VERSAR INC
Form 11-K
June 29, 2015

United States

Securities and Exchange Commission

Washington, D.C. 20549

FORM 11-K

x ANNUAL REPORT PURSUANT TO SECTION 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the year ended December 31, 2014

or

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

For the transition period from ________ to _________

Commission File Number: 001-09309

A. Full title of the plan and the address of the plan, if different from that of the issuer named below:

Versar Employee 401(k) Plan

C/O Versar, Inc.

6850 Versar Center

Springfield, VA

22151

B. Name of issuer of the securities held pursuant to the plan and the address of its principal executive office:

Versar, Inc.

6850 Versar Center

Springfield, VA

22151

Financial Statements and Report of Independent Registered Public Accounting Firm

Versar Employee 401(k) Plan

December 31, 2014 and 2013

Versar Employee 401(k) Plan

Contents

Report of Independent Registered Public Accounting Firm

Plan Administrator

Versar Employee 401(k) Plan

Springfield, Virginia

We have audited the accompanying Statements of Net Assets Available for Benefits of the **Versar Employee 401(k) Plan** (the "Plan") as of December 31, 2014 and 2013, and the related Statement of Changes in Net Assets Available for Benefits for the year ended December 31, 2014. These financial statements are the responsibility of the Plan's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Plan is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Plan's control over financial reporting. Accordingly we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the net assets available for benefits of the Plan as of December 31, 2014 and 2013, and the changes in net assets available for benefits for the year ended December 31, 2014, in conformity with accounting principles generally accepted in the United States of America.

The supplemental information in the accompanying Schedule H, Line 4i – Schedule of Assets (Held at End of Year) as of December 31, 2014, and Schedule H, Line 4a – Schedule of Delinquent Participant Contributions for the year then ended have been subjected to audit procedures performed in conjunction with the audit of **Versar Employees 401(k) Plan's** financial statements. The supplemental information is presented for the purpose of additional analysis and is not a required part of the financial statements but include supplemental information required by the Department of Labor's Rules and Regulations for Reporting and Disclosure under the Employee Retirement Income Security Act of 1974. The supplemental information is the responsibility of the Plan's management. Our audit procedures included determining whether the supplemental information reconciles to the financial statements or the underlying accounting and other records, as applicable, and performing procedures to test the completeness and accuracy of the information presented in the supplemental information. In forming our opinion on the supplemental information in the accompanying schedules, we evaluated whether the supplemental information, including its form and content, is presented in conformity with the with the Department of Labor's Rules and Regulations for Reporting and Disclosure under the Employee Retirement Income Security Act of 1974. In our opinion, the supplemental information in the accompanying schedules is fairly stated in all material respects in relation to the financial statements as a whole.

/s/ Aronson LLC

Versar Employee 401(k) Plan

Statements of Net Assets Available for Benefits

December 31,	2014	2013
Assets		
Cash – noninterest bearing	$4,892	$79,699
Investments, at fair value	41,398,334	34,779,506
Receivables		
Notes receivable from participants	401,991	375,865
Employer contributions	202,297	228,613
Employee contributions	852	—
Total receivables	605,140	604,478
Total assets	42,008,366	35,463,683
Liabilities		
Due to Broker	4,857	79,636
Total liabilities	4,857	79,636
Net Assets Available for Benefits, at Fair Value	42,003,509	35,384,047
Adjustment from fair value to contract value for interest in collective trust fund relating to fully benefit-responsive investment contracts	(61,568)	(37,329)
Net Assets Available for Benefits	$41,941,941	$35,346,718

4

Versar Employee 401(k) Plan

Statement of Changes in Net Assets Available for Benefits

Year ended December 31,	2014
Additions to Net Assets	
Contributions:	
Participant contributions	$2,093,257
Employer contributions	850,607
Rollover contributions	45,993
Total contributions	2,989,857
Investment income	
Interest and dividend income	185,324
Net appreciation in fair value of investments	1,696,064
Total investment income	1,881,388
Interest income on notes receivable from participants	16,848
Other income	134,728
Total Additions	5,022,821
Deductions from Net Assets	
Benefits paid to participants	6,939,134
Administrative expense	143,584
Total Deductions	7,082,718
Net Decrease Before Transfer	(2,059,897)
Transfer in from Geo-Marine, Inc. Savings and Retirement Plan	8,655,120
Net Increase	6,595,223
Net Assets Available for Benefits, beginning of year	35,346,718
Net Assets Available for Benefits, end of year	$41,941,941

Versar Employee 401(k) Plan

Notes to Financial Statements

December 31, 2014 and 2013

NOTE A¾PLAN DESCRIPTION

The following description of the Versar Employee 401(k) Plan (the Plan) provides only general information. The Plan's investments are held in a nondiscretionary trust by Wells Fargo Bank, N.A. (Wells Fargo or Trustee). Wells Fargo also serves as recordkeeper for the Plan. Participants should refer to the Plan document for a more complete description of the Plan's provisions.

General

The Plan is a defined contribution plan covering substantially all eligible employees of Versar, Inc. (Company or Plan Sponsor) who are age 18 or older except for leased employees, non resident aliens, employees covered by a collective bargaining agreement and Davis Bacon Act employees.

Effective January 1, 2014, the Plan was amended to exclude part-time employees from participation in the Plan until they are credited with at least 1,000 hours of service in a plan year.

On June 30, 2014, the Company acquired J.M. Waller Association, Inc. (JMWA). Effective July 1, 2014, the Plan was amended to temporarily exclude employees acquired from JMWA through December 31, 2014.

The Plan is subject to the provisions of the Employee Retirement Income Security Act of 1974, as amended (ERISA).

Contributions

Each year, participants may contribute a minimum of 1 percent up to 50 percent of pre-tax annual compensation, as defined in the Plan. Roth contributions are also permitted. Participants who have attained age 50 before the end of the Plan year are eligible to make catch-up contributions. Participants may also contribute amounts representing distributions from other qualified plans (rollover). The Plan includes an auto-enrollment provision whereby all newly eligible employees are automatically enrolled in the Plan unless they affirmatively elect not to participate in the Plan. Automatically enrolled participants have their deferral rate set at 3 percent of eligible compensation and their contributions invested in the Wells Fargo AdviceTrack program (see Investment Options below) until changed by the participant. The Plan's automatic enrollment provisions include an auto escalation feature that provides for a 1 percent automatic annual increase up to a maximum of a 6 percent deferral rate.

The Company makes a safe harbor matching contribution equal to 100 percent of the first 3 percent of eligible compensation a participant contributes and 50 percent of the next 2 percent of eligible compensation a participant contributes to the Plan. Employer safe harbor matching contributions are made on a quarterly basis in cash. The Company may make an additional discretionary matching contribution to all eligible participants employed as of the last day of the Plan year. No such discretionary contributions were made for the year ended December 31, 2014.

Contributions are subject to certain Internal Revenue Service (IRS) limitations.

Participant Accounts

The Plan maintains an account for each participant. Each participant's account is credited with the participant's contributions, allocations of the Company's contributions and Plan earnings and charged with an allocation of Plan losses and administrative expenses. Allocations are based on participant earnings, account balances, or specific participant transactions, as defined. The benefit to which a participant is entitled is the benefit that can be provided from the participant's vested account.

Versar Employee 401(k) Plan

Notes to Financial Statements—Continued

December 31, 2014 and 2013

NOTE A¾PLAN DESCRIPTION—Continued

Investment Options

Participants direct the investment of their contributions and can select from two available options, core investment funds (Core Funds) or the Wells Fargo AdviceTrack program (AdviceTrack). Under the Core Funds option, participants direct their contributions to mutual funds and collective trust funds (CTF) selected by the Company and offered by the Plan. Alternatively, participants can elect to invest 100 percent of their current balance and all future contributions to AdviceTrack. The investment funds available under AdviceTrack include, in general, a different group of mutual funds and CTFs than are available under the Core Funds option and are selected and maintained by Wells Fargo. Wells Fargo monitors the investment performance of the funds and makes changes as deemed appropriate; however, any changes must be consented to by the Plan Sponsor. Wells Fargo has retained an independent financial expert who provides the participant with an investment allocation strategy under AdviceTrack, using personal and financial information provided by the participant, which is then implemented by Wells Fargo. The participant's account is monitored and re-balanced based on investment performance, market conditions and changes in the participant's personal situation. Participants may terminate participation in AdviceTrack at any time and revert to the Core Funds option.

Company common stock is held in the Plan for certain participants who received in-kind employer matching contributions in prior years. Restrictions of participants' transfers, contributions (purchases) or distributions (sales) are described in Note D.

Voting Rights

Each participant is entitled to exercise voting rights attributable to the shares of Versar stock allocated to their account. Participants are sent a proxy by the Trustee for the shares they own and they may vote those shares. The Trustee is not permitted to vote any share for which instructions have not been given by a participant.

Vesting

Participants are immediately vested in their contributions and Company contributions plus actual earnings thereon. However, certain participants are subject to prior vesting schedules.

Notes Receivable from Participants

Plan participants may borrow from their employee contribution and rollover fund accounts a minimum of $500 up to a maximum equal to the lesser of $50,000 or 50 percent of their vested account balance. All loans bear interest at the current prime lending rate of Wells Fargo plus one percent and are secured by the balance in the participant's account. Generally, the loans must be repaid within five years unless the loan was used for the purchase of a primary residence, in which case the term may be up to 10 years. Participants may only have one loan outstanding at any time. Principal and interest is paid ratably through bi-weekly payroll deductions.

Forfeitures

During 2014, forfeitures totaling $108,983, due to certain participants' termination prior to full vesting and monies merged into the Plan (see Note K) were used to offset the safe harbor matching contribution for 2014. At December 31, 2014 and 2013, forfeited non-vested accounts totaled $14,441 and $18,852, respectively.

Versar Employee 401(k) Plan

Notes to Financial Statements—Continued

December 31, 2014 and 2013

NOTE A¾PLAN DESCRIPTION—Continued

Payment of Benefits

On termination of service including death, disability, early or normal retirement, a participant may elect to receive a lump-sum distribution equal to the value of the participant's vested account balance. Distributions of a participant's elective deferral and rollover contribution accounts are made in cash. The matching contribution is distributed in the form in which the employer match is invested (cash and/or Company common stock) at the time of the distribution.

Hardship distributions to employees are permitted from the participant's elective deferral account if certain conditions are met. After withdrawal, participants may not make savings or other contributions to the Plan for at least six months after receipt of the hardship distribution.

The Plan also provides for required minimum distributions (RMD) per IRS regulations by April 1 of the calendar year following the later of the calendar year in which the participant reaches age 70 ½ or the calendar year the participant retires. Installment payments are permitted for lifetime RMDs only. In addition, the Plan does permit in-service withdrawals from the participant's elective deferral and safe harbor matching contribution accounts after reaching age 59 ½.

NOTE B¾SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting

The financial statements of the Plan have been prepared on the accrual basis of accounting.

Investment Valuation and Income Recognition

The Plan's investments are stated at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. See Note E for discussion of fair value measurements.

Investment contracts held by the Plan, either directly or as an underlying asset of a CTF, must be reported at fair value. However, contract value is the relevant measurement attribute for the portion of the net assets available for benefits of a defined contribution plan attributable to fully benefit-responsive investment contracts, because contract value is the amount participants would receive if they were to initiate permitted transactions under the terms of the Plan. The Plan invests in stable return funds (SRF) which are CTFs that hold an investment in another CTF, which invests in fully benefit-responsive investment contracts. The statements of net assets available for benefits present the fair value of the SRFs as well as the adjustment of the funds from fair value to contract value. The statement of changes in net assets available for benefits is prepared on a contract value basis.

Purchases and sales of securities are recorded on a trade-date basis. Interest income is recorded on the accrual basis. Dividends are recorded on the ex-dividend date. Net appreciation (depreciation) in fair value of investments includes the Plan's gains and losses on investments bought and sold as well as held during the year.

Versar Employee 401(k) Plan

Notes to Financial Statements—Continued

December 31, 2014 and 2013

NOTE B¾SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued

Payment of Benefits

Benefits are recorded when paid.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and changes therein, and disclosure of contingent assets and liabilities. Actual results could differ from those estimates.

Administrative Expenses

Certain expenses of maintaining the Plan are paid directly by the Company and are excluded from these financial statements. Administrative expenses paid by the Plan include primarily investment related expenses and also include fees related to the administration of notes receivable from participants charged directly to the participant's account. Participants who are invested in AdviceTrack are charged an asset-based fee for program services, such as fund selection and monitoring, of 0.50 percent plus 0.13 percent to reimburse Wells Fargo for actual expenses.

Notes Receivable from Participants

Notes receivable from participants are measured at their unpaid principal balance plus any accrued but unpaid interest. Interest income is recorded on the accrual basis. Related fees are recorded as administrative expenses and are expensed when they are incurred. No allowance for credit losses has been recorded as of December 31, 2014 or 2013. If a participant, who has experienced a distributable event, ceases to make loan repayments and the Plan administrator deems the participant loan to be in default, the participant loan balance is reduced and a benefit payment is recorded.

Versar Employee 401(k) Plan

Notes to Financial Statements—Continued

December 31, 2014 and 2013

NOTE C¾INVESTMENTS

The following presents investments representing five percent or more of Plan net assets as of December 31, 2014 and 2013.

December 31,	2014	2013
T Rowe Price Blue Chip Growth Fund	$4,779,487	$3,626,212
WF Stable Return Fund - N *	4,054,115	4,363,771
WF Enhanced Stock Market Fund	3,942,836	3,618,478
WF Advantage Discovery Fund	2,516,403	2,396,675
WF MFS Value Fund – AT	2,271,491	N/A
WF MFS Value Fund – N	2,157,831	N/A
TCW Total Return Bond Fund	N/A	1,987,033
Thornburg International Value Fund	N/A	1,847,136

* Represents fair value; contract value as of December 31, 2014 and 2013 is $3,998,141 and $4,328,448, respectively.

N/A – The value of the investment does not represent 5% or more of the Plan's net assets at this date.

During 2014, the Plan's investments (including gains and losses on investments bought and sold, as well as held during the year) appreciated (depreciated) in value by $1,696,064 as follows:

Mutual funds	$811,376
Employer common stock	(426,097)
Collective trust funds	1,310,785
	$1,696,064

NOTE D¾NONPARTICIPANT-DIRECTED INVESTMENTS

As stated in Note A, certain participants who have received in-kind employer contributions in prior years hold Company common stock as an investment. In addition, all participants may direct funds from Company matching contributions to or from Company common stock without restriction. All Company common stock held in a source other than any Company matching contributions is restricted and may not be directed by the participant.

Information about the net assets related to all Company common stock is as follows:

	December 31,	
	2014	2013
Net Assets:		
Versar, Inc. common stock	$749,511	$1,307,790

10

Versar Employee 401(k) Plan

Notes to Financial Statements—Continued

December 31, 2014 and 2013

NOTE D¾NONPARTICIPANT-DIRECTED INVESTMENTS¾Continued

Information about the significant components of the changes in net assets related to all Company common stock is as follows:

	Year Ended December 31, 2014
Changes in Net Assets:	
Net depreciation	$ (426,097)
Benefits paid to participants	(111,675)
Transfers to participant-directed investments	(20,449)
Administrative expenses	(58)
	$ (558,279)

NOTE E¾FAIR VALUE MEASUREMENTS

Accounting Standards Codification (ASC) 820, *Fair Value Measurements and Disclosures*, provides the framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority to unobservable inputs (level 3 measurements). The three levels of the fair value hierarchy under ASC 820 are described as follows:

Level 1–Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Plan has the ability to access;

Level 2–Inputs to the valuation methodology include:

- Quoted prices for similar assets or liabilities inactive markets;
- Quoted prices for identical or similar assets or liabilities in inactive markets;
- Inputs other than quoted prices that are observable for the asset or liability;
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

Level 3–Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

Versar Employee 401(k) Plan

Notes to Financial Statements—Continued

December 31, 2014 and 2013

NOTE E¾FAIR VALUE MEASUREMENTS¾Continued

The following is a description of the valuation methodologies and inputs used for assets and liabilities measured at fair value, as well as the general classification pursuant to the valuation hierarchy. There have been no changes in the methodologies used at December 31, 2014 and 2013.

Common Stock: Valued at the closing price reported on the active market on which the individual securities are traded and are classified within Level 1 of the fair value hierarchy.

Mutual Funds – Core Funds: Valued at the daily closing price as reported by the fund. Such mutual funds held by the Plan are open-end mutual funds that are registered with the Securities and Exchange Commission. These funds are required to publish their daily net asset value ("NAV") and to transact at that price. The mutual funds held by the Plan are deemed to be actively traded and are classified within Level 1 of the fair value hierarchy.

Mutual Funds – AdviceTrack: Valued at the NAV of units of the AdviceTrack fund as provided by Wells Fargo. The mutual funds offered under AdviceTrack are held in Wells Fargo institutional accounts, in which transactions are effected on behalf of all investors in each AdviceTrack fund on an aggregated basis. Each AdviceTrack mutual fund is a unitized fund and consists primarily of an underlying investment in a specific actively traded open-end mutual fund. A daily NAV is calculated by Wells Fargo based on the fair value of the underlying mutual fund investment held by the fund plus other assets (i.e., cash, accrued income, and due from broker for securities sold) less its liabilities (i.e., accrued expenses and due to broker for securities purchases), and is classified within level 2 of the fair value hierarchy. Daily NAVs are available to Plan administrators and client investors on Wells Fargo's website and provide sufficient corroborative evidence to ascertain the relationship between each fund's NAV and the values of the individual underlying holdings.

Collective Trust Funds: Valued at fair value measured as the NAV of units of a bank collective trust. The NAV as provided by Wells Fargo is used as a practical expedient to estimate fair value. The NAV is based on the fair value of the underlying investments held by the fund less its liabilities. This practical expedient is not used when it is determined to be probable that the fund will sell the investment for an amount different than the reported NAV. Participant transactions (purchases and sales) may occur daily. Were the Plan to initiate a full redemption of a CTF, the investment advisor reserves the right to temporarily delay withdrawal from the trust in order to ensure that securities liquidations will be carried out in an orderly business manner. All CTFs except the SRFs are classified within Level 2 of the fair value hierarchy. SRFs are classified within Level 3 of the fair value hierarchy. With respect to the SRFs held by the Plan, in order to assess the reasonableness of the fair value methodology used, the Versar, Inc. Retirement Plan Committee, with the assistance of an investment advisor, does not independently develop quantifiable unobservable inputs, but rather evaluates a variety of factors including review of the funds' financial statements, economic conditions, industry and market developments, and overall credit ratings. See also Note F for further information on the SRFs. There are no unfunded commitments from participants in the Plan who invest in the CTFs.

Versar Employee 401(k) Plan

Notes to Financial Statements—Continued

December 31, 2014 and 2013

NOTE E¾FAIR VALUE MEASUREMENTS¾Continued

The following table sets forth by level, within the fair value hierarchy, the Plan's investments at fair value as of December 31:

	2014			
	Level 1	Level 2	Level 3	Total
Mutual Funds				
Fixed Income Funds –				
High yield bond	$—	$588,538	$—	$588,538
Inflation-protected bond	—	514,843	—	514,843
Intermediate bond	1,839,302	326,430	—	2,165,732
U.S. Equity Funds –				
Large cap	6,666,790	—	—	6,666,790
Mid cap	3,525,952	—	—	3,525,952
Small cap	2,044,084	—	—	2,044,084
International Equity –				
Large Cap	3,024,685	1,438,646	—	4,463,331
Equity – Real Estate	—	458,901	—	458,901
Sub-total mutual funds	17,100,813	3,327,358	—	20,428,171
Collective Trust Funds:				
Fixed Income –				
Intermediate Bond	—	2,035,764	—	2,035,764
International Bond	—	646,480	—	646,480
U.S. Equity –				
Large cap	—	11,049,841	—	11,049,841

Mid cap	—	86,764	—	86,764
Small cap	—	1,012,121	—	1,012,121
International Equity – Large Cap	—	930,408	—	930,408
Stable Value	—	—	4,459,274	4,459,274
Sub-total collective trust funds	—	15,761,378	4,459,274	20,220,652
Company Common Stock	749,511	—	—	749,511
Total assets at fair value	$17,850,324	$19,088,736	$4,459,274	$41,398,334

Versar Employee 401(k) Plan

Notes to Financial Statements—Continued

December 31, 2014 and 2013

NOTE E¾FAIR VALUE MEASUREMENTS¾Continued

The following table sets forth by level, within the fair value hierarchy, the Plan's investments at fair value as of December 31:

	2013 Level 1	Level 2	Level 3	Total
Mutual Funds				
Fixed Income Funds –				
High yield bond	$—	$347,270	$—	$347,270
Inflation-protected bond	—	358,567	—	358,567
Intermediate bond	1,987,033	1,179,871	—	3,166,904
U.S. Equity Funds –				
Large cap	6,663,501	—	—	6,663,501
Mid cap	3,012,170	—	—	3,012,170
Small cap	1,668,634	—	—	1,668,634
International Equity –				
Large Cap	3,169,392	988,080	—	4,157,472
Equity – Real Estate	—	280,747	—	280,747
Sub-total mutual funds	16,500,730	3,154,535	—	19,655,265
Collective Trust Funds:				
Fixed Income –				
Intermediate Bond	—	477,540	—	477,540
International Bond	—	446,510	—	446,510
U.S. Equity –				
Large cap	—	6,979,823	—	6,979,823

Small cap	—	628,864	—	628,864
International Equity – Large Cap	—	667,319	—	667,319
Stable Value	—	—	4,616,395	4,616,395
Sub-total collective trust funds	—	9,200,056	4,616,395	13,816,451
Company Common Stock	1,307,790	—	—	1,307,790
Total assets at fair value	$17,808,520	$12,354,591	$4,616,395	$34,779,506

14

Versar Employee 401(k) Plan

Notes to Financial Statements—Continued

December 31, 2014 and 2013

NOTE E¾FAIR VALUE MEASUREMENTS¾Continued

The table below sets forth a summary of changes in the fair value of the Plan's level 3 assets for the year ended December 31, 2014:

	WF Stable Return Fund N	WF Stable Return Fund AT	Total Stable Value Funds
Balance, January 1, 2014	$ 4,363,771	$ 252,624	$ 4,616,395
Change in adjustment from fair value to contract value	20,651	3,588	24,239
Realized gains	19,798	398	20,196
Unrealized gains related to instruments still held at the reporting date	44,770	2,594	47,364
Purchases Contributions, rollovers and transfers in	3,298,212	262,136	3,560,348
Sales: Withdrawals, distributions and transfers out	(3,693,087)	(116,181)	(3,809,268)
Balance, December 31, 2014	$ 4,054,115	$ 405,159	$ 4,459,274

Change in adjustment from fair value to contract value represents unrealized appreciation on fully benefit-responsive investment contracts held by the underlying CTF held by the Plan's SRFs and is not included in the statement of changes in net assets available for benefits as the contracts are recorded at contract value for purposes of the net assets available for benefits.

Transfers between Levels

The availability of observable market data is monitored to assess the appropriate classification of financial instruments within the fair value hierarchy. Changes in economic conditions or model-based valuation techniques may require the transfer of financial instruments from one fair value level to another. In such instances, the transfer is reported at the beginning of the reporting period.

The Plan evaluated the significance of transfers between levels based upon the nature of the financial instrument and size of the transfer relative to total net assets available for benefits. For the year ended December 31, 2014, there were no transfers in or out of levels 1, 2 or 3.

Versar Employee 401(k) Plan

Notes to Financial Statements—Continued

December 31, 2014 and 2013

NOTE E¾FAIR VALUE MEASUREMENTS¾Continued

Fair Value of Investments in Entities that Use NAV

In accordance with the fair value measurements and disclosures guidance, the following table presents the category, fair value, redemption frequency, and redemption notice period for Plan investments, the fair values of which are estimated using the NAV per share as of December 31, 2014 and 2013:

	Fair Value 2014	2013	Redemption Frequency	Redemption Notice Period
Collective Trust Funds:				
Fixed Income –				
Intermediate Bond[a]	$2,035,764	$477,540	Daily	Daily
International Bond[b]	646,480	446,510	Daily	Daily
U.S. Equities:				
Large cap[c]	11,049,841	6,979,823	Daily	Daily
Mid cap[d]	86,764	—	Daily	Daily
Small cap[e]	1,012,121	628,864	Daily	Daily
International Equity – Large Cap[f]	930,408	667,319	Daily	Daily
Stable Value[g]	4,459,274	4,616,395	See Note F	See Note F
Total	$20,220,652	$13,816,451		

[a] *Fixed Income – Intermediate Bond:* The investment objective of the fund in this category is to seek total return consisting of current income and capital appreciation. The fund invests primarily in investment-grade debt

securities, including U.S. government obligations, corporate bonds and mortgage and asset-backed securities.

(b) *Fixed Income – International Bond:* The investment objective of the fund in this category is to seek total return consisting of income and capital appreciation. Under normal circumstances, the fund invests primarily in foreign debt securities, including obligations of governments, corporate entities, or supranational agencies, denominated in various currencies.

(c) *U.S. Equities – Large Cap:* The investment objectives of the funds in this category are long-term capital growth or appreciation. These funds invest primarily in equity securities of large U.S. companies and includes funds which own a diversified portfolio of established companies which produce superior and sustainable earnings growth as well as a fund which focuses on stocks of companies that it believes are undervalued compared to their perceived worth (value companies).

(d) *U.S. Equities – Mid Cap:* The investment objective of the fund in this category is to approximate the total return, before deduction of fees and expenses, of the Standard & Poor’s 400 MidCap Index. The fund invests in equity securities of companies that compose the Index and pursues its objective through investments in one ore more underlying collective investment funds maintained by BlackRock Institutional Trust Company, N.A.

Versar Employee 401(k) Plan

Notes to Financial Statements—Continued

December 31, 2014 and 2013

NOTE E¾FAIR VALUE MEASUREMENTS¾Continued

(e) *U.S. Equities – Small Cap:* The investment objective of the funds in this category is primarily to provide certain qualified employee benefit plans with a vehicle for collective investment and reinvestment by primarily investing in three managed portfolios within the Russell 2000® Index.

(f) *International Equity – Large Cap:* The investment objectives of the funds in this category are long-term growth. The fund invests primarily in common stocks of companies located in developed countries outside the U.S.

(g) *Stable Value:* The investment objective of the SRFs is to provide investors with a moderate level of stable income without principal volatility. In order to meet this objective, the funds invest in another CTF that primarily invests in investment contracts, including traditional guaranteed investment contracts and security-backed contracts issued by insurance companies and other financial institutions.

NOTE F—STABLE RETURN FUNDS

The Plan has assets invested in two SRFs, Wells Fargo Stable Return Fund N and Wells Fargo Stable Return Fund AT, both of which have invested all of their assets in the Wells Fargo Stable Return Fund G (WF Fund G), a CTF sponsored by Wells Fargo. The daily value of the SRFs' investment is based on the underlying daily value reported by the WF Fund G. The NAV of the WF Fund G is calculated daily and net investment income is not distributed but reinvested and the NAV adjusted accordingly. The SRFs allow for daily liquidity with no additional days' notice required for redemption.

All withdrawals and transfers from the SRFs are payable at contract value. Contract value represents contributions made to the SRFs plus earnings less participant withdrawals and administrative expenses. Participant-directed transfers from the SRFs are permitted to non-competing funds, subject to a 90-day equity wash provision. However, Wells Fargo reserves the right to require a 12-month notification for any Plan Sponsor initiated withdrawal request.

Certain events may limit the ability of the Plan to transact at contract value with the SRFs' issuer. Such events include the following:

- Material amendment to WF Fund G's structure or administration;
- Changes to participating plans' competing investment options including elimination of the equity wash provisions;
- Complete or partial termination of WF Fund G, including merger with another fund;
- Failure of WF Fund G to qualify for exemption from federal income taxes or any required prohibited transaction exemption under ERISA;
- Redemption of all or a portion of the interests in the SRFs held by a participating plan at the direction of the participating plan sponsor including group layoffs, early retirement incentive programs, closing or sale of a subsidiary, bankruptcy or insolvency of the plan sponsor, merger of the plan with another plan, or the plan sponsor's establishment of another tax qualified defined contribution plan;
- Any change in law, regulation, ruling, administrative or judicial position, or accounting requirement, applicable to WF Fund G or participating plans;
- Delivery of any communication to plan participants designed to influence a participant not to invest in the SRFs.

Versar Employee 401(k) Plan

Notes to Financial Statements—Continued

December 31, 2014 and 2013

NOTE F—STABLE RETURN FUNDS¾Continued

The contract value of the investment in the SRFs as of December 31, 2014 and 2013 was $4,397,706 and $4,579,066, respectively. The crediting interest rates for the SRFs are derived from the underlying investments in the WF Fund G which consist of both (1) guaranteed investment contracts at fixed rates and (2) security-backed contracts with variable interest rates reset on a quarterly basis and a minimum interest rate of zero percent. For the years ended December, 31, 2014 and 2013, the average yield based on actual earnings was 1.40% and 1.36%, respectively. For the years ended December 31, 2014 and 2013, the interest rate credited to participants was 1.64% and 1.52%, respectively.

Plan management believes the occurrence of events and circumstances that would cause the SRFs to transact at less than contract value is not probable.

NOTE G¾RELATED PARTY AND PARTY-IN-INTEREST TRANSACTIONS

Certain investment options available to participants are shares of CTFs and AdviceTrack mutual funds managed by Wells Fargo, the Trustee and record-keeper. Therefore, transactions with these investments qualify as party-in-interest transactions and are exempt from the prohibited transaction rules of ERISA.

The Plan holds an investment in the Company common stock, and transactions with this investment qualify as party-in-interest and related party transactions. The Plan held 237,187 and 270,764 shares of the Company common stock as of December 31, 2014 and 2013, respectively.

During 2011, the Company failed to remit to the Plan certain employee contributions and loan payments totaling $463,936 within the period prescribed by Department of Labor regulations. These delinquent remittances are considered nonexempt party-in-interest transactions. The Company made corrective contributions to the Plan in 2014 to compensate affected participants for lost earnings on the delinquent remittances.

Fees paid by the Plan for investment management and other services to Wells Fargo amounted to $107,170 for the year ended December 31, 2014. Fees paid to Wells Fargo through revenue sharing amounted to $8,302 for the year ended December 31, 2014.

NOTE H¾PLAN TERMINATION

Although it has not expressed any intent to do so, the Company has the right under the Plan to discontinue its contributions at any time and to terminate the Plan subject to the provisions of ERISA. In the event of plan termination, participants would become 100 percent vested in their employer contributions.

18

Versar Employee 401(k) Plan

Notes to Financial Statements—Continued

December 31, 2014 and 2013

NOTE I¾TAX STATUS

The underlying non-standardized prototype plan has received an opinion letter from the IRS dated March 31, 2008 stating that the form of the Plan is qualified under Section 401 of the Internal Revenue Code (IRC), and therefore, the related trust is tax exempt. The Plan Sponsor has determined that it is eligible to and has chosen to rely on the current IRS prototype plan opinion letter. Once qualified, the Plan is required to operate in conformity with the IRC to maintain its qualification. The Plan has been amended since receiving the opinion letter. The Plan Sponsor has indicated that it will take the necessary steps, if any, to maintain the tax-qualified status of the Plan.

Accounting principles generally accepted in the United States of America require Plan management to evaluate tax positions taken by the Plan and recognize a tax liability (or asset) if the organization has taken an uncertain position that more likely than not would not be sustained upon examination by the IRS. The Plan Sponsor has analyzed the tax positions taken by the Plan, and has concluded that as of December 31, 2014 and 2013, there are no uncertain positions taken or expected to be taken that would require recognition of a liability (or asset) or disclosure in the financial statements. The Plan is subject to routine audits by taxing jurisdictions; however, there are currently no audits for any tax periods in progress. The Plan administrator believes it is no longer subject to income tax examinations for years prior to 2011.

