold, own or sell securities.

Pro Securities is a FINRA-registered broker dealer that owns and operates the Pro Securities alternative trading system ("ATS"), which is registered with the SEC. An ATS is a trading system that is not regulated as an exchange, but is a licensed venue for matching buy and sell orders. The Pro Securities ATS is a closed system available only to its broker dealer subscribers. Pro Securities does not accept orders from non-broker dealers, nor does it hold, own or sell securities.

SpeedRoute and Pro Securities are subject to the SEC's Uniform Net Capital Rule (SEC Rule 15c3-1), which requires the maintenance of minimum net capital and requires that the ratio of aggregate indebtedness to net capital, both as defined, shall not exceed 15 to 1 and that equity capital may not be withdrawn or cash dividends paid if the resulting net capital ratio would exceed 10 to 1. At September 30, 2018, SpeedRoute had net capital of \$873,707, which was \$746,775 in excess of its required net capital of \$126,932 and SpeedRoute's net capital ratio was 2.18 to 1. At September 30, 2018, Pro Securities had net capital of \$55,572 which was \$50,572 in excess of its required net capital of \$5,000 and Pro Securities net capital ratio was 0.34 to 1. At December 31, 2017, SpeedRoute had net capital of \$334,848, which was \$233,485 in excess of its required net capital of \$101,363 and SpeedRoute's net capital ratio was 4.5 to 1. At December 31, 2017, PRO Securities had net capital of \$24,175, which was \$19,175 in excess of its required net capital of \$5,000 and PRO Securities net capital ratio was 1.3 to 1.

SpeedRoute and Pro Securities did not have any securities owned or securities sold, not yet purchased at September 30, 2018 and December 31, 2017, respectively.

12. RELATED PARTY TRANSACTIONS

PCL L.L.C. term loan repayment

On November 6, 2017, we entered into a loan agreement with PCL L.L.C., an entity directly or indirectly wholly-owned by the mother and brother of our President and Chief Executive Officer, Dr. Patrick M. Byrne ("Dr. Byrne"). The agreement provides for a \$40.0 million term loan (the "PCL Loan") which carries an annual interest rate of 8.0%. On May 8, 2018, our Board of Directors approved a prepayment of the PCL Loan and we repaid the entire outstanding balance under the loan plus accrued interest.

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SiteHelix

On June 28, 2018, we entered into and concurrently closed a Stock Purchase Agreement with the stockholders of SiteHelix, Inc., a Delaware corporation ("SiteHelix") pursuant to which we purchased all of the common stock of SiteHelix for \$500,000 plus 100,000 shares of Overstock common stock with a transaction date fair value of \$2.9 million for an aggregate purchase price of \$3.4 million. The transaction was accounted for as an asset purchase. Saum Noursalehi, who owned approximately 62% of the SiteHelix common stock, is a member of our Board of Directors and served as President, Retail, of Overstock until May 8, 2018, when he became Chief Executive Officer of tZERO.

Bitsy Agreement

In July 2018, Medici Ventures entered into a stock purchase agreement with Bitsy, Inc. ("Bitsy") to acquire an additional 25% equity interest in Bitsy for \$3.0 million and \$1.5 million worth of Overstock.com common stock (47,378 shares). Subsequent to the purchase, Medici Ventures holds a 33% interest in Bitsy. Bitsy is a U.S.-based startup company founded and 25% owned by Medici Ventures' chief operating officer and general counsel, Steve Hopkins. Bitsy plans to build a regulatory-compliant bridge between the U.S. Dollar and cryptocurrencies and offer our customers the ability to purchase cryptocurrencies on or through the Bitsy app and our Website.

Chainstone Labs

In September 2018, Medici Ventures entered into a stock purchase agreement with Chainstone Labs, Inc. ("Chainstone") to acquire a 29% equity interest in Chainstone for \$3.6 million. Chainstone is a U.S.-based startup company founded and 71% owned by a Board member of Medici Ventures, Bruce Fenton. Chainstone is focused on blockchain, tokenization of securities, and decentralized asset management.

Medici Land Governance

Medici Land Governance Inc., a Delaware public benefit corporation ("MLG"), was recently formed by Medici Ventures with Dr. Byrne. Pursuant to the Subscription Agreements dated September 21, 2018, Medici Ventures contributed certain of its assets, including intellectual property relating to technologies regarding land governance and property rights, to MLG in exchange for 510,000 shares of MLG common stock and at the same time Dr. Byrne personally contributed \$6.7 million in cash to MLG in exchange for 390,000 shares of MLG common stock. At the same time MLG, Medici Ventures and Dr. Byrne entered into a Stockholders Agreement dated September 21, 2018 regarding MLG (the "MLG Stockholder Agreement"). The MLG Stockholder Agreement restricts the transfer of the shares held by Medici Ventures and Dr. Byrne, creates rights of first refusal in favor of MLG, Medici Ventures and Dr. Byrne to acquire shares to be sold by Medici Ventures or Dr. Byrne, creates purchase rights in favor of MLG and Medici Ventures in the event of the death or incapacity of Dr. Byrne, creates preemptive rights in favor of MLG and Medici Ventures if MLG proposes to sell capital stock to any other person (subject to certain exceptions), provides for voting for board members, and requires a supermajority consent of the stockholders for any sale of MLG or substantially all of its assets, merger, consolidation, or other transaction having substantially the same effect.

As a result of the transactions described above, Medici Ventures holds approximately 57% of the outstanding capital stock of MLG, and Dr. Byrne, our President and Chief Executive Officer, a member of our board of directors and our largest stockholder, holds approximately 43% of the outstanding capital stock of MLG. Dr. Byrne is also a member of the board of directors of MVI and is a member of the board of directors of MLG.

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

Special Note Regarding Forward-Looking Statements

This Report on Form 10-Q and the documents incorporated herein by reference, as well as our other public documents and statements our officers and representatives may make from time to time, contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. These statements relate to our financial condition, liquidity, results of operations, earnings outlook and prospects. You can find many of these statements by looking for words such as "may," "would," "could," "should," "will," "expect,"

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"anticipate," "predict," "project," "potential," "continue," "contemplate," "seek," "assume," "believe," "intend," "plan," "forecast," "goal," "estimate," or other similar expressions which identify these forward-looking statements. These forward-looking statements are not historical facts, and are based on current expectations, estimates and projections about our industry and business, and on management's beliefs and certain assumptions made by management, many of which, by their nature, are inherently uncertain and beyond our control. Accordingly, you are cautioned that any such forward-looking statements are not guarantees of future performance and are subject to assumptions, risks and uncertainties that are difficult to predict, and that actual results may be materially different from the results expressed or implied by any of our forward-looking statements. We claim the protection of the safe harbor provided by the Private Securities Litigation Reform Act of 1995, as amended, for all such forward-looking statements.

Unless otherwise required by law, we also disclaim any obligation to update our view of any such risks or uncertainties or to announce publicly any revisions to any forward-looking statements made or incorporated by reference in this report. A number of important factors could cause actual results to differ materially from those indicated by the forward-looking statements, including the risks set forth in the "Risk Factors" section of this report, and the risks described in our Annual Report on Form 10-K for the year ended December 31, 2017 and the risks described in our Quarterly Report on Form 10-Q for the quarters ended March 31, 2018 and June 30, 2018. Our forward-looking statements include all statements other than statements of historical fact including, without limitation, all statements regarding:

- our strategies and plans for our e-commerce business and our Medici businesses, including our tZERO initiatives; the possibility that we will pursue or attempt to pursue a strategic alternative that could change our business dramatically, including the possibility and potential effects of a sale of our e-commerce business, as well as the possibility that we will determine not to pursue any strategic alternative at all in the foreseeable future;
- our expectation that if we sell our e-commerce business for cash and retain the after-tax proceeds of the sale, we would return a portion of the after-tax proceeds to our stockholders within 12 months after any such sale, by means of a stock repurchase program, dividend, one or more issuer tender offers or other means;
- all statements of our expectations regarding the "Capital on Demand" Sales Agreement we have entered into with JonesTrading Institutional Services LLC, including any statement about our ability to raise additional capital pursuant to such agreement;
- all statements of our expectations regarding the term sheets we and tZERO signed with GSR Capital in August 2018 and the Token Purchase Agreement we signed with GSR Capital in August 2018;
- our expectations regarding the effects on us of the recent Tax Cuts and Jobs Act;
- our expectations regarding the costs, benefits and risks of Medici Ventures' efforts to develop blockchain applications and tZERO's efforts to develop financial technology ("fintech") applications, including applications using blockchain technology and how effectively that technology will be adopted, and including our expectations regarding the costs, benefits and risks of the operations of tZERO;
- all statements regarding the plans of tZERO or Medici Ventures;
- our expectations regarding the costs, benefits and risks of tZERO's ownership of SpeedRoute and PRO Securities, each of which is a registered broker dealer;
- our expectations regarding the costs, benefits and risks of having less than wholly-owned subsidiaries, including our indirect approximately 80% owned subsidiary tZERO and our currently wholly-owned subsidiary Medici Ventures, which has issued stock options to employees and consequently may not be wholly-owned in the future;
- all statements regarding the tZERO security token offering, including the possibility that the proceeds of the security token offering might be treated as income to us for federal income tax purposes, and might be treated as a liability rather than equity for accounting purposes;
- our expectations regarding the costs, benefits and risks of our efforts and plans to advertise or offer financial product and services offerings on our website, including discount stock brokerage trading services, automated investment advisory services, accredited investor verification services, and other financial service offerings and other businesses, innovations and projects that we or our subsidiaries may engage in, offer or advertise in the future;
- our expectations regarding Medici Ventures' funding of efforts to create a system to help areas of the world that lack reliable widely-recognized land-titling and record-keeping processes implement blockchain-based systems for doing

so;

• our plans to modify our branding and marketing strategy;

• our beliefs regarding our ability to attract and retain customers in a cost-efficient manner;

- the anticipated effectiveness of or potential improvements in our marketing;

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our future operating and financial results, including any projections of revenue, profits or losses, contribution, technology expense, general and administrative expense, cash flow, capital expenditures or other financial measures or amounts or non-GAAP financial measures or amounts or anticipated changes in any of them;

our beliefs and expectations regarding the adequacy of our facilities, including leased and any third-party operated warehouse facilities, as well as the possibility that we may add distribution centers or other distribution facilities to our distribution system and our expectations regarding the results of any such additions;

our future capital requirements and our ability to satisfy our capital needs;

the adequacy of our liquidity and our ability, if any, to increase our liquidity or capital resources through traditional capital raising or otherwise;

tZERO's plans, including without limitation its plans to develop its Token Trading System and all statements about tZERO's plans and expectations regarding tZERO's joint venture with Box Digital;

whether the tZERO Token Trading System will be able to comply with SEC rules and regulations;

our plans and expectations regarding the costs, benefits, and risks of attempting to develop technology applications including applications using or relating to blockchain technology and our plans to commercialize any of these potential applications;

the competition we currently face and anticipate;

the effects of current and future government regulation;

our expectations for our international sales efforts;

our efforts to provide multi-channel fulfillment services;

our plans for further changes to our business;

our expectations and beliefs regarding our ability to effectively change business strategies, including by increasing or decreasing our e-commerce branding and marketing expenditures;

our beliefs regarding current or future litigation or regulatory actions or fines, including our expectations regarding the investigation the Division of Enforcement of the Securities and Exchange Commission is conducting and its request for information and documents related to tZERO and the tZERO security token offering;

our beliefs and expectations regarding existing and future tax laws and related laws and the application of those laws to our business including the results of tax assessments we receive periodically;

our beliefs regarding the adequacy of our insurance coverage;

our beliefs regarding the adequacy and anticipated functionality of our infrastructure, including our backup facilities and beliefs regarding the adequacy of our disaster planning and our ability to recover from a disaster or other interruption of our ability to operate our Website;

our beliefs regarding our cybersecurity efforts and measures and our efforts to prevent data breaches and the costs we will incur in our ongoing efforts to avoid interruptions to our product offerings and other business processes from cyber-attacks and from data breaches;

our ability to maintain or improve upon customer service levels that we and our customers consider acceptable;

our beliefs regarding the adequacy of our order processing systems and our fulfillment and distribution capabilities;

our belief that we and our partners will be able to maintain inventory levels at appropriate levels despite the seasonal nature of our business and the rapid changes we encounter in customer demand for various products;

our expectations regarding our emphasis on home and garden product offerings;

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

our other statements about the anticipated benefits and risks of our business and plans.