NOTE J¾RISKS AND UNCERTAINTIES

The Plan invests in various investment securities. Investment securities are exposed to various risks, such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect participants' account balances and the amounts reported in the statements of net assets available for benefits.

NOTE K¾PLAN MERGER

On February 4, 2014, the plan assets of the Geo-Marine, Inc. Savings and Retirement Plan were liquidated and the assets of the plan in the amount of $8,655,120 were transferred to the Versar Employee 401(k) Plan. The Plan Sponsor had purchased all of the issued and outstanding shares of Geo-Marine, Inc. on September 3, 2013.

Versar Employee 401(k) Plan

Notes to Financial Statements—Continued

December 31, 2014 and 2013

NOTE L¾RECONCILIATION OF FINANCIAL STATEMENTS TO FORM 5500

The following is a reconciliation of net assets available for benefits per the financial statements to Form 5500:

December 31,	2014	2013
Net assets available for benefits per the financial statements	$41,941,941	$35,346,718
Less: Employer contributions receivable	(202,297)	(228,613)
Less: Employee contributions receivable	(852)	—
Less: Deemed distributions recorded on 5500 but not in financial statements	(221)	—
Rounding	1	2
Net assets available for benefits per Form 5500	$41,738,572	$35,118,107

The following is a reconciliation of changes in net assets per the financial statements to the Form 5500 for the year ended December 31, 2014:

Net increase in net assets per financial statements	$6,595,223
Change in employer contributions receivable	26,316
Change in employee contributions receivable	(852)
Less: Deemed distributions recorded on 5500 but not in financial statements	(221)
Rounding	(1)
Net increase in net assets and transfers in per Form 5500	$6,620,465

NOTE M—OPERATIONAL COMPLIANCE

In 2014, it was determined the Plan was not operating in compliance with certain provisions set forth in the plan document with respect to post severance compensation. The Company has discussed the operational errors with counsel and has determined the exposure to be for plan years 2011 through 2014 and, as the corrective contributions are not material, they will be corrected via the self-correction process. The corrective contributions plus lost earnings will be remitted to the Plan during the year ended December 31, 2015 to make the affected participants whole. The Company practices were corrected once the inconsistency was identified.

Versar Employee 401(k) Plan

Notes to Financial Statements—Continued

December 31, 2014 and 2013

NOTE N—SUBSEQUENT EVENTS

On June 30, 2014, the Company purchased all of the issued and outstanding stock of J.M. Waller Associates, Inc. (JMWA). JMWA sponsored a defined contribution plan, J.M. Waller Associates, Inc. 401(k) Profit Sharing Plan (JMWA 401(k) Plan) for its employees. The JMWA 401(k) Plan's net assets of $8,859,094 were merged into the Versar Employee 401(k) Plan effective January 1, 2015.

Effective January 1, 2015, the Plan was amended to allow employees of the Company, who were acquired from JMWA, to participate in the Plan. Further, the Plan was amended to grant 100% vesting in all JMWA company contributions for all employees who were acquired from JMWA and were employed with Versar, Inc. on January 1, 2015. However, non-active participants remain subject to a separate vesting schedule.

Effective January 1, 2015, the Plan was amended to include a prevailing wage contribution in which employees working under a prevailing wage contract are eligible to participate in the Plan. Employees are eligible, for purposes of the prevailing wage contribution, on the date their employment is covered under the contract. Further, the computation for the safe harbor matching contribution was amended to be made on a plan year basis.

Effective January 2, 2015, the Company directed Wells Fargo to freeze Company common stock as an investment option in the Plan and direct future funds from Company matching contributions to the Wells Fargo Stable Return Fund N.

Supplemental Information

22

Versar Employee 401(k) Plan

Schedule H, Line 4i - Schedule of Assets (Held at End of Year)

EIN: 54-0852979

Plan 002

December 31, 2014

	(b) Identity of Issue, Borrower, Lessor or	(c) Description of Investment, Including Maturity Date, Rate of Interest, Collateral,	(d)	(e)	
(a)	1,290		1,297		
Dilutive effect of equity incentive plans	18		18	19	20
Weighted average common shares - diluted	1,309		1,315	1,309	1,317
Net income per share:					
Basic	$0.54		$0.22	$0.98	$0.59
Diluted	$0.53		$0.22	$0.96	$0.58
Common stock equivalents excluded from income per diluted share because their effect would have been anti-dilutive	8		18	12	16

7

Note 3 - Business Combinations and Divestitures

During the six months ended June 30, 2012, we completed two acquisitions, which are included in our Marketplaces segment, for aggregate purchase consideration of approximately $138 million, consisting primarily of cash. The allocation of the purchase consideration resulted in net liabilities of $20 million, purchased intangible assets of $67 million and goodwill of $92 million. The allocations of the purchase price for these acquisitions has been prepared on a preliminary basis and changes to those allocations may occur as additional information becomes available. The consolidated financial statements include the operating results of the acquired businesses since the respective dates of the acquisitions. Pro forma results of operations have not been presented because the effect of the acquisitions were not material to our financial results.

In May 2012, we completed the sale of Rent.com for proceeds of approximately $145 million resulting in a gain of approximately $118 million. The results of operations from Rent.com are not material to any period presented.

GSI

We acquired GSI on June 17, 2011. In conjunction with the acquisition of GSI, we immediately divested 100 percent of GSI's licensed sports merchandise business and 70 percent of GSI's ShopRunner and RueLaLa businesses (together, the "divested businesses").

Pro forma financial information

The unaudited pro forma financial information in the table below summarizes the combined results of our operations and those of GSI for the period shown as though the acquisition of GSI and the sale of the divested businesses had occurred as of the beginning of fiscal year 2011. The unaudited pro forma financial information for the period presented includes the business combination accounting effects of the acquisition, including amortization charges from acquired intangible assets. The unaudited pro forma financial information presented below is for informational purposes only, is subject to a number of estimates, assumptions and other uncertainties, and is not indicative of the results of operations that would have been achieved if the acquisition and divestiture had taken place at January 1, 2011. The unaudited pro forma financial information is as follows (in millions, except per share amounts):

	Six Months Ended June 30, 2011
Total revenues	$5,692
Net income	700
Basic earnings per share	0.54
Diluted earnings per share	$0.53

8

eBay Inc.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Note 4 — Goodwill and Intangible Assets

Goodwill

The following table presents goodwill balances and adjustments to those balances for each of our reportable segments during the six months ended June 30, 2012:

	December 31, 2011 (In millions)	Goodwill Acquired	Disposals	Adjustments	June 30, 2012
Reportable segments:					
Marketplaces	$4,537	$92	$(21)	$(1)	$4,607
Payments	2,515	—	—	—	2,515
GSI	1,293	—	—	(18)	1,275
Corporate and other	47	—	—	1	48
	$8,392	$92	$(21)	$(18)	$8,445

Investments accounted for under the equity method of accounting are classified on our balance sheet as long-term investments. Such investment balances include any related goodwill. As of June 30, 2012 and December 31, 2011, the goodwill related to our equity method investments was approximately $27 million.

The adjustments to goodwill during the six months ended June 30, 2012 were due primarily to changes in tax items and foreign currency translation.

Intangible Assets

The components of identifiable intangible assets are as follows:

	June 30, 2012				December 31, 2011			
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Weighted Average Useful Life (Years)	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Weighted Average Useful Life (Years)
	(In millions, except years)							
Intangible assets:								
Customer lists and user base	$1,627	$ (865)	$762	5	$1,633	$(787)	$846	5
Trademarks and trade names	715	(499)	216	5	730	(469)	261	5
Developed technologies	518	(281)	237	4	498	(249)	249	3
All other	199	(142)	57	4	182	(132)	50	4
	$3,059	$ (1,787)	$1,272		$3,043	$(1,637)	$1,406	

Amortization expense for intangible assets was $109 million and $66 million for the three months ended June 30, 2012 and 2011, respectively. Amortization expense for intangible assets was $218 million and $123 million for the six months ended June 30, 2012 and 2011, respectively.

9

eBay Inc.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Note 5 — Segments

We have three reporting segments: Marketplaces, Payments and GSI. We allocate resources to and assess the performance of each reporting segment using information about its revenue and operating income (loss). We do not evaluate operating segments using discrete asset information. We do not allocate gains and losses from equity investments, interest and other income, or taxes to operating segments.

The corporate and other category includes income, expenses and charges such as:

- results of operations of our X.commerce initiative, which supports our businesses;
- corporate management costs, such as human resources, finance and legal, not allocated to our segments;
- amortization of intangible assets;
- restructuring charges; and
- stock based compensation expense.

The following tables summarize the financial performance of our reporting segments and reconciliation to our consolidated operating results for the periods reflected below (data for the three and six months ended June 30, 2011 include GSI since the date of acquisition):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
	(In millions)			
Net Revenue				
Marketplaces				
Net transaction revenues	$1,491	$1,350	$2,916	$2,634
Marketing services and other revenues	323	313	626	583
	1,814	1,663	3,542	3,217
Payments				
Net transaction revenues	1,234	991	2,450	1,934
Marketing services and other revenues	123	82	216	131
	1,357	1,073	2,666	2,065
GSI				
Net transaction revenues	164	16	346	16
Marketing services and other revenues	57	8	112	8
	221	24	458	24
Corporate and other				
Marketing services and other revenues	10	—	16	—
Elimination of inter-segment net revenue [1]	(4)	—	(7)	—
Total consolidated net revenue	$3,398	$2,760	$6,675	$5,306
Operating income (loss)				
Marketplaces	$719	$645	$1,388	$1,274
Payments	350	235	695	456
GSI	10	—	33	—
Corporate and other	(384)	(361)	(768)	(646)
Total operating income (loss)	$695	$519	$1,348	$1,084

(1) Represents revenue generated between our reportable segments.

eBay Inc.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Note 6 — Fair Value Measurement of Assets and Liabilities

The following tables summarize our financial assets and liabilities measured at fair value on a recurring basis as of June 30, 2012 and December 31, 2011:

Description	Balance as of June 30, 2012	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)
	(In millions)		
Assets:			
Cash and cash equivalents	$4,038	$4,038	$—
Short-term investments:			
Restricted cash	17	17	—
Corporate debt securities	990	—	990
Government and agency securities	1	—	1
Time deposits	92	—	92
Equity instruments	616	616	—
Total short-term investments	1,716	633	1,083
Derivatives	96	—	96
Long-term investments:			
Corporate debt securities	2,393	—	2,393
Government and agency securities	57	—	57
Total long-term investments	2,450	—	2,450
Total financial assets	$8,300	$4,671	$3,629
Liabilities:			
Derivatives	$39	$—	$39

11

eBay Inc.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Description	Balance as of December 31, 2011	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)
	(In millions)		
Assets:			
Cash and cash equivalents	$4,691	$4,691	$—
Short-term investments:			
Restricted cash	20	20	—
Corporate debt securities	448	—	448
Government and agency securities	42	—	42
Time deposits	82	—	82
Equity instruments	646	646	—
Total short-term investments	1,238	666	572
Derivatives	112	—	112
Long-term investments:			
Restricted cash	1	1	—
Corporate debt securities	2,186	—	2,186
Government and agency securities	71	—	71
Total long-term investments	2,258	1	2,257
Total financial assets	$8,299	$5,358	$2,941
Liabilities:			
Derivatives	$60	$—	$60

Our financial assets and liabilities are valued using market prices on both active markets (level 1) and less active markets (level 2). Level 1 instrument valuations are obtained from real-time quotes for transactions in active exchange markets involving identical assets. Level 2 instrument valuations are obtained from readily available pricing sources for comparable instruments or identical instruments in less active markets. The majority of our derivative instruments are valued using pricing models that take into account the contract terms as well as multiple inputs where applicable, such as equity prices, interest rate yield curves, option volatility and currency rates. Our derivative instruments are primarily short-term in nature, generally one month to one year in duration. Cash and cash equivalents are short-term, highly liquid investments with original or remaining maturities of three months or less when purchased and are comprised primarily of bank deposits and money market funds.

In addition to the long-term investments noted above, we had approximately $175 million and $190 million of cost and equity method investments included in long-term investments on our condensed consolidated balance sheet at June 30, 2012 and our consolidated balance sheet at December 31, 2011, respectively. At June 30, 2012 and December 31, 2011, we also held $5 million of time deposits classified as held to maturity, which are recorded at amortized cost.

Other financial instruments, including accounts receivable, loans and interest receivable, funds receivable, customer accounts, commercial paper, accounts payable, funds payable and amounts due to customers, are carried at cost, which generally approximates their fair value because of the short-term nature of these instruments.

12

eBay Inc.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Note 7 — Derivative Instruments

Fair Value of Derivative Contracts

The fair value of our outstanding derivative instruments as of June 30, 2012 and December 31, 2011 was as follows:

	Derivative Assets Reported in Other Current Assets		Derivative Liabilities Reported in Other Current Liabilities	
	June 30, 2012	December 31, 2011	June 30, 2012	December 31, 2011
	(In millions)			
Foreign exchange contracts designated as cash flow hedges	$60	$75	$5	$3
Foreign exchange contracts not designated as hedging instruments	24	29	34	57
Other contracts not designated as hedging instruments	12	8	—	—
Total fair value of derivative instruments	$96	$112	$39	$60

Effect of Derivative Contracts on Accumulated Other Comprehensive Income

The following table summarizes the activity of derivative contracts that qualify for hedge accounting as of June 30, 2012 and December 31, 2011, and the impact of designated derivative contracts on accumulated other comprehensive income for the six months ended June 30, 2012:

	December 31, 2011	Amount of gain (loss) recognized in other comprehensive income (effective portion)	Amount of gain (loss) reclassified from accumulated other comprehensive income to net revenue and operating expense (effective portion)	June 30, 2012
	(In millions)			
Foreign exchange contracts designated as cash flow hedges	$72	$24	$41	$55

The following table summarizes the activity of derivative contracts that qualify for hedge accounting as of June 30, 2011 and December 31, 2010, and the impact of designated derivative contracts on accumulated other comprehensive income for the six months ended June 30, 2011:

	December 31, 2010	Amount of gain (loss) recognized in other comprehensive income (effective portion)	Amount of gain (loss) reclassified from accumulated other comprehensive income	June 30, 2011

			to net revenue and operating expense (effective portion)	
	(In millions)			
Foreign exchange contracts designated as cash flow hedges	$14	$(41)	$2	$(29)

13

eBay Inc.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Effect of Derivative Contracts on Condensed Consolidated Statement of Income

The following table provides the location in our financial statements of the recognized gains or losses related to our derivative instruments:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
	(In millions)			
Foreign exchange contracts designated as cash flow hedges recognized in net revenues	$14	$(10)	$26	$(17)
Foreign exchange contracts designated as cash flow hedges recognized in operating expenses	4	(5)	9	(5)
Foreign exchange contracts not designated as hedging instruments recognized in interest and other, net	(11)	—	(8)	(7)
Other contracts not designated as hedging instruments recognized in interest and other, net	—	—	4	—
Total gain (loss) recognized from derivative contracts in the condensed consolidated statement of income	$7	$(15)	$31	$(29)

Note 8 - Debt

The following table summarizes the carrying value of our outstanding debt:

	Coupon Rate	Carrying Value as of June 30, 2012	Effective Interest Rate	Carrying Value as of December 31, 2011	Effective Interest Rate
	(In millions, except percentages)				
Long-Term Debt					
Senior notes due 2013	0.875 %	$400	0.946 %	$400	0.946 %
Senior notes due 2015	1.625 %	598	1.703 %	598	1.703 %
Senior notes due 2020	3.250 %	498	3.319 %	497	3.319 %
Total senior notes		1,496		1,495	
Note payable		14		15	
Capital lease obligations		8		15	
Total long-term debt		$1,518		$1,525	
Short-Term Debt					
Commercial paper		$550		$550	
Note payable		2		2	
Capital lease obligations		12		13	
Total short-term debt		564		565	
Total Debt		$2,082		$2,090	

Senior Notes

The effective rates for the fixed-rate debt include the interest on the notes and the accretion of the discount. Interest on these notes is payable semiannually on April 15 and October 15. Interest expense associated with these notes, including amortization of debt issuance costs, during the three and six months ended June 30, 2012 was approximately $8 million and $16 million, respectively. At June 30, 2012, the estimated fair value of all these senior notes included in long-term debt was approximately $1.5 billion based on market prices on less active markets (Level 2).

The indenture pursuant to which the senior notes were issued includes customary covenants that, among other things, limit our ability to incur, assume or guarantee debt secured by liens on specified assets or enter into sale and lease-back transactions with respect to specified properties, and also includes customary events of default.

Notes Payable
Notes payable consists primarily of a note that bears interest at 6.3% per annum and has a maturity date of December 2015.
Capital Lease Obligations
We acquired certain warehouse equipment and computer hardware and software under capital leases as part of our acquisition of GSI. The capital leases have maturity dates ranging from July 2012 to February 2016 and bear interest at rates ranging from 3% to 9% per annum. The present value of future minimum capital lease payments as of June 30, 2012 was as follows (in millions):

Gross capital lease obligations	$21
Imputed interest	(1)
Total present value of future minimum capital lease payments	$20

Commercial Paper
We have a $2 billion commercial paper program pursuant to which we may issue commercial paper notes with maturities of up to 397 days from the date of issue. As of June 30, 2012, $550 million aggregate principal amount of commercial paper notes were outstanding, with a weighted average interest rate of 0.19% per annum, and a weighted average remaining term of 79 days.
Credit Agreement
As of June 30, 2012, no borrowings or letters of credit were outstanding under our $3 billion credit agreement. As described above, we have a $2 billion commercial paper program and maintain $2 billion of available borrowing capacity under our credit agreement in order to repay commercial paper borrowings in the event we are unable to repay those borrowings from other sources when they become due. As a result, at June 30, 2012, $1 billion of borrowing capacity was available for other purposes permitted by the credit agreement.
As of June 30, 2012, we were in compliance with all covenants in our outstanding debt instruments.

Note 9 — Commitments and Contingencies

Commitments

As of June 30, 2012, approximately $11 billion of unused credit was available to Bill Me Later accountholders. The individual lines of credit that make up this unused credit are subject to periodic review and termination by the chartered financial institution that is the issuer of Bill Me Later credit products based on, among other things, account usage and customer creditworthiness. Currently, when a consumer makes a purchase using a Bill Me Later credit product, the chartered financial institution extends credit to the consumer, funds the extension of credit at the point of sale and advances funds to the merchant. We subsequently purchase the receivables related to the consumer loans extended by the chartered financial institution and, as a result of the purchase, bear the risk of loss in the event of loan defaults. Although the chartered financial institution continues to own each customer account, we own the related receivable, and Bill Me Later is responsible for all servicing functions related to the account.

Litigation and Other Legal Matters

Overview
We are involved in legal proceedings on an ongoing basis. If we believe that a loss arising from such matters is probable and can be reasonably estimated, we accrue the estimated liability in our financial statements. If only a range of estimated losses can be determined, we accrue an amount within the range that, in our judgment, reflects the most likely outcome; if none of the estimates within that range is a better estimate than any other amount, we accrue the low end of the range. Amounts accrued for legal proceedings for which we believe a loss is probable were not material for the six months ended June 30, 2012. Except as otherwise noted, we have concluded that reasonably possible losses arising directly from the proceedings (i.e., monetary damages or amounts paid in judgment or settlement) in excess of our accruals are also not material. For those proceedings in which an unfavorable outcome is reasonably possible but

not probable, we have disclosed an estimate of the reasonably possible loss or range of losses or we have concluded that an estimate of the reasonably possible loss or range of

15

eBay Inc.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

losses arising directly from the proceeding (i.e., monetary damages or amounts paid in judgment or settlement) are not material. If we cannot estimate the probable or reasonably possible loss or range of losses arising from a legal proceeding, we have disclosed that fact.

In assessing the materiality of a legal proceeding, we evaluate, among other factors, the amount of monetary damages claimed, as well as the potential impact of non-monetary remedies sought by plaintiffs (e.g., injunctive relief) that may require us to change our business practices in a manner that could have a material adverse impact on our business. With respect to the matters disclosed in this Note 9, we are unable to estimate the possible loss or range of losses that could potentially result from the application of such non-monetary remedies.

Specific Matters

In August 2006, Louis Vuitton Malletier and Christian Dior Couture filed two lawsuits in the Paris Court of Commerce against eBay Inc. and eBay International AG. Among other things, the complaint alleged that we violated French tort law by negligently broadcasting listings posted by third parties offering counterfeit items bearing plaintiffs' trademarks and by purchasing certain advertising keywords. Around September 2006, Parfums Christian Dior, Kenzo Parfums, Parfums Givenchy, and Guerlain Société also filed a lawsuit in the Paris Court of Commerce against eBay Inc. and eBay International AG. The complaint alleged that we had interfered with the selective distribution network the plaintiffs established in France and the European Union by allowing third parties to post listings offering genuine perfumes and cosmetics for sale on our websites. In June 2008, the Paris Court of Commerce ruled that eBay and eBay International AG were liable for failing to prevent the sale of counterfeit items on its websites that traded on plaintiffs' brand names and for interfering with the plaintiffs' selective distribution network. The court awarded plaintiffs approximately EUR 38.6 million in damages and issued an injunction (enforceable by daily fines of up to EUR 100,000) prohibiting all sales of perfumes and cosmetics bearing the Dior, Guerlain, Givenchy and Kenzo brands over all worldwide eBay sites to the extent that they are accessible from France. We appealed this decision, and in September 2010, the Paris Court of Appeal reduced the damages award to EUR 5.7 million and modified the injunction. We further appealed this decision to the French Supreme Court, and in May 2012, the French Supreme Court ruled that the appeal court should not have assumed jurisdiction upon activity that took place on the eBay.com site and that the injunction was too broad insofar as it did not exclude private sales. The court also noted that the appeal court had not sufficiently dealt with assertions that the plaintiffs' distribution contracts were not valid. Those matters will now be remanded to the Paris Court of Appeal. In 2009, plaintiffs filed an action regarding our compliance with the original injunction, and in November 2009, the court awarded the plaintiffs EUR 1.7 million (the equivalent of EUR 2,500 per day) and indicated that as a large Internet company we should do a better job of enforcing the injunction. Parfums Christian Dior has filed another motion relating to our compliance with the injunction. We have taken measures to comply with the injunction and have appealed these rulings, noting, among other things, the modification of the initial injunction. In light of the French Supreme Court ruling mentioned above, we asked the court to stay proceedings with respect to enforcement of the injunction pending the retrial of the matters on appeal, and this request has been granted. However, these and similar suits may force us to modify our business practices, which could lower our revenue, increase our costs, or make our websites less convenient to our customers. Any such results could materially harm our business. Other brand owners have also filed suit against us or have threatened to do so in numerous different jurisdictions, seeking to hold us liable for, among other things, alleged counterfeit items listed on our websites by third parties, “tester” and other not for resale consumer products listed on our websites by third parties, alleged misuse of trademarks in listings, alleged violations of selective distribution channel laws, alleged violations of parallel import laws, alleged non-compliance with consumer protection laws and in connection with paid search advertisements. We have prevailed in some of these suits, lost in others, and many are in various stages of appeal. We continue to believe that we have meritorious defenses to these suits and intend to defend ourselves vigorously.

In May 2009, the U.K. High Court of Justice ruled in the case filed by L'Oréal SA, Lancôme Parfums et Beauté & Cie, Laboratoire Garnier & Cie and L'Oréal (UK) Ltd against eBay International AG, other eBay companies, and several eBay sellers (No. HC07CO1978) that eBay was not jointly liable with the seller co-defendants as a joint tortfeasor, and indicated that it would certify to the European Court of Justice ("ECJ") questions of liability for the use of L'Oréal trademarks, hosting liability, and the scope of a possible injunction against intermediaries. On July 12, 2011 the ECJ ruled on the questions certified by the U.K. High Court of Justice. It held that (a) brand names could be used by marketplaces as keywords for paid search advertising without violating a trademark owner's rights if it were clear to consumers that the goods reached via the key word link were not being offered by the trademark owner or its designees but instead by third parties, (b) that marketplaces could invoke the limitation from liability provided by Article 14 of the ecommerce directive if they did not take such an active role with respect to the listings in question that the limitation would not be available, but that even where the limitation was available, the marketplace could be liable if it had awareness (through notice or its own investigation) of the illegality of the listings, (c) that a marketplace would be liable in a specific jurisdiction only if the offers on the site at issue were targeting that jurisdiction, a question of fact, (d) that injunctions may be issued to a marketplace in connection with infringing third party

16

eBay Inc.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

content, but that such injunctions must be proportionate and not block legitimate trade and (e) that trademark rights can only be evoked by a rights owner as a result of a seller's commercial activity as opposed to private activity. The matter will now return to the U.K. High Court of Justice for further action in light of the ECJ opinion. The case was originally filed in July 2007. L'Oréal's complaint alleged that we were jointly liable for trademark infringement for the actions of the sellers who allegedly sold counterfeit goods, parallel imports and testers (not for resale products). Additionally, L'Oréal claimed that eBay's use of L'Oréal brands on its website, in its search engine and in sponsored links, and purchase of L'Oréal trademarks as keywords, constitute trademark infringement. The suit sought an injunction preventing future infringement, full disclosure of the identity of all past and present sellers of infringing L'Oréal goods, and a declaration that our Verified Rights Owner (VeRO) program as then operated was insufficient to prevent such infringement. The scope of a possible injunction claimed is to be specified after the trial upon remand from the ECJ.

eBay's Korean subsidiary, IAC (which has merged into Gmarket and is now named eBay Korea), has notified its approximately 20 million users of a January 2008 data breach involving personally identifiable information including name, address, resident registration number and some transaction and refund data (but not including credit card information or real time banking information). Approximately 149,000 users have sued IAC over this breach in several lawsuits in Korean courts and more may do so in the future (including after final determination of liability). Trial for a group of four representative suits began in August 2009 in the Seoul District Court, and trial for a group of 23 other suits began in September 2009 in the Seoul District Court. There is some precedent in Korea for a court to grant "consolation money" for data breaches without a specific finding of harm from the breach. Such precedents have involved payments of up to approximately $200 per user. In January 2010, the Seoul District Court ruled that IAC had met its obligations with respect to defending the site from intrusion and, accordingly, had no liability for the breach. This ruling has been appealed by approximately 34,000 plaintiffs to the Seoul High Court, where it is currently being heard de novo. A decision is expected in the second half of 2012 or in early 2013.

General Matters

Other third parties have from time to time claimed, and others may claim in the future, that we have infringed their intellectual property rights. We are subject to patent disputes, and expect that we will increasingly be subject to additional patent infringement claims involving various aspects of our Marketplaces, Payments and GSI businesses as our services continue to expand in scope and complexity. Such claims may be brought directly against our companies and/or against our customers (who may be entitled to contractual indemnification under their contracts with us), and we are subject to increased exposure to such claims as a result of our recent acquisitions, particularly in cases where we are entering into new businesses in connection with such acquisitions. We have in the past been forced to litigate such claims. We may also become more vulnerable to third-party claims as laws such as the Digital Millennium Copyright Act, the Lanham Act and the Communications Decency Act are interpreted by the courts, and as we expand the range and geographical scope of our services and become subject to laws in jurisdictions where the underlying laws with respect to the potential liability of online intermediaries like ourselves are either unclear or less favorable. We believe that additional lawsuits alleging that we have violated patent, copyright or trademark laws will be filed against us. Intellectual property claims, whether meritorious or not, are time consuming and costly to defend and resolve, could require expensive changes in our methods of doing business, or could require us to enter into costly royalty or licensing agreements on unfavorable terms.

From time to time, we are involved in other disputes or regulatory inquiries that arise in the ordinary course of business, including suits by our users (individually or as class actions) alleging, among other things, improper disclosure of our prices, rules or policies, that our prices, rules, policies or customer/user agreements violate applicable law, or that we have not acted in conformity with such prices, rules, policies or agreements. The number and significance of these disputes and inquiries are increasing as our company has grown larger, our businesses have expanded in scope and our products and services have increased in complexity. Any claims or regulatory actions against us, whether meritorious or not, could be time consuming, result in costly litigation, damage awards (including statutory damages for certain causes of action in certain jurisdictions), injunctive relief or increased costs of doing business through adverse judgment or settlement, require us to change our business practices in expensive ways, require significant amounts of management time, result in the diversion of significant operational resources or otherwise harm our business.

Indemnification Provisions

In the ordinary course of business, we have included limited indemnification provisions in certain of our agreements with parties with which we have commercial relations, including our standard marketing, promotions and application-programming-interface license agreements. Under these contracts, we generally indemnify, hold harmless and agree to reimburse the indemnified party for losses suffered or incurred by the indemnified party in connection with claims by a third party with respect to our domain names, trademarks, logos and other branding elements to the extent that such marks are applicable to our

eBay Inc.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

performance under the subject agreement. In certain cases, we have agreed to provide indemnification for intellectual property infringement. GSI has provided in many of its major online commerce agreements an indemnity for other types of third-party claims, which are indemnities mainly related to various intellectual property rights, and we have provided similar indemnities in a limited number of agreements for our other businesses. In our PayPal business, we have provided an indemnity to our payment processors in the event of certain third-party claims or card association fines against the processor arising out of conduct by PayPal or PayPal customers. In connection with the sale of Skype Technologies, S.A. ("Skype") in November 2009, we made certain customary warranties to the buyer in the purchase agreement. Our liability to the buyer for inaccuracies in these warranties is generally subject to certain limitations. With respect to certain specified litigation matters involving Skype that were pending as of the closing of the transaction, we also agreed, among other things, to bear 50% of the cost of any monetary judgment that is rendered in respect of those matters. It is not possible to determine the maximum potential loss under these indemnification provisions due to our limited history of prior indemnification claims and the unique facts and circumstances involved in each particular provision. To date, losses recorded in our statement of income in connection with our indemnification provisions have not been significant, either individually or collectively.

Off-Balance Sheet Arrangements

As of June 30, 2012, we had no off-balance sheet arrangements that have, or are reasonably likely to have, a current or future material effect on our consolidated financial condition, results of operations, liquidity, capital expenditures or capital resources.

In Europe, we have two cash pooling arrangements with a financial institution for cash management purposes. These arrangements allow for cash withdrawals from this financial institution based upon our aggregate operating cash balances held in Europe within the same financial institution (“Aggregate Cash Deposits”). These arrangements also allow us to withdraw amounts exceeding the Aggregate Cash Deposits up to an agreed-upon limit. The net balance of the withdrawals and the Aggregate Cash Deposits are used by the financial institution as a basis for calculating our net interest expense or income. As of June 30, 2012, we had a total of $5 billion in cash withdrawals offsetting our $5 billion in Aggregate Cash Deposits held within the same financial institution under these cash pooling arrangements.

Based on differences in regulatory requirements and commercial law in the jurisdictions where PayPal operates, PayPal holds customer balances either as direct claims against PayPal or as an agent or custodian on behalf of PayPal's customers. Customer funds held by PayPal as an agent or custodian on behalf of our customers are not reflected in our condensed consolidated balance sheet. These off-balance sheet funds totaled approximately $3 billion as of June 30, 2012 and December 31, 2011. These funds include funds held on behalf of U.S. customers that are deposited in bank accounts insured by the Federal Deposit Insurance Corporation (subject to applicable limits).