Our forward-looking statements are only predictions. Actual events or results may differ materially from those contemplated by our forward-looking statements for a variety of reasons, including among others:

any changes we may make to our business as a result of our current ongoing review of potential strategic alternatives, which could involve a sale of our e-commerce business, additional equity or debt financings, or other significant changes to our business;

the possibility that we may sell our e-commerce business for cash and retain some or all of the after-tax proceeds of the sale for use in our blockchain initiatives, which could result in our stockholders owning equity interests in a

publicly-held corporation seeking to develop entirely new businesses and revenue streams, without the benefits of our current e-commerce business and the approximately \$1.7 billion it generates in annual net revenues but with most if not all of the expenses of operating a publicly-held corporation;
the potentially substantial corporate level income tax expense we could incur if we were to sell our e-commerce business in a taxable transaction;

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the possibility that our publicly-disclosed review of potential strategic alternatives may distract our management and other employees, may cause members of our management and/or other employees to seek employment elsewhere, and may have adverse effects on our business and financial results;

the technical, operational, financial, regulatory, legal, reputational, marketing and other obstacles we face in trying to create a profitable business with significant revenues from our blockchain initiatives;

the possibility that we will be unable to raise the amount of capital we may need to continue funding both our e-commerce business losses and our blockchain initiatives as contemplated by the GSR term sheets or otherwise;

the possibility that the recent Tax Cuts and Jobs Act will have adverse effects on us in addition to those we have already identified;

the possibility that the proceeds of the tZERO security token offering might be treated as income to us for federal income tax purposes;

the possibility that the tZERO security token offering could result in claims against tZERO and/or us;

the effects of changes we have recently made and of additional changes we may make in the future to the amount of our sales and marketing expenditures, which could continue to have an adverse effect on our near-term financial results as they did in the first nine months of 2018;

the costs of, and difficulties we have encountered and may continue to encounter with, the implementation of our strategies for our e-commerce business;

the possibility that we may be unable to fund our plans for sales and marketing activities, additional new distribution facilities, our technology platforms, our Club O rewards program, our private label strategy, and other e-commerce initiatives, and also continue to fund our blockchain initiatives at the level we think appropriate;

the efficiency of our e-commerce marketing and its effect on our business strategy;

the cost and availability of online and traditional advertising, and the results of our various brand building and marketing campaigns;

difficulties we have encountered and continue to encounter with our natural search results;

increasing competition, including competition from well-established competitors including Amazon.com, competition from competitors based in China or in other relatively low-cost jurisdictions, competition from well-funded companies, including Wayfair, and from others including Amazon and other competitors with business models that include delivery capabilities that we cannot currently match and do not expect to be able to match in the foreseeable future;

- difficulties we may encounter in connection with our efforts to offer services to our customers outside of our e-commerce business, including the credit, insurance, discount brokerage trading services, automated investment advisory services, and accredited investor verification services we advertise or offer;

difficulties, including expense and any operational or regulatory issues we may encounter in connection with tZERO or its subsidiaries, including its two registered broker-dealers, SpeedRoute and PRO Securities;

technical, operational, regulatory or other difficulties we may encounter with our Medici or tZERO blockchain or financial technology initiatives, including difficulties we or tZERO may have marketing any products or services tZERO may offer, whether due to lack of market size or acceptance or as a result of competition from any of the numerous competitors seeking to develop competing technologies or systems or as a result of patents that may be granted to other companies or persons; and losses we may continue to incur in connection with our Medici and tZERO blockchain and financial technology initiatives;

the possibility that blockchain technology may be adopted more slowly than we anticipate;

the fact that tZERO necessarily allocates its limited resources among the projects it is pursuing, and at present has re-allocated developers from working on its DLR Software to working on other projects, and at present does not have an agreement with a retail broker-dealer that will be necessary for the operation of the DLRs;

the difficulties tZERO will face in attempting to market its DLR Software, and the possibility that we and/or tZERO have overestimated the demand for, and/or the size of the intended market for the DLR Software or may face regulatory issues related to the DLR Software;

the substantial technical, operational, financial, regulatory, legal, marketing and other obstacles to tZERO's plans to create and launch a U.S. national exchange with regulatory approval to trade security tokens, including any

difficulties tZERO may have with its joint venture with Box Digital;
the difficulties tZERO will face in attempting to generate revenues from blockchain-based applications of any nature;
Medici Ventures' current business model of providing the services of its developers at Medici Ventures' cost to
companies in which Medici Ventures owns an interest;

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- any difficulties we may have with the interests in other companies that we or Medici Ventures or tZERO may own or acquire in the future, including any additional impairment charges we may recognize with respect to any of them; the substantial obstacles Medici Ventures faces in connection with its efforts to fund the creation of a system to help areas of the world that lack reliable widely-recognized land-titling and record-keeping processes implement blockchain-based systems for doing so, including the substantial difficulties it may encounter with persons who benefit from existing locally-recognized systems currently in use in many places;
- any liability or expense we may incur as a result of our interests in other companies, whether as a result of regulatory issues or otherwise;
- the current downturn in portions of the U.S. housing market, which at least one article published in late July 2018 by a nationally-recognized online news service said "appears to be headed for the broadest slowdown in years," and any broader or deeper downturn in the U.S. housing market or other changes in U.S. and global economic conditions or U.S. consumer spending;
- the effects of recent tariffs or the imposition of additional tariffs or occurrence of other events or circumstances that increase the price of importing into the U.S. the types of merchandise we sell in our e-commerce business or make it more difficult to import or obtain such merchandise;
- our failure to maintain our existing relationships with our fulfillment partners or build new relationships with fulfillment partners on acceptable terms;
- our failure to maintain optimal levels of product quality, quantity and assortment or to attract sufficient consumer interest in our product offerings;
- any claims we may face regarding the quality, safety or labelling of the products we offer;
- modifications we may make to our business model from time to time, including aspects relating to our product mix and the mix of direct/partner sourcing of the products we offer, and difficulties we may encounter as a result of our efforts to change various aspects of our business model frequently and rapidly;
- the mix of products purchased by our customers and changes to that mix;
- any claims we may face regarding cyber security issues or data breaches or difficulties we encounter regarding Internet or other infrastructure or communications impairment problems or the costs of preventing or responding to any such problems, including cyber security issues or data breaches that could result from cyber security issues or data breaches at companies with which we do business or at companies with which our customers do business;
- any problems with or affecting our payment card processors, including cyber-attacks, Internet or other infrastructure or communications impairment or other events that could interrupt the normal operation of the payment card processors or any difficulties we may have maintaining compliance with the rules of the payment card processors;
- any future substantial decrease in our liquidity, whether as a result of our e-commerce business operations, our blockchain or fintech initiatives, or as a result of the expenses or results of governmental inquiries or investigations or litigation or other claims against us, and the possibility that we will be unable to obtain financing or any other source of liquidity adequate to enable us to continue our operations;
- problems with or affecting the facility where substantially all of our computer and communications hardware is located or other problems that result in the unavailability of our Website or reduced performance of our transaction systems;
- any liabilities that may be asserted against us for not having collected sales tax in jurisdictions in which we did not do so;
- any losses or issues we may encounter as a consequence of accepting or holding bitcoin or other cryptocurrencies, whether as a result of regulatory, tax or other legal issues, technological issues, value fluctuations, lack of widespread adoption of bitcoin or other cryptocurrencies as an acceptable medium of exchange or otherwise;
- difficulties we may have in responding to technological changes;
- losses we may incur due to fraud or our inability to prevent or limit fraud;
- claims or other problems we may encounter as a result of the listing or sale on our Website of pirated, counterfeit or illegal items;
 - any environmental liabilities we may incur relating to the real estate owned by one of our wholly-owned subsidiaries and on which our corporate headquarters is located;

- any failure of any of our product or service offerings outside of our main shopping Website offerings to provide the benefits we expect from them;
- any difficulties we may encounter as a result of our reliance on numerous third parties that we do not control for the performance of critical functions material to our business;

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- any difficulties we may encounter in connection with the rapid shift of e-commerce and online payments to mobile and multi-channel commerce and payments;
- our inability to increase market share or revenue in accordance with our plans;
- additional difficulties we may have with our efforts to increase our revenues at an acceptable cost in accordance with our plans and to return to profitability;
 - difficulties we may encounter in connection with our efforts to emphasize our home and garden product offerings and to brand ourselves as a home and garden shopping destination, including the risk that our sales of home and garden product offerings could decrease substantially as a result of a significant downturn in some or all of the U.S. housing market;
- fluctuations in our operating results;
- difficulties we may encounter in connection with our efforts to expand internationally, including claims we may face and liabilities we may incur in connection with those efforts;
- adverse results in legal proceedings, investigations or other claims, and costs we may incur in connection with any of them, including the costs of responding to the investigation the Division of Enforcement of the Securities and Exchange Commission is conducting;
- any difficulties we may have optimizing our warehouse operations;
- the risks of inventory management and seasonality, particularly with inventory subject to rapid price declines;
- any decrease in the rate of growth of e-commerce, particularly in home goods, and the occurrence of any event that would adversely affect e-commerce or discourage or prevent consumers from shopping online or via mobile apps;
- the possibility that we will suffer adverse consequences as a result of one or more of the related party transactions we have entered into or other related party transactions that we may enter into in the future; and
- the other risks described in this report or in our other public filings.

In evaluating all forward-looking statements, you should specifically consider the risks outlined above or elsewhere in this report and the risks described in our Report on Form 10-K for the year ended December 31, 2017 filed with the SEC on March 15, 2018 and those described in our Quarterly Report on Form 10-Q for the quarter ended March 31, 2018 filed with the SEC on May 8, 2018, and in our Quarterly Report on Form 10-Q for the quarter ended June 30, 2018 filed with the SEC on August 9, 2018, especially under the headings "Risk Factors," "Legal Proceedings," and "Management's Discussion and Analysis of Financial Condition and Results of Operations." These factors may cause our actual results to differ materially from those contemplated by any forward-looking statement in this report. Although we believe that our expectations reflected in the forward-looking statements are reasonable, we cannot guarantee or offer any assurance of future results, levels of activity, performance or achievements or other future events.