Note 10 — Stock Repurchase Programs

In September 2010, our Board of Directors authorized a stock repurchase program that provides for the repurchase of up to $2 billion of our common stock, with no expiration from the date of authorization. In June 2012, our Board authorized an additional stock repurchase program that provides for the repurchase of up to an additional $2 billion of our common stock, with no expiration from the date of authorization. These stock repurchase programs are intended to offset the impact of dilution from our equity compensation programs. The stock repurchase activity under our stock repurchase programs during the first six months of 2012 is summarized as follows:

	Shares Repurchased	Average Price per Share	Value of Shares Repurchased	Remaining Amount Authorized
	(In millions, except per share amounts)			
Balance at January 1, 2012	35	$31.55	$1,119	$881
Authorization of additional plan in June 2012				2,000
Repurchase of common stock	16	37.16	595	(595)
Balance at June 30, 2012	51	$33.30	$1,714	$2,286

These repurchased shares were recorded as treasury stock and were accounted for under the cost method. No repurchased shares have been retired.

18

eBay Inc.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Note 11 — Stock-Based Plans

Stock Option Activity

The following table summarizes stock option activity for the six-month period ended June 30, 2012:

	Options (In millions)
Outstanding at January 1, 2012	40
Granted and assumed	2
Exercised	(7)
Forfeited/expired/canceled	(2)
Outstanding at June 30, 2012	33

The weighted average exercise price of stock options granted during the period was $36.34 per share and the related weighted average grant date fair value was $11.10 per share.

Restricted Stock Unit Activity

The following table summarizes restricted stock unit ("RSU") activity for the six-month period ended June 30, 2012:

	Units (In millions)
Outstanding at January 1, 2012	40
Awarded and assumed	16
Vested	(12)
Forfeited	(2)
Outstanding at June 30, 2012	42

The weighted average grant date fair value for RSUs awarded during the period was $36.60 per share.

Stock-Based Compensation Expense

The impact on our results of operations of recording stock-based compensation expense for the three and six months ended June 30, 2012 and 2011 was as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
	(In millions)			
Cost of net revenues	$14	$14	$28	$29
Sales and marketing	34	34	64	68
Product development	37	34	67	65
General and administrative	42	37	79	76
Total stock-based compensation expense	$127	$119	$238	$238
Capitalized in product development	$3	$4	$10	$8

eBay Inc.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Valuation Assumptions

We calculated the fair value of each stock option award on the date of grant using the Black-Scholes option pricing model. The following weighted average assumptions were used for the three and six months ended June 30, 2012 and 2011:

	Three Months Ended June 30,				Six Months Ended June 30,			
	2012		2011		2012		2011	
Risk-free interest rate	0.73	%	1.18	%	0.72	%	1.24	%
Expected life (in years)	4.0		3.7		4.0		3.8	
Dividend yield	—	%	—	%	—	%	—	%
Expected volatility	38	%	38	%	38	%	38	%

Our computation of expected volatility is based on a combination of historical and market-based implied volatility from traded options on our common stock. Our computation of expected life is based on historical experience of similar awards, giving consideration to the contractual terms of the stock-based awards, vesting schedules and expectations of future employee behavior. The interest rate for periods within the contractual life of the award is based on the U.S. Treasury yield curve in effect at the time of grant.

Note 12 — Income Taxes

The following table reflects changes in unrecognized tax benefits for the six-month period ended June 30, 2012:

	(In millions)	
Gross amounts of unrecognized tax benefits as of January 1, 2012	$286	
Increases related to prior period tax positions	33	
Decreases related to prior period tax positions	(4	)
Increases related to current period tax positions	7	
Settlements	—	
Gross amounts of unrecognized tax benefits as of June 30, 2012	$322	

As of June 30, 2012 and December 31, 2011, our liabilities for unrecognized tax benefits were included in deferred and other tax liabilities, net. The increase in liabilities for unrecognized tax benefits for the first six months of 2012 relates to the point at which certain foreign earnings became subject to U.S taxation.

We recognize interest and/or penalties related to uncertain tax positions in income tax expense. The amount of interest and penalties accrued as of June 30, 2012 and December 31, 2011 was approximately $109 million and $83 million, respectively.

We are subject to both direct and indirect taxation in the U.S. and various states and foreign jurisdictions. We are under examination by certain tax authorities for the 2003 to 2009 tax years. We believe that adequate amounts have been reserved for any adjustments that may ultimately result from these examinations. The material jurisdictions where we are subject to potential examination by tax authorities for tax years after 2002 include, among others, the U.S. (Federal and California), France, Germany, Italy, Korea, Israel, Switzerland, Singapore and Canada.

Although the timing of the resolution and/or closure of audits is highly uncertain, it is reasonably possible that the balance of gross unrecognized tax benefits could significantly change in the next 12 months. However, given the number of years remaining subject to examination and the number of matters being examined, we are unable to estimate the full range of possible adjustments to the balance of gross unrecognized tax benefits.

During the three and six months ended June 30, 2012, we provided for U.S. income and foreign withholding taxes on approximately 15% of our non-U.S. subsidiaries' undistributed earnings. The remaining portion of our non-U.S. subsidiaries undistributed earnings is intended to be indefinitely reinvested in our international operations; upon distribution of those earnings in the form of dividends or otherwise, we would be subject to U.S. income taxes (subject to adjustments for foreign

eBay Inc.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

tax credits). It is not practicable to determine the income tax liability that might be incurred if the indefinitely reinvested earnings were to be distributed. On a regular basis, we develop cash forecasts to estimate our cash needs internationally and domestically. We consider projected cash needs for, among other things, investments in our existing businesses, potential acquisitions and capital transactions, including repurchases of our common stock and debt repayments. We estimate the amount of cash available or needed in the jurisdictions where these investments are expected, as well as our ability to generate cash in those jurisdictions and our access to capital markets. Such an analysis enables us to conclude whether or not we will indefinitely reinvest the current period's foreign earnings.

Our effective tax rate differs from the U.S. federal statutory rate due primarily to lower tax rates associated with certain earnings from our operations outside the U.S.

Note 13 - Loans and Interest Receivable, Net

Loans and interest receivable represent purchased consumer receivables arising from loans made by a partner chartered financial institution to individual consumers in the U.S. to purchase goods and services through our Bill Me Later merchant network. During the three months ended June 30, 2012 and 2011, we purchased approximately $696 million and $499 million, respectively, in consumer receivables. During the six months ended June 30, 2012 and 2011, we purchased approximately $1.3 billion and $930 million, respectively, in consumer receivables. Loans and interest receivable are reported at their outstanding principal balances, net of allowances, including unamortized deferred origination costs and estimated collectible interest and fees. We use a consumer's FICO score, among other measures, in evaluating the credit quality of our consumer receivables. A FICO score is a type of credit score that lenders use to assess an applicant's credit risk and whether to extend credit. Individual FICO scores generally are obtained each quarter the consumer has an outstanding loan receivable owned by Bill Me Later. The weighted average consumer FICO score related to our loans and interest receivable balance outstanding at June 30, 2012 was 690 as compared to 692 at December 31, 2011. As of June 30, 2012 and December 31, 2011, approximately 56.4% and 59.3%, respectively, of our loans and interest receivable balance was due from consumers with FICO scores greater than 680, which is generally considered "prime" by the consumer credit industry. As of June 30, 2012, approximately 90% of our loans and interest receivable portfolio was current.

The following table summarizes the activity in the allowance for loans and interest receivable:

	Six Months Ended June 30,	
	2012	2011
	(In millions)	
Balance as of January 1	$59	$42
Charge-offs	(59)	(36)
Recoveries	5	4
Provision	66	34
Balance as of June 30	$71	$44

Item 2: Management's Discussion and Analysis of Financial Condition and Results of Operations

FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, including statements that involve expectations, plans or intentions (such as those relating to future business, future results of operations or financial condition, new or planned features or services, or management strategies). You can identify these forward-looking statements by words such as “may,” “will,” “would,” “should,” “could,” “expect,” “anticipate,” “believe,” “estimate,” “intend,” other similar expressions. These forward-looking statements involve risks and uncertainties that could cause our actual results to differ materially from those expressed or implied in our forward-looking statements. Such risks and uncertainties include, among others, those discussed in“Part II — Item 1A: Risk Factors” of this Quarterly Report on Form 10-Q as well as in our condensed consolidated financial statements, related notes, and the other information appearing elsewhere in this report and our other filings with the Securities and Exchange Commission, or the SEC. We do not intend, and undertake no obligation, to update any of our forward-looking statements after the date of this report to reflect actual results or future events or circumstances. Given these risks and uncertainties, readers are cautioned not to place undue reliance on such forward-looking statements.

You should read the following Management's Discussion and Analysis of Financial Condition and Results of Operations in conjunction with the unaudited condensed consolidated financial statements and the related notes that appear elsewhere in this report.

Overview

eBay is a global commerce platform and payments leader. We enable commerce through eBay, the world's largest online marketplace, which allows users to buy and sell in nearly every country on earth; through PayPal, which enables individuals and businesses to securely, easily and quickly send and receive online payments; and through GSI, which facilitates ecommerce, multichannel retailing and interactive marketing for global enterprises. X.commerce brings together the technology assets and developer communities of eBay, PayPal and Magento, an ecommerce storefront platform, to support our mission of enabling commerce. We also reach millions of people through specialized marketplaces such as StubHub, the world's largest ticket marketplace, and eBay classifieds sites, which together have a presence in more than 1,000 cities around the world.

We have three reportable business segments: Marketplaces, Payments and GSI. Our Marketplaces segment includes our eBay.com platform and its localized counterparts and our other online trading platforms, such as our online classifieds sites and StubHub. Our Payments segment is comprised of PayPal, Bill Me Later and Zong. Our GSI segment consists of GSI Commerce, Inc. ("GSI"), and was added upon the completion of our acquisition of GSI on June 17, 2011. The results of our GSI segment have been included in our consolidated results of operations from the acquisition date.

Net revenues for the three months ended June 30, 2012 increased 23% to $3.4 billion, compared to the same period of the prior year, driven primarily by increases in net revenues from PayPal of 26%, Marketplaces of 9% and net revenues of $221 million from GSI. For the three months ended June 30, 2012, our operating margin increased to 20% from 19% in the same period of the prior year, driven primarily by the impact of GSI acquisition-related costs incurred in the second quarter 2011. For the three months ended June 30, 2012, our diluted earnings per share increased to $0.53, a $0.31 increase compared to the same period of the prior year, driven primarily by a loss from the divestiture of certain GSI businesses and GSI acquisition-related costs incurred in 2011, a gain from the divestiture of a business and strong growth in net revenues, partially offset by increased investment in the shopping experience and the impact of acquisitions. For the three months ended June 30, 2012, we generated cash flow from operations of approximately $768 million, compared to $783 million for the same period of the prior year.

Our Marketplaces segment total net revenues increased $151 million, or 9%, for the three months ended June 30, 2012 compared to the same period of the prior year. The increase in total net revenues was driven primarily by a year-over-year increase in GMV (as defined below) excluding vehicles of 10%, which was due primarily to strong growth across all regions partially offset by the negative impact of foreign currency movements relative to the U.S. dollar. Marketplaces segment operating margin increased 0.8 percentage points for the three months ended June 30, 2012 compared to the same period of the prior year due to the favorable resolution of an indirect tax dispute, partially offset by increased investments in technology and marketing.

22

Our Payments segment total net revenues increased $284 million, or 26%, for the three months ended June 30, 2012 compared to the same period of the prior year. The increase in total net revenues was driven primarily by a year-over-year increase in net TPV (as defined below) of 20% and strong growth in Bill Me Later. Our Payments segment operating margin increased 3.9 percentage points for the three months ended June 30, 2012 compared to the same period of the prior year, due primarily to higher take rate, lower processing costs and operating leverage.
Our GSI segment was formed as a result of our acquisition of GSI in June 2011. For the three months ended June 30, 2012, GSI contributed $221 million in revenue and had a segment operating margin of 4.5%.
Some key operating metrics that members of our senior management regularly review to evaluate our financial results include net promoter score (NPS), market share, GMV, GMV excluding vehicles, number of sold items, net TPV, Merchant Services net TPV (as defined below), on eBay net TPV (as defined below), net number of payments, global ecommerce (GeC) merchandise sales, penetration rates, active registered accounts, same store sales, funding mix (the mix of payments vehicles such as credit cards, debit cards, bank accounts and PayPal accounts, used by customers to make payments through our Payments networks), free cash flow (which we define as net cash provided by operating activities less purchases of property and equipment, net) and revenue excluding acquisitions and foreign currency impact.

We define GMV as the total value of all successfully closed items between users on our eBay Marketplaces trading platforms (excluding eBay's classified websites and Shopping.com) during the applicable period, regardless of whether the buyer and seller actually consummated the transaction. We define net TPV as the total dollar volume of payments, net of payment reversals, successfully completed through our Payments networks, Bill Me Later accounts and Zong during the applicable period, excluding PayPal's payment gateway business. We define Merchant Services net TPV as the total dollar volume of payments, net of reversals, successfully completed through our Payments networks, Bill Me Later accounts and Zong during the applicable period, excluding PayPal's payment gateway business and payments for transactions on eBay Marketplaces and GSI platforms. We define on eBay net TPV as the total dollar volume of payments, net of reversals, successfully completed through our payments networks for transactions on eBay Marketplaces or GSI platforms.

Results of Operations

Summary of Net Revenues

We generate two types of net revenues: net transaction revenues and marketing services and other revenues. Our net transaction revenues are derived principally from listing fees, final value fees (which are fees payable on transactions completed on our Marketplaces trading platforms), fees paid by merchants for payment processing services and ecommerce service fees. Our marketing services revenues are derived principally from the sale of advertisements, revenue sharing arrangements, classifieds fees, marketing service fees and lead referral fees. Other revenues are derived principally from interest and fees earned on the Bill Me Later portfolio of receivables from loans, interest earned on certain PayPal customer account balances and fees from contractual arrangements with third parties that provide services to our users.

The following table sets forth the breakdown of net revenues by type and geography for the periods presented.

	Three Months Ended June 30,		Percent	Six Months Ended June 30,		Percent
	2012	2011[1]	Change	2012	2011[1]	Change
	(In millions, except percentage changes)					
Net Revenues by Type:						
Net transaction revenues						
Marketplaces	$1,491	$1,350	10 %	$2,916	$2,634	11 %
Payments	1,234	991	25 %	2,450	1,934	27 %
GSI	164	16	N/A	346	16	N/A
Total net transaction revenues	2,889	2,357	23 %	5,712	4,584	25 %
Marketing services and other revenues						
Marketplaces	323	313	3 %	626	583	7 %
Payments	123	82	50 %	216	131	65 %
GSI	57	8	N/A	112	8	N/A
Corporate and other	10	—	N/A	16	—	N/A
Total marketing services and other revenues	513	403	27 %	970	722	34 %
Elimination of inter-segment net revenue [2]	(4)	—	N/A	(7)	—	N/A
Total net revenues	$3,398	$2,760	23 %	$6,675	$5,306	26 %
Net Revenues by Geography:						
U.S.	$1,611	$1,249	29 %	$3,192	$2,390	34 %
International	1,787	1,511	18 %	3,483	2,916	19 %
Total net revenues	$3,398	$2,760	23 %	$6,675	$5,306	26 %

(1) Includes data for GSI since June 17, 2011 the date the acquisition of GSI was completed. Accordingly, the percent changes in GSI's revenues between the 2011 and 2012 periods are not meaningful.
(2) Represents revenue generated between our reportable segments.

Revenues are attributed to U.S. and international geographies based primarily upon the country in which the seller, payment recipient, customer, website that displays advertising, or other service provider, as the case may be, is located.

Because we generate substantial net revenues internationally, we are subject to the risks of doing business in foreign countries as discussed under "Part II - Item 1A - Risk Factors." In that regard, fluctuations in foreign currency exchange rates impact our results of operations. We have a foreign exchange risk management program that is designed to reduce our exposure to fluctuations in foreign currencies; however, the effectiveness of this program in mitigating the impact of foreign currency fluctuations on our results of operations varies from period to period, and in any given period, our operating results are usually affected, sometimes significantly, by changes in currency exchange rates. Fluctuations in exchange rates also directly affect our cross-border revenue. We calculate the year-over-year impact of foreign currency movements on our business using prior period foreign currency rates applied to current year transactional currency amounts.

For the three months ended June 30, 2012, foreign currency movements relative to the U.S. dollar negatively impacted net revenues by approximately $99 million (net of a $14 million positive impact from hedging activities included in PayPal's net revenue) compared to the same period of the prior year. On a business segment basis, for the three months ended June 30, 2012, foreign currency movements relative to the U.S. dollar negatively impacted Marketplaces, Payments and GSI net revenues by approximately $80 million, $18 million and $1 million, respectively, in each case compared to the same period of the prior year (net of the impact of hedging activities noted above).

For the six months ended June 30, 2012, foreign currency movements relative to the U.S. dollar negatively impacted net revenues by approximately $122 million (net of a $26 million positive impact from hedging activities included in PayPal's net revenue) compared to the same period of the prior year. On a business segment basis, for the six months ended June 30, 2012, foreign currency movements relative to the U.S. dollar negatively impacted Marketplaces, Payments and GSI net revenues by approximately $104 million, $17 million and $1 million, respectively, in each case compared to the same period of the prior year (net of the impact of hedging activities noted above).

The following table sets forth, for the periods presented, certain key operating metrics that we believe are significant factors affecting our net revenues.

	Three Months Ended June 30,		Percent	Six Months Ended June 30,		Percent
	2012	2011	Change	2012	2011	Change
	(In millions, except percentage changes)					
Supplemental Operating Data:						
Marketplaces Segment: (1)						
GMV excluding vehicles (2)	$16,171	$14,680	10 %	$32,377	$29,176	11 %
GMV vehicles only (3)	$2,021	$2,238	(10)%	$3,892	$4,288	(9)%
Total GMV (4)	$18,192	$16,918	8 %	$36,269	$33,464	8 %
Payments Segment:						
Merchant services net TPV (5)	$23,114	$18,860	23 %	$45,547	$36,427	25 %
On eBay net TPV (6)	$11,337	$9,882	15 %	$22,761	$19,677	16 %
Total net TPV (7)	$34,451	$28,742	20 %	$68,308	$56,104	22 %
GSI Segment:						
GeC Merchandise Sales (8)	$674	$76	787 %	$1,389	$76	1,728 %

(1) eBay's classifieds websites and Shopping.com are not included in these metrics.

(2) Total value of all successfully closed items between users on eBay Marketplaces trading platforms during the period, regardless of whether the buyer and seller actually consummated the transaction, excluding vehicles GMV.

(3) Total value of all successfully closed vehicle transactions between users on eBay Marketplaces trading platforms during the period, regardless of whether the buyer and seller actually consummated the transaction.

(4) Total value of all successfully closed items between users on eBay Marketplaces trading platforms during the period, regardless of whether the buyer and seller actually consummated the transaction.

(5) Total dollar volume of payments, net of payment reversals, successfully completed through our Payments networks, Bill Me Later accounts and Zong during the period, excluding PayPal's payment gateway business and payments for transactions on eBay Marketplaces and GSI platforms.

(6) Total dollar volume of payments, net of payment reversals, successfully completed through our Payments networks during the period for transactions on eBay Marketplaces and GSI platforms during the period.

(7) Total dollar volume of payments, net of payment reversals, successfully completed through our Payments networks, Bill Me Later accounts and Zong during the period, excluding PayPal's payment gateway business.

(8) Represents the retail value of all sales transactions, inclusive of freight charges and net of allowance for returns and discounts, which flow through the GSI ecommerce services platform, whether we record the full amount of such transaction as a product sale or a percentage of such transaction as a service fee.

Seasonality

The following table sets forth, for the periods presented, our total net revenues and the sequential quarterly movements of these net revenues:

	Quarter Ended			
	March 31	June 30	September 30	December 31
	(In millions, except percentage changes)			
2010				
Net revenues	$2,196	$2,215	$2,249	$2,495
Percent change from prior quarter	(7)%	1 %	2 %	11 %
2011(1)				

Net revenues	$2,546	$2,760	$2,966	$3,380
Percent change from prior quarter	2 %	8 %	7 %	14 %
2012				
Net revenues	$3,277	3,398	—	—
Percent change from prior quarter	(3)%	4 %	—	—

(1) Net revenues attributable to the GSI segment are reflected from June 17, 2011 (the date the acquisition of GSI was completed).

25

We expect transaction activity patterns on our websites to mirror general consumer buying patterns. Our GSI segment is highly seasonal. The fourth calendar quarter typically accounts for a disproportionate amount of GSI's total annual revenue because consumers increase their purchases and businesses increase their advertising to consumers during the fourth quarter holiday season.

Marketplaces Net Transaction Revenues

Marketplaces net transaction revenues increased $141 million, or 10%, while GMV excluding vehicles increased 10% during the second quarter of 2012 compared to the same period in the prior year. The increase in net transaction revenue and GMV excluding vehicles was due primarily to strong growth across all regions partially offset by the negative impact of foreign currency movements relative to the U.S. dollar. Additionally, net transaction revenue increased due to the favorable resolution of an indirect tax dispute.

Marketplaces net transaction revenues increased $282 million, or 11%, while GMV excluding vehicles increased 11% during the first six months of 2012 compared to the same period in the prior year. The increase in net transaction revenue and GMV excluding vehicles was due to the same factors noted above.

Marketplaces net transaction revenues earned internationally (i.e., outside the U.S.) totaled $848 million and $1.6 billion during the second quarter and first six months of 2012, respectively, representing 57% of total Marketplaces net transaction revenues during both periods. Marketplaces net transaction revenues earned internationally (i.e., outside the U.S.) totaled $759 million and $1.5 billion during the second quarter and first six months of 2011, respectively, representing 56% of total Marketplaces net transaction revenues during both periods. The increase in international net transaction revenues was due primarily to growth in our existing international markets, partially offset by the impact of foreign currency movements relative to the U.S. dollar.

Payments Net Transaction Revenues

Payments net transaction revenues increased $243 million, or 25%, during the second quarter of 2012 compared to the same period of the prior year, due primarily to net TPV growth of 20% and a higher take rate. The increase in net TPV was due primarily to growth in consumer and merchant adoption and use of PayPal both on and off eBay. Our Merchant Services net TPV increased 23% during the second quarter of 2012, compared to the same period of the prior year, and represented 67% of PayPal's net TPV in the second quarter of 2012, compared with 66% in the second quarter of 2011. On eBay net TPV increased 15% during the second quarter of 2012, compared to the same period of the prior year and represented 33% of PayPal's net TPV in the second quarter of 2012, compared to 34% for the same period in the prior year. The increase in the take rate was driven primarily by foreign exchange income and gains from hedging.

Payments net transaction revenues increased $516 million, or 27%, during the first six months of 2012 compared to the same period of the prior year, due primarily to net TPV growth of 22% and a higher take rate. The increase in net TPV and take rate are due to the same factors noted above. Our Merchant Services net TPV increased 25% during the first six months of 2012, compared to the same period of the prior year, and represented 67% of PayPal's net TPV in the first six months of 2012, compared with 65% in the first six months of 2011. On eBay net TPV increased 16% during the first six months of 2012, compared to the same period of the prior year and represented 33% of PayPal's net TPV for the first six months of 2012, compared to 35% for the same period of the prior year.

Payments net transaction revenues earned internationally totaled $680 million and $1.3 billion during the second quarter and first six months of 2012, respectively, representing 55% of total Payments net transaction revenues during both periods. Payments net transaction revenues earned internationally totaled $515 million and $991 million during the second quarter and first six months of 2011, respectively, representing 52% and 51% of total Payments net transaction revenues during those respective periods. The increase in international net transaction revenues was due primarily to the growth of our Merchant Services business and increased penetration on eBay Marketplaces platforms internationally.

GSI Net Transaction Revenues

GSI net transaction revenues were $164 million and $346 million during the second quarter and first six months of 2012, respectively, compared to $16 million for the both periods of the prior year. Net transaction revenues attributable to the GSI segment for the second quarter and first six months of 2011 are reflected from June 17, 2011 (the date the acquisition of GSI was completed). Accordingly, comparisons with GSI's net transaction revenues in the corresponding 2011 periods are not meaningful.

Marketing Services and Other Revenues

Marketing services and other revenues increased $110 million and $248 million, or 27% and 34%, during the second quarter and first six months of 2012, respectively, compared to the same periods of the prior year, and represented 15% of total net revenues for both periods in 2012. The increase in marketing services and other revenues during the second quarter and first six months of 2012 was due primarily to revenues attributable to GSI and growth in our Bill Me Later (BML) portfolio of receivables from loans, as well as increased revenue from our classifieds and advertising business.

Summary of Cost of Net Revenues

The following table summarizes changes in cost of net revenues for the periods presented:

	Three Months Ended June 30,				Change from 2011 to 2012			Six Months Ended June 30,				Change from 2011 to 2012		
	2012		2011[1]		in Dollars	in %		2012		2011[1]		in Dollars	in %	
	(In millions, except percentages)													
Cost of net revenues:														
Marketplaces	$310		$304		$6	2	%	$609		$600		$9	2	%
As a percentage of total Marketplaces net revenues	17.1	%	18.3	%				17.2	%	18.6	%			
Payments	525		457		68	15	%	1,040		890		150	17	%
As a percentage of total Payments net revenues	38.7	%	42.6	%				39.0	%	43.1	%			
GSI	147		12		135	N/A		292		12		280	N/A	
As a percentage of total GSI net revenues	66.5	%	52.2	%				63.8	%	52.2	%			
Corporate and other	5		—		5	N/A		29		—		29	N/A	
Total cost of net revenues	$987		$773		$214	28	%	$1,970		$1,502		$468	31	%
As a percentage of net revenues	29.0	%	28.0	%				29.5	%	28.3	%			

(1) Cost of net revenues attributable to the GSI segment are reflected from June 17, 2011 (the date the acquisition of GSI was completed). Accordingly, the percent changes in GSI's cost of revenues between the 2011 and 2012 periods are not meaningful.

Cost of Net Revenues

Cost of net revenues consists primarily of costs associated with payment processing, customer support, site operations, fulfillment and inventory. Significant components of these costs include bank transaction fees, credit card interchange and assessment fees, interest expense on indebtedness incurred to finance the purchase of consumer loans receivable by Bill Me Later, employee compensation, contractor costs, facilities costs, depreciation of equipment and amortization expense.

Marketplaces

Marketplaces cost of net revenues increased $6 million and $9 million, or 2%, during both the second quarter and first six months of 2012, compared to the same periods of the prior year. The increase was due primarily to an increase in our customer support costs associated with our volume growth.

Marketplaces cost of net revenues as a percentage of Marketplaces net revenues decreased 1.2 and 1.4 percentage points during the second quarter and first six months of 2012, respectively, compared to the same periods of the prior year, due primarily to improved operating leverage from our site operation infrastructure partially offset by investment in customer support programs.

Payments

Payments cost of net revenues increased $68 million and $150 million, or 15% and 17%, during the second quarter and first six months of 2012, respectively, compared to the same periods of the prior year. The increase in Payments cost of net revenues was due primarily to the impact of growth in net TPV.

Payments cost of net revenues as a percentage of Payments net revenues decreased 3.9 and 4.1 percentage points during the second quarter and first six months of 2012, respectively, compared to the same periods of the prior year, due primarily to a lower transaction expense rate. The improvement in our transaction expense rate was driven primarily by lower payment processing costs and improvement in funding mix.

GSI

GSI cost of net revenues was $147 million and $292 million during the second quarter and first six months of 2012, respectively. Cost of net revenues attributable to the GSI segment for the second quarter and first six months of 2011 are reflected from June 17, 2011 (the date the acquisition of GSI was completed). Accordingly, comparisons with GSI's cost of revenues in the corresponding 2011 periods are not meaningful.

Summary of Operating Expenses, Non-Operating Items and Provision for Income Taxes

The following table summarizes changes in operating expenses, non-operating items and provision for income taxes for the periods presented:

	Three Months Ended June 30,		Change from 2011 to 2012		Six Months Ended June 30,		Change from 2011 to 2012	
	2012	2011	in Dollars	in %	2012	2011	in Dollars	in %
	(In millions, except percentage changes)							
Sales and marketing	$717	$608	$109	18%	$1,394	$1,141	$253	22%
Product development	394	297	97	33%	768	572	196	34%
General and administrative	390	392	(2)	(1)%	762	685	77	11%
Provision for transaction and loan losses	131	118	13	11%	265	225	40	18%
Amortization of acquired intangible assets	84	53	31	58%	168	97	71	73%
Interest and other, net	38	28	10	36%	69	31	38	123%
Gain (loss) on divested business	118	(256)	374	(146)%	118	(256)	374	(146)%
Provision for income taxes	(159)	(8)	(151)	1,888%	(273)	(100)	(173)	173%

Sales and Marketing

Sales and marketing expenses consist primarily of advertising costs and marketing programs (both online and offline), employee compensation, contractor costs, facilities costs and depreciation on equipment. Online marketing expenses represent traffic acquisition costs in various channels such as paid search, affiliates marketing and display advertising. Offline advertising includes brand campaigns, buyer/seller communications and general public relations expenses. A significant portion of our sales and marketing expense is attributable to our online marketing programs, primarily paid search, which include keyword advertising and third party lead generation costs, in order to drive traffic to our Marketplaces and Payments websites.

Sales and marketing expenses increased $109 million and $253 million, or 18% and 22%, during the second quarter and first six months of 2012, respectively, compared to the same periods of the prior year. The increase in sales and marketing expense was due primarily to higher employee-related expenses (including consultant costs, facility costs and equipment-related costs), marketing program costs (including product launches), and the impact from acquisitions, primarily GSI.

Product Development

Product development expenses consist primarily of employee compensation, contractor costs, facilities costs and depreciation on equipment. Product development expenses are net of required capitalization of major site and other product development efforts, including the development of our next generation platform architecture, migration of certain platforms, seller tools and Payments services projects. Our top technology priorities include search, catalog, mobile, platform and user experience. Capitalized site and product development costs were $59 million and $116 million in the second quarter and first six months of 2012, respectively, compared to $44 million and $81 million in the second quarter and first six months of 2011, respectively, and are primarily reflected as a cost of net revenues when amortized in future periods.

Product development expenses increased $97 million and $196 million, or 33% and 34%, during the second quarter and first six months of 2012, respectively, compared to the same periods of the prior year. The increase was due primarily to higher employee-related costs (including consultant costs, facility costs and equipment-related costs) driven by increased investment in our top technology priorities and the impact from acquisitions, primarily GSI.

General and Administrative

General and administrative expenses consist primarily of employee compensation, contractor costs, facilities costs, depreciation of equipment, employer payroll taxes on stock-based compensation, legal expenses, insurance premiums and professional fees. Our legal expenses, including those related to various ongoing legal proceedings, may fluctuate substantially from period to period.

General and administrative expenses decreased $2 million during the second quarter of 2012, compared to the same period of the prior year. The decrease was due primarily to GSI acquisition-related costs incurred in 2011, partially offset by an increase in payroll and related expenses.

General and administrative expenses increased $77 million, or 11%, during the first six months of 2012, compared to the same period of the prior year. The increase was due primarily to an increase in payroll and related expenses and the impact of acquisitions, primarily GSI, partially offset by GSI acquisition related costs incurred in 2011.

Provision for Transaction and Loan Losses

Provision for transaction and loan losses consists primarily of transaction loss expense associated with our consumer protection programs, fraud, chargebacks, and merchant credit losses; bad debt expense associated with our accounts receivable balance; and loan loss reserves associated with our principal loan receivable balance. We expect our provision for transaction and loan loss expense to fluctuate depending on many factors, including macroeconomic conditions, our consumer protection programs and the impact of regulatory changes.
Provision for transaction and loan losses increased $13 million and $40 million, or 11% and 18%, during the second quarter and first six months of 2012, respectively, compared to the same periods of the prior year. This increase was due primarily to higher transaction volume and growth in our BML portfolio of receivables from loans. The increase was partially offset by a reduction in our Marketplaces consumer protection program expense as a result of certain loss prevention programs and lower Marketplaces bad debt expense.