Available Information

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

Overview

We are an online retailer and advancer of blockchain technology. Through our online retail business, we offer a broad range of price-competitive products, including furniture, home decor, bedding and bath, housewares, jewelry and watches, among other products. We sell our products and services through our Internet websites located at www.overstock.com, www.o.co and www.o.biz (referred to collectively as the "Website"). Although our three websites are located at different domain addresses, the technology and equipment and processes supporting the

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

In late 2014, we began working on initiatives to develop and advance blockchain technology, which we refer to collectively as Medici. As part of our Medici initiatives, we have formed a wholly-owned subsidiary Medici Ventures, Inc. ("Medici Ventures") and acquired a majority interest in a financial technology company and two related registered broker dealers which are owned by our majority-owned subsidiary tZERO Group, Inc. ("tZERO"), formerly tØ.com, Inc. In 2015, we were the first public company to issue a private security using blockchain technology and in December 2016, as a demonstration of our technology, we issued publicly traded blockchain preferred shares of Overstock.com, Inc. Medici Ventures

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also holds minority interests in several blockchain technology companies. Medici Ventures has assembled a core blockchain development group of software engineers, developers, and other technologists that provide services to the blockchain community on a contract basis as requested, including the companies in which we hold a minority interest. In 2018, tZERO acquired majority-ownership interests in a registered investment adviser entity and an accredited investor verification entity and further purchased minority interests in multiple financial services companies, including an equity interest in a joint venture with BOX Digital Markets LLC to pursue the development of the first U.S. security token exchange.

Our company, based near Salt Lake City, Utah, was founded in 1997. We launched our initial website in March 1999 and were re-incorporated in Delaware in 2002. As used herein, "Overstock," "the Company", "we," "our" and similar terms include Overstock.com, Inc. and our majority-owned subsidiaries, unless the context indicates otherwise.

Our Business

Retail Business

In our retail business, we deal primarily in price-competitive, new and replenishable merchandise and use the Internet to aggregate both supply and demand to create an efficient marketplace for selling these products. We provide our customers an opportunity to conveniently shop for a broad range of price-competitive products. We continually add new, and sometimes limited, inventory to our Website in order to create an atmosphere that encourages customers to visit frequently and purchase products before our inventory sells out. We provide suppliers with access to a large customer base and convenient services for order fulfillment, customer service, returns handling, and other services. The merchandise offered on our Website is from a variety of sources including well-known, brand-name manufacturers. Consumers and businesses are able to access and purchase our products 24 hours a day from the convenience of a computer, Internet-enabled mobile telephone or other Internet-enabled device. Our team of customer service representatives assists customers by telephone, instant online chat and e-mail. We also derive revenue from other businesses advertising products or services on our Website. Our sales are primarily to customers located in the United States.

We have organized our retail business (sales of product offered through the Shopping Section of our Website) into two principal segments—a "direct" business and a "partner" business. Our retail direct business includes sales made to individual consumers and businesses from our owned inventory and that are fulfilled primarily from our warehouses in Salt Lake City, Utah, Carlisle, Pennsylvania, and Kansas City, Kansas.

For our retail partner business, we sell merchandise from manufacturers, distributors and other suppliers ("partners") primarily through our Website. We are considered to be the principal and control the specific good or service before it is transferred to the customer 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" does not mean that we have formed any legal partnerships with any of our partners. These third-party partners generally perform the same fulfillment operations as our warehouses, such as order picking and shipping; however, we handle returns and customer service related to substantially all orders placed through our Website. Revenue generated from sales on our Shopping site from both the direct and partner businesses is recorded net of returns, coupons and other discounts.

Both direct and 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 for the foreseeable future. To the extent possible we maintain supplier relationships, and seek new supplier relationships, for both our direct and partner businesses, and also use our working capital, to ensure a continuous allotment of product offerings for our customers. Because a portion of our product offerings are closeout merchandise, some of our suppliers cannot supply products to us on a continuous basis.

Medici business

Our Medici business initiatives seek to leverage the security, transparency and immutability of cryptographically protected, distributed ledgers, such as blockchains, and are focused on solving important problems, including financial transaction issues, particularly in the areas of securities settlement, commercial blockchain applications, capital markets applications, digital currency, money and banking applications, compliance, personal identity, voting, supply chain, social media, and property and land applications. Our wholly-owned subsidiary, Medici Ventures, conducts its primary business through its majority-owned subsidiary tZERO, which includes a financial technology company, two related registered broker dealers, a registered investment advisor, and an accredited investor verification company. tZERO also holds minority interests

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in multiple financial services companies, including an equity interest in a joint venture with BOX Digital Markets LLC to pursue the development of the first U.S. security token exchange.

As described further in Item 1 of Part I, "Financial Statements (Unaudited)"—Note 10. Business Segments, we determined our segments based on how we manage our business, which, in our view, consists primarily of our Retail and Medici businesses. As described above, our Retail business consists of our Direct and Partner reportable segments. We use gross profit as the measure to determine our reportable segments because there is not discrete financial information available below gross profit for our Direct and Partner segments. As a result, our Medici business risk is not significant as compared to our Direct and Partner segments and is included in Other. Our Other segment consists of Medici Ventures and its subsidiaries, including tZERO.

Recent tZERO Business Developments

An important part of tZERO's strategy is to buy, build, or partner with other entities in order to aggregate all the necessary components to have end-to-end ownership of the first fully regulated security token trading, clearing and settlement platform. As previously announced in early 2018, tZERO purchased a 24% equity interest in StockCross Financial Services, Inc. ("StockCross"), which is an affiliate of Siebert Financial Corp. ("Siebert"), and an interest in Siebert, for \$12 million. tZERO also purchased a 1% interest in Kennedy Cabot Acquisition, the majority stockholder of Siebert, and an interest in Siebert, for \$1 million. Our equity interest in StockCross was a step toward achieving our strategy by adding a partner with the custodial and clearing functionality of a U.S. DTCC member firm. We also intended to enter into definitive agreements with StockCross to act as an Introducing Broker and Clearing Broker for security token trading. tZERO has decided not to enter into a definitive agreement with StockCross for security token trading. tZERO anticipates that StockCross may license tZERO's Digital Locate Receipt software upon agreement of mutually acceptable terms. tZERO expects that the stock loan agreement currently in place between StockCross and tZERO's subsidiary SpeedRoute will remain in place.

In addition, as previously announced in early 2018, tZERO entered into a letter of intent contemplating that tZERO would acquire 81% of the outstanding membership interests of Weeden Prime Services, LLC ("WPS"), a U.S. registered broker-dealer, for \$18 million through a series of transactions beginning in the third quarter of 2018. tZERO has also decided not to enter into a definitive agreement with WPS. Accordingly, in October 2018, tZERO notified these parties that it no longer intends to pursue such agreements.

During the third quarter of 2018, tZERO began evaluating alternative strategic relationships that may replace one or more roles tZERO expected StockCross to fulfill. tZERO believes it has identified suitable candidates to perform these roles but has not yet entered into definitive agreements with those parties. Management of tZERO will continue to devote time and resources to identify the necessary components for tZERO's trading ecosystem and enter into appropriate licensing and/or other contractual arrangements with one or more entities. Doing so will likely require capital and may cause delays to the development and launch of tZERO's planned trading platform.

tZERO and StockCross, including their affiliates, have a number of business relationships, and the resolution of some of those relationships are undetermined at this time but could include tZERO's sale of its equity interest in StockCross and its affiliates, and/or the possibility of entering into new business relationships with StockCross under terms not previously considered. At present, tZERO expects that the stock loan agreement currently in place between StockCross and tZERO's subsidiary SpeedRoute will remain in place through its expiration date of March 31, 2019. tZERO does not currently expect the foregoing matters to affect the December 31, 2017 agreement among tZERO, SpeedRoute and Muriel Siebert & Co. Inc. ("Muriel Siebert") pursuant to which Muriel Siebert is currently advertising discounted online trading of U.S. equity securities on Overstock's website; however, revenues associated with such services are currently immaterial to Overstock.

Executive Commentary

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

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Revenue in Q3 2018 increased 4% compared to Q3 2017. The growth in revenue was primarily driven by increased marketing expenses as we continued our strategy to more aggressively pursue revenue growth and new customers early in the quarter. However, we shifted our marketing strategy in early August as we sought to minimize losses, which tapered our revenue growth throughout the quarter. We also saw a 6% increase in average order size (excluding promotional activities) primarily due to a continued sales mix shift into home and garden products. These increases were partially offset by increased promotional activities, including coupons and site sales (which we recognize as a reduction of revenue) due to our driving a higher proportion of our sales using such promotions, and an increase in marketplace sales (for which we record only our commission as revenue). While our marketing spend efficiency has improved significantly during Q3 2018, we continue to face challenges in our natural search marketing.

Gross profit in Q3 2018 increased 4% compared to Q3 2017 primarily as a result of revenue growth. Gross margin was 19.7% in Q3 2018, unchanged from Q3 2017. Gross margin was negatively impacted by increased promotional activities, but this was offset by a continued shift in sales mix into higher margin home and garden products and an increase in marketplace sales (for which we record only our commission as revenue).

Sales and marketing expenses as a percentage of revenue increased from 10.6% to 12.6% in Q3 2018 as compared to Q3 2017, primarily due to our effort to aggressively pursue increased revenue and new customers early in the quarter. This included significantly increased spending in the display ads on social media, sponsored search, and direct mail marketing channels, as well as increased staff-related costs.

Technology expenses in Q3 2018 increased \$5.1 million compared to Q3 2017, primarily due to an increase in staff-related costs of \$3.4 million and an increase in technology licenses and maintenance of \$1.6 million.

General and administrative expenses in Q3 2018 increased \$23.7 million compared to Q3 2017 primarily due to \$10.8 million in special legal costs in Q3 2018 largely related to our gift card escheatment case in Delaware and capital raising efforts, a \$5.1 million increase in staff-related costs, and a \$3.2 million increase in consulting and outside services.

Liquidity

In Q3 2018, our consolidated cash and cash equivalents balance increased \$29.8 million, from \$152.2 million to \$182.0 million, primarily as the result of cash inflows of \$94.6 million, net of offering costs, from the sale of common stock under our "at the market" sales agreement with JonesTrading and a \$6.7 million cash inflow from the capital contributions received by a consolidated subsidiary, Medici Land Governance, which was partially offset by cash outflows from operating activities of \$50.2 million for the quarter and \$14.1 million in cash outflows related to acquisitions of equity interests in other entities and \$7.9 million in expenditures for fixed assets.

We continue to seek opportunities for growth in our retail business, through our Medici blockchain and financial technology initiatives, and through other means. As a result of these initiatives, we will continue to incur additional expenses and may purchase interests in, or make acquisitions of, other technologies or businesses. We anticipate that our initiatives may cause us to continue to incur losses in the foreseeable future. These losses, additional expenses, acquisitions or purchases may be material, and, coupled with existing marketing expense trends, and potential strategic changes in our retail business, may lead to increased consolidated losses in some periods, and to reduced liquidity. Additionally, we may recognize additional impairment charges from our ownership interests in other entities.

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

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Results of Operations

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

	Three months ended September 30, 2018		2017		Nine months ended September 30, 2018		2017	
	(as a percentage of total net revenue)		(as a percentage of total net revenue)		(as a percentage of total net revenue)		(as a percentage of total net revenue)	
Revenue, net								
Direct	3.5	%	4.6	%	3.4	%	5.0	%
Partner and other	96.5		95.4		96.6		95.0	
Total net revenue	100.0		100.0		100.0		100.0	
Cost of goods sold								
Direct	3.7		4.6		3.3		4.8	
Partner and other	76.6		75.6		76.8		75.4	
Total cost of goods sold	80.3		80.3		80.1		80.2	
Gross profit	19.7		19.7		19.9		19.8	
Operating expenses:								
Sales and marketing	12.6		10.6		16.6		9.8	
Technology	7.7		6.8		7.1		6.7	
General and administrative	10.3		5.1		8.5		5.2	
Total operating expenses	30.5		22.5		32.2		21.6	
Operating loss	(10.9	)	(2.8	)	(12.3	)	(1.9)
Other income (expense), net	(0.4	)	1.3		(0.1	)	0.1	
Loss before income taxes	(11.2	)	(1.5	)	(12.4	)	(1.8)
Benefit from income taxes	—		(1.3	)	—		(0.6)
Consolidated net loss	(11.2	)%	(0.3	)%	(12.4	)%	(1.2)%

Comparisons of Three Months Ended September 30, 2018 to Three Months Ended September 30, 2017, and Nine Months Ended September 30, 2018 to Nine Months Ended September 30, 2017

Revenue

The following table reflects our net revenues for the three and nine months ended September 30, 2018 and 2017 (in thousands):

	Three months ended September 30,				Nine months ended September 30,			
	2018	2017	\$ Change	% Change	2018	2017	\$ Change	% Change
Revenue, net								
Direct	\$15,424	\$19,645	\$(4,221)	(21.5)%	\$46,409	\$64,572	\$(18,163)	(28.1)%
Partner and other	425,156	404,362	20,794	5.1	1,322,635	1,223,894	98,741	8.1
Total revenue, net	\$440,580	\$424,007	\$16,573	3.9%	\$1,369,044	\$1,288,466	\$80,578	6.3%

The increased total net revenue for the three months ended September 30, 2018, as compared to the same period in 2017, was primarily driven by increased marketing expenses as we continued our strategy to more aggressively pursue revenue growth and new customers early in the quarter. However, we shifted our marketing strategy in early August as we sought to minimize losses, which tapered our revenue growth throughout the quarter. We also saw a 6% increase in average order size (excluding promotional activities) primarily due to a continued sales mix shift into

home and garden products. These increases were partially offset by increased promotional activities, including coupons and site sales (which we recognize as a reduction of revenue) due to our driving a higher proportion of our sales using such promotions, and an increase in marketplace sales (for which we record only our commission as revenue). While our marketing spend efficiency has improved significantly during Q3, we continue to face challenges in our natural search marketing.

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The increased total net revenue for the nine months ended September 30, 2018, as compared to the same period in 2017, was primarily driven by increased marketing expenses as we more aggressively pursued revenue growth and new customers. Our increased marketing expenses resulted in a 5% increase in orders, and we also saw a 6% increase in average order size (excluding promotional activities) primarily due to a continued sales mix shift into home and garden products. These increases were partially offset by increased promotional activities, including coupons and site sales (which we recognize as a reduction of revenue) due to our driving a higher proportion of our sales using such promotions, and an increase in marketplace sales (for which we record only our commission as revenue).

The decreased direct revenue for the three months ended September 30, 2018, as compared to the same period in 2017, was primarily due to a decrease in direct sales of home and garden products.

The decreased direct revenue for the nine months ended September 30, 2018, as compared to the same period in 2017, was primarily due to a decrease in direct sales of home and garden and clothing products, and increased promotional activities.

The increase in partner revenue for the three months ended September 30, 2018, as compared to the same period in 2017, was primarily driven by increased marketing expenses and an increase in partner sales of home and garden products. This increase was partially offset by increased promotional activities, including coupons and site sales due to our driving a higher proportion of our sales using such promotions and an increase in marketplace sales (for which we record only our commission as revenue).

The increase in partner revenue for the nine months ended September 30, 2018, as compared to the same period in 2017, was primarily driven by increased marketing expenses and an increase in partner sales of home and garden products. This increase was partially offset by increased promotional activities, including coupons and site sales due to our driving a higher proportion of our sales using such promotions and an increase in marketplace sales (for which we record only our commission as revenue).

We continue to seek increased participation in our Club O loyalty program, including, in certain instances, by increasing Club O Rewards to our Club O members in lieu of coupons we offer to all customers. For additional information regarding our Club O loyalty program see Item 1 of Part I, "Financial Statements (Unaudited)"—Note 2. Accounting Policies, Club O loyalty program.

The shift of business from direct to partner (or vice versa) is an economic result based on the economics of each particular product offering at the time and we generally do not have particular goals for an "appropriate" mix or percentage for the size of either. Although we have experienced a trend from direct revenue to partner revenue in recent years, we believe that the mix of the business between direct and partner remains consistent with our strategic objectives for our business model and we do not currently foresee material shifts in this trend.

The products and product lines we offer, and their respective percentages of our revenue, are based on many factors including customer demand, our marketing efforts, promotional pricing, joint-marketing offered by our suppliers, the types of inventory we are able to obtain and the number of SKUs we offer. These factors change frequently and can affect the mix of the product lines we sell. We have experienced a trend toward our home and garden category in recent years and we have recently focused our marketing and branding efforts towards our home and garden product line. We are also working to increase the number of SKUs we offer. While we do not currently expect any material shifts in our product line mix, the relative amounts of the product lines we sell, and the revenue we earn from those product lines, are generally an economic result of the factors described above, which may change from time to time.

International net revenues were less than 3% of total net revenues for the three and nine months ended September 30, 2018 and 2017.

Change in estimate of average transit times (days)

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

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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 pre-tax income for the three months ended September 30, 2018 (in thousands):

Change in the Estimate of Average Transit Times (Days)	Three Months Ended September 30, 2018	
	Increase (Decrease) Revenue	Increase (Decrease) Pre-Tax Income
2	\$(14,450)	\$(1,532)
1	\$(5,967)	\$(624)
As reported	As reported	As reported
-1	\$5,048	\$ 483
-2	\$9,361	\$ 905

Gross profit and gross margin

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

The following table reflects our net revenues, cost of goods sold and gross profit for the three and nine months ended September 30, 2018 and 2017 (in thousands):

	Three months ended September 30,				Nine months ended September 30,			
	2018	2017	\$ Change	% Change	2018	2017	\$ Change	% Change
Revenue, net								
Direct	\$15,424	\$19,645	\$(4,221)	(21.5)%	\$46,409	\$64,572	\$(18,163)	(28.1)%
Partner and other	425,156	404,362	20,794	5.1	1,322,635	1,223,894	98,741	8.1
Total net revenue	\$440,580	\$424,007	\$16,573	3.9 %	\$1,369,044	\$1,288,466	\$80,578	6.3 %
Cost of goods sold								
Direct	\$16,205	\$19,577	\$(3,372)	(17.2)%	\$45,649	\$61,687	\$(16,038)	(26.0)%
Partner and other	337,659	320,755	16,904	5.3	1,051,067	972,026	79,041	8.1
Total cost of goods sold	\$353,864	\$340,332	\$13,532	4.0 %	\$1,096,716	\$1,033,713	\$63,003	6.1 %
Gross Profit								
Direct	\$(781)	\$68	\$(849)	(1,249)%	\$760	\$2,885	\$(2,125)	(73.7)%
Partner and other	87,497	83,607	3,890	4.7	271,568	251,868	19,700	7.8
Total gross profit	\$86,716	\$83,675	\$3,041	3.6 %	\$272,328	\$254,753	\$17,575	6.9 %

Gross margins for the past seven quarterly periods and fiscal year ending 2017 were:

	Q1 2017	Q2 2017	Q3 2017	Q4 2017	FY 2017	Q1 2018	Q2 2018	Q3 2018
Direct	8.2 %	4.3 %	0.3 %	(2.3)%	3.0 %	9.2 %	0.3 %	(5.1)%
Partner and other	20.8 %	20.3 %	20.7 %	19.7 %	20.3 %	21.5 %	19.6 %	20.6 %
Combined	20.1 %	19.5 %	19.7 %	18.8 %	19.5 %	21.1 %	19.0 %	19.7 %

Gross profit for the three months ended September 30, 2018 increased 4% compared to the same period in 2017 primarily as a result of increased revenue. Gross margin was 19.7% for the three months ended September 30, 2018,

unchanged from the same period in 2017. Gross margin was negatively impacted by increased promotional activities, but this was offset by a continued shift in sales mix into higher margin home and garden products and an increase in marketplace sales (for which we record only our commission as revenue).

Gross profit for the nine months ended September 30, 2018 increased 7% compared to the same period in 2017 as a result of increased revenue and increased gross margin. Gross margin increased to 19.9% for the nine months ended September

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30, 2018 compared to 19.8% for the same period in 2017. This increase in gross margin was primarily due to a continued shift in sales mix into higher margin home and garden products and an increase in marketplace sales (for which we record only our commission as revenue), partially offset by increased promotional activities.

The 541 basis point decrease in direct gross margin for the three months ended September 30, 2018, as compared to the same period in 2017, was primarily due to increased promotional activities.

The 283 basis point decrease in direct gross margin for the nine months ended September 30, 2018, as compared to the same period in 2017, was primarily due to increased promotional activities, partially offset by a shift in sales mix into higher margin home and garden products.

The 10 basis point decrease in partner gross margin for the three months ended September 30, 2018, as compared to the same period in 2017, was primarily due to increased promotional activities, partially offset by a continued shift in sales mix into higher margin home and garden products and an increase in marketplace sales (which we recognize on a net basis).

The 5 basis point decrease in partner gross margin for the nine months ended September 30, 2018, as compared to the same period in 2017 was primarily due to increased promotional activities, partially offset by a continued shift in sales mix into higher margin home and garden products and an increase in marketplace sales (which we recognize on a net basis).

Cost of goods sold includes stock-based compensation expense of \$41,000 and \$46,000 for the three months ended September 30, 2018 and 2017, respectively, and \$152,000 and \$134,000 for the nine months ended September 30, 2018 and 2017, respectively.

Fulfillment costs

Fulfillment costs include all warehousing costs, including fixed overhead and variable handling costs (excluding packaging costs), as well as credit card fees and customer service costs, all of which we include as costs in calculating gross margin. We believe that some companies in our industry, including some of our competitors, account for fulfillment costs within operating expenses, and therefore exclude fulfillment costs from gross margin. As a result, our gross margin may not be directly comparable to others in our industry.

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

	Three months ended				Nine months ended			
	September 30,				September 30,			
	2018	2017	2018	2017	2018	2017	2018	2017
Total revenue, net	\$440,580	100%	\$424,007	100%	\$1,369,044	100%	\$1,288,466	100%
Cost of goods sold								
Product costs and other cost of goods sold	334,156	76%	321,678	76%	1,039,518	76%	977,827	76%
Fulfillment and related costs	19,708	4%	18,654	4%	57,198	4%	55,886	4%
Total cost of goods sold	353,864	80%	340,332	80%	1,096,716	80%	1,033,713	80%
Gross profit	\$86,716	20%	\$83,675	20%	\$272,328	20%	\$254,753	20%

Fulfillment costs as a percentage of sales may vary due to several factors, such as our ability to manage costs at our warehouses, significant changes in the number of units received and fulfilled, the extent to which we use third-party fulfillment services and warehouses, and our ability to effectively manage customer service costs and credit card fees.

Fulfillment and related costs remained flat during the three and nine months ended September 30, 2018 as compared to the same periods in 2017.

See "Gross profit" above for additional discussion.

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Operating expenses

Sales and marketing expenses

We use a variety of methods to target our consumer audience, including online campaigns, such as advertising through keywords, product listing ads, display ads, search engines, affiliate marketing programs, social coupon websites, portals, banners, e-mail, direct mail and viral and social media campaigns. We also do brand advertising through television, radio, print ads, and event sponsorships.