Amortization of Acquired Intangible Assets
From time to time we have purchased, and we expect to continue to purchase, assets and businesses. These purchase transactions generally result in the creation of acquired intangible assets with finite lives and lead to a corresponding increase in our amortization expense in periods subsequent to acquisition. We amortize intangible assets over the period of estimated benefit, using the straight-line method and estimated useful lives ranging from one to eight years. Amortization of acquired intangible assets is also impacted by our sales of assets and businesses and timing of acquired intangible assets becoming fully amortized.

Amortization of acquired intangible assets increased by $31 million and $71 million, or 58% and 73%, during the second quarter and first six months of 2012, respectively, compared to the same periods of the prior year due primarily to the impact of acquisitions, primarily GSI.

Interest and Other, Net

Interest and other, net, consists of interest earned on cash, cash equivalents and investments, as well as foreign exchange transaction gains and losses, our portion of operating results from investments accounted for under the equity method of accounting, investment gain/loss on acquisitions and interest expense consisting of interest charges on our outstanding commercial paper and debt securities and on the amounts, if any, drawn under our credit agreement. Interest and other income, net excludes interest expense on borrowings incurred to finance Bill Me Later's portfolio of loan receivables, which is included in cost of net revenues.

Interest and other, net increased $10 million and $38 million during the second quarter and first six months of 2012, respectively, compared to the same periods of the prior year. The increase in interest and other, net was due primarily to a favorable resolution of an indirect tax dispute, favorable impact from foreign currency activity and higher interest income,

29

partially offset by losses from investments accounted for under the equity method of accounting and higher interest expense.

Gain (Loss) on Divested Business

We incurred a gain on the divestiture of Rent.com of $118 million during the second quarter and first six months of 2012. We incurred a loss on the divestiture of certain GSI businesses of $256 million during the second quarter and first six months of 2011. We sold these businesses as they were not core to our long-term strategy.

Provision for Income Taxes

Our effective tax rate was 18.7% for the second quarter of 2012, compared to 2.7% for the same period in the prior year. The increase in our effective tax rate during the second quarter of 2012 compared to the same period of the prior year was due primarily to a tax benefit received in 2011 and the year-over-year unfavorable impact of discrete items related primarily to uncertain tax positions. The tax benefit was associated with the loss on the divestiture of certain GSI businesses and resulted in a 12 percentage point favorable impact to the effective tax rate.

Our effective tax rate was 17.8% for the first six months of 2012, compared to 11.6% for the same period in the prior year. The increase in our effective tax rate during the first six months of 2012 compared to the same period of the prior year was due primarily to the same factors noted above. The tax benefit was associated with the loss on the divestiture of certain GSI businesses and resulted in a four percentage point favorable impact to the effective tax rate.

From time to time, we engage in certain intercompany transactions and legal entity restructurings. We consider many factors when evaluating these transactions, including the alignment of our corporate structure with our organizational objectives and the operational and tax efficiency of our corporate structure, as well as the long-term cash flows and cash needs of our different businesses. These transactions may impact our overall tax rate and/or result in additional cash tax payments. The impact in any period may be significant. These transactions may be complex and the impact of such transactions on future periods may be difficult to estimate.

We are regularly under examination by tax authorities both domestically and internationally. We believe that adequate amounts have been reserved for any adjustments that may ultimately result from these examinations, although we cannot assure you that this will be the case given the inherent uncertainties in these examinations. Due to the ongoing tax examinations, we believe it is impractical to determine the amount and timing of these adjustments.

Liquidity and Capital Resources

Cash Flows

	Six Months Ended June 30,	
	2012	2011
	(In millions)	
Net cash provided by (used in):		
Operating activities	$1,299	$1,482
Investing activities	(1,474)	(3,805)
Financing activities	(434)	(166)
Effect of exchange rates on cash and cash equivalents	(44)	178
Net increase/(decrease) in cash and cash equivalents	$(653)	$(2,311)

Operating Activities

We generated cash from operating activities of $1.3 billion and $1.5 billion in the six months ended June 30, 2012 and June 30, 2011, respectively. Non-cash charges to earnings were $1.1 billion and $864 million in the six months ended June 30, 2012 and 2011, respectively. Non-cash charges to earnings include depreciation and amortization on our long-term assets, stock-based compensation and the provision for transaction and loan losses. The decrease in cash provided by operating activities during the six months ended June 30, 2012 compared to the same period of the prior year was due primarily to cash paid for income taxes in the first six months of 2012 of $639 million, which were primarily associated with the gain on the sale of our remaining equity interest in Skype in October 2011, compared to $136 million in the first six months of 2011.

Investing Activities

The net cash used in investing activities of $1.5 billion in the six months ended June 30, 2012 was due primarily to cash paid for the purchases of investments of $1.3 billion and purchases of property and equipment of $599 million, partially offset by proceeds of $629 million from the maturities and sale of investments and $144 million from the disposition of a business.

The net cash used in investing activities of $3.8 billion in the six months ended June 30, 2011 was due primarily to cash paid for the purchases of investments of $1.2 billion, acquisition of businesses of $2.8 billion and purchases of property and equipment of $388 million, partially offset by proceeds of $860 million from the maturities and sale of investments.

Financing Activities

The net cash used in financing activities of $434 million in the six months ended June 30, 2012 was due primarily to cash outflows of $595 million to repurchase common stock as well as cash paid for tax withholdings in the amount of $132 million related to net share settlements of restricted stock units and awards. These cash outflows were partially offset by $225 million from the issuance of common stock in connection with the exercise of stock options and $68 million of excess tax benefits from stock-based compensation.

The net cash used in financing activities of $166 million in the six months ended June 30, 2011 was due primarily to cash outflows of $781 million to repurchase common stock and $186 million to repay acquired debt, as well as cash paid for tax withholdings in the amount of $114 million related to net share settlements of restricted stock awards and units. These cash outflows were partially offset by proceeds of $700 million from additional borrowings under our commercial paper program, $156 million from the issuance of common stock in connection with the exercise of stock options and $59 million of excess tax benefits from stock-based compensation.

The negative effect of exchange rate movements on cash and cash equivalents during the six months ended June 30, 2012 was due to the strengthening of the U.S. dollar against other currencies, primarily the Euro. The positive effect of exchange rate movements on cash and cash equivalents during the six months ended June 30, 2011 was due to the weakening of the U.S. dollar against other currencies, primarily the Euro.

Stock Repurchases

In September 2010, our Board authorized a stock repurchase program that provides for the repurchase of up to $2 billion of our common stock, with no expiration from the date of authorization. In June 2012, our Board authorized an additional stock repurchase program that provides for the repurchase of up to $2 billion of our common stock, with no expiration from the date of authorization. These stock repurchase programs are intended to offset the impact of dilution from our equity compensation programs. During the six months ended June 30, 2012, we repurchased approximately $595 million of our common stock under our stock repurchase programs. As of June 30, 2012, approximately $2.3 billion remained for further repurchases of our common stock under our stock repurchase programs.

Shelf Registration Statement and Long-Term Debt

At June 30, 2012, we had an effective shelf registration statement on file with the Securities and Exchange Commission that allows us to issue various types of debt securities, such as fixed or floating rate notes, U.S. dollar or foreign currency denominated notes, redeemable notes, global notes, and dual currency or other indexed notes. Issuances under the shelf registration will require the filing of a prospectus supplement identifying the amount and terms of the securities to be issued. The registration statement does not limit the amount of debt securities that may be issued thereunder. Our ability to issue debt securities is subject to market conditions and other factors impacting our borrowing capacity, including our credit ratings and compliance with the covenants in our credit agreement.

We issued $1.5 billion of senior unsecured debt securities under a prior shelf registration statement in an underwritten public offering in 2010. These debt securities remain outstanding and consist of $400 million aggregate principal amount of 0.875% notes due 2013, $600 million aggregate principal amount of 1.625% notes due 2015 and $500 million aggregate principal amount of 3.250% notes due 2020.

Commercial Paper

We have a $2 billion commercial paper program pursuant to which we may issue commercial paper notes with maturities of up to 397 days from the date of issue in an aggregate principal amount of up to $2 billion at any time outstanding. As of June 30, 2012, $550 million aggregate principal amount of commercial paper was outstanding, the weighted average interest rate on those notes was 0.19% per annum and the weighted average remaining term on those notes was 79 days.

Credit Agreement
As of June 30, 2012, no borrowings or letters of credit were outstanding under our $3 billion credit agreement. As described above, we have a $2 billion commercial paper program and maintain $2 billion of available borrowing capacity under our credit agreement in order to repay commercial paper borrowings in the event we are unable to repay those borrowings from other sources when they become due. As a result, at June 30, 2012, $1 billion of borrowing capacity was available for other purposes permitted by the credit agreement.
Notes Payable and Capital Lease Obligations
In addition to the debt described above, as of June 30, 2012, we had notes payable of $16 million and capital lease obligations of $20 million.
Commitments
As of June 30, 2012, approximately $11 billion of unused credit was available to Bill Me Later accountholders. The individual lines of credit that make up this unused credit are subject to periodic review and termination by the chartered financial institution that is the issuer of Bill Me Later credit products based on, among other things, account usage and customer creditworthiness. Currently, when a consumer makes a purchase using a Bill Me Later credit product, the chartered financial institution extends credit to the consumer, funds the extension of credit at the point of sale and advances funds to the merchant. We subsequently purchase the receivables related to the consumer loans extended by the chartered financial institution and, as a result of the purchase, bear the risk of loss in the event of loan defaults. Although the chartered financial institution continues to own each customer account, we own the related receivable, and Bill Me Later is responsible for all servicing functions related to the account.
Liquidity and Capital Resource Requirements
As of June 30, 2012 and December 31, 2011, we had assets classified as cash and cash equivalents, as well as time deposits and fixed income securities classified as short-term and long-term investments, in an aggregate amount of $8 billion. As of June 30, 2012, this amount included assets of these types held outside the U.S. in certain of our foreign operations totaling approximately $7 billion. If these assets were distributed to the U.S., we may be subject to additional U.S. taxes in certain circumstances. We actively monitor the third-party depository institutions and money market funds that hold these assets, primarily focusing on the safety of principal and secondarily on yield on these assets. We diversify our cash and cash equivalents and investments among various financial institutions and money market funds in order to reduce our exposure should any one of these financial institutions or money market funds fail or encounter difficulties. To date, we have not experienced any material loss or lack of access to our invested cash, cash equivalents or short-term investments; however, we can provide no assurances that access to our invested cash, cash equivalents or short-term investments will not be impacted by adverse conditions affecting those depository institutions or money market funds or the financial markets generally. At any point in time we have funds in our operating accounts and customer accounts that are deposited with third party financial institutions. These balances in the U.S. may exceed the Federal Deposit Insurance Corporation (FDIC) insurance limits. While we monitor the cash balances in our operating accounts, these cash balances could be adversely impacted if the underlying financial institutions fail and could be subject to other adverse conditions in the financial markets.

To the extent that our Bill Me Later products become more widely available through improved and more comprehensive product integrations with eBay, PayPal and other channels, and as we further promote Bill Me Later products, customer adoption and usage of Bill Me Later products may expand. Any resulting growth in the portfolio of Bill Me Later loan receivables would increase our liquidity needs and any failure to meet those liquidity needs could adversely affect the Bill Me Later business. We currently fund the expansion of the Bill Me Later portfolio of loan receivables with borrowings and domestic and international cash resources.

We believe that our existing cash, cash equivalents and investments, together with cash expected to be generated from operations, borrowings available under our credit agreement and commercial paper program, and our access to capital markets will be sufficient to fund our operating activities, anticipated capital expenditures, Bill Me Later portfolio of receivables from loans and stock repurchases for the foreseeable future.
Off-Balance Sheet Arrangements

As of June 30, 2012, we had no off-balance sheet arrangements that have, or are reasonably likely to have, a current or future material effect on our consolidated financial condition, results of operations, liquidity, capital expenditures or capital resources.

In Europe, we have two cash pooling arrangements with a financial institution for cash management purposes. These arrangements allow for cash withdrawals from this financial institution based upon our aggregate operating cash balances held in Europe within the same financial institution (“Aggregate Cash Deposits”). These arrangements also allow us to withdraw amounts exceeding the Aggregate Cash Deposits up to an agreed-upon limit. The net balance of the withdrawals and the Aggregate Cash Deposits are used by the financial institution as a basis for calculating our net interest expense or income. As of June 30, 2012, we had a total of $5 billion in cash withdrawals offsetting our $5 billion in Aggregate Cash Deposits held within the same financial institution under these cash pooling arrangements.

Based on differences in regulatory requirements and commercial law in the jurisdictions where PayPal operates, PayPal holds customer balances either as direct claims against PayPal or as an agent or custodian on behalf of PayPal's customers. Customer funds held by PayPal as an agent or custodian on behalf of our customers are not reflected in our condensed consolidated balance sheet. These off-balance sheet funds totaled approximately $3 billion as of June 30, 2012 and December 31, 2011. These funds include funds held on behalf of U.S. customers that are deposited in bank accounts insured by the FDIC (subject to applicable limits). PayPal's California regulator, the California Department of Financial Institutions (DFI), recently notified PayPal that PayPal's current practice of holding the funds underlying U.S. customer balances as an agent on behalf of its customers, rather than as owner of those funds, causes PayPal to be in violation of the liquidity rules applicable to California money transmitter licensees. PayPal has requested the DFI to grant a waiver that would allow PayPal to continue to hold those funds as an agent or custodian on behalf of customers and still qualify those funds as liquid assets. The DFI has indicated that it cannot grant a waiver under its interpretation of current law and that PayPal must become compliant before the end of 2012. A change to direct ownership of these funds would result in these funds moving onto our consolidated balance sheet (along with the accompanying liabilities). Additionally, please see the information in "Part II - Item 1A: Risk Factors" under the caption "If our Payments business is found to be subject to or in violation of any laws or regulations, including those governing money transmission, electronic funds transfers, money laundering, terrorist financing, sanctions, consumer protection, banking and lending, it could be subject to liability, licensure and regulatory approval and may be forced to change its business practices."

Indemnification Provisions

In the ordinary course of business, we have included limited indemnification provisions in certain of our agreements with parties with which we have commercial relations, including our standard marketing, promotions and application-programming-interface license agreements. Under these contracts, we generally indemnify, hold harmless and agree to reimburse the indemnified party for losses suffered or incurred by the indemnified party in connection with claims by a third party with respect to our domain names, trademarks, logos and other branding elements to the extent that such marks are applicable to our performance under the subject agreement. In certain cases, we have agreed to provide indemnification for intellectual property infringement. GSI has provided in many of its major ecommerce agreements an indemnity for other types of third-party claims, which are indemnities mainly related to various intellectual property rights, and we have provided similar indemnities in a limited number of agreements for our other businesses. In our PayPal business, we have provided an indemnity to our payment processors in the event of certain third-party claims or card association fines against the processor arising out of conduct by PayPal or PayPal customers. In connection with the sale of Skype Technologies, S.A. (Skype) in November 2009, we made certain customary warranties to the buyer in the purchase agreement. Our liability to the buyer for inaccuracies in these warranties is generally subject to certain limitations. With respect to certain specified litigation matters involving Skype that were pending as of the closing of the transaction, we also agreed, among other things, to bear 50% of the cost of any monetary judgment that is rendered in respect of those matters. It is not possible to determine the maximum potential loss under these indemnification provisions due to our limited history of prior indemnification claims and the unique facts and circumstances involved in each particular provision. To date, losses recorded in our statement of income in connection with our indemnification provisions have not been significant, either individually or collectively.

Item 3: Quantitative and Qualitative Disclosures About Market Risk

The information in this section should be read in connection with the information on financial market risk related to changes in interest rates and non-U.S. currency exchange rates in Part II, Item 7A, "Quantitative and Qualitative Disclosures About Market Risk," in our Annual Report on Form 10-K for the year ended December 31, 2011. Our market risk profile has not changed significantly during the first six months of 2012.

Interest Rate Risk

The primary objective of our investment activities is to preserve principal while at the same time improving yields without significantly increasing risk. To achieve this objective, we maintain our portfolio of cash equivalents and short-term

and long-term investments in a variety of available for sale securities, including government and corporate securities and money market funds. As of June 30, 2012, approximately 48% of our total cash and investment portfolio was held in bank deposits and money market funds. As such, changes in interest rates will impact interest income. Fixed rate securities may have their fair market value adversely affected due to a rise in interest rates, and we may suffer losses in principal if we are forced to sell securities that have declined in market value due to changes in interest rates. Additionally, changes in interest rates will impact our interest rate sensitive credit agreement and the interest rate on our commercial paper borrowings, and accordingly will impact interest expense or cost of net revenues.
As of June 30, 2012, we held no direct investments in auction rate securities, collateralized debt obligations, structured investment vehicles or mortgage-backed securities.

Investment Risk

As of June 30, 2012, our cost and equity method investments totaled $175 million, which represented approximately 2% of our total cash and investment portfolio. We review our investments for impairment when events and circumstances indicate a decline in fair value of such assets below carrying value is other-than-temporary. Our analysis includes a review of recent operating results and trends, recent sales/acquisitions of the investee securities and other publicly available data.

Equity Price Risk

We are exposed to equity price risk on marketable equity instruments due to market volatility. At June 30, 2012, the total fair value of our marketable equity instruments (primarily related to our equity holdings in MercadoLibre) was $616 million, which represented approximately 7% of our total cash and investment portfolio.

Foreign Currency Risk

We have significant operations internationally that are denominated in foreign currencies, primarily the Euro, British pound, Korean won and Australian dollar, subjecting us to foreign currency risk which may adversely impact our financial results. We transact business in various foreign currencies and have significant international revenues as well as costs. In addition, we charge our international subsidiaries for their use of intellectual property and technology and for certain corporate services provided by eBay and by PayPal.

We have a foreign exchange exposure management program whose objectives are to identify material foreign currency exposures, manage these exposures and reduce the potential effects of currency fluctuations on our reported consolidated cash flow and results of operations through the purchase of foreign currency exchange contracts. These foreign currency exchange contracts are accounted for as derivative instruments; for additional details related to our derivative instruments, please see “Note 7 – Derivative Instruments” to the condensed consolidated financial statements included in this report.

European Debt Exposures

We actively monitor our exposure to the European markets, including the impact of sovereign debt issues associated with Greece, Ireland, Portugal, Italy and Spain. As of June 30, 2012, we did not have any direct or indirect investments in the sovereign debt of these countries or in debt securities issued by corporations or financial institutions organized in these countries. We maintain a small number of operating bank accounts with Spanish and Italian banks that have balances that we do not consider material.

Item 4: Controls and Procedures

(a) Evaluation of disclosure controls and procedures. Based on the evaluation of our disclosure controls and procedures (as defined in Securities Exchange Act of 1934 Rules 13a-15(e) and 15d-15(e)) required by Securities Exchange Act Rules 13a-15(b) or 15d-15(b), our Chief Executive Officer and our Chief Financial Officer have concluded that as of the end of the period covered by this report, our disclosure controls and procedures were effective.

(b) Changes in internal controls. There were no changes in our internal control over financial reporting that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II: OTHER INFORMATION

Item 1: Legal Proceedings

The information set forth under “Note 9 — Commitments and Contingencies — Litigation and Other Legal Matters” to the condensed consolidated financial statements included in Part I, Item 1 of this report is incorporated herein by reference.

Item 1A: RISK FACTORS

Risk Factors That May Affect Results of Operations and Financial Condition

Our operations and financial results are subject to various risks and uncertainties that could adversely affect our business, financial condition, results of operations and cash flows, as well as the trading price of our common stock.

Our operating results have varied on a quarterly basis during our operating history. Our operating results may fluctuate significantly as a result of a variety of factors, many of which are outside our control. Factors that may affect our operating results include risks described elsewhere in this section and the following:

- general economic conditions, including the possibility of a prolonged period of limited economic growth or possible economic decline in the U.S. and Europe; adverse effects of the ongoing sovereign debt crisis in Europe, including increased Euro currency exchange rate volatility, the negative impact of the crisis and related austerity measures on European economic growth, potential negative spillover effects to the rest of the world, the “contagion” risk of the crisis spreading to additional countries in Europe, the possibility that one or more countries leaves the Euro zone and re-introduces its individual currency, and, in more extreme circumstances, the possible dissolution of the Euro currency; disruptions to the credit and financial markets in Europe, the U.S., and elsewhere; contractions or limited growth in consumer spending or consumer credit; and adverse economic conditions that may be specific to the Internet, ecommerce and payments industries; the primary and secondary effects of previously announced and possible future changes to our pricing, products and policies, including, among other changes, restrictions or holds on payments made to certain sellers or in connection with certain transactions; changes to our dispute resolution process; upgrades to eBay checkout services, including the introduction of a new eBay shopping cart/basket that enables buyers to add items from multiple sellers and pay in a single checkout; and changes to our fee structure, including new requirements to qualify for "eBay Trusted Seller" discounts;
- our ability to manage the rapid shift from online commerce and payments to mobile commerce and payments;
- our ability to improve the quality of the user experience on our websites and through mobile devices (including our customer support in the event of a problem) in light of the improved quality generally of the user experience offered by competitive merchants;
- our ability to retain an active user base, attract new users, and encourage existing users to list items for sale, purchase items through our websites and mobile platforms, or use our payment services, especially when consumer spending is weak;
- consumer confidence in the safety and security of transactions using our websites or technology and the effect of any changes in our practices and policies on such confidence;
- our ability to manage the costs of and effectively implement our user protection programs;
- our ability to comply with existing and new laws and regulations, especially those affecting our Payments business, as we expand the range and geographical scope of our products and services and as we grow larger, including those laws and regulations discussed below under the caption "If our Payments business is found to be subject to or in violation of any laws or regulations, including those governing money transmission, electronic funds transfers, money laundering, terrorist financing, sanctions, consumer protection, banking and lending, it could be subject to liability, licensure and regulatory approval and may be forced to change its business practices;"
- new laws or regulations (such as those that may stem from the proposed Anti-Counterfeiting Trade Agreement (ACTA) and Trans-Pacific Partnership Agreement (TPP) and the proposed revisions to the European Data Directive)

and interpretations of existing laws or regulations, including national court interpretations of the European Court of Justice's decision in the L'Oréal case (see “Item 1: Legal Proceedings” above), that impose liability on us for the actions of our users or otherwise harm our business models, especially as we become more actively involved in various aspects of transactions on our platforms;

- regulatory and legal actions imposing obligations on our businesses or our users, including the injunction related to certain cosmetic and perfume brands (see “Item 1: Legal Proceedings” above);
- the impact on PayPal or Bill Me Later of regulations enacted pursuant to new laws regulating financial institutions, including the Dodd-Frank Wall Street Reform and Consumer Protection Act in the U.S.;

35

- our ability to manage the costs of compliance with existing and new laws and regulations that affect our businesses;
- the volume, velocity, size, timing, monetization, and completion rates of transactions using our websites or technology;
- our ability to reduce the loss of active buyers and sellers and increase activity of the users of our Marketplaces business, especially with respect to our top buyers and sellers, and increase activity of PayPal account holders, particularly in merchant services business;
- our ability to develop product enhancements, programs, and features on different platforms and mobile devices at a reasonable cost and in a timely manner, including our initiatives to make PayPal solutions available at the retail point of sale;
- changes to our use of advertising on our sites;
- our ability to upgrade and develop our systems (including the migration to GSI's new technology platform), infrastructure and customer service capabilities to accommodate growth and to improve the functionality and reliability of our websites and services at a reasonable cost while maintaining 24/7 operations;
- the actions of our competitors, including the introduction of new stores, channels, sites, applications, services, products and functionality;
- the costs and results of litigation or regulatory actions that involve us;
- technical difficulties or service interruptions involving our websites or services provided to us or our users by third parties;
- our ability to manage the transaction loss rate in our Marketplaces, Payments and GSI ecommerce services businesses;
- our ability to manage funding costs, credit risk and interest-rate risk associated with our Bill Me Later business;
- our ability to successfully and cost-effectively integrate and manage businesses that we acquire, including GSI;
- the amount and timing of operating costs and capital expenditures relating to the maintenance and expansion of our businesses, operations and infrastructure;
- our ability to comply with the requirements of entities whose services are required for our operations, such as payment card networks and banks;
- the cost and availability of traditional and online advertising, and the success of our brand building and marketing campaigns;
- our ability to attract new personnel in a timely and effective manner and to retain key employees;
- the continued healthy operation of our technology suppliers and other parties with which we have commercial relations;
- continued consumer acceptance of the Internet and emerging consumer acceptance of mobile devices as a medium for ecommerce and payments in the face of increasing publicity about fraud, spoofing, phishing, viruses, spyware, malware and other dangers; and
- macroeconomic and geopolitical events affecting commerce generally.

It is difficult for us to forecast the level or source of our revenues or earnings accurately. In view of the rapidly evolving nature of our business, we believe that period-to-period comparisons of our operating results may not be meaningful, and you should not rely upon them as an indication of future performance. We do not have backlog, and substantially all of our net revenues each quarter come from transactions involving sales or payments during that quarter. Due to the inherent difficulty in forecasting revenues, it is also difficult to forecast income statement expenses as a percentage of net revenues. Quarterly and annual income statement expenses as a percentage of net revenues may be significantly different from historical or projected rates. Our operating results in one or more future quarters may fall below the expectations of securities analysts and investors. In that event, the trading price of our common stock would almost certainly decline.
We invest heavily in technology, marketing and promotion, customer support, protection programs and further development of the operating infrastructure for our core and non-core operations. Some of this investment entails long-term contractual commitments. As a result, we may be unable to adjust our spending rapidly enough to compensate for any unexpected revenue shortfall, which may harm our profitability.

Growth rates of our Marketplaces businesses in some of our most established markets have been slower than that for ecommerce generally and have declined in certain periods. The growth of Internet users is slowing in many countries where we have a significant presence. Despite our efforts to stem our loss of share in these and other markets, we may not be successful. As our growth rates in established markets slow, we will increasingly need to focus on keeping existing Marketplaces users (especially our top buyers and sellers) and PayPal account holders (especially in our merchant services business) active and increasing their activity level on our websites and mobile platforms and their use of our payment services, respectively, in order to continue to grow those respective businesses. The growth of Internet users is accelerating in some countries and regions where we do not have a significant presence (e.g., Brazil/Latin America, Russia, China and certain developing countries in which we do not have a meaningful (or, in some cases, any) domestic business). If we are unable to establish our businesses

and drive adoption of our services in such markets, our future growth would be negatively impacted.
Our Marketplaces business continues to face increased competitive pressure both online and offline. In particular, the competitive norm for, and the expected level of service from, Internet ecommerce websites has significantly increased, due to, for example, improved user experience, greater ease of buying goods, lower (or no) shipping costs, faster shipping times and more favorable return policies. If we are unable to change our services in ways that reflect the changing demands of the ecommerce marketplace, particularly the higher growth of sales of fixed-price items and higher service levels (some of which depend on services provided by sellers on our platforms), our business will suffer.
We have announced changes to our Marketplaces business that are intended to drive more sales and improve seller efficiency and buyer experiences. For example, in the U.S., the U.K. and Canada, we may request that PayPal place temporary holds on seller funds in certain instances (e.g., for sellers with a limited selling history or below-standard performance ratings), which is intended to help improve seller performance and increase buyer satisfaction. We may expand the scope of such programs in the future and introduce and implement additional programs with similar aims in different businesses and geographies. Some of the changes that we have announced to date have been controversial with, and led to dissatisfaction among, our sellers, and additional changes that we announce in the future may also be negatively received by some of our sellers. This may not only impact the supply of items listed on our websites, but because many sellers also buy from our sites, it may adversely impact demand as well. Given the number of recent changes that we have made to our policies and pricing, it may take our sellers some time to fully assess and adjust to these changes, and sellers may elect to reduce volume on our sites while making such assessments and adjustments or in response to these changes. If any of these changes cause sellers to move their business (in whole or in part) away from our websites or otherwise fail to improve gross merchandise volume or the number of successful listings, our operating results and profitability will be harmed.
We believe that the mix of sales under our traditional auction-style listing format and fixed-price listing format will continue to shift towards our fixed-price format. Accordingly, we have eliminated some of the features related to our traditional auction-style format and expect others will continue to become less meaningful to, and used less frequently by, our sellers, resulting in a corresponding decrease in revenues from those features. We also expect that the costs associated with our seller discount programs will increase as more sellers become eligible for such discounts. In addition, because a large percentage of PayPal transactions originate on the eBay platform, declines in growth rates in major Marketplaces markets also adversely affect PayPal's growth. The expected future growth of our PayPal, GSI, StubHub and our other lower margin businesses may also cause downward pressure on our profit margins because those businesses have lower gross margins than our Marketplaces platforms.
The sluggish economy and the sovereign debt crisis could harm our business.
Our Marketplaces, Payments and GSI ecommerce services businesses are dependent on consumer purchases, and our GSI business is also impacted by the offline businesses of our GSI clients. The economic downturn resulted in reduced buyer demand and reduced selling prices and the slow recovery in the U.S. and the impact of the sovereign debt crisis in Europe may reduce the volume and prices of purchases on our Marketplaces platforms and the volume and prices of transactions paid for using our Payment services and the online and offline businesses of our GSI clients, any of which would adversely affect our business. The sovereign debt crisis could also have a negative and adverse impact on companies with which we do business, which in turn could have an adverse effect on our business.
We are exposed to fluctuations in currency exchange rates and interest rates.
Because we generate substantial revenues outside the U.S. but report our financial results in U.S. dollars, we face exposure to adverse movements in currency exchange rates. In connection with its multi-currency service, PayPal fixes exchange rates twice per day, and may face financial exposure if it incorrectly fixes the exchange rate or if exposure reports are delayed. Given that PayPal also holds some corporate and customer funds in non-U.S. currencies, its financial results are affected by the translation of these non-U.S. currencies into U.S. dollars. In addition, the results of operations of many of our internationally focused websites are exposed to foreign exchange rate fluctuations as the financial results of the applicable subsidiaries are translated from the local currency into U.S. dollars upon consolidation. If the U.S. dollar weakens against foreign currencies, the translation of these foreign currency denominated transactions will result in increased revenues, operating expenses and net income. Similarly, if the U.S.

dollar strengthens against foreign currencies, our translation of foreign currency denominated transactions will result in lower net revenues, operating expenses and net income. If the U.S. dollar continues to strengthen against major European currencies (e.g., the Euro and British pound) whether because of the ongoing sovereign debt crisis in Europe or worsening economic conditions, our revenues and operating results would be adversely impacted. For the six months ended June 30, 2012, foreign currency movements relative to the U.S. dollar negatively impacted net revenues of $6.7 billion by approximately $122 million (net of a $26 million positive impact from hedging activities

37

included in PayPal's net revenue) compared to the prior year. As exchange rates vary, net revenues and other operating results, when translated, may differ materially from expectations. In particular, to the extent the U.S. dollar strengthens against the Euro, British pound, Korean won, Australian dollar or Canadian dollar, our foreign revenues and profits will be reduced as a result of these translation adjustments. While from time to time we enter into transactions to hedge portions of our foreign currency translation exposure, it is impossible to predict or completely eliminate the effects of this exposure. In addition, to the extent the U.S. dollar strengthens against the Euro, the British pound, the Australian dollar or other currencies, cross-border trade related to purchases of dollar-denominated goods (or goods from Asia-Pacific countries whose currencies tend to follow the dollar) by non-U.S. purchasers will likely decrease, and that decrease will likely not be offset by a corresponding increase in cross-border trade involving purchases by U.S. buyers of goods denominated in other currencies, which would adversely affect our business. In addition, we face exposure to fluctuations in interest rates. Relatively low interest rates have continued to limit our investment income, including income we earn on PayPal customer balances.