Costs associated with our discounted shipping and other promotions, such as coupons, are not included in sales and marketing expense. Rather, they are accounted for as a reduction in revenue as they reduce the amount of consideration we expect to receive in exchange for goods or services and therefore affect net revenues and gross margin. We consider discounted shipping and other promotions, such as our policy of free shipping on orders over \$45, as an effective marketing tool, and intend to continue to offer them as we deem appropriate as part of our overall marketing plan.

The following table reflects our sales and marketing expenses for the three and nine months ended September 30, 2018 and 2017 (in thousands):

	Three months ended				Nine months ended			
	September 30,		\$ Change	% Change	September 30,		\$ Change	% Change
	2018	2017			2018	2017		
Sales and marketing expenses	\$55,312	\$45,153	\$10,159	22.5 %	\$226,942	\$126,068	\$100,874	80.0 %
Sales and marketing expenses as a percent of net revenues	12.6	% 10.6	%		16.6	% 9.8	%	

The 191 basis point increase in sales and marketing expenses as a percentage of revenue for the three months ended September 30, 2018, as compared to the same period in 2017, was primarily due to our effort to aggressively pursue increased revenue and new customers early in the quarter through significantly increased spending in the display ads on social media, sponsored search, and direct mail marketing channels, as well as increased staff-related costs.

The 679 basis point increase in sales and marketing expenses as a percentage of revenue for the nine months ended September 30, 2018, as compared to the same period in 2017, was primarily due to our effort to aggressively pursue increased revenue and new customers. This effort consisted of significantly increased spending in the sponsored search, display ads on social media, and television marketing channels, and continued through early August when we shifted our retail strategy to reduce these expenses. We also had a \$7.9 million increase in staff-related costs, including \$2.9 million at tZERO for employee severance and a special restricted stock grant which fully vested during Q1 2018.

Sales and marketing expenses include stock-based compensation expense of \$277,000 and \$109,000 for the three months ended September 30, 2018 and 2017, respectively, and \$1.5 million and \$318,000 for the nine months ended September 30, 2018 and 2017, respectively. The increase during the nine months ended September 30, 2018 was primarily due to \$600,000 of expense related to the tZERO equity awards granted, vested, and fully expensed in January 2018.

Technology expenses

We seek to invest efficiently in technology, including web services, customer support solutions, website search, expansion of new and existing product categories, and in investments in technology to enhance the customer experience, improve our process efficiency and support and expand our logistics infrastructure. We expect to continue to increase our technology expenses to support these initiatives and these increases may be material.

The frequency and variety of cyberattacks on our Website, our corporate systems, and on third parties that we use to support our technology continue to increase. The impact of such attacks, their costs, and the costs we incur to protect ourselves against future attacks have not been material. However, we consider the threat from cyberattacks to be serious and will continue to incur costs related to efforts to protect ourselves against them.

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The following table reflects our technology expenses for the three and nine months ended September 30, 2018 and 2017 (in thousands):

	Three months ended				Nine months ended			
	September 30,		\$ Change	% Change	September 30,		\$ Change	% Change
	2018	2017			2018	2017		
Technology expenses	\$33,880	\$28,746	\$ 5,134	17.9 %	\$97,597	\$85,982	\$ 11,615	13.5 %
Technology expenses as a percent of net revenues	7.7	% 6.8	%		7.1	% 6.7	%	

The \$5.1 million increase in technology costs for the three months ended September 30, 2018, as compared to the same period in 2017, was primarily due to an increase in staff-related costs of \$3.4 million and an increase in technology licenses and maintenance of \$1.6 million.

The \$11.6 million increase in technology costs for the nine months ended September 30, 2018, as compared to the same period in 2017, was primarily due to an increase in staff-related costs of \$9.7 million, and an increase in technology licenses and maintenance costs of \$4.9 million, partially offset by a decrease in depreciation expense of \$2.8 million.

Technology expenses include stock-based compensation expense of \$583,000 and \$166,000 for the three months ended September 30, 2018 and 2017, respectively, and \$1.7 million and \$476,000 for the nine months ended September 30, 2018 and 2017, respectively.

General and administrative expenses

The following table reflects our general and administrative expenses for the three and nine months ended September 30, 2018 and 2017 (in thousands):

	Three months ended				Nine months ended			
	September 30,		\$ Change	% Change	September 30,		\$ Change	% Change
	2018	2017			2018	2017		
General and administrative expenses	\$45,356	\$21,651	\$ 23,705	109.5 %	\$ 116,551	\$66,622	\$ 49,929	74.9 %
General and administrative expenses as a percent of net revenues	10.3	% 5.1	%		8.5	% 5.2	%	

The \$23.7 million increase in general and administrative expenses for the three months ended September 30, 2018, as compared to the same period in 2017, was primarily due to \$10.8 million in special legal costs in Q3 2018, related to our gift card escheatment case in Delaware and capital raising efforts, a \$5.1 million increase in staff-related costs, and a \$3.2 million increase in consulting and outside services.

The \$49.9 million increase in general and administrative expenses for the nine months ended September 30, 2018, as compared to the same period in 2017, was primarily due to an \$18.7 million increase in legal costs largely related to our gift card escheatment case in Delaware and costs related to the tZERO SEC investigation and capital raising efforts, a \$15.3 million increase in staff-related costs, and a \$9.3 million increase in consulting and outside services. In addition, we had a \$2.5 million increase in travel expenses, a \$1.5 million increase in office and facilities expenses and a \$1.2 million increase in impairments on cryptocurrencies.

General and administrative expenses include stock-based compensation expense of approximately \$1.3 million and \$703,000 for the three months ended September 30, 2018 and 2017, respectively, and \$8.3 million and \$2.1 million

for the nine months ended September 30, 2018 and 2017, respectively. The increase was primarily due to \$3.4 million of expense related to the tZERO equity awards granted, vested, and fully expensed in January 2018.

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Depreciation and amortization expense

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

	Three months ended		Nine months ended	
	September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017
Cost of goods sold - direct	\$85	\$72	\$252	\$230
Technology	5,330	5,940	16,103	18,802
General and administrative	1,038	974	3,082	2,863
Total depreciation, including internal-use software and website development	\$6,453	\$6,986	\$19,437	\$21,895

Amortization of intangible assets other than goodwill is classified within the corresponding operating expense categories on our consolidated statements of operations as follows (in thousands):

	Three months ended		Nine months ended	
	September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017
Technology	\$885	\$905	\$2,534	\$2,715
Sales and marketing	119	22	442	62
General and administrative	542	21	620	62
Total amortization of intangible assets other than goodwill	\$1,546	\$948	\$3,596	\$2,839

Other income (expense), net

Other income (expense), net for the three months ended September 30, 2018 was (\$1.8 million) as compared to \$5.9 million in 2017. The decrease is primarily due to \$5.5 million from gains on the sale of cryptocurrencies and precious metals in Q3 2017 that was not repeated in Q3 2018, a \$1.0 million increase in equity method loss, a \$692,000 decrease in Club O and gift card breakage which we began recognizing as a component of revenue in 2018 following the adoption of ASC 606, and a \$584,000 increase in unrealized losses, including impairments, on equity securities that were recognized in Q3 2018.

Other income (expense), net for the nine months ended September 30, 2018 was (\$1.5 million) as compared to \$2.8 million for the same period in 2017. The decrease is primarily due to \$5.5 million from gains on the sale of cryptocurrencies and precious metals in Q3 2017 that was not repeated in Q3 2018, a \$1.9 million decrease in Club O and gift card breakage which we began recognizing as a component of revenue in 2018 following the adoption of ASC 606, and a \$2.4 million increase in losses on equity method investments. These were partially offset by a \$4.5 million decrease in impairment charges on equity securities, and a \$1.3 million increase in unrealized gains, net of impairments, on equity securities.

Income taxes

Our income tax provision for interim periods is determined using an estimate of our annual effective tax rate adjusted for discrete items, if any, for relevant interim periods. We update our estimate of the annual effective tax rate each quarter and make cumulative adjustments if our estimated annual effective tax rate changes.

Our quarterly tax provision and our quarterly estimate of our annual effective tax rate are subject to significant variations due to several factors including variability in predicting our pre-tax and taxable income and the mix of jurisdictions to which those items relate, relative changes in expenses or losses for which tax benefits are not recognized, how we do business, fluctuations in our stock price, and changes in law, regulations, and administrative practices. Our effective tax rate can be volatile based on the amount of pre-tax income. For example, the impact of discrete items on our effective tax rate is greater when pre-tax income is lower.

Our benefit from income taxes for the nine months ended September 30, 2018 and 2017 was \$445,000 and \$7.7 million. The effective tax rate for the nine months ended September 30, 2018 and 2017 was 0.3% and 33.8%, respectively. The decrease in the effective tax rate is primarily attributable to the valuation allowance we are maintaining on our net deferred tax

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assets and a decrease in pre-tax income during the nine months ended September 30, 2018 as compared to the same period in 2017.

We have indefinitely reinvested foreign earnings of \$1.3 million at September 30, 2018. We would need to accrue and pay various taxes on this amount if repatriated. We do not intend to repatriate these earnings.

We are subject to taxation in the United States and several state and foreign jurisdictions. Tax years beginning in 2013 are subject to examination by taxing authorities, although net operating loss and credit carryforwards from all years are subject to examinations and adjustments for at least three years following the year in which the attributes are used. We are under audit by the Ireland Revenue Agency for the calendar year 2016. We expect the audit to continue during 2018.

Each quarter we assess the recoverability of our deferred tax assets under ASC 740. We assess the available positive and negative evidence to estimate whether we will generate sufficient future taxable income to use our existing deferred tax assets. We have limited carryback ability and do not have significant taxable temporary differences to recover our existing deferred tax assets, therefore we must rely on future taxable income, including tax planning strategies, to support their realizability. We have established a valuation allowance for our deferred tax assets not supported by carryback ability or taxable temporary differences, primarily due to uncertainty regarding our future taxable income. We have considered, among other things, the cumulative loss incurred over the three-year period ended September 30, 2018 as a significant piece of objective negative evidence. We intend to continue maintaining a valuation allowance on our net deferred tax assets until there is sufficient evidence to support the reversal of all or some portion of these allowances. The amount of the deferred tax asset considered realizable could be adjusted if objective negative evidence in the form of cumulative losses is no longer present and additional weight may be given to subjective evidence such as long-term projections for growth. We will continue to monitor the need for a valuation allowance against our remaining deferred tax assets on a quarterly basis.

Seasonality

Based upon our historical experience, revenue typically increases during the fourth quarter because of the holiday retail season and gross margin decreases due to increased sales of certain lower margin products, such as electronics. Revenue typically decreases in the following quarter(s), as shown in the table below. The actual quarterly results for each quarter could differ materially depending upon consumer preferences, availability of product and competition, among other risks and uncertainties. Accordingly, there can be no assurances that seasonal variations will not materially affect our results of operations in the future.

The following table reflects our total net revenues for each of the quarters in 2018, 2017 and 2016 (in thousands):

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
2018	\$445,331	\$483,134	\$440,580	\$N/A
2017	432,435	432,024	424,007	456,290
2016	413,677	418,540	441,564	526,182

Liquidity and Capital Resources

Overview

Although we believe that our cash and cash equivalents currently on hand and expected cash flows from future operations will be sufficient to continue operations for at least the next twelve months, we also believe that we may need to raise additional capital and/or obtain significant additional debt financing to be able to fully pursue some or all of our plans discussed below, including plans for our retail business while also funding our Medici initiatives, beyond

the next twelve months.

We continue to seek opportunities for growth in our retail business, through our Medici blockchain and financial technology initiatives, and through other means. We also want to invest in additional distribution facilities to speed shipping and improve our customer service; in additional automation, technology and engineering resources because we believe they can improve our customers' shopping experience and increase our sales; in our Club O rewards program, primarily to increase member benefits and to develop additional personalization programs; and in expansion of our private label initiative because we believe that private label brands can generate significant brand equity and customer loyalty.

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Our Medici initiatives also require substantial funding. Medici Ventures and its majority-owned subsidiary, tZERO, continue to identify, evaluate and pursue various opportunities for strategic acquisitions or purchases of interests to expand the services and expertise they offer their customers. As a result of these initiatives, we will continue to incur additional expenses and expect to purchase interests in, or make acquisitions of, other technologies and businesses.

We anticipate that our initiatives will cause us to incur additional losses in the foreseeable future. These losses, additional expenses, acquisitions or purchases may be material, and, coupled with existing marketing expense trends, and potential strategic changes in our retail business, may lead to increased consolidated losses in some periods, and to reduced liquidity.

Current sources of liquidity

We believe that our cash and cash equivalents currently on hand and expected cash flows from future operations will be sufficient to continue operations for at least the next twelve months. However, our failure to generate sufficient revenues or profits or to obtain additional financing or raise additional capital could have a material adverse effect on our operations and on our ability to achieve our business objectives, and could require us to decrease or cease funding initiatives we consider important in our retail business, our Medici business or both. Any projections of future cash needs and cash flows are subject to substantial uncertainty.

On November 8, 2017, we issued warrants to purchase up to a combined aggregate of 3,722,188 shares of our common stock to two purchasers in privately negotiated transactions, for an aggregate purchase price of \$6.5 million, net of issuance costs. The exercise price for the warrants was \$40.45 per share of common stock. On December 29, 2017, one of the warrant holders exercised its warrant in full and purchased a total of 2,472,188 shares of common stock for \$100.0 million. On January 17, 2018, the other warrant holder exercised its warrant in full and purchased 1,250,000 shares of common stock for \$50.6 million.

In December 2017, tZERO launched an offering (the "security token offering") of the right to acquire tZERO Preferred Equity Tokens (the "tZERO Security Token") through a Simple Agreement for Future Equity ("SAFE"). The security token offering closed on August 6, 2018. As of September 30, 2018, tZERO has received \$104.8 million in cumulative proceeds, net of withdrawals, and incurred \$21.3 million of offering costs. On October 12, 2018, tZERO issued the tZERO Security Tokens in settlement of the SAFEs. The tZERO Security Tokens are subject to a 90 day trading lock-up period.

In August 2018, we entered into a sales agreement with JonesTrading Institutional Services LLC ("JonesTrading"), under which we conducted "at the market" public offerings of our common stock during the quarter ended September 30, 2018 and may conduct additional "at the market" public offerings of our common stock from time to time. Under the sales agreement, JonesTrading, acting as our agent, may offer our common stock in the market on a daily basis or otherwise as we request from time to time. We have no obligation to sell additional shares under the sales agreement, but expect to do so from time to time. We will pay JonesTrading up to a 2.0% sales commission on all sales. The sales agreement contemplates sales of up to \$150 million of our common stock over a period of up to three years. As of September 30, 2018, we had sold 2,883,344 shares of our common stock pursuant to the sales agreement and have received \$94.6 million in proceeds, net of \$2.6 million of offering costs, including commissions paid to JonesTrading. The average price per share of stock sold pursuant to the sales agreement during the quarter ended September 30, 2018, excluding offering costs, was \$33.71.

In August 2018, we also entered into a standby equity underwriting agreement with JonesTrading. We did not sell any shares under the standby equity underwriting agreement, and the agreement terminated in accordance with its terms during the quarter ended September 30, 2018. Under the standby underwriting agreement, we had the right, but no obligation, to sell up to \$50 million of our common stock to JonesTrading, as underwriter, for sale to the public in a firm commitment public offering. We paid a 1% commitment fee to JonesTrading for entering into the underwriting

agreement.

At September 30, 2018, our principal sources of liquidity are cash flows generated from operations, our existing cash and cash equivalents, and proceeds from the warrants, shares sold under the at the market offering, and tZERO's security token offering. At September 30, 2018, we had cash and cash equivalents of \$182.0 million. The intramonthly balance of our cash and cash equivalents on hand fluctuates significantly, generally reaching the highest balance at the end of month and the lowest balances after the first and sixteenth of the month when we make our regular partner and supplier payments.

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Contemplated Financing Transactions

As previously announced, in August 2018, Overstock signed a Token Purchase Agreement with GSR Capital Ltd., a Cayman Islands exempted company ("GSR"), and a term sheet contemplating a sale of Overstock common stock to GSR. Concurrently, tZERO signed a term sheet contemplating a sale of tZERO common stock to GSR.

The Token Purchase Agreement sets forth the terms on which GSR agreed to purchase, for \$30 million, on May 6, 2019 or such other date as may be agreed by the parties, security tokens at a price of \$6.67 per security token. These security tokens were issued by tZERO to Overstock in satisfaction of \$30 million of tZERO's indebtedness to Overstock. We may be required to obtain additional tokens in order to fulfill our obligations under the agreement. The agreement states that the obligations of GSR to complete the transaction described will be subject to conditions, some of which are unidentified.

Overstock, tZERO and GSR are currently negotiating definitive agreements for GSR's purchase of Overstock common stock and tZERO common stock. Although we continue to negotiate the terms, GSR has proposed purchasing fewer shares and at a lower price per share than those described in the Overstock term sheet. We believe that if a definitive agreement is reached regarding the purchase of tZERO shares, the terms, including the post money valuation of tZERO, may be less favorable than those described in the tZERO term sheet. Both the Overstock and tZERO term sheets constitute binding agreements for the parties to negotiate in good faith the terms of the transaction documents; however, the obligation to negotiate in good faith terminates on December 15, 2018, if any of the closing conditions, one of which is the negotiation, execution and delivery of mutually acceptable transaction documents, have not been satisfied. While we expect to complete these transactions, there can be no assurance that Overstock, tZERO or GSR will enter into definitive agreements regarding either of the proposed transactions.

Cash flow information is as follows (in thousands):

	Nine months ended September 30,		Twelve months ended September 30,	
	2018	2017	2018	2017
Cash provided by (used in):				
Operating activities	\$(120,300)	\$(62,448)	\$(93,073)	\$(7,445)
Investing activities	(89,508)	(14,368)	(93,100)	(28,649)
Financing activities	189,575	(13,884)	276,782	4,021

Cash flows from operating activities

Our operating cash flows result primarily from cash received from our customers, offset by cash payments we make for employee compensation (less amounts capitalized related to internal-use software that are reflected as cash used in investing activities), and changes in working capital and other related activities. Working capital at any specific point in time is subject to many variables, including seasonality, inventory management, expansion efforts, the timing of cash receipts and payments, and vendor payment terms. Cash received from customers generally corresponds to our net revenues as our customers primarily use credit cards to buy from us causing our receivables from these sales transactions to settle quickly. We have payment terms with our partners that generally extend beyond the amount of time necessary to collect proceeds from our customers. As a result, following our typically seasonally strong fourth quarter sales, at December 31 of each year, our cash, cash equivalents, accounts payable and accrued liability balances normally reach their highest level (other than as a result of cash flows provided by or used in investing and financing activities).

The \$120.3 million of net cash used in operating activities during the nine months ended September 30, 2018 was primarily due to consolidated net loss of \$169.6 million, partially offset by cash provided by operating assets and liabilities of \$12.3 million, and certain non-cash items including depreciation and amortization expense of \$23.0 million, stock-based compensation of \$11.7 million, and impairment losses, net of realized gains, recognized on cryptocurrency holdings of \$1.2 million.

The \$62.4 million of net cash used in operating activities during the nine months ended September 30, 2017 was primarily due to consolidated net loss of \$15.1 million, cash used in operating assets and liabilities of \$68.5 million, and certain non-cash items including deferred income taxes of \$8.7 million and other non-cash items of \$1.5 million, partially offset by certain non-cash items including depreciation and amortization expense of \$24.7 million, stock-based compensation of \$3.0

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million, impairments recognized on cost method investments of \$4.5 million, and net of realized gains recognized on cryptocurrency holdings of \$845,000.

Notwithstanding our current negative cash flows from operating activities, we believe that our cash and cash equivalents currently on hand and expected cash flows from future operations will be sufficient to continue operations for at least the next twelve months. However, we also believe that we may need to raise additional capital and/or obtain significant additional debt financing to be able to fully pursue some or all of our plans, including plans for our retail business while also funding our Medici initiatives, beyond the next twelve months.

Cash flows from investing activities

For the nine months ended September 30, 2018, investing activities resulted in net cash outflows of \$89.5 million primarily due to \$43.7 million investment in equity securities, \$12.9 million acquisition of businesses, net of cash acquired, \$20.7 million of expenditures for fixed assets, and \$9.6 million purchase of intangible assets.

For the nine months ended September 30, 2017, investing activities resulted in net cash outflows of \$14.4 million primarily due to \$20.9 million of expenditures for fixed assets and \$4.2 million investment in equity securities, partially offset by \$11.6 million in proceeds from the sale of precious metals.

Cash flows from financing activities

For the nine months ended September 30, 2018, financing activities resulted in net cash inflows of \$189.6 million primarily due to \$94.6 million of net proceeds from the sale of common stock under the at the market offering, \$82.6 million of net proceeds from the security token offering, \$50.6 million of proceeds from the sale and exercise of stock warrants, and \$6.7 million of proceeds from capital contributions received by a consolidated subsidiary, partially offset by a \$40.0 million repayment of long-term debt and \$4.6 million of taxes withheld upon vesting of restricted stock.

For the nine months ended September 30, 2017, financing activities resulted in net cash outflows of \$13.9 million primarily due to the purchase of treasury stock for \$10.0 million, \$2.4 million of payments on finance obligations, and \$1.1 million of taxes withheld upon vesting of restricted stock.

Free cash flow

"Free Cash Flow" (a non-GAAP measure) for the nine months ended September 30, 2018 and 2017, was \$(141.0) million and \$(83.3) million, respectively, and \$(116.5) million and \$(41.2) million for the twelve months ended September 30, 2018 and 2017, respectively. See Non-GAAP Financial Measures below for a reconciliation of Free Cash Flow to net cash provided by (used in) operating activities.

Contractual Obligations and Commitments

The following table summarizes our contractual obligations as of September 30, 2018 and the effect such obligations and commitments are expected to have on our liquidity and cash flow in future periods (in thousands):

Contractual Obligations	Payments Due by Period						Total
	Remainder of 2018	2019	2020	2021	2022	Thereafter	
Operating leases	1,757	7,446	5,648	6,038	6,156	17,515	44,560
Purchase obligations	2,927	—	—	—	—	—	2,927

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Technology services	508	2,031	1,693	—	—	—	4,232
High Bench Senior Credit Agreement	—	—	3,069	—	—	—	3,069
Total contractual cash obligations	\$5,192	\$9,477	\$10,410	\$6,038	\$6,156	\$17,515	\$54,788

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Operating leases

From time to time we enter into operating leases for facilities and equipment for use in our operations. In August 2018, we entered into a new agreement to lease a warehouse located in Kansas City, Kansas. The term of the lease is for a period of 61 months, beginning August 2018 and ending August 2023.

Purchase obligations

The amount of purchase obligations shown above is based on assumptions regarding the legal enforceability against us of inventory purchase orders we had outstanding at September 30, 2018. 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.