Bill Me Later's operations depend on lending services provided by an unaffiliated lender.

In November 2008, we acquired Bill Me Later, a company that facilitates credit services offered by an unaffiliated bank. Bill Me Later is neither a chartered financial institution nor is it licensed to make loans in any state. Accordingly, Bill Me Later must rely on a bank or licensed lender to issue the Bill Me Later credit products and extend credit to customers to offer the Bill Me Later service. Currently, when a consumer makes a purchase using a Bill Me Later credit product, the chartered financial institution extends credit to the consumer, funds the extension of credit at the point of sale and advances funds to the merchant. We subsequently purchase the receivables related to the extensions of credit made by the chartered financial institution and, as a result of the purchase, bear the risk of loss in the event of loan defaults. Although the chartered financial institution continues to own each customer account, we own the related receivable and Bill Me Later is responsible for all servicing functions related to the account.

In September 2010, WebBank became the issuer of the Bill Me Later credit products. WebBank is an industrial bank chartered by the State of Utah. Any termination or interruption of WebBank's ability to lend could result in our being unable to originate any new transactions for the Bill Me Later service, which would require us to either reach a similar arrangement with another chartered financial institution, which may not be available on favorable terms, if at all, or to obtain our own bank charter, which would be a time-consuming and costly process and would subject us to a number of additional laws and regulations, compliance with which would likely be burdensome.

A lawsuit was filed against Bill Me Later, PayPal and eBay in the U.S. District Court for the Northern District of California, alleging that in its relationship with the chartered financial institution, Bill Me Later is acting as the true lender to customers in violation of various California laws, including the state's usury law. The court dismissed the usury claims in December 2010, but breach of contract and other claims remain. WebBank requested to intervene in the action and has been added as a party to the action, and in October 2011, the court transferred the case to the U.S. District Court for the District of Utah. The Utah Court allowed plaintiffs the opportunity to amend the complaint, the complaint was amended and plaintiffs re-alleged the usury claims previously dismissed. We and WebBank have filed a motion to dismiss the lawsuit. We believe that plaintiffs' allegations are without merit and intend to defend ourselves vigorously. However, this area of law is uncertain and if the lawsuit is successful, Bill Me Later may be required to change its methods of operations, pay very substantial damages and reduce some of its charges and fees, which would adversely affect our business.

If our Payments business is found to be subject to or in violation of any laws or regulations, including those governing money transmission, electronic funds transfers, money laundering, terrorist financing, sanctions, consumer protection, banking and lending, it could be subject to liability, licensure and regulatory approval and may be forced to change its business practices.

Our Payments business is subject to various laws and regulations in the U.S. and other countries where it operates, including those governing money transmission, electronic funds transfers, money laundering, terrorist financing, sanctions, consumer protection, banking and lending. The legal and regulatory requirements that apply to our Payments business vary in the markets where we operate. While PayPal has a compliance program focused on compliance with applicable laws and regulations and has significantly increased the resources of that program in the last several years, there can be no assurance that we will not be subject to fines or other enforcement actions in one or more jurisdictions or be required to make changes to our business practices or compliance programs to comply in the future.

While PayPal currently allows its customers with credit cards to send payments from 190 markets, PayPal only allows customers in 110 of those markets (including the U.S.) to receive payments, in some cases with significant restrictions on the manner in which customers can withdraw funds. These limitations may affect PayPal's ability to grow in these markets. Of the 190 markets whose residents can use the PayPal service, 31 (27 countries plus four French overseas departments) are members of the European Union, or EU. Since 2007, PayPal has provided localized versions of its service to customers in the EU through PayPal (Europe) S.à r.l. et Cie, SCA, a wholly-owned subsidiary of PayPal that is licensed and subject to regulation as a bank in Luxembourg by the Commission de Surveillance du Secteur Financier (CSSF). Accordingly, PayPal (Europe) is subject to significant fines or other enforcement action if it violates the disclosure, reporting, anti-money laundering, capitalization, funds management, corporate governance, information security, sanctions or other requirements imposed on Luxembourg banks. Any fines or other enforcement actions imposed by the Luxembourg regulator could adversely affect PayPal's business. PayPal (Europe) implements its localized services in EU countries through a “passport” notification process through the Luxembourg regulator to regulators in other EU member states pursuant to EU Directives, and has completed the “passport” notification process in all EU member countries. The regulators in these countries could notify PayPal (Europe) of local consumer protection laws that will apply to its business, in addition to Luxembourg consumer protection law, and could also seek to persuade the Luxembourg regulator to order PayPal (Europe) to conduct its activities in the local country through a branch office. These or similar actions by these regulators could increase the cost of, or delay, PayPal's plans for expanding its business in EU countries. In addition, national interpretations of regulations implementing the EU Payments Service Directive, which established a new regulatory regime for payment services providers, may be inconsistent, which could make compliance more costly and operationally difficult to manage.

In 2011, we began implementing a new payment process in Germany and Austria in which eBay intermediated payments, receiving funds directly from buyers for items purchased from newly registered sellers on the localized eBay websites in those countries and subsequently paying the sellers upon shipment of the items. The German Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin) and the Austrian Finanzmarktaufsicht (FMA) subsequently determined that eBay was required to obtain a license in order to introduce the new payment method. eBay's payment processing unit is based in Luxembourg and is governed by the CSSF, which had advised that there was no need for such a license. In accordance with the BaFin and FMA positions, eBay has agreed to stop intermediating payments and is working with the CSSF with respect to obtaining an appropriate license.

In Australia, PayPal serves its customers through PayPal Australia Pty. Ltd., which is licensed by the Australian Prudential Regulatory Authority as a purchased payment facility provider, which is a type of authorized depository institution. Accordingly, PayPal Australia is subject to significant fines or other enforcement action if it violates the disclosure, reporting, anti-money laundering, capitalization, corporate governance or other requirements imposed on Australian depository institutions. In China, PayPal is affiliated with Shanghai Wangfuyi Information Technology Ltd., which is licensed as an Internet Content Provider and operates a payments service only for Chinese customers and only for transactions denominated in Chinese currency. The People's Bank of China (PBOC) has enacted regulations to establish a new type of license, called a Payment Clearing Organization (PCO) license, which will be required for non-bank payment services. The PBOC regulations leave unclear whether a foreign-owned company such as PayPal can control or invest in a Payment Clearing Organization, and whether Wangfuyi or PayPal's wholly-owned subsidiary in China would be eligible to obtain a PCO license.

To date, PayPal has obtained licenses to operate as a money transmitter in 42 U.S. states, the District of Columbia and Puerto Rico. PayPal is also licensed as an escrow agent in one U.S. state. PayPal is applying for money transmitter licenses in five additional states to facilitate its planned offering of payment services at the retail point of sale. The two remaining U.S. states do not currently regulate money transmitters. As a licensed money transmitter, PayPal is subject to restrictions on its investment of customer funds, reporting requirements, bonding requirements, and inspection by state regulatory agencies. If PayPal were found to be in violation of money services laws or regulations, PayPal could be subject to liability and/or additional restrictions, forced to cease doing business with residents of certain states, forced to change its business practices, or required to obtain additional licenses or regulatory approvals that could impose a substantial cost on PayPal. Any change to PayPal's business practices that makes the service less attractive to customers or prohibits its use by residents of a particular jurisdiction could also decrease the velocity of trade on eBay and websites operated by GSI's clients that accept PayPal as a form of payment, which would further harm our business. PayPal's California regulator, the California Department of Financial Institutions (DFI), recently notified PayPal that PayPal's current practice of holding the funds underlying U.S. customer balances as an agent on behalf of its customers, rather than as owner of those funds, causes PayPal to be in violation of the liquidity rules applicable to California money transmitter licensees. PayPal has established this current practice in part to maintain potential eligibility of those funds for pass-through Federal Deposit Insurance Corporation (FDIC) insurance coverage when those funds are placed in U.S. bank accounts. PayPal has requested the DFI to grant a waiver that would allow PayPal to continue to hold those funds as an agent or custodian on behalf of customers and still qualify those funds as liquid assets. The DFI has indicated that it cannot grant a waiver under its interpretation of current law and that PayPal must become compliant before the end of 2012. A change to direct ownership will likely disqualify the funds from pass-through FDIC insurance, and could also result in decreased revenue to PayPal if it decides to shift the funds from interest-bearing bank accounts to securities that bear lower interest rates. Any potential decrease in revenue to PayPal resulting from this change is not expected to be material. This would also result in these funds, which are currently not reported as assets owned by PayPal on our consolidated balance sheet, moving onto our consolidated balance sheet (along with the accompanying liabilities). For additional information, please see "Part I - Item 2: Management's Discussion and Analysis of Financial Condition and Results of Operations" under the caption "Off-Balance Sheet Arrangements," above. As of June 30, 2012, these funds totaled approximately $3 billion.

In markets other than the U.S., the EU, Australia, the China domestic business and Brazil, PayPal serves its customers through PayPal Private Ltd., a wholly-owned subsidiary of PayPal that is based in Singapore. PayPal Private Ltd. is regulated in Singapore as a stored value issuer. In many of these markets, it is not clear whether PayPal's Singapore-based service is subject only to Singaporean law or, if it were subject to local laws, whether such local law would require a payment processor like PayPal to be licensed as a bank or financial institution or otherwise. In such markets, the business may rely on partnerships with local banks to process payments and conduct foreign exchange in local currency. Local regulators who do not have direct jurisdiction over Singapore-based PayPal Private Ltd. may use their local regulatory power to slow or halt payments to local merchants conducted through the local banking partner. Such regulatory actions impacting local banking partner arrangements could impose substantial costs and involve considerable delay to the provision or development of PayPal services in that market, or could prevent PayPal from providing any services in a given market. The Reserve Bank of India has asserted that PayPal's previous offering of payment services to customers outside of India to send personal, non-commercial payments to recipients in India required a license from the Reserve Bank. For a period of time in 2010, the Reserve Bank directed the Indian affiliate of PayPal's processing bank to suspend withdrawals to the Indian bank accounts of PayPal customers for both personal and business customers. PayPal has ended personal non-commercial payments to and from Indian accounts and has ended the ability of Indian sellers to spend payments they receive, and has also stopped offering certain commercial payments between Indian buyers and Indian sellers. In November 2010, the Reserve Bank of India issued guidelines to Indian banks on the requirements for processing export-related transactions for online payment gateway service providers such as PayPal, including a limitation on the amount of individual transactions to no more than $500 (increased in October 2011 to $3,000). The Reserve Bank may again impose a suspension if it is not satisfied with PayPal's and its partner bank's actions to comply with these guidelines. In the event of any non-compliance, PayPal could be subject to fines from the Reserve Bank, and PayPal's prospects for future business in India, both cross-border and domestic, could be materially and adversely affected.

Even if PayPal is not currently required to be licensed in some jurisdictions, future localization or targeted marketing of PayPal's service or expansion of the financial products offered by PayPal (whether alone, through a commercial alliance or through an acquisition) in those countries could subject PayPal to additional licensure requirements, laws and regulations and increased regulatory scrutiny, any of which may harm PayPal's business. For example, PayPal will be required to obtain licenses in Japan and Russia to expand its services in those countries, and has applied for such licenses. There can be no assurance that PayPal will be able to obtain such licenses. Even if PayPal were able to obtain such licenses, there would be substantial costs involved in maintaining such licenses, and PayPal would be subject to fines or other enforcement action if it violates disclosure, reporting, anti-money laundering, capitalization, corporate governance or other requirements of such licenses. These factors could impose substantial costs and involve considerable delay to the provision or development of PayPal's products. Delay or failure to receive such a license or regulatory approval could require PayPal to change its business practices or features in ways that would adversely affect PayPal's expansion plans, and force PayPal to suspend providing products and services to customers in one or more countries.

PayPal is also subject to various anti-money laundering and counter-terrorist financing laws and regulations around the world that prohibit, among other things, its involvement in transferring the proceeds of criminal activities. PayPal is focused on compliance with these laws and regulations and has programs designed to comply with new and existing legal and regulatory requirements. However, any errors, failures or delays in complying with federal, state or foreign anti-money laundering and counter-terrorist financing laws could result in significant criminal and civil lawsuits, penalties and forfeiture of significant assets or other enforcement actions. In the U.S., PayPal is subject to regulations that require it to report, within required timeframes, suspicious activities involving transactions of $2,000 or more, and may be required to obtain and keep more detailed records on the senders and recipients in certain transfers of $3,000 or more. New regulations on prepaid access programs which took full effect in March 2012 require PayPal to take additional steps to verify the identity of customers who pre-fund a PayPal balance. U.S. regulators have increased scrutiny of compliance with these obligations. Existing and new regulations may require PayPal to revise further its compliance program, including the procedures it uses to verify the identity of its customers and to monitor international and domestic transactions.

Several countries in which PayPal is regulated, including Australia, Luxembourg and Singapore, have implemented new anti-money laundering and counter-terrorist financing laws and regulations, and PayPal has had to make changes to its procedures in response. In November 2009, the Australian anti-money laundering and counter-terrorist financing regulator (AUSTRAC) accepted an enforceable undertaking from PayPal Australia pursuant to which PayPal Australia agreed, among other things, to appoint an independent auditor to assess PayPal Australia's anti-money laundering compliance policies and procedures and issue a report identifying any unremediated deficiencies accompanied by a plan by PayPal to remedy any such deficiencies. In the enforceable undertaking, AUSTRAC expressed concern that PayPal Australia did not have systems and controls in place to manage adequately its money laundering and terrorist financing risk. In September 2010, the independent auditor completed its review and issued its report, and PayPal Australia submitted a remediation plan, which has been accepted by AUSTRAC. PayPal Australia has invested in improvements to its anti-money laundering and counter-terrorist financing systems, policies and operations as part of its remediation plan. In addition, PayPal Australia is required to obtain additional information from customers, verify that information, and monitor its customers' activities more closely. As PayPal continues to localize its services in additional jurisdictions, it could be required to meet standards similar to or more burdensome than those in Australia. The European Commission has also announced a consultation process to consider revisions to the European Anti-Money Laundering Directive. These requirements could impose significant costs on PayPal, cause delay to other planned product improvements, make it more difficult for new customers to join its network and reduce the attractiveness of its products.

Although there have been no definitive interpretations to date, PayPal has taken actions as though its service is subject to the Electronic Fund Transfer Act and Regulation E of the U.S. Federal Reserve Board. Under such regulations, among other things, PayPal is required to provide advance disclosure of changes to its service, to follow specified error resolution procedures and to reimburse consumers for losses from certain transactions not authorized by the consumer. PayPal seeks to pass most of these losses on to the relevant merchants, but PayPal incurs losses if the merchant does not have sufficient funds in its PayPal account. Additionally, even technical violations of these laws can result in penalties of up to $1,000 for each non-compliant transaction or up to $500,000 per violation in any class action, and we could also be liable for plaintiffs' attorneys' fees. In the second quarter of 2010, two putative class-action lawsuits (Devinda Fernando and Vadim Tsigel v. PayPal, Inc. and Moises Zepeda v. PayPal, Inc.) were filed in the U.S. District Court in the Northern District of California. These lawsuits contain allegations related to violations of aspects of the Electronic Fund Transfer Act and Regulation E and violations of a previous settlement agreement related to Regulation E, and/or allege that PayPal improperly held users' funds or otherwise improperly limited users' accounts. These lawsuits seek damages as well as changes to PayPal's practices among other remedies. A determination that there have been violations of the Electronic Fund Transfer Act, Regulation E or violations of other laws relating to PayPal's practices could expose PayPal to significant liability. Any changes to PayPal's practices resulting from these lawsuits could require PayPal to incur significant costs and to expend substantial resources, which could delay other planned product launches or improvements and further harm our business.

In January 2012, the Consumer Financial Protection Bureau finalized new rules under Regulation E, mandated by the Dodd-Frank Wall Street Reform and Consumer Protection Act, which will require PayPal, starting in February 2013, to provide additional disclosures, error resolution rights and cancellation rights to U.S. consumers who make international remittance payments. These new requirements could increase our costs of processing international payments and could adversely affect our business.

Our Bill Me Later service is similarly subject to a variety of laws and regulations. Although we do not originate loans under the Bill Me Later service, we do purchase receivables related to the consumer loans extended by the bank which originates them. One or more jurisdictions may conclude that the eBay company which purchases those receivables is a lender or money transmitter or loan broker, which could subject us to liability or regulation in such jurisdictions. As described under the caption “Bill Me Later's operations depend on lending services provided by an unaffiliated lender” above, a lawsuit was filed against Bill Me Later in the U.S. District Court for the Northern District of California alleging that in its relationship with the former issuer of the Bill Me Later credit products, Bill Me Later was acting as the true lender to customers in violation of various California laws, including the state's usury law. Additionally, federal regulators could mandate changes to the relationship between us and the issuing bank of the Bill Me Later credit products. Any termination or interruption of the issuing bank's lending services to consumers could result in an interruption of Bill Me Later services, as described under the caption “Bill Me Later's operations depend on lending services provided by an unaffiliated lender” above.

Given that our Payments business is subject to regulations in the manner described above, any determination that we have not properly complied with laws and regulations or any instances in which we are criminally indicted or found to have violated a criminal statute or regulation could adversely impact our regulatory status in one or more jurisdictions, which would harm our business.

The listing or sale by our users of pirated or counterfeit items may harm our business.

We have received in the past, and we anticipate receiving in the future, communications alleging that certain items listed or sold through our service by our users infringe third-party copyrights, trademarks and trade names, or other intellectual property rights. See “Item 1: Legal Proceedings” above. Although we have sought to work actively with the owners of intellectual property rights to eliminate listings offering infringing items on our websites, some rights owners have expressed the view that our efforts are insufficient. Content owners and other intellectual property rights owners have actively asserted their purported rights against online companies, including eBay. Allegations of infringement of intellectual property rights have resulted in threatened and actual litigation against us from time to time by rights owners, including litigation brought by luxury brand owners such as Tiffany & Co. in the U.S.; Rolex S.A. and Coty Prestige Lancaster Group GmbH in Germany; Louis Vuitton Malletier and Christian Dior Couture in France; and L'Oréal SA, Lancôme Parfums et Beauté & Cie and Laboratoire Garnier & Cie in several European countries. The plaintiffs in these cases seek to hold eBay liable for alleged counterfeit items listed on our sites by third parties; for "tester" and other consumer products labeled in a manner to prevent resale and for unboxed and other allegedly nonconforming products in each case listed on our sites by third parties; for the alleged misuse of trademarks or copyrights in listings or otherwise on our sites and in connection with paid search advertisements; for alleged violations of selective distribution channel laws or parallel import laws for listings of authentic items; and for alleged non-compliance with consumer protection laws. Such plaintiffs seek, among other remedies, injunctive relief and damages. In the aggregate, these suits could result in significant damage awards and injunctions that could, individually or in the aggregate, adversely affect our business. There are approximately 36,000 rights owners in our verified rights owner (VeRO) program, and each rights owner has anywhere from one to several hundred brands. Statutory damages for copyright or trademark violations could range up to $30,000 per copyright violation and $100,000 per trademark violation in the U.S., and may be even higher in other jurisdictions. These and similar suits may force us to modify our business practices, which could lower our revenue, increase our costs or make our websites less convenient to our customers, any of which could materially harm our business. In addition, rights owners have aggressively sought to reduce the applicability of limitations to intellectual property rights such as copyright exhaustion and the first sales doctrine in cases such as Vernor v. Autodesk Inc. (Ninth Circuit Court of Appeals) and Wiley v. Kirtsaeng (Second Circuit Court of Appeals, currently on appeal to the U.S. Supreme Court). To the extent such doctrines are limited, the supply of goods available for resale on our sites may be adversely affected.

In addition to litigation from rights owners, we may be subject to regulatory, civil or criminal proceedings and penalties if governmental authorities believe we have aided in the sale of counterfeit goods. While we have had some early success in defending against such litigation, more recent cases have been based, at least in part, on different legal theories than those of earlier cases, and there is no guarantee that we will continue to be successful in defending against such litigation. Plaintiffs in recent cases have argued that we are not entitled to safe harbors under the Digital Millennium Copyright Act in the U.S. or as a hosting provider in the European Union under the Electronic Commerce Directive because of the alleged active nature of our involvement with our sellers, and that whether or not such safe harbors are available, we should be found liable because we supposedly have not adequately removed listings that are counterfeit or are authentic but allegedly violate trademark or copyright law or effectively suspended users who have created such listings. While we do not believe the European Court of Justice decision in the L'Oréal case (see "Item 1: Legal Proceedings" above) changes the standard for hosting immunity under the Electronic Commerce directive, rights owners in European jurisdictions have asserted that our degree of participation in the transaction should cause us to be unable to take advantage of the hosting immunity exception. Final resolution of this issue has been left to the national courts of countries in the European Union. We believe that the legal climate, especially in Europe, is becoming more adverse to our positions, which may require us to take actions which could lower our revenues, increase our costs, or make our websites less convenient to our customers, any of which could materially harm our business. In addition, a public perception that counterfeit or pirated items are commonplace on our sites, even if factually incorrect, would damage our reputation, lower the price our sellers receive for their items and damage our business.

We are continuously seeking to improve and modify our efforts to eliminate counterfeit and pirated items through ongoing business initiatives designed to reduce bad buyer experiences and improve customer satisfaction and by responding to new patterns we are seeing among counterfeiters and others committing fraud on our users. Increased intermediation of transactions between buyers and sellers, which we generally refer to as our Managed Marketplace initiative, may result in us being unable to rely, to the same extent that we have in the past, on hosting immunity and other secondary liability safe harbors when sued by users and rights owners over actions taken on our site by our users. While we are taking steps to mitigate this impact on our safe harbor defenses, we may be subject to more intellectual property litigation and may lose more cases as a result of these business model changes, which would adversely affect our business.

Content owners and other intellectual property rights owners may also seek to bring legal action against entities that are peripherally involved in the sale of infringing items, such as payment companies. To the extent that intellectual property rights owners bring legal action against PayPal based upon the use of PayPal's payment services in a transaction involving the sale of infringing items, including on our websites, our business could be harmed. Several jurisdictions have adopted new laws in these areas, and others are considering imposing additional restrictions.

In addition, new laws have been proposed regulating Internet companies with respect to intellectual property issues. For example, ACTA and TPP are trade agreements that include international standards for enforcing intellectual property rights, including provisions regarding counterfeit goods and online piracy. The European Commission is considering revising the Intellectual Property Enforcement Directive, which could potentially increase our exposure to enforcement actions from rights owners. Implementation of these or similar laws could require us to change our business practices, increase our compliance costs and harm our business.

We are subject to patent litigation.

We have repeatedly been sued for allegedly infringing other parties' patents. We are a defendant in a number of patent suits and we have been notified of several other potential patent disputes. We expect that we will increasingly be subject to patent infringement claims involving various aspects of our Marketplaces, Payments and GSI segments as our products and services continue to expand in scope and complexity (e.g., our mobile, local, social and digital initiatives), as we expand into new businesses, including through acquisitions, and as the universe of patent owners who may claim that we, companies that we have acquired, or our customers infringe their patents and the aggregate number of patents controlled by such patent owners correspondingly increases. Such claims may be brought directly against our companies and/or against our customers (whom we may indemnify either because we are contractually obligated to do so or as a business matter). We and other technology companies have seen more of these claims from an increasing number of third parties whose sole or primary business is to assert such claims. In addition, we have seen significant patent disputes between operating companies in some technology industries (e.g., mobile telephony). Patent claims, whether meritorious or not, are time consuming and costly to resolve, and could require expensive changes in our methods of doing business, could require us to enter into costly royalty or licensing agreements, or could require us to cease conducting certain operations, which would harm our business.

Use of our services for illegal purposes could harm our business.

We may be unable to prevent our users from selling unlawful or stolen goods or unlawful services, or selling goods or services in an unlawful manner, and we may be subject to allegations of civil or criminal liability for unlawful activities carried out by users through our services. We have been subject to several lawsuits based upon such allegations. In December 2004, an executive of Baazee.com, our Indian subsidiary, was arrested in connection with a user's listing of a pornographic video clip on that website. The charges related to this arrest were recently quashed. Similarly, one of our Korean subsidiaries (IAC) and one of its employees were found criminally liable for listings (which occurred prior to our acquisition of IAC) on IAC's website. The German Federal Supreme Court has ruled that we may have a duty to take reasonable measures to prevent prohibited DVDs from being sold on our site to minors and that competitors may be able to enforce this duty. In a number of circumstances, third parties, including government regulators and law enforcement officials, have alleged that our services aid and abet certain violations of certain laws, including antiscalping laws with respect to the resale of tickets, laws regarding the sale of counterfeit items, the fencing of stolen goods, selective distribution channel laws, distance selling laws and the sale of items outside of the U.S. that are regulated by U.S. export controls. As we seek to reduce bad buying experiences and improve the customer experience on our sites, our level of interaction with buyers and sellers may increase over time, which could in turn increase our potential exposure to allegations of civil or criminal liability for unlawful activities carried out by users through our services.

Although we have prohibited the listing of illegal and stolen goods and certain high-risk items and implemented other protective measures, we may be required to spend substantial resources to take additional protective measures or discontinue certain service offerings, any of which could harm our business. Any costs incurred as a result of potential liability relating to the alleged or actual sale of unlawful goods or the unlawful sale of goods could harm our business. Certain manufacturers and large retailers have sought new U.S. federal and state legislation regarding stolen goods that could limit our ability to allow sellers to use our sites without confirming the source of, and their legal rights to sell, the underlying goods. In addition, from time to time we have received significant media attention relating to the listing or sale of illegal goods and stolen goods using our services. This negative publicity could damage our reputation, diminish the value of our brand names and make users reluctant to use our services.

PayPal's payment system is also susceptible to potentially illegal or improper uses, including illegal online gambling, fraudulent sales of goods or services, illicit sales of prescription medications or controlled substances, piracy of software, movies, music and other copyrighted or trademarked goods, money laundering, terrorist financing, bank fraud, child pornography trafficking, prohibited sales of alcoholic beverages or tobacco products, online securities fraud and encouraging, promoting, facilitating or instructing others to engage in illegal activities. There has been an increased focus by rights owners and U.S. government officials on the role that payments systems play in the sale of, and payment for, pirated digital goods on the Internet. Recent changes in law have increased the penalties for intermediaries providing payment services for certain illegal activities and additional payments-related proposals are under active consideration by government policymakers. Despite measures PayPal has taken to detect and lessen the risk of this kind of conduct, illegal activities could still be funded using PayPal. Any resulting claims, liabilities or loss of transaction volume could harm our business.

If our GSI business is unable to enhance its platform and migrate clients to its new platform in a timely and cost-effective manner, it would be substantially harmed.

Our GSI business is in the process of enhancing and unbundling the components of its ecommerce and payments platform and migrating its existing customers to its new platform. This project is very expensive and time consuming and involves significant technical risk. Previously planned migrations of certain clients to the new platform have been delayed into 2012 and beyond. If client migrations to the new platform continue to be delayed, the functionality of the new platform is not accepted by GSI's existing clients or prospective clients targeted by GSI, the new platform contains an unacceptable amount of design flaws or does not perform or operate as expected, or GSI fails to meet client commitments and services level agreements, GSI could be subject to substantial penalties under its agreements with its clients (including significant financial penalties and termination rights for its affected clients), its relationships with its clients and their respective businesses could be substantially harmed, and GSI clients may seek to terminate their contracts with GSI early based on actual or proposed breach. In addition, GSI's new platform also provides for substantially more client control over certain platform functionality, such as promotions and marketing, operations and performance analytics. If GSI is unable to help clients understand, assess and address their internal preparedness needs for the new platform, this could result in delays in deployment, client dissatisfaction due to lack of preparedness, degraded site performance, and additional support costs attributable to client-induced issues. We believe that GSI's ability to secure new clients and retain current clients will be negatively impacted until GSI is able to successfully roll out the new platform in a live client implementation. Any of these events or circumstances could materially and adversely affect our GSI business. Even if accomplished successfully, this development and migration project may cost more than expected or take longer than currently planned, which could harm our GSI business.

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

The law relating to the liability of online services companies for information carried on or disseminated through their services remains unsettled in many jurisdictions. Claims could be made against online services companies under both U.S. and foreign law for defamation, libel, invasion of privacy, negligence, copyright or trademark infringement, or other theories based on the nature and content of the materials disseminated through their services. Several private lawsuits seeking to impose liability under a number of these theories have been brought against us, as well as other online service companies. In addition, domestic and foreign legislation has been proposed that would prohibit or impose liability for the transmission over the Internet of certain types of information. Our Marketplaces service features a Feedback Forum, which includes information from users regarding other users. Although all such feedback is generated by users and not by us, claims of defamation or other injury have been made in the past and could be made in the future against us for not removing content posted in the Feedback Forum.

Furthermore, several court decisions arguably have narrowed the scope of the immunity provided to Internet service providers like us in the U.S. under the Communications Decency Act. For example, the Ninth Circuit has held that certain immunity provisions under the Communications Decency Act might not apply to the extent that a website owner materially contributes to the development of unlawful content on its website. As our websites evolve, challenges to the applicability of these immunities can be expected to continue. In addition, the Paris Court of Appeal has ruled in the Louis Vuitton Malletier and Christian Dior Couture cases that applicable laws protecting passive Internet “hosts” from liability are inapplicable to eBay given that eBay actively promotes bidding on its sellers' listings and receives a commission on successful transactions, and is therefore a broker. The ECJ decision in the L'Oréal case (see “Item 1: Legal Proceedings” above) gave broad discretion to national courts in Europe to determine if Internet hosting immunity applies to eBay. Accordingly, our potential liability to third parties for the user-provided content on our sites, particularly in jurisdictions outside the U.S. where laws governing Internet transactions are unsettled, may increase. If we become liable for information provided by our users and carried on our service in any jurisdiction in which we operate, we could be directly harmed and we may be forced to implement new measures to reduce our exposure to this liability, including expending substantial resources or discontinuing certain service offerings, which would negatively affect our financial results. In addition, the increased attention focused upon liability issues as a result of these lawsuits and legislative proposals could require us to incur additional costs and harm our reputation and our business.

Government inquiries may lead to charges or penalties.

A large number of transactions occur on our websites on a daily basis. Government regulators have received a significant number of consumer complaints about eBay, PayPal and GSI, which, while small as a percentage of our total transactions, are large in aggregate numbers. As a result, from time to time we have been contacted by various U.S. and foreign governmental regulatory agencies that have questions about our operations and the steps we take to protect our users from fraud. PayPal has received inquiries regarding its restriction and disclosure practices from the Federal Trade Commission and regarding these and other business practices from the attorneys general of a number of states. In September 2006, PayPal entered into a settlement agreement with the attorneys general of a number of states under which it agreed to pay $1.7 million to the attorneys general, shorten and streamline its user agreement, increase educational messaging to users about funding choices and communicate more information regarding protection programs to users.

From time to time, we face inquiries from government regulators in various jurisdictions related to actions that we have taken that are designed to improve the security of transactions and the quality of the user experience on our websites and we may face similar inquiries from other government regulators in the future. For example, in 2008, the Australian Competition and Consumer Commission and the Reserve Bank of Australia reviewed our policies requiring sellers to offer PayPal as a payment alternative on most transactions on our localized Australian website and precluding sellers from imposing a surcharge or any other fee for accepting PayPal or other payment methods. Other regulators have requested information concerning PayPal's limitations of customer accounts. Similarly, Bill Me Later has from time to time received customer complaints that could result in investigations into Bill Me Later's business practices by state or federal regulators. As a result of the recent credit crisis, new laws have been, and additional new laws and regulations are expected to be, adopted that impose additional obligations and restrictions on the provision of credit, among other requirements. We are likely to receive additional inquiries from regulatory agencies in the future, including under existing or new credit laws or regulations, which may lead to action against us. We have responded to all inquiries from regulatory agencies by describing our current and planned antifraud efforts, customer support procedures, operating procedures and disclosures of the relevant business. If one or more of these agencies is not satisfied with our response to current or future inquiries, we could be subject to enforcement actions, fines or other penalties, or forced to change our operating practices in ways that could harm our business.

We are subject to general litigation and regulatory disputes.

From time to time, we are involved in other disputes or regulatory inquiries that arise in the ordinary course of business. The number and significance of these disputes and inquiries have increased as our company has grown larger, our businesses have expanded in scope (e.g., our mobile, local, social and digital initiatives) and our products and services have increased in complexity. We have in the past been forced to litigate such claims. We may also become more vulnerable to third-party claims as laws such as the Digital Millennium Copyright Act, the Lanham Act and the Communications Decency Act are interpreted by the courts as our products and services to users continues to expand and as we expand geographically into jurisdictions where the underlying laws with respect to the potential liability of online intermediaries such as ourselves are either unclear or less favorable. As an increasing portion of our business shifts to mobile, we may be subject to additional laws, such as the Telephone Consumer Protection Act, which have significant penalties. The Federal Communications Commission has recently amended its regulations under the Telephone Consumer Protection Act, effective in July 2012, which could increase our exposure to liability for certain types of telephonic communication with customers, including but not limited to text messages to mobile phones. We are also subject to federal, state, local and foreign laws of general applicability, including laws regulating working conditions. Any claims or regulatory actions against us, whether meritorious or not, could be time consuming, result in costly litigation, damage awards (including statutory damages for certain causes of action in certain jurisdictions), injunctive relief, or increased costs of doing business through adverse judgment or settlement, require us to change our business practices in expensive ways, require significant amounts of management time, result in the diversion of significant operational resources, or otherwise harm our business.

Changes to our dispute resolution process could increase our costs and loss rate.

Beginning in 2009, we have transitioned buyers in the U.S., U.K. and Germany to a dispute resolution (“resolutions”) process provided by eBay customer support, which now serves as the primary entry point for buyers in these countries if they are unable to resolve their disputes with eBay sellers. Among other things, the resolutions process provides that eBay will generally reimburse the buyer for the full amount of an item's purchase price (including original shipping costs) in cases where the item was not received or the item they received was different from that described in the listing and the seller does not provide adequate resolution to the buyer. eBay then attempts to recoup amounts paid to the buyer from the seller's PayPal accounts or through other collection methods. Our costs associated with resolutions have increased as a result of these changes to our resolutions policies and process, in part because eBay may not have the same level of rights of recoupment against sellers as PayPal, resulting in higher costs to operate the program. These changes, together with any further changes that we may make to our resolutions process in the future, may be negatively received by, and lead to dissatisfaction on the part of, some of our sellers, and may also result in an increase in buyer fraud and associated transaction losses.

In the event of the bankruptcy or other business interruption of a merchant that sells goods or services in advance of the date of their delivery or use (e.g., airline, cruise or concert tickets, custom-made goods and subscriptions), eBay and/or PayPal could be liable to the buyers of such goods or services, either through its buyer protection program or through chargebacks on payment cards used by customers to fund their payment through PayPal. While we have established reserves based on assumptions and estimates that we believe are reasonable to cover such eventualities, these reserves may be insufficient and our operating results could be adversely affected.

Failure to deal effectively with bad transactions and customer disputes would increase our loss rate and harm our business.
Over the last several years, we have enhanced the buyer and seller protections offered by PayPal in certain eBay marketplaces, and in certain countries for transactions outside of eBay marketplaces. These changes to PayPal's buyer and seller protection program could result in future changes and fluctuations in our Payments transaction loss rate. For the fiscal year ended December 31, 2011 and the six months ended June 30, 2012, our Payments transaction losses (including both direct losses and buyer protection payouts) totaled $246 million and $130 million, representing 0.21% and 0.19% of our net total payment volume, respectively. Beginning in 2009, we have also changed the dispute resolution process for transactions on eBay.com, eBay.co.uk and eBay.de, as described in more detail above under the caption “Changes to our dispute resolution process could increase our costs and loss rate,” which could result in an increase in our combined eBay and PayPal transaction losses.
PayPal's highly automated and liquid payment service makes PayPal an attractive target for fraud. In configuring its service, PayPal continually strives to maintain the right balance of appropriate measures to promote both convenience and security for customers. Identity thieves and those committing fraud using stolen credit card or bank account numbers can potentially steal large amounts of money from businesses such as PayPal. We believe that several of PayPal's current and former competitors in the electronic payments business have gone out of business or significantly restricted their businesses largely due to losses from this type of fraud. While PayPal uses advanced anti-fraud technologies, we expect that technically knowledgeable criminals will continue to attempt to circumvent PayPal's anti-fraud systems using increasingly sophisticated methods. From time to time, such fraudsters may discover and exploit vulnerabilities that may not immediately be identified and remediated, which may in turn result in one-time increases in fraud and associated transaction losses. In addition, because users frequently use the same passwords for different sites, a data breach of a third party site can result in a spike in transaction losses. Finally, PayPal's service could be subject to employee fraud or other internal security breaches, and PayPal may be required to reimburse customers for any funds stolen as a result of such breaches. Merchants could also request reimbursement, or stop using PayPal, if they are affected by buyer fraud or other types of fraud. Additional fraud risks associated with PayPal's point of sale solutions are described below under the caption “PayPal's point of sale solutions expose us to additional risks."
PayPal incurs substantial losses due to claims from buyers that merchants have not performed or that their goods or services do not match the merchant's description, whether those claims arise from merchant fraud or from an unintentional failure to perform by the merchant. PayPal seeks to recover such losses from the merchant, but may not be able to recover in full if the merchant is unwilling or unable to pay. PayPal also incurs losses from claims that the customer did not authorize the purchase, from buyer fraud, from erroneous transmissions and from customers who have closed bank accounts or have insufficient funds in them to satisfy payments. In addition, if losses incurred by PayPal related to payment card transactions become excessive, they could potentially result in PayPal losing the right to accept payment cards for payment, which would materially and adversely affect PayPal's business both on and off eBay. In the event that PayPal was unable to accept payment cards, the velocity of trade on eBay and websites operated by GSI's clients that accept PayPal as a form of payment could also decrease, in which case our business would further suffer. The Bill Me Later service is similarly subject to the risk of fraudulent activity associated with merchants, users of the Bill Me Later service and third parties handling its user information. Our Payments business has taken measures to detect and reduce the risk of fraud, but these measures need to be continually improved and may not be effective against new and continually evolving forms of fraud or in connection with new product offerings. If these measures do not succeed, our business will suffer.
eBay faces similar risks with respect to fraudulent activities on its websites. eBay periodically receives complaints from users who may not have received the goods that they had purchased. In some cases, individuals have been arrested and convicted for fraudulent activities using our websites. eBay also receives complaints from sellers who have not received payment for the goods that a buyer had contracted to purchase. Non-payment may occur because of miscommunication, because a buyer has changed his or her mind and decided not to honor the contract to purchase the item, or because the buyer bid on the item maliciously in order to harm either the seller or eBay. In some European and Asian jurisdictions, buyers may also have the right to withdraw from a sale made by a professional seller within a

specified time period. While eBay can, in some cases, suspend the accounts of users who fail to fulfill their payment or delivery obligations to other users, eBay does not have the ability to require users to make payment or deliver goods, or otherwise make users whole other than through our buyer protection programs.

Our limited eBay and PayPal buyer protection programs represent the means by which we compensate users who believe that they have been defrauded, have not received the item that they purchased, or have received an item different than what was described. However, users who pay through PayPal may have reimbursement rights from their credit card company or bank, which in turn will seek recovery from PayPal. eBay also periodically receives complaints from buyers as to the quality of the goods purchased. We expect to continue to receive communications from users requesting reimbursement or threatening or

commencing legal action against us if no reimbursement is made. Our liability for these sort of claims is only beginning to be clarified in some jurisdictions and may be higher in some non-U.S. jurisdictions than it is in the U.S. Litigation involving liability for third-party actions could be costly and time consuming for us, divert management attention, result in increased costs of doing business, lead to adverse judgments, or otherwise harm our business. In addition, affected users will likely complain to regulatory agencies that could take action against us, including imposing fines or seeking injunctions.
Negative publicity and user sentiment generated as a result of fraudulent or deceptive conduct by users of our Marketplaces, Payments and GSI services could damage our reputation, reduce our ability to attract new users or retain our current users and diminish the value of our brand names. We believe that negative user experiences are one of the primary reasons users stop using our services.
From time to time, we have considered more active mechanisms designed to combat bad buyer experiences and increase buyer satisfaction, including evaluating sellers on the basis of their transaction history and restricting or suspending their activity as a result. For example, in the U.S. and the U.K., we may request that PayPal hold seller funds in certain instances (e.g., for sellers with a limited selling history or below-standard performance ratings), which is intended to help improve seller performance and increase buyer satisfaction. We may expand the scope of such programs in the future and introduce other programs with similar aims in these and other countries. Our increased usage of these or other mechanisms to attempt to improve buyer satisfaction could result in dissatisfaction on the part of sellers, loss of share to competing marketplaces, reduced selection of inventory on our sites and other adverse effects.
Governmental regulators worldwide are also evaluating approaches intended to reduce online fraud. Some of the current proposals (e.g., two-factor authentication in France to verify a user's identity) could increase our costs or require us to change our business practices in a manner that could harm our business.
Any factors that reduce cross-border trade could harm our business.
Cross-border trade has become an increasingly important source of both revenue and profits for us. Cross-border transactions using our websites generally provide higher revenues and gross margins than similar transactions that take place within a single country or market. We generally earn higher transaction fees for cross-border transactions involving PayPal, and our Marketplaces business continues to represent a relatively straightforward way for buyers and sellers to engage in cross-border trade compared with other alternatives. Cross-border trade also represents our primary (or in some cases, only) presence in certain markets in which Internet use is accelerating and we have a limited (or no) domestic Marketplaces business (e.g., Brazil/Latin America, China, Russia and various developing countries).
The interpretation and application of specific national or regional laws, such as those related to intellectual property rights of authentic products and those related to selective distribution networks to sellers in other countries listing on the Internet and the potential interpretation and application of laws of multiple jurisdictions (e.g., the jurisdiction of the buyer, the seller, and/or the location of the item being sold) are extremely complicated in the context of cross-border trade. Some of these issues are involved in the L'Oréal and Louis Vuitton Malletier cases (see “Item 1: Legal Proceedings” above). To the extent any interpretation or application of such laws imposes restrictions on, or increases the costs of, purchasing, selling or shipping goods across national borders, our business would be harmed. Any additional factors that increase the costs of purchasing, selling or shipping goods across national borders or make it more difficult to do so in practice, including fluctuations in currency exchange rates, delivery service rates, currency restrictions, export control laws, customs enforcement, court rulings and the application of (or increases in) tariffs, duties or other taxes on imports or exports, or that otherwise would result in a net reduction in cross-border trade on our sites, would adversely affect our business. As part of our ongoing efforts to drive more sales and improve seller efficiency and buyer experience, we are evaluating opportunities to potentially become more actively involved in different aspects of cross-border transactions, which could potentially expose us to additional liability based upon our involvement in aspects of such transactions and/or the actions of our users in more countries.
Our cross-border trade is also subject to, and impacted by currency exchange rate fluctuations, as discussed under the caption “We are exposed to fluctuations in currency exchange rates and interest rates” above.
Our business is subject to online security risks, including security breaches.

Our businesses involve the storage and transmission of users' proprietary information, and security breaches could expose us to a risk of loss or misuse of this information, litigation and potential liability. An increasing number of websites, including several other large Internet companies, have recently disclosed breaches of their security, some of which have involved sophisticated and highly targeted attacks on portions of their sites. Because the techniques used to obtain unauthorized access, disable or degrade service, or sabotage systems, change frequently and often are not recognized until launched against a target,

47

we may be unable to anticipate these techniques or to implement adequate preventative measures. If an actual or perceived breach of our security occurs, public perception of the effectiveness of our security measures could be harmed and we could lose users. A party that is able to circumvent our security measures could misappropriate our or our users' proprietary information, cause interruption in our operations, damage our computers or those of our users, or otherwise damage our reputation and business. Any compromise of our security could result in a violation of applicable privacy and other laws, significant legal and financial exposure, damage to our reputation and a loss of confidence in our security measures, which could harm our business. Data security breaches may also result from non-technical means, for example, actions by a suborned employee. GSI's clients also face similar risks of security breaches, and to the extent that such clients are harmed as a result of a security breach, GSI's business would also be adversely affected.

A significant number of our users authorize us to bill their payment card accounts directly for all transaction fees charged by us. For example, PayPal's users routinely provide credit card and other financial information, and GSI customers routinely provide credit card information and other personally identifiable information which we maintain to facilitate the ease of future transactions. We rely on encryption and authentication technology licensed from third parties to provide the security and authentication to effectively secure transmission of confidential information, including customer payment card numbers. Advances in computer capabilities, new discoveries in the field of cryptography or other developments may result in the technology used by us to protect transaction data being breached or compromised. Financial services regulators in various jurisdictions, including the U.S. and the EU, have implemented or are considering proposals to impose new authentication requirements on banks and payment processors. These requirements could impose significant costs on PayPal, make it more difficult for new customers to join its network and reduce the ease of use of its products.

Under payment card rules and our contracts with our card processors, if there is a breach of payment card information that we store, or that is stored by PayPal's direct payment card processing customers, we could be liable to the payment card issuing banks for their cost of issuing new cards and related expenses. In addition, if we fail to follow payment card industry security standards, even if customer information has not been compromised, we could incur significant fines or lose our ability to give customers the option of using payment cards to fund their payments or pay their fees. If we were unable to accept payment cards, our businesses would be seriously damaged.

Our servers are also vulnerable to computer viruses, physical or electronic break-ins and similar disruptions, and we have experienced “denial-of-service” type attacks on our system that have, in certain instances, made all or portions of our websites unavailable for periods of time. For example, in December 2010, PayPal was subject to a series of distributed “denial of service” attacks following PayPal's decision to indefinitely restrict the account used by WikiLeaks due to an alleged violation of PayPal's Acceptable Use Policy. We may need to expend significant resources to protect against security breaches or to address problems caused by breaches. These issues are likely to become more difficult as we expand the number of places where we operate. Security breaches, including any breaches of our security measures or those of parties with which we have commercial relationships (e.g., our clients and third-party service providers) that result in the unauthorized release of users' personal information, could damage our reputation and expose us to a risk of loss or litigation and possible liability. Our insurance policies carry low coverage limits, which may not be adequate to reimburse us for losses caused by security breaches.

Our users, as well as those of other prominent Internet companies, have been and will continue to be targeted by parties using fraudulent “spoof” and “phishing” emails to misappropriate passwords, credit card numbers, or other personal information or to introduce viruses or other malware through “trojan horse” programs to our users' computers. These emails appear to be legitimate emails sent by eBay, PayPal, a GSI client, or one of our other businesses (e.g., StubHub), or by a user of one of our businesses, but direct recipients to fake websites operated by the sender of the email or request that the recipient send a password or other confidential information via email or download a program. Despite our efforts to mitigate “spoof” and “phishing” emails through product improvements and user education, “spoof” and “phishing” activities remain a serious problem that may damage our brands, discourage use of our websites and increase our costs.

Changes in regulations or user concerns regarding privacy and protection of user data could adversely affect our business.

We are subject to laws relating to the collection, use, retention, security and transfer of personally identifiable information about our users, especially for financial information and for users located outside of the U.S. As an entity licensed and subject to regulation as a bank in Luxembourg, PayPal (Europe) S.à r.l et Cie, SCA is subject to banking secrecy laws. In many cases, these laws apply not only to third-party transactions, but also to transfers of information between ourselves and our subsidiaries, and between ourselves, our subsidiaries and other parties with which we have commercial relations. In particular, the collection and use of personal information by companies has come under increased regulatory scrutiny. The interpretation and application of user data protection laws are in a state of flux, and may be interpreted and applied inconsistently from country to country. The European Union recently proposed new data laws that give customers additional rights and provide additional restrictions and harsher penalties on companies for illegal collection and misuse of personal information, including restrictions on the use of Internet tracking tools called “cookies”. While the European Union directive on cookies has taken effect, the manner in which member states adopt implementing legislation, and whether the European Union deems that legislation sufficient, continues to evolve. To the extent implementing legislation by member states is more restrictive, it could negatively impact the manner in which we use cookies for many of our services, ranging from advertising to anti-fraud, and require us to incur additional costs or change our business practices, any of which could harm our business. The European Union has announced proposed changes to the European Data Protection Directive, the Federal Trade Commission, or FTC, and the White House have both proposed U.S. privacy frameworks, and a number of other countries in which we operate have either recently passed privacy legislation or are in the process of doing so. Our current data protection policies and practices may not be consistent with new laws and regulations or evolving interpretations and applications. It is unclear how the application of existing privacy laws and regulations will impact mobile services and technologies, which are evolving rapidly. Complying with these varying international requirements could cause us to incur substantial costs or require us to change our business practices in a manner adverse to our business.

In addition, we have and post on our websites our own privacy policies and practices concerning the collection, use and disclosure of user data. Any failure, or perceived failure, by us to comply with our posted privacy policies or with any regulatory requirements or orders or other federal, state or international privacy or consumer protection-related laws and regulations (or, in the case of our GSI businesses, any such failure or perceived failure on the part of GSI or GSI's clients) could result in proceedings or actions against us by governmental entities or others (e.g., class action privacy litigation), subject us to significant penalties and negative publicity, require us to change our business practices, increase our costs and adversely affect our business. For example, the FTC has recently entered into a number of consent decrees with major online companies, including Facebook and Google, to settle allegations of unfair or deceptive privacy practices. The FTC's consent decrees with Facebook and Google require those companies to implement a comprehensive privacy program and undergo regular, independent privacy audits for the next 20 years, among other requirements.

Certain of our businesses, including GSI's interactive marketing services business, utilize “behavioral marketing” (generally, the tracking of a user's online activities) to deliver relevant content to Internet users. The FTC has released a Staff Report with principles to address consumer privacy issues that may arise from behavioral marketing and to encourage industry self-regulation. In March 2012, the FTC issued a final report titled “Protecting Consumer Privacy in an Era of Rapid Change: Recommendations for Businesses and Policymakers,” which details the FTC's perspective on best practices for companies that collect and use consumer data to protect the privacy of consumers. Legislators and regulators in various jurisdictions are increasingly focusing on the capture and use of location-based information relating to users of smartphones and other mobile devices, which may result in additional restrictions being placed on the collection and use of such information. Any such regulations or legislation could, if enacted, prohibit the use of certain technologies, including those that track individuals' activities on the Internet or geolocation via mobile devices. Such laws and regulations could restrict our ability to collect and use page viewing data and personal information, which may reduce demand for our services or require changes to our current business models, such as advertising, which could harm our business.

Data collection, privacy and security have become the subject of increasing public concern. If Internet and mobile users were to reduce their use of our websites and services as a result, our business could be harmed. As noted above, we are also subject to the possibility of security breaches, which themselves may result in a violation of these laws.

Our revenue from advertising is subject to factors beyond our control.

We derive significant revenue from advertising on our websites and applications. Revenues from online advertising are sensitive to events and trends that affect advertising expenditures, such as general changes in the economy and changes in consumer spending, the effectiveness of online advertising versus offline advertising media and the value our websites provide to advertisers relative to other websites. The economic downturn adversely impacted our advertising revenue. In addition, major search engine operators have the ability to change from time to time, at their sole discretion, the rules and search algorithms governing the pricing, availability and placement of online advertising. Any changes in these rules or search algorithms could materially reduce the value that we derive from online advertising on our websites, either directly or indirectly. For example, retailers pay a fee to Shopping.com for online shoppers directed to their websites by our Shopping.com website. Rule changes made by search engines beginning in 2008 disrupted traffic to our Shopping.com website, which in turn adversely affected click-through traffic to retailers from our Shopping.com website and associated fee revenue. Finally, legislators and regulators in various jurisdictions, including the U.S. and the European Union, are reviewing Internet advertising models and the use of user-related data, including location-based information relating to users of smartphones and other mobile devices, and are considering proposals that could restrict or otherwise impact these business models and practices. If we experience a reduction in our advertising revenues due to economic, competitive, regulatory, technological or other factors, or the renegotiation of the terms of our contracts with major advertising companies, or a reduction in our ability to effectively place advertisements on our

sites, or are otherwise unable to provide value to our advertisers, our business and financial results would suffer.
Our growth will depend on our ability to develop our brands, and these efforts may be costly.
We believe that continuing to strengthen our brands will be critical to achieving widespread acceptance of our services, and will require a continued focus on active marketing efforts across all of our brands. We will need to continue to spend substantial amounts of money on, and devote substantial resources to, advertising, marketing, and other efforts to create and maintain brand loyalty among users. Since 2005, we have significantly increased the number of brands we are supporting, adding Shopping.com, our classified websites (including Den Blå Avis, BilBasen, eBay Classifieds (including eBay Anuncios, eBay Kleinanzeigen and eBay Annunci), Gumtree, Kijiji, LoQUo, Marktplaats.nl, mobile.de and Alamaula), StubHub, Bill Me Later, Gmarket, Milo, WHERE, RedLaser, Zong and GSI, among others. Each of these brands requires its own resources, increasing the costs of our branding efforts. Brand promotion activities may not yield increased revenues, and even if they do, any increased revenues may not offset the expenses incurred in building our brands. Also, major search engine operators that we use to advertise our brands have frequently changing rules that govern the pricing, availability and placement of online advertisements (e.g., paid search, keywords), and changes to these rules could negatively affect our ability to use online advertising to promote our brands in a cost-effective manner. If we fail to promote and maintain our brands, or if we incur substantial expenses in an unsuccessful attempt to promote and maintain our brands, our business would be harmed.
New and existing regulations could harm our business.
We are subject to the same foreign and domestic laws as other companies conducting business on and off the Internet. It is not always clear how existing laws governing issues such as property ownership, copyrights, trademarks and other intellectual property issues, parallel imports and distribution controls, taxation, libel and defamation, obscenity and personal privacy apply to online businesses such as ours. The majority of these laws were adopted prior to the advent of the Internet and related technologies and, as a result, do not contemplate or address the unique issues of the Internet and related technologies. Those laws that do reference the Internet, such as the U.S. Digital Millennium Copyright Act, the U.S. “CAN-SPAM” Act and the European Union's Directives on Distance Selling and Electronic Commerce, are being interpreted by the courts, but their applicability and scope remain uncertain. As our activities, the types of goods and services listed on our websites, and products and services we offer expand, including through acquisitions such as Bill Me Later and StubHub, regulatory agencies or courts may claim or hold that we or our users are subject to licensure or prohibited from conducting our business in their jurisdiction, either generally or with respect to certain actions (e.g., the sale of real estate, event tickets, cultural goods, boats and automobiles). Recent financial and political events may increase the level of regulatory scrutiny on large companies in general, and financial services companies in particular, and regulatory agencies may view matters or interpret laws and regulations differently than they have in the past and in a manner adverse to our businesses.
Our success and increased visibility has driven some existing businesses that perceive our business model to be a threat to their business to raise concerns about our business models to policymakers and regulators. These established businesses and their trade association groups employ significant resources in their efforts to shape the legal and regulatory regimes in countries where we have significant operations. They may employ these resources in an effort to change the legal and regulatory regimes in ways intended to reduce the effectiveness of our businesses and the ability of users to use our products and services. In particular, these established businesses have raised concerns relating to pricing, parallel imports, professional seller obligations, selective distribution networks, stolen goods, copyrights, trademarks and other intellectual property rights and the liability of the provider of an Internet marketplace for the conduct of its users related to those and other issues. Changing the legal or regulatory regimes in a manner that would increase our liability for third-party listings could negatively impact our business.
Over the last few years some large retailers and their trade associations have sought legislation in a number of states and the U.S. Congress that would make eBay liable for the sale of stolen property or would ban certain categories of goods from sale on our platform, including gift cards and health and beauty products. While no such legislation has passed to date, the proponents continue to seek passage of such legislation, and if any of these laws are adopted they could harm our business.
Numerous states and foreign jurisdictions, including the State of California, where our headquarters are located, have regulations regarding “auctions” and the handling of property by “secondhand dealers” or “pawnbrokers.” Several states and

some foreign jurisdictions, including France, have attempted, and may attempt in the future, to impose such regulations upon us or our users. Attempted enforcement of these laws against some of our users appears to be increasing. In France, we have been sued by Conseil des Ventes, the French auction regulatory authority, which has alleged that sales on our French website constitute illegal auctions that cannot be performed without its consent. We have won this lawsuit at the trial and appeals court levels, but it may be subject to further appeal. A lawsuit alleging similar claims has been brought against us by two associations of French antique dealers, and is now pending on appeal after we won in the first instance. We intend to vigorously defend against these lawsuits. However, these and other regulatory and licensure claims and enforcement actions could result in costly

50

litigation and, if unsuccessful, we could be required to change the way we or our users do business in ways that increase costs or reduce revenues (for example, by forcing us to prohibit listings of certain items or restrict certain listing formats in some locations). We could also be subject to fines or other penalties, and any of these outcomes could harm our business.
A number of the lawsuits against us relating to trademark issues seek to have our websites subject to unfavorable local laws. For example, “trademark exhaustion” principles provide trademark owners with certain rights to control the sale of a branded authentic product until it has been placed on the market by the trademark holder or with the holder's consent. The application of “trademark exhaustion” principles is largely unsettled in the context of the Internet, and if trademark owners are able to force us to prohibit listings of certain items in one or more locations, our business could be harmed.
As we expand and localize our international activities, we become obligated to comply with the laws of the countries or markets in which we operate. In addition, because our services are accessible worldwide and we facilitate sales of goods and provide services to users worldwide, one or more jurisdictions may claim that we or our users are required to comply with their laws based on the location of our servers or one or more of our users, or the location of the product or service being sold or provided in an ecommerce transaction. For example, in the Louis Vuitton Malletier litigation, we were found liable in France, under French law, for transactions on some of our websites worldwide that did not involve French buyers or sellers (see “Item 1: Legal Proceedings” above). Laws regulating Internet and ecommerce companies outside of the U.S. are generally be less favorable than those in the U.S., giving greater rights to consumers, content owners, competitors, users and other third parties. Compliance may be more costly or may require us to change our business practices or restrict our service offerings, and the imposition of any regulations on us or our users may harm our business. In addition, we may be subject to multiple overlapping legal or regulatory regimes that impose conflicting requirements on us (e.g., in cross-border trade). Our alleged failure to comply with foreign laws could subject us to penalties ranging from criminal prosecution to significant fines to bans on our services, in addition to the significant costs we may incur in defending against such actions.
Following the global financial crisis, U.S. federal lawmakers enacted the Dodd-Frank Wall Street Reform and Consumer Protection Act in 2010 overhauling the federal government's oversight of consumer financial products and systemic risk in the U.S. financial system. Although the full effect of the new legislation will be dependent on regulations to be adopted by a number of different agencies (including the recently created Consumer Financial Protection Bureau), we expect the general effect of the financial reform law will be to require PayPal and Bill Me Later to make additional disclosures to their users and to impose new restrictions on certain of their activities. These new obligations will impose new compliance requirements and obligations on us, increase our costs and may result in increased litigation, the need to make expensive product changes and other adverse impacts on our business. In addition, we also expect that the continued implementation of the financial reform law enacted in 2010 will adversely impact some significant traditional revenue streams for banks. For example, in June 2011, the Federal Reserve Board issued a final rule capping debit card interchange fees. As a result of this and other regulations implementing the financial reform law, banks may need to revise their business models to remain profitable, which may lead them to charge more for services which were previously provided for free or at lower cost. Any resulting increases in service fees required for PayPal to process transactions (e.g., service fees for automated clearing house transactions) would increase our costs and could adversely affect our business. In addition, in January 2012, the Consumer Financial Protection Bureau finalized new regulations, required by the Dodd-Frank Wall Street Reform and Consumer Protection Act, which will require PayPal, starting in February 2013, to provide additional disclosures, error resolution rights and cancellation rights to U.S. consumers who make international remittance payments. These new requirements could increase our costs of processing international payments and could adversely affect our business.
Changes to payment card networks or bank fees, rules, or practices could harm PayPal's business.
PayPal does not directly access payment card networks, such as Visa and MasterCard, which enable PayPal's acceptance of credit cards and debit cards (including some types of prepaid cards). As a result, PayPal must rely on banks or other payment processors to process transactions, and must pay fees for this service. From time to time, payment card networks have increased, and may increase in the future, the interchange fees and assessments that they charge for each transaction using one of their cards. PayPal's payment card processors have the right to pass any

increases in interchange fees and assessments on to PayPal as well as increase their own fees for processing. Changes in interchange fees and assessments could increase PayPal's operating costs and reduce its profit margins. In addition, in some jurisdictions, governments have required Visa and MasterCard to reduce interchange fees, or have opened investigations as to whether Visa or MasterCard's interchange fees and practices violate antitrust law. In the U.S., the Dodd-Frank Wall Street Reform and Consumer Protection Act enacted in 2010 authorizes the Federal Reserve Board to regulate debit card interchange rates and debit card network exclusivity provisions, and in June 2011, the Federal Reserve Board issued a final rule capping debit card interchange fees at significantly lower rates than Visa or MasterCard previously charged. Any material reduction in credit or debit card interchange rates in the U.S. or other markets could jeopardize PayPal's competitive position against traditional credit and debit card processors. While the regulations adopted by the Federal Reserve Board in June 2011 do not treat PayPal as a “payment card network,” future changes to those regulations or to PayPal's business could potentially cause PayPal to be treated as a payment card network, which could subject PayPal to additional regulation and require PayPal to change its business practices, which could reduce PayPal's revenue and adversely affect PayPal's business.

PayPal is required by its processors to comply with payment card network operating rules, and PayPal has agreed to reimburse its processors for any fines they are assessed by payment card networks as a result of any rule violations by PayPal or PayPal's customers. The payment card networks set and interpret the card rules. Payment card networks could adopt new operating rules or re-interpret existing rules that PayPal or its processors might find difficult or even impossible to follow, or costly to implement. As a result, PayPal could lose its ability to give customers the option of using payment cards to fund their payments, or could lose its ability to give customers the choice of currency in which they would like their card to be charged, which would reduce PayPal's revenues from cross-border trade. If PayPal were unable to accept payment cards, its business would be seriously damaged. In addition, the velocity of trade on eBay and websites operated by GSI's clients that accept PayPal as a form of payment could decrease and our business would further suffer.

PayPal is also required to comply with payment card networks' special operating rules for Internet payment services. PayPal and its payment card processors have implemented specific business processes for merchant customers in order to comply with these rules, but any failure to comply could result in fines, the amount of which would be within the payment card networks' discretion. PayPal also could be subject to fines from payment card networks if it fails to detect that merchants are engaging in activities that are illegal or that are considered “high risk,” primarily the sale of certain types of digital content. For “high risk” merchants, PayPal must either prevent such merchants from using PayPal or register such merchants with payment card networks and conduct additional monitoring with respect to such merchants. PayPal has incurred fines from its payment card processors relating to PayPal's failure to detect the use of its service by “high risk” merchants. The amount of these fines has not been material, but did increase in 2011 compared to prior years. Any additional fines in the future would likely be for larger amounts, could become material and could result in a termination of PayPal's ability to accept payment cards or changes in PayPal's process for registering new customers, which would seriously damage PayPal's business.