Technology services

From time to time we enter into long-term contractual agreements for technology services and capital leases for equipment included in such service agreements.

High Bench Senior Credit Agreement

We are party to a financing agreement acquired in connection with our acquisition of Mac Warehouse, LLC (see Borrowings below). The amounts presented reflect our related principal payments.

Tax contingencies

We are involved in various tax matters, the outcomes of which are uncertain. As of September 30, 2018, accrued tax contingencies were \$1.4 million. Changes in state, federal, and foreign tax laws may increase our tax contingencies. The timing of the resolution of income tax contingencies is highly uncertain, and the amounts ultimately paid, if any, upon resolution of issues raised by the taxing authorities may differ from the amounts accrued. It is reasonably possible that within the next 12 months we will receive additional assessments by various tax authorities. These assessments may or may not result in changes to our contingencies related to positions on prior years' tax filings.

Borrowings

High Bench Senior Credit Agreement

On June 25, 2018, we became party to a senior credit agreement, as amended, with High Bench-Mac Warehouse-Senior Debt, LLC ("High Bench Loan"), in connection with our acquisition of Mac Warehouse, LLC. Under the amended agreement, the loan carries an annual interest rate of 11.0% and a default rate of 18.0%. The High Bench Loan is subject to monthly interest only payments with the remaining principal amount and any then unpaid interest due and payable on April 18, 2020. The High Bench Loan is subject to mandatory prepayment under certain circumstances, and is prepayable at our election at any time without penalty or premium. There are no financial covenants associated the High Bench Loan. At September 30, 2018, our outstanding balance on the High Bench Loan was \$3.1 million.

Letters of credit

At September 30, 2018 and December 31, 2017, letters of credit totaling \$280,000 and \$355,000, were issued on our behalf collateralized by compensating cash balances held at a bank, which are included in Restricted cash in the

accompanying consolidated balance sheets.

Commercial purchasing card agreement

We have a commercial purchasing card (the "Purchasing Card") agreement. We use the Purchasing Card for business purpose purchasing and must pay it in full each month. At September 30, 2018, \$107,000 was outstanding and \$893,000 was available under the Purchasing Card. At December 31, 2017, \$822,000 was outstanding and \$4.2 million was available under the Purchasing Card.

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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.

Transactions with Related Parties

Our related party Transactions are discussed in Item 1 of Part I, "Financial Statements (Unaudited)"—Note 12. Related Party Transactions, contained in the "Notes to Unaudited Consolidated Financial Statements" of this Quarterly Report on Form 10-Q.

Critical Accounting Policies and Estimates

The preparation of our financial statements requires that we make estimates and judgments. We base these on historical experience and on other assumptions that we believe to be reasonable. Our critical accounting policies are discussed in Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" section of our Annual Report on Form 10-K for the year ended December 31, 2017, and our accounting policies and use of estimates are further discussed in Item 1 of Part I, "Financial Statements (Unaudited)"—Note 2. Accounting Policies, contained in the "Notes to Unaudited Consolidated Financial Statements" of this Quarterly Report on Form 10-Q and elsewhere in this Management's Discussion and Analysis of Financial Condition and Results of Operations.

During Q1 2018, we implemented ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606) on a modified retrospective basis and recognized \$5.0 million of additional breakage income related to the unredeemed portion of our gift cards and loyalty program rewards through a cumulative effect adjustment in retained earnings as of January 1, 2018. In addition, we now recognize estimated breakage on our gift cards and loyalty program rewards in Partner and other revenue in our consolidated statement of operations rather as a component of Other expense, net. The adoption of these new accounting standards is discussed further in Item 1 of Part I, "Financial Statements (Unaudited)"—Note 2. Accounting Policies, contained in the "Notes to Unaudited Consolidated Financial Statements" of this Quarterly Report on Form 10-Q. There have been no other material changes to the critical accounting policies previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2017.

For information about recently issued accounting standards not yet adopted, see Recently issued accounting standards not yet adopted, included in Item 1 of Part I, "Financial Statements (Unaudited)"—Note 2. Accounting Policies, contained in the "Notes to Unaudited Consolidated Financial Statements" of this Quarterly Report on Form 10-Q.

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.

Retail and Medici pre-tax income or loss

Retail and Medici pre-tax income or loss (non-GAAP financial measures - which we reconcile to Consolidated pre-tax income or loss) consists of income or loss before taxes of our Retail (which consists of Direct and Partner) and Medici (which is included in Other) businesses, excluding intercompany transactions eliminated in consolidation. We believe these measures provide management and users of the financial statements useful information because they provide financial results for our separate businesses which are distinct in nature. The material limitation associated with these measures is that they are an incomplete measure of our consolidated operations. These measures should be used in addition to and in conjunction with results presented in accordance with GAAP and should not be relied upon to the

exclusion of GAAP financial measures. You should review our financial statements and publicly-filed reports in their entirety and not rely on any single financial measure. For additional information regarding our segment reporting, and a reconciliation of Retail and Medici pre-tax income or loss, please see Item 1 of Part I, "Financial Statements (Unaudited)"—Note 10. Business Segments, contained in the "Notes to Unaudited Consolidated Financial Statements" of this Quarterly Report on Form 10-Q.

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Free cash flow

Free cash flow (a non-GAAP financial measure) reflects an additional way of viewing our cash flows and liquidity that, when viewed with our GAAP results, provides a more complete understanding of factors and trends affecting our cash flows and liquidity. Free cash flow, which we reconcile below to "Net cash used in operating activities," the nearest GAAP financial measure, is net cash provided by operating activities reduced by "Expenditures for fixed assets, including internal-use software and website development." We believe that net cash provided by operating activities is an important measure, since it includes both the cash impact of the continuing operations of the business and changes in the balance sheet that impact cash. We believe free cash flow is a useful measure to evaluate our business since purchases of fixed assets are a necessary component of ongoing operations and free cash flow measures the amount of cash we have available for mandatory debt service and financing obligations, changes in our capital structure, and future investments after purchases of fixed assets. Free cash flow measures have limitations as they omit certain components of the overall consolidated statement of cash flows and do not represent the residual cash flow available for discretionary expenditures. Free cash flow should not be considered a substitute for net income (loss) or cash flow data prepared in accordance with GAAP and may not be comparable to similarly titled measures used by other companies. Therefore, we believe it is important to view free cash flow as a complement to our entire consolidated statements of cash flows as reconciled below (in thousands):

	Nine months ended		Twelve months ended	
	September 30,		September 30,	
	2018	2017	2018	2017
Net cash used in operating activities	\$(120,300)	\$(62,448)	\$(93,073)	\$(7,445)
Expenditures for fixed assets, including internal-use software and website development	(20,677)	(20,873)	(23,390)	(33,772)
Free cash flow	\$(140,977)	\$(83,321)	\$(116,463)	\$(41,217)

Government Regulation

Our e-commerce business is subject to general business regulations and laws, as well as regulations and laws specifically governing the Internet, e-commerce and other services. Existing and future laws and regulations may result in increasing expense and may impede our growth. These regulations and laws cover taxation, privacy, data protection, pricing, content, copyrights, distribution, mobile communications, electronic device certification, electronic waste, energy consumption, environmental regulation, electronic contracts and other communications, competition, consumer protection, information reporting requirements, the design and operation of websites, and the characteristics and quality of products and services. On June 21, 2018, the U.S. Supreme Court issued an opinion in our South Dakota sales tax case and overruled the 1992 Quill Corp v. North Dakota case, and states may now require remote sellers to withhold sales tax under certain circumstances. In June 2018, we began withholding sales tax in all 45 states that have sales tax. If any state were to assert that we have any liability for sales tax for prior periods, it could have an adverse effect on us. New legislation or regulations, 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 or tax collection obligations could have an adverse effect on us. Further, there is a possibility that we may be subject to significant fines or other payments for any past failures to comply with these requirements. In addition, it is not clear how existing laws governing issues such as property ownership, libel, and personal privacy apply to the Internet, e-commerce and digital content. Laws and regulations may diminish the demand for our products and services and increase our cost of doing business. Certain of our services are subject to federal and state consumer protection laws, including laws protecting the privacy of consumer information and regulations prohibiting unfair and deceptive trade practices. In particular, under federal and state financial privacy laws and regulations, we must provide notice to consumers of our policies on sharing non-public information with third parties, advance notice of any changes to our policies and, with limited exceptions, we must give consumers the right to prevent sharing of their non-public personal

information with unaffiliated third parties. Further, the growth and demand for online commerce could result in more stringent consumer protection laws that could impose additional compliance burdens on us. These consumer protection laws could result in substantial compliance costs.

In addition, our broker dealers are subject to additional extensive regulatory requirements under federal and state laws and regulations and self-regulatory organization ("SRO") rules. Broker dealers are subject to regulation, examination and disciplinary action by the SEC, FINRA and state securities regulators, as well as other governmental authorities and SROs with which they are registered or licensed or of which they are members. See our Annual Report on Form 10-K for the year ended December 31, 2017, Part I - Item 1A - "Risk Factors - PRO Securities and SpeedRoute, two subsidiaries of tZERO that currently generate substantially all of tZERO's revenues, are registered broker-dealers and are subject to extensive regulation."

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Further, some of the business opportunities that the companies in which Medici Ventures holds an interest are pursuing may be subject to approvals by the SEC and/or other governmental authorities, and we have no ability to ensure that they can obtain any such approvals on a timely basis or at all.

Our efforts to expand our sales outside of the U.S. expose us to additional U.S. and foreign laws and regulations, including but not limited to, laws and regulations relating to taxation, business licensing or certification requirements, advertising practices, online services, the use of cryptocurrency, the importation of specified or proscribed items, importation quotas, consumer protection, intellectual property rights, consumer and data protection, privacy, encryption, restrictions on pricing or discounts, and the U.S. Foreign Corrupt Practices Act and other applicable U.S. and foreign laws prohibiting corrupt payments to government officials and other third parties. Our ownership interests in Bitt Inc. and Bitsy, Inc. also may expose us to additional laws and regulations relating to money transmitters and money services businesses. See our Annual Report on Form 10-K for the year ended December 31, 2017, Part I - Item 1A - "Risk Factors - Our ownership interest in Bitt Inc. may expose us to additional risks."

Other Factors that May Affect Future Results

We believe that our cash and cash equivalents currently on hand and expected cash flows from future operations will be sufficient to continue operations for at least the next twelve months. Any projections of future cash needs and cash flows are subject to substantial uncertainty, including those set forth under Item 1A of Part II, "Risk Factors" of this report and in our Annual Report on Form 10-K for the year ended December 31, 2017, Part I - Item 1A - "Risk Factors."

We periodically evaluate opportunities to repurchase our equity securities, obtain credit facilities, or issue additional debt or equity securities. In addition, we may, from time to time, consider purchases of equity interests in, or acquisition of, complementary businesses, products, services, or technologies, whether related to our retail business, our Medici initiatives or otherwise, any of which might affect our liquidity requirements or cause us to issue additional debt or equity securities. There can be no assurance that financing arrangements will be available in amounts or on terms acceptable to us, or at all.