Similarly, consumers of the websites operated by GSI's clients typically pay for purchases by payment card or similar payment method. Accordingly, our GSI ecommerce services business faces risks similar to the risks described above for PayPal.

Bill Me Later's operations expose us to additional risks.

Risks associated with our reliance on an unaffiliated lender in providing the Bill Me Later service are discussed in more detail under the caption “Bill Me Later's operations depend on lending services provided by an unaffiliated lender” above.

The Bill Me Later service relies on third-party merchant processors and payment gateways to process transactions. For the fiscal year ended December 31, 2011 and the six months ended June 30, 2012, approximately 69% and 63%, respectively, of all transaction volume by dollar amount through the Bill Me Later service was settled through the facilities of a single vendor. Any disruption to these third party payment processing and gateway services would adversely affect the Bill Me Later service.

The Bill Me Later service is offered to a wide range of consumers, and the financial success of this business depends on the ability of the issuing bank of the Bill Me Later credit products to manage credit risk related to those products. The lender extends credit using Bill Me Later's proprietary segmentation and credit scoring algorithms and other analytical techniques designed to analyze the credit risk of specific customers based on their past purchasing and payment history as well as their credit scores. Based on these performance criteria, the lender may extend or increase lines of credit to consumers at the point of sale. These algorithms and techniques may not accurately predict the creditworthiness of a consumer due to inaccurate assumptions about a particular consumer or the economic environment, among other factors. The accuracy of the predictions and the ability of the lender and Bill Me Later to manage credit risk related to the Bill Me Later service may also be affected by legal or regulatory changes (e.g., bankruptcy laws and minimum payment regulations), competitors' actions, changes in consumer behavior and other factors. The lender may incorrectly interpret the data produced by these algorithms in setting its credit policies, which may impact the financial performance of the Bill Me Later service. In addition, economic and financial conditions in the U.S. may affect consumer confidence levels and reduce consumers' ability or willingness to use credit, including the credit extended by the lender to consumers who use the Bill Me Later service, which could impair the growth and profitability of this business.

We anticipate that the volume of credit extended by WebBank (the financial institution issuing the Bill Me Later credit products) will increase as we continue to enable qualified buyers with a PayPal account to use Bill Me Later as a payment funding option for transactions on eBay.com and on certain merchant websites that accept PayPal. We purchase the receivables relating to these consumer loans extended by the issuing bank, and therefore bear the risk of loss. Like other businesses with

52

significant exposure to losses from consumer credit, the Bill Me Later service faces the risk that account holders will default on their payment obligations, making the receivables uncollectible and creating the risk of potential charge-offs. The rate at which receivables were charged off as uncollectible, or the net charge-off rate, was approximately 4.46% and 4.59%, respectively, for the fiscal year ended December 31, 2011 and the six months ended June 30, 2012. The nonpayment rate among Bill Me Later users may increase due to, among other things, worsening economic conditions, such as a recession in the U.S., and high unemployment rates. Consumers who miss payments on their obligations often fail to repay them, and consumers who file for protection under the bankruptcy laws generally do not repay their credit.

We currently fund the purchase of receivables related to Bill Me Later accounts through the sale of commercial paper, our cash balances and free cash flow generated from our portfolio of businesses. Effective September 1, 2010, we have funded the purchase of receivables generated through new Bill Me Later accounts using funds from our international subsidiaries, and this funding is facilitated through our Luxembourg-based bank. A downgrade in our credit ratings, particularly our short-term credit ratings, would likely reduce the amount of commercial paper we could issue (or, in certain circumstances, could prevent us from making commercial paper borrowings), increase our commercial paper borrowing costs, or both. If we are unable to fund our purchase of receivables related to the Bill Me Later business adequately or in a cost-effective manner, the growth and profitability of this business would be significantly and adversely affected.

Additionally, in providing the Bill Me Later service, we face other risks similar to those faced by PayPal described elsewhere in these Risk Factors, including under the captions “Government inquiries may lead to charges or penalties” and “If our Payments business is found to be subject to or in violation of any laws or regulations, including those governing money transmission, electronic funds transfer, money laundering, terrorist financing, sanctions, consumer protection, banking and lending, it could be subject to liability, licensure and regulatory approval and may be forced to change its business practices.”

PayPal's retail point of sale solutions expose us to additional risks.

PayPal has recently announced several retail point of sale solutions, including PayPal Here, which enables merchants to use a card reader attached to a mobile device (or to scan cards and checks using the device's embedded camera) to accept payment, as well as in-store pilot programs for new point of sale technologies, which are being rolled out on a limited basis to certain retailers in the U.S. As PayPal expands into point of sale transactions, PayPal will face even greater expectations from offline retailers regarding the reliability and availability of its systems and services and correspondingly lower amounts of downtime. PayPal's point of sale solutions may also be targeted by fraudsters; given that our fraud models are less developed in this area, we may experience increases in fraud and associated transaction losses as we adjust to fraudulent activity at the point of sale. The manufacturing and sale of a hardware product (the PayPal Here device) exposes us to potential product liability claims for which we could have substantial liability, and could require product recalls or other actions. PayPal's point of sale solutions also may subject us to increased exposure to other laws and regulations (e.g., export control regulations related to the shipment of the PayPal Here reader across national borders). There is significant competition at the retail point of sale, and there can be no assurance that merchants will adopt, or consumers will use, PayPal's retail point of sale solutions. Retail point of sale transactions also have lower profit margins than PayPal's other payment solutions. Unless we are able to drive adoption of, and significant volume through, our point of sale solutions over time, our business may suffer.

Changes in PayPal's funding mix could adversely affect PayPal's results.

PayPal pays significant transaction fees when customers fund payment transactions using credit cards, lower fees when customers fund payments with debit cards, nominal fees when customers fund payment transactions by electronic transfer of funds from bank accounts, and no fees when customers fund payment transactions from an existing PayPal account balance or through the Bill Me Later service, or use buyer credit issued by GE Money Bank. Customers fund a significant portion of PayPal's payment volume using credit and debit cards, and PayPal's financial success will remain highly sensitive to changes in the rate at which its senders fund payments using credit and debit cards. Customers may prefer funding payment transactions using credit cards or debit cards rather than bank account transfers for a number of reasons, including the ability to dispute and reverse charges directly with their payment card provider if merchandise is not delivered or is not as described, the ability to earn frequent flier miles, cash rebates, or other incentives offered by payment card issuers, the ability to defer payment, or a reluctance to provide bank account information to PayPal. In addition, some of PayPal's offerings, including the ability for buyers to make a limited number of payments without opening a PayPal account, have a higher rate of payment card funding than PayPal's basic product offering. Some of PayPal's plans to lower its funding costs, including both the Bill Me Later service and the ability for buyers to defer payment for a short period of time on some transactions, may increase the risk to PayPal of non-payment by buyers,

PayPal's failure to manage customer funds properly could harm its business.

53

PayPal's ability to manage and account accurately for customer funds requires a high level of internal controls. In some of the markets that PayPal serves and currencies that PayPal offers, PayPal has a limited operating history and limited experience in managing these internal controls. As PayPal's business continues to grow, it must continue to strengthen its internal controls accordingly. PayPal's success requires significant public confidence in its ability to handle large and growing transaction volumes and amounts of customer funds. Any failure to maintain necessary controls or to manage customer funds accurately could severely diminish customer use of PayPal's products.

Systems failures and resulting interruptions in the availability of our websites, applications, products or services could harm our business.

We have experienced system failures from time to time, and any interruption in the availability of our websites, applications, products or services will reduce our current revenues and profits, could harm our future revenues and profits and could subject us to regulatory scrutiny. Our eBay.com website has been interrupted for periods of up to 22 hours. In April 2012, technical systems issues resulted in eBay.com users being unable to checkout on our sites for a period of several hours. Our PayPal website has suffered intermittent unavailability for periods as long as five days, including unavailability for approximately three hours affecting payments primarily on our ebay.co.uk site in May 2011. Other of our websites (e.g., StubHub, Milo and others), as well as websites of GSI clients and hosted services offered by GSI's interactive marketing services business, have experienced intermittent unavailability from time to time. Any unscheduled interruption in our services results in an immediate, and possibly substantial, loss of revenues, as well as potential service credits or other payments by GSI to its clients. Frequent or persistent interruptions in our services could cause current or potential users to believe that our systems are unreliable, leading them to switch to our competitors or to avoid our sites, and could permanently harm our reputation and brands. Reliability is particularly critical for PayPal, which faces increased expectations on the part of users and merchants regarding the full-time availability of PayPal's services as it seeks to expand its Merchant Services business and gain acceptance of its retail point of sale solutions. Because PayPal is a regulated financial institution, frequent or persistent site interruptions could lead to fines, penalties, or mandatory and costly changes to PayPal's business practices, and ultimately could cause PayPal to lose existing licenses it needs to operate or prevent it from obtaining additional licenses that it needs to expand. Finally, because our customers may use our products for critical transactions, any system failures could result in damage to our customers' businesses. These customers could seek significant compensation from us for their losses. Even if unsuccessful, this type of claim likely would be time-consuming and costly for us to address.

Although our systems have been designed around industry-standard architectures to reduce downtime in the event of outages or catastrophic occurrences, they remain vulnerable to damage or interruption from earthquakes, floods, fires, power loss, telecommunication failures, terrorist attacks, cyber attacks, computer viruses, computer denial-of-service attacks, human error, hardware or software defects or malfunctions (including defects or malfunctions of components of our systems that are supplied by third-party service providers), and similar events or disruptions. Some of our systems, including our Shopping.com website and the systems related to the Bill Me Later business, are not fully redundant, and our disaster recovery planning is not sufficient for all eventualities. Our systems are also subject to break-ins, sabotage, and intentional acts of vandalism. Despite any precautions we may take, the occurrence of a natural disaster, a decision by any of our third-party hosting providers to close a facility we use without adequate notice for financial or other reasons, or other unanticipated problems at our hosting facilities could cause system interruptions and delays, and result in loss of critical data and lengthy interruptions in our services. We do not carry business interruption insurance sufficient to compensate us for losses that may result from interruptions in our service as a result of system failures.

If we are unable to cost-effectively upgrade and expand our websites, services and platforms, our business would suffer.

We must constantly add new hardware, update software and add new engineering personnel to accommodate the increased use of our websites and platforms, and the new products and features we regularly introduce. As our PayPal business continues to grow and expand both in terms of geographies and product offerings (e.g., PayPal's retail point of sale solutions), we are focused on updating our PayPal platform to provide increased scale, improved performance and additional built-in functionality addressing regulatory compliance matters (e.g., anti-money laundering). This upgrade process is expensive and time-consuming, and the increased complexity of our websites and the need to support multiple platforms as our portfolio of brands grows increases the cost of additional enhancements. Failure to upgrade our technology, features, transaction processing systems, security infrastructure, or network infrastructure in a timely and cost-effective manner to accommodate increased traffic or transaction volume or changes to our site functionality could harm our business. Adverse consequences could include unanticipated system disruptions, slower response times, degradation in levels of customer support, impaired quality of users' experiences of our services, impaired quality of services for third-party application developers using our externally accessible application programming interfaces and delays in reporting accurate financial information, and could result in customer dissatisfaction and the loss of existing users on our websites. We may be unable to effectively upgrade and expand our systems in a timely manner or smoothly integrate any newly developed or purchased technologies or businesses with our existing systems, and any failure to do so could result in problems on our sites. Further, steps to increase the reliability and redundancy of our systems are expensive, reduce our margins and may not be successful in reducing the frequency or duration of unscheduled downtime.

Risks associated with our ongoing efforts to enhance and unbundle the components of GSI's ecommerce and payments platform and to migrate GSI's existing customers to its new platform are discussed in more detail under the caption “If our GSI business is unable to enhance its platform and migrate clients to its new platform in a timely and cost-effective manner, it would be substantially harmed” above.

There are many risks associated with our international operations.

Our international expansion has been rapid and our international business, especially in Germany, Korea and the U.K., has also become critical to our revenues and profits. Net revenues outside the U.S. accounted for approximately 53% of our net revenues in both the fiscal year ended December 31, 2011 and the six months ended June 30, 2012. Expansion into international markets, such as our entry into Turkey in May 2011 upon the completion of our acquisition of additional shares in GittiGidiyor and PayPal's entry into emerging markets, are an increasing focus of our business. Geographical expansion requires significant management attention and resources and requires us to localize our services to conform to local cultures, laws, regulations, standards and policies. The commercial, financial, Internet, and transportation infrastructure in developing countries may make it more difficult for us to replicate our business models. Some of these developing countries may have legal regimes in which the application of laws and regulations in the online or mobile context is subject to greater uncertainty, as well as a higher incidence of corruption and fraudulent or unethical business practices, than countries in which we are historically accustomed to operating. In many countries, we compete with local companies that understand the local market better than we do, and we may not benefit from first-to-market advantages. We may not be successful in expanding into particular international markets or in generating revenues from foreign operations. For example, in 2002 we withdrew our eBay marketplace offering from the Japanese market, and in 2007 we contributed our business in China to a joint venture with a local Chinese company. Even if we are successful in developing new markets, we often expect the costs of operating new sites to exceed our net revenues from those sites for at least 12 months in most countries.

As we continue to expand our businesses internationally, including through acquisitions, we are increasingly subject to risks of doing business internationally, including the following:

- strong local competitors;
- regulatory requirements, including regulation of Internet and mobile services, auctioneering, professional selling, distance selling, privacy and data protection, banking and money transmitting, that may limit or prevent the offering of our services in some jurisdictions, prevent enforceable agreements between sellers and buyers, prohibit the listing of certain categories of goods, require product changes, require special licensure, subject us to various taxes, penalties or audits, or limit the transfer of information between us and our affiliates;
- customs and duties, including the possibility of significant delays at the border and the possibility that our services may be viewed as facilitating customs fraud;
- greater liability or legal uncertainty regarding our liability for the listings and other content provided by our users, including uncertainty as a result of legal systems that are less developed with respect to the Internet, unique local laws, conflicting court decisions and lack of clear precedent or applicable law;
- risks associated with cross-border transactions, including those described under the risk factor caption "Any factors that reduce cross-border trade could harm our business," above;
- potentially higher incidence of fraud and corruption and higher credit and transaction loss risks;
- cultural ambivalence towards, or non-acceptance of, trading or payments over the Internet or through mobile devices;
- laws and business practices that favor local competitors or prohibit or limit foreign ownership of certain businesses;
- difficulties in integrating with local payment providers, including banks, credit and debit card networks and electronic fund transfer systems;
- differing levels of retail distribution, shipping and Internet and mobile infrastructures;
- different employee/employer relationships and labor laws, and the existence of workers' councils and labor unions;
- difficulties in staffing and managing foreign operations;
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- challenges associated with joint venture relationships and minority investments, including dependence on our joint venture partners;
- difficulties in implementing and maintaining adequate internal controls;
- longer payment cycles, different accounting practices and greater problems in collecting accounts receivable;
- potentially adverse tax consequences, including local taxation of our fees or of transactions on our websites;

55

- higher Internet service provider costs;
- differing intellectual property laws;
- different and more stringent user protection, data protection, privacy and other laws;
- seasonal reductions in business activity;
- expenses associated with localizing our products and services, including offering customers the ability to transact business in the local currency and adapting our products and services to local preferences (e.g., payment methods) with which we may have limited or no experience;
- foreign exchange rate fluctuations;
- our ability to repatriate funds from abroad without adverse tax consequences;
- the possibility that foreign governments may impose currency controls or other restrictions on the repatriation of funds;
- volatility in a specific country's or region's political, economic or military conditions (e.g., in South Korea relating to its disputes with North Korea);
- challenges associated with maintaining relationships with local law enforcement and related agencies.

Some of these factors may cause our international costs of doing business to exceed our comparable domestic costs. As we expand our international operations and have additional portions of our international revenues denominated in foreign currencies, we also could become subject to increased difficulties in collecting accounts receivable and repatriating money without adverse tax consequences, as well as increased risks relating to foreign currency exchange rate fluctuations. The impact of currency exchange rate fluctuations on our business is discussed in more detail under the caption “We are exposed to fluctuations in currency exchange rates and interest rates” above.

Compliance with complex foreign and U.S. laws and regulations that apply to our international operations increases our cost of doing business. These numerous and sometimes conflicting laws and regulations include internal control and disclosure rules, data privacy and filtering requirements, anti-corruption laws, such as the Foreign Corrupt Practices Act, and other local laws prohibiting corrupt payments to governmental officials, and antitrust and competition regulations, among others. Violations of these laws and regulations could result in fines and penalties, criminal sanctions against us, our officers, or our employees, prohibitions on the conduct of our business and on our ability to offer our products and services in one or more countries, and could also materially affect our brands, our international expansion efforts, our ability to attract and retain employees, our business, and our operating results. Although we have implemented policies and procedures designed to ensure compliance with these laws and regulations, there can be no assurance that our employees, contractors, or agents will not violate our policies.

In addition, we conduct certain functions, including product development, customer support and other operations, in regions outside the U.S., particularly in India and China. We are subject to both U.S. and local laws and regulations applicable to our offshore activities, and any factors which reduce the anticipated benefits associated with providing these functions outside of the U.S., including cost efficiencies and productivity improvements, could adversely affect our business.

We maintain a portion of Shopping.com's research and development facilities and personnel in Israel, and have acquired other Israeli companies. Political, economic and military conditions in Israel affect those operations. Increased hostilities or terrorism within Israel or armed hostilities between Israel and neighboring countries or other entities could make it more difficult for us to continue our operations in Israel, which could increase our costs. In addition, many of our employees in Israel could be required to serve in the military for extended periods of time under emergency circumstances. Our Israeli operations could be disrupted by the absence of employees due to military service, which could adversely affect our business.

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

We have acquired a significant number of businesses, technologies, services and products, including most recently WHI Solutions, Inc. We expect to continue to evaluate and consider a wide array of potential strategic transactions as part of our overall business strategy, including business combinations, acquisitions and dispositions of businesses, technologies, services, products and other assets, as well as strategic investments and joint ventures. At any given time we may be engaged in discussions or negotiations with respect to one or more of these types of transactions. Any of these transactions could be material to our financial condition and results of operations.

These transactions involve significant challenges and risks. Some of the areas where we may face risks or difficulties include:

- the need to integrate the operations, systems (including accounting, management, information, human resource and other administrative systems), technologies, products and personnel of each acquired company, which is itself an inherently risky process; the inefficiencies and lack of control that may result if such integration is delayed or not implemented; and unforeseen difficulties and expenditures that may arise in connection with integration;
- diversion of management time, as well as a shift of focus from operating the businesses to issues related to integration and administration, particularly given the number, size and varying scope of our recent acquisitions;
- declining employee morale and retention issues resulting from changes in, or acceleration of, compensation, or changes in management, reporting relationships, future prospects, or the direction of the business;
- the need to implement controls, procedures and policies appropriate for a larger public company at companies that prior to acquisition had lacked such controls, procedures and policies;
- risks associated with our expansion into new international markets and doing business internationally, including those described under the risk factor caption "There are many risks associated with our international operations" above;
- difficulties in entering new markets where we have no or limited direct prior experience or where competitors may have stronger market positions;
- in the case of foreign acquisitions, the need to integrate operations across different cultures and languages and to address the particular economic, currency, political and regulatory risks associated with specific countries;
- the potential loss of key customers, vendors and other business partners of the companies we acquire following and continuing after announcement of our acquisition plans;
- in some cases, the need to transition operations, users and customers onto our existing or new platforms;
- liability for activities of the acquired company before the acquisition, including intellectual property and other litigation claims or disputes, violations of laws, rules and regulations, commercial disputes, tax liabilities and other known and unknown liabilities;
- the acquisition of new customer and employee personal information, in and of itself, may require regulatory approval and or additional controls, policies and procedures and subject us to additional exposure; and
- for investments in which an investee's financial performance is incorporated into our financial results, either in full or in part, the dependence on the investee's accounting, financial reporting and similar systems, controls and processes.

It may take us longer than expected to fully realize the anticipated benefits, such as increased revenue and enhanced efficiencies, of any or all of our acquisitions, and those benefits may ultimately be smaller than anticipated or may not be realized at all, which could adversely affect our business and operating results. Future acquisitions may also require us to issue additional equity securities, spend our cash, or incur debt (and increased interest expense), liabilities and amortization expenses related to intangible assets or write-offs of goodwill, which could adversely affect our results of operations and dilute the economic and voting rights of our stockholders.

In addition, we have made certain investments, including through joint ventures, in which we have a minority equity interest and lack management and operational control. The controlling joint venture partner in a joint venture investment may have business interests, strategies or goals that are inconsistent with ours, and business decisions or other actions or omissions of the controlling joint venture partner or the joint venture company may result in harm to our reputation or adversely affect the value of our investment in the joint venture. Our strategic investments may expose us to additional risks. For example, GSI's minority interest in Intershop Communications AG is governed by German law, which could subject us to liability for certain disadvantages to Intershop if we were deemed to be in control of Intershop under German law. We have also been sued by craigslist, which has alleged that we improperly misused confidential information from craigslist that we received as a minority investor. The complaint alleges breach of contract, breach of fiduciary duty, fraud, unfair competition and false advertising and seeks compensatory and punitive damages, recission and other relief.

Our acquisition of GSI Commerce, Inc. exposes us to additional risks.

Our GSI business faces certain risks and challenges not shared by our other businesses, including those described under the risk factor captions "If our GSI business is unable to enhance its platform and migrate clients to its new platform in a timely and cost-effective manner, it would be substantially harmed" and "Changes in regulations or user concerns regarding privacy and protection of user data could adversely affect our business."

Competition for GSI's existing and potential clients is intense, and our GSI business may not be able to add new clients or keep existing clients on favorable terms, or at all. For example, a change in the management of a GSI client could adversely

57

affect our relationship with that client. In addition, many of GSI's client contracts contain service level commitments. If our GSI business is unable to meet these commitments, its relationships with its clients could be damaged, and client rights to terminate their contracts with GSI and/or financial penalty provisions payable by GSI may be triggered. If any existing GSI clients were to exit the business we provide services to, be acquired, declare bankruptcy, suffer other financial difficulties, fail to pay amounts owed to GSI and/or terminate or modify their relationships with GSI in a manner unfavorable to us (in particular with respect to the large merchants and brands that GSI serves), our GSI business could be adversely affected.

A portion of GSI's ecommerce services revenue is derived from the value of ecommerce transactions that flow through GSI's ecommerce services business. Accordingly, growth in GSI's ecommerce services revenue depends upon the continued growth of the online businesses of its clients. GSI's ecommerce services business may be substantially impacted by any adverse conditions in the offline businesses of a GSI client that negatively impact that client's online businesses. Any impairment of the offline business of GSI clients, whether due to financial difficulties, impairment of client brands, reduction in marketing efforts, reduction in the number of client retail stores or otherwise, could negatively affect consumer traffic and sales through GSI's clients' websites, which would result in lower revenues generated by our GSI business. Our GSI business also relies on its clients' ability to accurately forecast product demand and select and buy the inventory for their corresponding online businesses. Under such arrangements, the client establishes product prices and pays GSI service fees based either on a fixed or variable percentage of revenues, or on the activity performed. As a result, if GSI's clients fail to accurately forecast product demand or optimize or maintain access to inventory, the client's ecommerce business (and, in turn, GSI's service fees) could be adversely affected.

Our GSI business holds some inventory on behalf of its ecommerce services customers. If GSI is unable to effectively manage and handle this inventory, this may result in unexpected costs that could adversely affect our GSI business. Any theft of such inventory, or damage or interruption to such inventory, including as a result of earthquakes, floods, fire, power loss, labor disputes, terrorist attacks and similar events and disruptions, could result in losses related to such inventory and disruptions to GSI's customers' businesses, which could in turn adversely affect our GSI business.

Our GSI business processes personal information on behalf of its ecommerce services clients. The personal information of customers of certain websites operated by GSI's clients may be regulated under the Gramm-Leach-Bliley Act, the Health Insurance Portability and Accountability Act, the Children's Online Privacy Protection Act, or other privacy laws and regulations. In some cases, GSI's use or disclosure of that information may be restricted by contractual terms, laws and regulations, and any misuse or unpermitted disclosure of that information could negatively impact GSI and its clients.

GSI's interactive marketing services business relies on email marketing to drive consumer traffic to the websites operated by its clients. Email could become a less effective means of communicating with and marketing to consumers for a variety of reasons, including: problems with technology that make GSI's email communications more difficult to deliver and for consumers to read (e.g., the inability of smart phones or similar communication devices to adequately display email); consumers may disregard marketing emails due to the large volume of such emails they receive; the inability of filters to effectively screen for unwanted emails, resulting in increased levels of junk mail, or “SPAM,” which may overwhelm consumer's email accounts; increased use of social networking sites, which may result in decreased use of email as a primary means of communication; continued security concerns regarding Internet usage in general from viruses, worms or similar problems; and increased governmental regulation or restrictive policies adopted by Internet service providers that make it more difficult or costly to utilize email for marketing communications. If any of our GSI entities were to end up on SPAM lists or lists of entities that have been involved in sending unwanted, unsolicited emails, their ability to contact customers through email could be significantly restricted. If any of the foregoing were to occur, the demand for GSI's email marketing solutions could decrease and our GSI business could be harmed. GSI's interactive marketing services business also utilizes mobile messaging as a means of communicating with consumers, which carries risks similar to the risks described above for email marketing.

Our GSI business has relationships with search engines, comparison shopping sites, affiliate marketers, online advertising networks and other websites to provide content, advertising banners and other links to its clients' ecommerce businesses. Our GSI business relies on these relationships as significant sources of traffic to clients' ecommerce businesses. If we are unable to maintain these relationships or enter into new relationships on acceptable terms, our ability to attract new customers could be harmed.

Immediately following our acquisition of GSI, eBay sold 100% of GSI's sports merchandise business and 70% of its RueLaLa and ShopRunner businesses (which we refer to collectively as the divested entities), to Kynetic LLC, which we refer to as Kynetic. Kynetic is primarily owned by GSI's former Chairman, President and Chief Executive Officer, Mr. Michael Rubin. Each of the divested entities was a direct or indirect wholly-owned subsidiary of GSI Commerce. In connection with (and as a result of) the divestiture to Kynetic, our GSI business maintains certain commercial and financial relationships with

58

the divested entities which expose it to certain risks of the businesses of Kynetic and the divested entities.
As part of the Kynetic divestiture, we loaned Kynetic and the divested entities $467 million, which is secured by certain assets of the divested entities. Kynetic and the divested entities' ability to repay this obligation is dependent on the financial performance of Kynetic and the divested entities. If Kynetic is unable to repay this obligation, our results of operations and financial condition could be harmed.
Finally, our GSI business is also party to certain acquisition agreements relating to entities purchased by GSI prior to our acquisition, and which relate to businesses owned by the divested entities. Kynetic has agreed to indemnify GSI for certain liabilities incurred by GSI under these acquisition agreements. If such liabilities were realized and Kynetic was not able or willing to meet its indemnification obligations, GSI would be liable for them and its business could be harmed.
Our business and users may be subject to sales tax and other taxes.
The application of indirect taxes (such as sales and use tax, value-added tax (VAT), goods and services tax, business tax and gross receipt tax) to ecommerce businesses such as eBay and to our users is a complex and evolving issue. Many of the fundamental statutes and regulations that impose these taxes were established before the adoption and growth of the Internet and ecommerce. In many cases, it is not clear how existing statutes apply to the Internet or ecommerce. In addition, some jurisdictions have implemented or may implement laws specifically addressing the Internet or some aspect of ecommerce. For example, the State of New York has passed legislation that requires any out-of-state seller of tangible personal property to collect and remit New York use tax if the seller engages affiliates above certain financial thresholds in New York to perform certain business promotion activities. Several ecommerce companies are challenging this new law. In June 2011, California enacted legislation that required certain out-of-state retailers to collect and remit California use tax on taxable sales to California purchasers when the retailer has a relationship with a person in California that refers customers to the retailer. In September 2011, the California Governor signed into law AB 155, which superseded the prior law and delayed the implementation of such collection and remittance requirements until September 15, 2012 or January 1, 2013. The effective date of the law was dependent on whether or not the U.S. Congress enacted legislation in this area by July 1, 2012. Because federal legislation has not been enacted, the effective date of California's new law will be September 15, 2012. The new law is similar to the law passed in New York, but provides exclusions for certain forms of Internet marketing and is limited to retailers who exceed prescribed sales volume thresholds. However, if our sellers who are not already required to collect California sales or use tax believe that their use of our websites requires them to collect California use tax, they may elect to limit their use of our websites rather than collect the tax, which would harm our business. North Carolina, Rhode Island, Illinois, Arkansas and South Dakota have also enacted similar laws related to affiliates, and a number of other states appear to be considering similar legislation. In addition, the Pennsylvania Department of Revenue has ruled that an out-of-state retailer using Pennsylvania-based affiliates could have nexus in Pennsylvania under existing statutes. Most of these new laws and positions are being challenged and in May 2012, a Cook County Circuit Court judge ruled that the Illinois Internet Affiliate Nexus Law was unconstitutional. The State of Illinois has filed a direct appeal to the Illinois Supreme Court. The adoption of such legislation by states where eBay has significant operations that perform certain business promotion activities could result in a use tax collection responsibility for certain of our sellers. This collection responsibility and the additional costs associated with complex use tax collection, remittance and audit requirements would make selling on our websites less attractive for small business retailers, and would harm our business.
The State of Colorado has enacted legislation that takes a different approach by imposing a set of use tax notice and reporting requirements (but not the actual tax collection responsibility) on certain retailers with no physical presence in Colorado. The law is designed to aid Colorado in collecting use tax from Colorado residents who purchase taxable items from out-of-state retailers. The regulation promulgated by the Colorado Department of Revenue excludes from these reporting obligations businesses that sell $100,000 or less into the state in a calendar year, thus limiting the impact on our sellers. The law has been challenged in Federal Court by a number of out-of-state retailers and a Federal District Court has issued an injunction blocking enforcement of the regulations pending a resolution of the case. In March 2012, a federal judge struck down the Colorado law as unconstitutional finding that it discriminated against interstate commerce. It is expected that the State will appeal the decision. Oklahoma has enacted a similar law. While

the recent laws in California, New York, North Carolina, Rhode Island, Illinois, Arkansas, South Dakota, Oklahoma and Colorado do not specifically apply to our Marketplaces business, the proliferation of such state legislation, to expand sales and use tax collection on Internet sales, could adversely affect some of our sellers and indirectly harm our business.

In conjunction with the Streamlined Sales Tax Project - an ongoing, multi-year effort by U.S. state, and local governments to require collection and remittance of remote sales tax by out-of-state sellers - S. 1452 and H.R. 2701, U.S. Senate and U.S. House versions of the Main Street Fairness Act, have been introduced in the 112th Congress. These measures would allow states that meet certain simplification and other standards to require out-of-state sellers to collect and remit sales taxes on goods purchased by in-state residents. Sellers meeting an as yet undefined small seller exception would be excluded from the requirements of the Act. Other legislation introduced in the US Congress, including H.R. 3179 and S. 1832, would grant states the authority to require out-of-state retailers to collect and remit sales taxes without requiring the state to join the Streamlined Sales Tax Project. The adoption of remote sales tax collection legislation that lacks a robust small business exemption would result in the imposition of sales taxes and additional costs associated with complex sales tax collection, remittance and audit compliance requirements on a number of our sellers. This would make selling online less attractive for small retailers, and could harm our business.