Any investment in our securities involves a high degree of risk. Investors should consider carefully the risks and uncertainties described in this Form 10-Q, including the risks described in Item 1A of Part II, "Risk Factors" of this report and in our Annual Report on Form 10-K for the year ended December 31, 2017, Part I - Item 1A - "Risk Factors," and all other information in this Form 10-Q and in our other filings with the SEC including those we file after we file this Form 10-Q, before deciding whether to purchase or hold our securities. Additional risks and uncertainties not currently known to us or that we currently deem immaterial may also become important factors that may harm our business. The occurrence of any of the risks described under "Risk Factors" in this report or in our Annual Report on Form 10-K for the year ended December 31, 2017 could harm our business. The trading price of our securities could decline due to any of these risks and uncertainties, and investors may lose part or all of their investment.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our financial instruments consist of cash and cash equivalents, trade accounts and contracts receivable, accounts payable and long-term obligations. We consider highly-liquid instruments with a remaining maturity of 90 days or less at the date of purchase to be cash equivalents. We currently do not hold any derivative financial instruments or foreign exchange contracts.

Our exposure to market risk for changes in interest rates relates primarily to our short-term investments and short-term obligations; thus, fluctuations in interest rates would not have a material impact on the fair value of these securities.

However, the fair values of our investments may be subject to fluctuations due to volatility of the stock market in general, investment-specific circumstances, and changes in general economic conditions.

At September 30, 2018, we had \$182.0 million in cash and cash equivalents. Hypothetically, an increase or decrease in interest rates of one hundred basis points would have an estimated impact of \$1.8 million on our earnings or loss, or the cash flows of these instruments.

At September 30, 2018, letters of credit totaling \$280,000 were outstanding under our credit facilities. Hypothetically, an increase or decrease in interest rates of one hundred basis points would have an estimated impact of \$2,800 on our earnings or loss if the letters of credit were fully drawn.

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At September 30, 2018, we had cryptocurrency-denominated assets totaling \$3.1 million. Hypothetically, a decrease in the market value of one hundred basis points would have an estimated impact of \$31,000 on our earnings or loss, and the recorded value of these instruments. Reported earnings resulting from increases in the market value of cryptocurrency would be limited to realized gains.

ITEM 4. CONTROLS AND PROCEDURES

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

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

Evaluation of Disclosure Controls and Procedures

We carried out an evaluation required by the Exchange Act under the supervision and with the participation of our principal executive officer and principal financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rule 13a-15(e) of the Exchange Act, as of the end of the period covered by this report. Based on this evaluation, our principal executive officer and principal financial officer concluded that our disclosure controls and procedures were effective to provide reasonable assurance that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and to provide reasonable assurance that such information is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

Beginning January 1, 2018, we implemented ASU 2014-09, Revenue from Contracts with Customers (Topic 606). In connection with its adoption, we implemented changes to our processes and internal control activities over financial reporting to ensure compliance with the new accounting and disclosure rules.

Except for the preceding changes, there has not occurred any change in our internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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

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PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The information set forth under Item 1 of Part I, "Financial Statements"—Note 6—"Commitments and Contingencies," subheading "Legal Proceedings and Contingencies," contained in the "Notes to Unaudited Consolidated Financial Statements" of this Quarterly Report on Form 10-Q is incorporated by reference in answer to this Item.

ITEM 1A. RISK FACTORS

Any investment in our securities involves a high degree of risk. Please consider the following risk factors carefully. If any one or more of the following risks were to occur, it could have a material adverse effect on our business, prospects, financial condition and results of operations, and the market price of our securities could decrease significantly. Statements below to the effect that an event could or would harm our business (or have an adverse effect on our business or similar statements) mean that the event could or would have a material adverse effect on our business, prospects, financial condition and results of operations, which in turn could or would have a material adverse effect on the market price of our securities. Many of the risks we face involve more than one type of risk. Consequently, you should read all of the risk factors below carefully, as well as the risk factors described in our Form 10-K for the year ended December 31, 2017, the risk factors described in our Form 10-Q for the quarters ended March 31, 2018 and June 30, 2018, and in any reports we file with the SEC after we file this Form 10-Q, before deciding whether to purchase or hold our securities. The occurrence of any of these risks could harm our business, the trading price of our securities could decline, and investors could lose part or all of their investment.

Other than the risk factors set forth below, there are no material changes from the risk factors previously disclosed in Part I - Item 1A - "Risk Factors," of our Annual Report on Form 10-K for the year ended December 31, 2017, and disclosed in Part II - Other Information - Item 1A - "Risk Factors," of our Quarterly Report on Form 10-Q for the quarters ended March 31, 2018 and June 30, 2018.

Our ownership interest in Bitsy Inc. may expose us to additional risks.

In the third quarter of 2018, Medici Ventures increased its ownership interest in Bitsy, Inc., a U.S.-based company founded and partially owned by Medici Ventures' chief operating officer and general counsel, to approximately 33%. In September 2018, Bitsy announced that it had begun a limited beta launch of a digital wallet service intended to create a bridge between traditional fiat currencies and cryptocurrencies. Various aspects of the business that Bitsy is engaging in are heavily regulated. Virtually every state in the U.S. regulates money transmitters and money services businesses. In some states the licensing requirements and regulations expressly cover companies engaged in digital currency activities; in other states it is not clear whether or how the existing laws and regulations apply to digital currency activities. These licenses and registrations subject companies to various anti-money laundering, know-your-customer, record-keeping, reporting and capital and bonding requirements, limitations on the investment of customer funds, and inspection by state and federal regulatory agencies. Bitsy has registered with FinCEN and has confirmed to us that it intends to obtain all licenses it is required to obtain. Under U.S. federal law, it is a crime for a person, entity or business that is required to be registered with FinCEN or licensed in any state to fail to do so. Further, under U.S. federal law, anyone who owns all or part of an unlicensed money transmitting business may be subject to civil and criminal penalties.

Our discussions with potential bidders for our e-commerce business could result in the compromise of our intellectual property.

Although we enter into confidentiality agreements with potential bidders for our e-commerce business prior to disclosing confidential information to them, it may be possible for potential bidders to misappropriate intellectual property and other confidential information from us.

We may have additional exposure to claims under Delaware's Abandoned Property Law.

In September 2018 we lost a jury trial in Delaware brought on Delaware's behalf alleging that we had violated Delaware's unclaimed property laws by failing to report and turn over to Delaware certain unused gift card balances. The time period covered by the lawsuit was 2004 through 2007. The jury returned a verdict, which we expect to result in a judgment

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against us of approximately \$7.3 million plus attorneys' fees and costs. We may have additional exposure for the time period 2008 through 2014.

We may be required to write off amounts relating to our interests in startup businesses.

At September 30, 2018, Overstock and its subsidiaries held minority interests totaling approximately \$57.4 million in several companies that are in the startup or development stages and may acquire additional minority interests in other entities in the future. These interests are inherently risky because the markets for the technologies or products these companies are developing are typically in the early stages and may never materialize. Additionally, since these interests are in companies that are in the early startup or development stages, even if their technology or products are viable, they may not be able to obtain the capital or resources necessary to successfully bring their technology or products to market. Furthermore, we have no assurance that the technology or products of companies we have funded would be successful, even if they were brought to market. We have written off amounts related to these interests in the past and may in the future write off additional amounts related to these interests. Any such write-offs could be material, and could have a material adverse effect on our financial results and business.

tZERO's recent decision not to use StockCross as the introducing broker for the trading of its security tokens may result in additional expense and may delay the trading of tZERO's security tokens.

Management of tZERO will need to devote significant time and resources to identify a suitable broker dealer and to enter into an appropriate licensing and/or other contractual arrangements with one or more options, which may divert management's time and attention from other matters. If tZERO is unable to enter into the necessary contractual arrangements with an appropriate broker dealer promptly or at a reasonable cost, it could have a material adverse effect on tZERO's plans to begin the trading of its security tokens in January 2019. Although tZERO believes it has identified suitable candidates to perform these roles and intends to identify additional candidates, tZERO does not have a licensing or other contractual arrangement with any other broker dealer to perform the roles of introducing broker.

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

Unregistered issuance of equity securities

On June 28, 2018, we issued 100,000 shares of our common stock in a private placement to the stockholders of SiteHelix, Inc., including Saum Noursalehi, who owned approximately 62% of the SiteHelix common stock, as part of the acquisition price for our acquisition of all of the common stock of SiteHelix. Mr. Noursalehi is a member of our Board of Directors and served as President, Retail, of Overstock until May 8, 2018, when he became Chief Executive Officer of tZERO. The issuance was exempt from the registration requirements of the Securities Act of 1933, as amended, as a private placement under Rule 506(b) of Regulation D.

On September 20, 2018, we issued 47,378 shares of our common stock in a private placement to Bitsy, Inc. ("Bitsy"), as part of the acquisition price for our equity interest in Bitsy. Subsequent to the purchase, we hold, through our wholly-owned subsidiary, Medici Ventures, a 33% interest in Bitsy. Bitsy is a U.S.-based startup company founded and 25% owned by Medici Ventures' chief operating officer and general counsel. The issuance was exempt from the registration requirements of the Securities Act of 1933, as amended, as a private placement under section 4(a)(1) thereof.

Issuer purchases of equity securities

None.

Limitations upon the payment of 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 on our common stock in the foreseeable future. Any future determination to pay dividends on our common stock 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 of directors deems relevant.

In December 2016, we issued a total of 695,898 shares of our preferred stock (the "Preferred Stock"), of which 681,259 shares remained outstanding at September 30, 2018. The Preferred Stock ranks senior to our common stock with respect to dividends. Holders of the Preferred Stock are entitled to an annual cash dividend of \$0.16 per share, in preference to any dividend payment to the holders of the common stock, out of funds legally available for payment of dividends and subject

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to declaration by our Board of Directors. Holders of the Preferred Stock are also entitled to participate in any cash dividends we pay to the holders of the common stock and are also entitled to participate in non-cash dividends we pay to holders of the common stock, subject to potentially different treatment if we effect a stock dividend, stock split or combination of the common stock. There are no arrearages in cumulative preferred dividends. We declared and paid a cash dividend of \$0.16 per share on our preferred stock during 2017.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

(a) Exhibits

- 10.1 Capital on DemandTM Sales Agreement with JonesTrading Institutional Services LLC, as agent, dated August 9, 2018 (incorporated by reference to exhibit 1.1 to our Form S-3 filed on August 9, 2018, File No. 333-226729)
- 10.2 Standby Equity Underwriting Agreement with JonesTrading Institutional Services LLC, as underwriter, dated August 9, 2018 (incorporated by reference to exhibit 1.2 to our Form S-3 filed on August 9, 2018, File No. 333-226729)
- 10.3 Stockholders Agreement dated September 21, 2018 by and among Medici Land Governance, Inc., Medici Ventures, Inc. and Patrick M. Byrne (incorporated by reference to exhibit 10.1 to our Form 8-K filed on September 26, 2018, File No. 000-49799)
- *31.1 Exhibit 31.1 Certification of Chief Executive Officer
- *31.2 Exhibit 31.2 Certification of Chief Financial Officer
- *32.1 Exhibit 32.1 Section 1350 Certification of Chief Executive Officer
- *32.2 Exhibit 32.2 Section 1350 Certification of Chief Financial Officer
- 101 Attached as Exhibit 101 to this report are the following documents formatted in XBRL (Extensible Business Reporting Language): (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Operations, (iii) Consolidated Statements of Comprehensive Income (Loss), (iv) Consolidated Statements of Cash Flows, (v) Consolidated Statements of Stockholders' Equity, and (vi) Notes to Consolidated Financial Statements.

* Filed herewith.

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SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Date: November 9, 2018 OVERSTOCK.COM, INC.

/s/ GREGORY J. IVERSON
Gregory J. Iverson
Chief Financial Officer
(Principal Financial Officer and Principal Accounting Officer)