From time to time, some taxing authorities have notified us that they believe we owe them certain taxes. In May 2008, the City of Chicago notified both eBay and StubHub that they are liable for a city amusement tax on tickets to events in Chicago, irrespective of the location of the buyer or seller, and filed suit to enforce collection of taxes it claims are due. In March 2009, the court ruled that StubHub is not required to collect and remit the city amusement tax. The City of Chicago requested reconsideration of this ruling and StubHub sought clarification of the ruling relative to the remaining counts as well. In August 2009, the court entered a final order dismissing the case against StubHub. In December 2009, the court also dismissed the case against eBay. The City of Chicago appealed both matters to the Seventh Circuit Court of Appeals. The Seventh Circuit has issued an opinion in the StubHub matter rejecting the federal arguments advanced by StubHub and certifying the state law arguments to the Illinois State Supreme Court. In October 2011, the Illinois Supreme Court ruled that state municipalities may not require electronic intermediaries such as StubHub to collect and remit amusement taxes on resold tickets. The City of Chicago has requested a rehearing before the Illinois Supreme Court and the court has not yet ruled on that request. The application of similar existing or future laws could adversely affect our business.

Several proposals have been made at the U.S. state and local level that would impose additional taxes on the sale of goods and services over the Internet. These proposals, if adopted, could substantially impair the growth of ecommerce and our brands, and could diminish our opportunity to derive financial benefit from our activities. The U.S. federal government's moratorium on state and local taxation of Internet access or multiple or discriminatory taxes on ecommerce has been extended through November 2014. This moratorium does not prohibit federal, state, or local authorities from collecting taxes on our income or from collecting certain taxes that were in effect prior to the enactment of the moratorium and/or one of its extensions.

Similar issues exist outside of the U.S., where the application of VAT or other indirect taxes on ecommerce providers such as eBay is uncertain and evolving. While we attempt to comply in those jurisdictions where it is clear that a tax is due, certain of our subsidiaries have, from time to time, received claims relating to the applicability of indirect taxes to our fees. In April 2012, we received Notices of Reassessments for tax years 2001-2005 from the Canadian Revenue Agency ("CRA") which assert goods and service tax (GST) and harmonized sales tax (HST) on our fees charged to Canadian users. These reassessments of GST/HST were the result of an audit of eBay International AG and are based on the CRA's assertion that we were "doing business" in Canada for GST/HST purposes. We disagree with the reassessments and filed a Notice of Appeal with the Tax Court of Canada in July 2012. Should such taxes become applicable, our business could be harmed. We collect and remit indirect taxes in certain jurisdictions. However, tax authorities may raise questions about our obligation to collect and remit such taxes, as well as the proper calculation of such taxes. For example, the Korean tax authority asserted that certain coupons and incentives available on our sites should not be deducted when computing taxes on our fees. We challenged these assessments and in June 2012 the National Tax Tribunal issued a final ruling in our favor. Should any new taxes become applicable to our fees or if the taxes we pay are found to be deficient, our business could be harmed.

We do not collect taxes on the goods or services sold by users of our services. One or more states or the federal government or foreign countries may seek to impose a tax collection, reporting or record-keeping obligation on companies that engage in or facilitate ecommerce. Such an obligation could be imposed by legislation intended to improve tax compliance (and legislation to such effect has been contemplated by several states and a number of foreign jurisdictions) or if an eBay company was ever deemed to be the legal agent of the users of our services by a jurisdiction in which eBay operates. In July 2008, the Housing and Economic Recovery Act of 2008 (H.R. 3221) was signed into law. This law contains provisions that require companies that provide payments over electronic means to users to report to the Internal Revenue Service (IRS) information on payments received by certain customers. The legislation, effective for payments received after December 31, 2010, requires PayPal and other electronic payments processors, as well as StubHub and similar companies, to report to the IRS on customers subject to U.S. income tax who receive more than $20,000 in payments and more than 200 payments in a calendar year, to request tax ID numbers from U.S. taxpayers, track payments by tax ID number and withhold a proportion of payments and forward such withholding to the IRS if customers who receive more than 200 payments do not provide correct and complete information. We have had to modify our software to meet these requirements and expect increased operational costs and changes to our user experience in connection with complying with these reporting obligations. The IRS regulations also require us to collect a certification of non-U.S. taxpayer status from certain international merchants. These requirements may decrease seller activity on our sites and harm our business. Any failure by us to meet these new requirements could result in substantial monetary penalties and other sanctions and could harm our business.

One or more other jurisdictions may also seek to impose tax collection or reporting obligations based on the location of the product or service being sold or provided in an ecommerce transaction, regardless of where the respective users are located. Imposition of a discriminatory record keeping or tax collecting requirement could decrease seller activity on our sites and would harm our business. Foreign authorities may also require eBay to help ensure compliance by our users with local laws regulating professional sellers, including tax requirements. In addition, we have periodically received requests from tax authorities in many jurisdictions for information regarding the transactions of large classes of sellers on our sites, and in some cases we have been legally obligated to provide this data. The imposition of any requirements on us to disclose transaction records for all or a class of sellers to tax or other regulatory authorities or to file tax forms on behalf of any sellers, especially requirements that are imposed on us but not on alternative means of ecommerce, and any use of those records to investigate, collect taxes from, or prosecute sellers, could decrease seller activity on our sites and harm our business.

We pay input VAT on applicable taxable purchases within the various countries in which we operate. In most cases, we are entitled to reclaim this input VAT from the various countries. However, because of our unique business model, the application of the laws and rules that allow such reclamation is sometimes uncertain. A successful assertion by one or more countries that we are not entitled to reclaim VAT could harm our business.

We continue to work with the relevant tax authorities and legislators to clarify eBay's obligations under new and emerging laws and regulations. Passage of new legislation and the imposition of additional tax or tax-related reporting requirements could harm our users and our business. There have been, and will continue to be, substantial ongoing costs associated with complying with the various indirect tax requirements in the numerous markets in which eBay conducts or will conduct business.

Our tickets business is subject to regulatory, competitive, and other risks that could harm this business.

Our tickets business, which includes our StubHub business, is subject to numerous risks. Many jurisdictions have laws and regulations covering the resale of event tickets. Some jurisdictions prohibit the resale of event tickets at prices above the face value of the tickets or at all, or highly regulate the resale of tickets, and new laws and regulations or changes to existing laws and regulations imposing these or other restrictions may be adopted that could limit or inhibit our ability to operate, or our users' ability to continue to use, our tickets business. For example, in 2012, France passed a law prohibiting the habitual resale of event tickets without permission from the event organizer. In addition, the unauthorized resale of football (soccer) tickets is illegal in the U.K., where a StubHub site was recently launched. Regulatory agencies or courts may claim or hold that we are responsible for ensuring that our users comply with these laws and regulations or that we or our users are either subject to licensure or prohibited from reselling event tickets in their jurisdictions. In October 2007, two plaintiffs filed a purported class action lawsuit in North Carolina Superior Court alleging that StubHub sold (and facilitated and participated in the sale) of concert tickets to plaintiffs with the knowledge that the tickets were resold in violation of North Carolina's maximum ticket resale price law (which has been subsequently amended). In February 2011, the trial court granted plaintiffs' motion for summary judgment, concluding that immunity under the Communications Decency Act did not apply. The trial court further held that StubHub violated the North Carolina unfair and deceptive trade practices statute as it pertained to the two named plaintiffs, and certified its decision for immediate appeal to the North Carolina Court of Appeals. In February 2012, the North Carolina Court of Appeals overturned the lower court's decision. The plaintiffs are appealing the appellate court ruling.

Some event organizers and professional sports teams have expressed concern about the resale of their event tickets on our sites. Suits alleging a variety of causes of actions have in the past, and may in the future, be filed against StubHub and eBay by venue owners, competitors, ticket buyers and unsuccessful ticket buyers. Such litigation could result in damage awards, could require us to change our business practices in ways that may be harmful to our business, or could otherwise negatively affect our tickets business.

Our tickets business is subject to seasonal fluctuations and the general economic and business conditions that impact the sporting events and live entertainment industries. The economic downturn resulted in a decrease in ticket prices sold on our sites and negatively impacted revenue and profits. In addition, a work stoppage, strike or lockout by a professional sports league (for example, the recent National Basketball Association lockout) that results in the cancellation of all or a portion of the games in a league's season would harm our tickets business. In addition, a portion of the tickets inventory sold by sellers on the StubHub website is processed by StubHub in digital form. Systems failures, security breaches, theft or other disruptions that result in the loss of such sellers' tickets inventory could materially harm our tickets business.

Our tickets business also faces significant competition from a number of sources, including ticketing service companies (such as Live Nation Entertainment/Ticketmaster, AEG, Comcast-Spectacor and Tickets.com), event organizers (such as professional sports teams and leagues), ticket brokers and online and offline ticket resellers, such as TicketsNow (which is owned by Live Nation Entertainment) and RazorGator. In addition, some ticketing service companies and event organizers

61

have begun to issue event tickets through various forms of electronic ticketing systems that are designed to restrict or prohibit the transferability (and by extension, the resale) of such event tickets. Ticketing service companies have also begun to use market-based pricing strategies or dynamic pricing to charge much higher prices than they historically have for premium tickets. Besides charging higher prices, these ticketing service companies have also imposed additional restrictions on transferability for these types of tickets, such as requiring customers to pick up these tickets at will-call with the purchasing credit card. To the extent that event tickets issued in this manner cannot be resold on our websites, or to the extent that we are otherwise unable to compete with these competitors, our tickets business would be harmed. Pursuant to commercial arrangements with certain of its partners, StubHub provides some of its sellers with the ability to conduct integrated resale transactions, which consumers may prefer due to, among other factors, much quicker delivery and lower fraud concerns. These integrations are largely deal-dependent, and these arrangements may not be renewed on favorable terms, or at all.

We depend on key personnel.

Our future performance depends substantially on the continued services of our senior management and other key personnel and our ability to retain and motivate them. We do not have long-term employment agreements with any of our key personnel and do not maintain any “key person” life insurance policies, and some members of our senior management team have fully vested the vast majority of their in-the-money equity incentives. The loss of the services of any of our executive officers or other key employees could harm our business.

Our businesses all depend on attracting and retaining key personnel. Our future success will depend on our ability to attract, train, retain and motivate highly skilled technical, managerial, marketing and customer support personnel. Competition for these personnel is intense, and we may be unable to successfully attract, integrate, or retain sufficiently qualified personnel. In making employment decisions, particularly in the Internet and high-technology industries, job candidates often consider the value of the equity awards they would receive in connection with their employment. Fluctuations in our stock price may make it more difficult to retain and motivate employees.

Problems with or price increases by third parties who provide services to us or to our users could harm our business.

A number of parties provide services to us or to our users that benefit us. Such services include seller tools that automate and manage listings, merchant tools that manage listings and interface with inventory management software, storefronts that help our users list items, caching services that make our sites load faster and shipping providers that deliver goods sold on our platform, among others. In some cases we have contractual agreements with these companies that give us a direct financial interest in their success, while in other cases we have none. PayPal is dependent on the processing companies and banks that link PayPal to the payment card and bank clearing networks. Similarly, Bill Me Later relies on an unaffiliated lender in providing the Bill Me Later service and also relies heavily on third parties to operate its services, including merchant processors and payment gateways to process transactions. Financial or regulatory issues, labor issues (e.g., strikes or work stoppages) or other problems that prevent these companies from providing services to us or our users could reduce the number of listings on our websites or make completing transactions or payments on our websites more difficult, thereby harming our business.

Price increases by, or service terminations, disruptions or interruptions at, companies that provide services to our users and clients (such as postal and delivery services, and our recently announced plans for a global shipping solution intended to facilitate cross-border transactions between buyers and sellers) could also reduce the number of listings on our websites or make it more difficult for our sellers to complete transactions or for us to timely fulfill and ship products sold on the websites operated by GSI's clients, thereby harming our business. Some third-parties who provide services to us may have or gain market power and be able to increase their prices to us without competitive constraint. In addition, the U.S. Postal Service has announced that it is considering closing thousands of local post offices and ending Saturday mail delivery. While we continue to work with global carriers to offer our sellers a variety of shipping options and to enhance our shipping experience, these closures could require certain sellers to utilize alternatives which could be more expensive or inconvenient, which could in turn decrease the velocity of trade on our site, thereby harming our business. Any security breach at a company providing services to our users could also adversely affect our customers and harm our business. We have outsourced certain functions to third-party providers, including some customer support and product development functions, which are critical to our operations. If our service providers do not perform satisfactorily, our operations could be disrupted, which could result in user

dissatisfaction and adversely affect our velocity of trade, business, reputation and operating results
Although we generally have been able to renew or extend the terms of contractual arrangements with, or if necessary replace, third parties who provide services to us on acceptable terms, there can be no assurance that we will continue to be able to do so in the future. If any third parties were to stop providing services to us on acceptable terms, including as a result of bankruptcy due to poor economic conditions, we may be unable to procure alternatives from other third parties in a timely and efficient manner and on acceptable terms, or at all. In addition, there can be no assurance that third parties who provide services

directly to our users will continue to do so on acceptable terms, or at all.
Customer complaints or negative publicity about our customer support or anti-fraud measures could diminish use of our services.
Customer complaints or negative publicity about our customer support could severely diminish consumer confidence in and use of our services. Measures that we sometimes take to combat risks of fraud and breaches of privacy and security have the potential to damage relations with our customers or decrease activity on our sites by making our sites more difficult to use or restricting the activities of certain users. These measures heighten the need for prompt and accurate customer support to resolve irregularities and disputes. Effective customer support requires significant personnel expense, and if not managed properly, this expense could significantly impact our profitability. Failure to manage or train our own or outsourced customer support representatives properly could compromise our ability to handle customer complaints effectively. Negative publicity about, or negative experiences with, customer support for any of our businesses could cause our reputation to suffer or affect consumer confidence in our brands individually or as a whole. Because PayPal is providing a financial service and operating in a more regulated environment, PayPal must provide both telephone and email customer support and resolve certain customer contacts within shorter time frames. As part of PayPal's program to reduce fraud losses and prevent money laundering, PayPal may temporarily restrict the ability of customers to withdraw their funds if those funds or the customer's account activity are identified by PayPal's risk models as suspicious. PayPal has in the past received negative publicity with respect to its customer support and account restrictions, and has been the subject of purported class action lawsuits and state attorney general inquiries alleging, among other things, failure to resolve account restrictions promptly. In the second quarter of 2010, two putative class-action lawsuits (Devinda Fernando and Vadim Tsigel v. PayPal, Inc.; and Moises Zepeda v. PayPal, Inc.) were filed in the U.S. District Court in the Northern District of California. These lawsuits contain allegations that PayPal improperly held users' funds or otherwise improperly limited user's accounts. These lawsuits seek damages as well as changes to PayPal's practices among other remedies. A determination that there have been violations of laws relating to PayPal's practices could expose PayPal to significant liability. Any changes to PayPal's practices resulting from these lawsuits could require PayPal to incur significant costs and to expend product resources, which could delay other planned product launches or improvements and further harm our business. If PayPal is unable to provide quality customer support operations in a cost-effective manner, PayPal's users may have negative experiences, PayPal may receive additional negative publicity, its ability to attract new customers may be damaged and it could become subject to additional litigation. As a result, current and future revenues could suffer, losses could be incurred and its operating margins may decrease.
Our industries are intensely competitive.
Marketplaces
Our Marketplaces businesses currently or potentially compete with a large number of online and offline companies providing particular categories of goods and/or broader ranges of goods. The Internet provides new, rapidly evolving and intensely competitive channels for the sale of all types of goods. We expect competition to intensify in the future. The barriers to entry into these channels can be relatively low, and current offline and new competitors, including small businesses who want to create and promote their own stores, can easily launch online sites at nominal cost using commercially available software or partnering with any one of a number of successful ecommerce companies. Online and offline businesses increasingly are competing with each other, consumers who purchase or sell goods and services through our Marketplaces businesses have more and more alternatives, and merchants have more channels to reach consumers.
Our competitors include the vast majority of traditional department, warehouse, boutique, discount and general merchandise stores (as well as the online operations of these traditional retailers), online retailers, online classified services and other shopping channels such as offline and online home shopping networks. In the U.S., these include Wal-Mart, Target, Sears, Macy's, JC Penney, Costco, Office Depot, Staples, OfficeMax, Sam's Club, Amazon.com (which continues to expand into new geographies and lines of business), Buy.com (owned by Rakuten), AOL.com, Yahoo! Shopping, MSN, QVC and Home Shopping Network, among others.
A number of companies offer a variety of services that provide channels for buyers to find and buy items from sellers of all sizes, including online aggregation and classifieds websites such as craigslist (in which we own a minority

equity stake), Google Merchant Center, Oodle.com and a number of international websites operated by Schibsted ASA. In certain markets, our fixed-price listing and traditional auction-style listing formats are increasingly being challenged by other formats, such as classifieds. Our classifieds websites, including Den Blå Avis, BilBasen, eBay Classifieds (including eBay Anuncios, eBay Kleinanzeigen and eBay Annunci), Gumtree, Kijiji, LoQUo, Marktplaats.nl, mobile.de and Alamaula, offer classifieds listings in the U.S. and a variety of local international markets. In many markets in which they operate, including in the U.S., our classified platforms compete against more established online and offline classifieds platforms.

Our online shopping comparison site, Shopping.com, competes with sites such as Bing Shopping, Buy.com, Google Product Search/Google Shopping, Nextag.com, Pricegrabber.com, Shopzilla and Yahoo! Product Search, which offer shopping search engines that allow consumers to search the Internet for specified products. Recent legal developments may affect the utility of shopping comparison sites if manufacturers limit variation in product pricing. In addition, sellers are increasingly utilizing multiple sales channels, including the acquisition of new customers by paying for search-related advertisements on horizontal search engine sites such as Bing, Google, Yahoo!, Naver and Baidu. We use product search engines and paid search advertising to help users find our sites, but these services also have the potential to divert users to other online shopping destinations. Consumers may choose to search for products and services with a horizontal search engine instead of our sites, and horizontal search engines may send users to other shopping destinations instead of our sites.

We also compete with many local, regional, and national specialty retailers and exchanges in each of the major categories of products offered on our site. For example, category-specific competitors to offerings in our Motors (Parts and Accessories) category include: Advanceautoparts.com, Auto Parts Warehouse, AutoAnything, Autozone, Car Domain, Discount Tire Direct, jcwhitney.com, Motorcycle Superstore, O'Reilly Auto Parts, Rockauto.com, Tirerack.com, newspaper and online classifieds, used car dealers, swap meets, car clubs and vehicle recyclers.

Our international Marketplaces websites compete with similar online and offline channels in each of their vertical categories in most countries. In addition, they compete with general online ecommerce sites such as: Amazon, Rakuten.de, Quelle and Otto in Germany; Leboncoin.fr and PriceMinister (owned by Rakuten) in France; Taobao in China; Tradus (owned by Naspers) in Poland; Yahoo-Kimo in Taiwan; Lotte, Naver and 11th Street in South Korea; Trading Post, OZtion and Aussie Bidder in Australia; and Amazon and Play.com (owned by Rakuten) in the United Kingdom and other countries. In some of these countries, there are online sites that have much larger customer bases and greater brand recognition than we do, as well as competitors that may have a better understanding of local culture and commerce than we do. As our businesses in developing countries grow, we increasingly may compete with domestic competitors which have advantages we do not possess, such as a greater ability to operate under local regulatory authorities.

The principal competitive factors for Marketplaces include the following:

- ability to attract, retain and engage buyers and sellers;
- volume of transactions and price and selection of goods;
- trust in the seller and the transaction;
- customer service; and
- brand recognition.

With respect to our online competition, additional competitive factors include:

- community cohesion, interaction and size;
- website ease-of-use and accessibility;
- system reliability;
- reliability of delivery and payment;
- level of service fees; and
- quality of search tools.

We may be unable to compete successfully against current and future competitors. Some current and potential competitors have longer operating histories, larger customer bases and greater brand recognition in other business and Internet sectors than we do. Other online ecommerce sites may be acquired by, receive investments from, or enter into other commercial relationships with well-established and well-financed companies. As a result, some of our competitors with other revenue sources may be able to devote more resources to marketing and promotional campaigns, adopt more aggressive pricing policies and devote substantially more resources to website and systems development than we can. Some of our competitors may offer or continue to offer free shipping, favorable return policies or other transaction-related services which improve the user experience on their sites and which could be impractical or inefficient for eBay sellers to match. Our competitors may be able to innovate faster than we can, and new technologies may further increase the competitive pressures by enabling our competitors to offer more efficient or lower-cost services. Our competitors may be able to use the advantages of brick-and-mortar stores or other sorts of physical presence.

64

In addition, certain established retailers may encourage manufacturers to limit or cease distribution of their products to dealers who sell through online channels such as eBay. Retailers may attempt to use existing or future government regulation to prohibit or limit online commerce in certain categories of goods or services. Manufacturers may attempt to enforce minimum resale price maintenance or minimum advertised price arrangements to prevent distributors from selling on our websites or on the Internet generally, or at prices that would make our site attractive relative to other alternatives. For example, in June 2012, Adidas Group announced that it intends to restrict its dealers, on a global basis, from listing and selling Adidas and Reebok products on sites including eBay.com. The adoption by manufacturers of policies, or the adoption of new laws or regulations or interpretations of existing laws or regulations by government authorities, in each case discouraging or restricting the sales of goods or services over the Internet, could force eBay users to stop selling certain products on our websites. Increased competition or anti-Internet distribution policies or regulations may result in reduced operating margins, loss of market share and diminished value of our brands. As we respond to changes in the competitive environment, we may, from time to time, make pricing, service or marketing decisions or acquisitions that may be controversial with and lead to dissatisfaction among some of our sellers, which could reduce activity on our websites and harm our profitability.
Although we have established Internet traffic arrangements with several large online services and search engine companies, these arrangements may not be renewed on favorable terms or these companies may decide to promote competitive services. Even if these arrangements are renewed, they may not result in increased usage of our sites. In addition, companies that control user access to transactions through network access, Internet browsers, mobile networks or search engines could promote our competitors, channel current or potential users to their vertically integrated electronic commerce sites or their advertisers' sites, attempt to restrict access to our sites, or charge us substantial fees for inclusion. Search engines are increasingly becoming a starting point for online shopping, and as the costs of operating an online store continue to decline, online sellers may increasingly sell goods through multiple channels, which could reduce the number and value of transactions these sellers conduct through our sites. PayPal
The markets for PayPal's products and services are intensely competitive and are subject to rapid technological change, including but not limited to: mobile payments, electronic funds transfer networks allowing Internet access, cross-border access to networks, creation of new networks, expansion of prepaid cards and bill pay networks. PayPal faces competition and potential competition from existing online and offline payment methods, including, among others:

- payment card processors that offer their services to online merchants and multi-channel merchants, including American Express, Chase Paymentech, First Data, Wells Fargo, WorldPay, Barclays Merchant Services, Global Payments, Inc., Square and Stripe, and payment gateways, including CyberSource and Authorize.net (both owned by Visa), Braintree and First Data;
- money remitters such as MoneyGram, Western Union, Global Payments, Inc. and Euronet;
- bill payment services, including CheckFree, a subsidiary of Fiserv;
- processors that provide online merchants the ability to offer their customers the option of paying for purchases from their bank account or paying on credit, including ClearXchange (a joint venture among Wells Fargo, Bank of America and JP Morgan Chase), Western Union's WU Pay, Dwolla, Acculynk, TeleCheck (a subsidiary of First Data), iDEAL in the Netherlands, Sofortuberweisung in Germany and the recently-announced MyBank pan-European initiative;
- providers of “digital wallet” services that offer customers the ability to pay online or on mobile devices through a variety of payment methods, including the new V.me announced by Visa, American Express's Serve and Google Wallet;
- providers of traditional payment methods, particularly credit cards, checks, money orders and Automated Clearing House transactions;
- issuers of stored value targeted at online payments, including VisaBuxx, NetSpend, Green Dot, PayNearMe and UKash;
- mobile payments, including ISIS, Buyster, Mpass, O2 Money, Project Oscar, Boku, Venmo and Crandy, many of which are owned by or supported by major mobile carriers;
- Amazon Payments, which offers merchants the ability to accept credit card- and bank-funded payments from Amazon's base of online and mobile customers on the merchant's own website;

- Google Checkout, which has been integrated into the Google Wallet service and which enables the online and mobile payment of merchants using credit cards;
- AliPay, an online payment services provider which operates primarily in China but has announced plans to expand internationally;
- Other providers of online account-based payments, such as Skrill (formerly known as MoneyBookers), ClickandBuy (owned by Deutsche Telekom), Barclays Pingit and Kwixo (primarily in the EU), Paymate and Visa PayClick in Australia;
- payment services targeting users of social networks and online gaming, including PlaySpan (which Visa has

65

acquired) and Boku;

- payment services enabling banks to offer their online banking customers the ability to send and receive payments through their bank account, including ZashPay from Fiserv and Popmoney from CashEdge, both of which have announced collaboration agreements with Visa (CashEdge has been acquired by Fiserv); and
- online shopping services that provide special offers linked to a specific payment provider, such as Visa's RightCliq, MasterCard MarketPlace, TrialPay and Tapjoy.

Some of these competitors have longer operating histories, significantly greater financial, technical, marketing, customer service and other resources, greater brand recognition, or a larger base of customers than PayPal, and may be also be able to leverage other affiliated businesses for competitive advantage. PayPal's competitors may be able to innovate and respond to new or emerging technologies and changes in customer requirements faster and more effectively than PayPal. Some of these competitors may also be subject to less burdensome licensing, anti-money laundering, counter-terrorist financing and other regulatory requirements than PayPal, which is subject to additional regulations based on, among other factors, its licensure as a bank in Luxembourg. They may devote greater resources to the development, promotion, and sale of products and services than PayPal, and they may offer lower prices. For example, Google Checkout (now integrated into Google Wallet) has in the past offered free payments processing on transactions in an amount proportionate to certain advertising spending with Google. Competing services tied to established banks and other financial institutions may offer greater liquidity and engender greater consumer confidence in the safety and efficacy of their services than PayPal. In addition, in certain countries, such as Germany, Netherlands and Australia, electronic funds transfer is a leading method of payment for both online and offline transactions. As in the U.S., established banks and other financial institutions that do not currently offer online payments could quickly and easily develop such a service.

The principal competitive factors for PayPal include the following:

- ability to attract, retain and engage both buyers and sellers with relatively low marketing expense;
- ability to show that sellers will achieve incremental sales by offering PayPal;
- security of transactions and the ability for buyers to use PayPal without sharing their financial information with the seller;
- low fees and simplicity of fee structure;
- ability to develop services across multiple commerce channels, including mobile payments and payments at the physical point of sale;
- trust in PayPal's dispute resolution and buyer and seller protection programs;
- customer service; and
- brand recognition.

With respect to our online competition, additional competitive factors include:

- website and onboarding ease-of-use and accessibility;
- system reliability;
- data security; and
- quality of developer tools such as our Application Programming Interfaces and Software Development Kits.

Some of PayPal's competitors, such as Wells Fargo, First Data, American Express and Royal Bank of Scotland, also provide processing or foreign exchange services to PayPal. If PayPal were to seek to expand the financial products that it offers, either alone or through a commercial alliance or an acquisition, these processing and foreign exchange relationships could be negatively affected, or these competitors and other processors could make it more difficult for PayPal to deliver its services.

GSI

Our GSI business segment has two main businesses: ecommerce services and interactive marketing services.

Ecommerce Services

The market for the development and operation of ecommerce services that enable companies to operate ecommerce businesses and integrate their ecommerce businesses into their multichannel retail offerings is continuously evolving and intensely competitive. In our ecommerce services business, we face competition from in-house ecommerce solutions, technology and service providers which supply one or more components of an ecommerce solution, and other providers of integrated ecommerce solutions. Many of our prospective ecommerce services clients evaluate managing all or some aspects of an ecommerce operation with internal resources. As a result, we often compete with in-house solutions promoted and supported by internal information technology staffs, merchandising groups, and other internal corporate constituencies as well

66

as with technology and service providers that supply one or more components of an ecommerce solution that allow prospective clients to develop and operate their ecommerce business in-house. This group of providers may include the prospective client itself and companies that offer: Web platforms (e.g., Art Technology Group (which is owned by Oracle), IBM, Demandware and Microsoft); customer care/call center services (e.g., West Communications, Sykes Enterprises, and Convergys); fulfillment and logistics (e.g., PFS Web, Innotrac, DHL, and UPS); and systems integrators and technology providers (e.g., Accenture, EDS, Sapient, Infosys, Oracle and IBM).
We believe that we compete with ecommerce services competitors primarily on the basis of the following:
- offering the choice of a complete integrated solution or a component-based solution;
- promoting the client's brand and business, rather than our own;
- providing scale and operating leverage with an enterprise focus;
- establishing a commitment to invest in and enhance our platform; and
- aligning our financial interests with those of our clients.

Interactive Marketing Services
The market for interactive marketing services is continuously evolving and intensely competitive. In our interactive marketing services business, we face competition from other providers of interactive marketing services, other providers of traditional marketing services and in-house marketing departments, as our prospective interactive marketing services clients evaluate managing their marketing services with internal resources as well as through interactive marketing agencies. As a result, we often compete with in-house solutions promoted and supported by internal marketing departments as well as with service providers that supply one or more interactive marketing services. This group of providers may include the prospective client itself and companies that offer: email management and data aggregation (e.g., Experian, Harte-Hanks and Epsilon); online marketing and design services (digital marketing services agencies such as Omnicom Group, WPP Group, Publicis and the Interpublic Group of Companies); and other interactive marketing services (e.g., Google, LinkShare (owned by Rakuten), TradeDoubler, and ValueClick). Low barriers to entry in the interactive marketing industry could also increase the number of competitors our interactive marketing services business may face.
We believe that we compete with interactive marketing services competitors primarily on the basis of the following:
- offering digital marketing solutions that are integrated with our ecommerce services platform, which we believe provides a more strategic, cohesive and optimized approach to growing ecommerce businesses; and
- providing services that utilize proprietary technology to promote stronger customer engagement designed to increase clients' return on investment.

Our ecommerce services and interactive marketing services businesses have competitors with longer operating histories, larger customer bases, greater brand recognition and greater financial, marketing and other resources. Those competitors may be able to secure components of their technology and services on more favorable terms and devote more resources to technology development and marketing than our ecommerce services and interactive marketing services business. In addition, as we expand our ecommerce services and interactive marketing services businesses internationally, we will face increased competition from local companies which may have a greater understanding of, and focus on, the local customer.
We are subject to regulatory activity and antitrust litigation under competition laws.
We receive scrutiny from various government agencies under U.S. and foreign competition laws. Some jurisdictions also provide private rights of action for competitors or consumers to assert claims of anti-competitive conduct. Other companies and government agencies have in the past and may in the future allege that our actions violate the antitrust or competition laws of the U.S., individual states, the European Commission, or other countries, or otherwise constitute unfair competition. Contractual agreements with buyers, sellers, or other companies could give rise to regulatory action or antitrust litigation. Also, our unilateral business practices could give rise to regulatory action or antitrust litigation. Some regulators, particularly those outside of the U.S., may perceive our business to have so much market power that otherwise uncontroversial business practices could be deemed anticompetitive. For example, in the U.S., we have been sued by a plaintiff representing a putative class of sellers who alleges that we have illegally monopolized a market for online auctions. In Korea, the national competition authority has investigated allegations

that we have engaged in illegal exclusive conduct and rendered a decision against us in October 2010. The main case was conclusively resolved in our favor, and a related administrative action is on appeal. A further investigation was concluded by the Seoul prosecutor's office, which chose not to bring any charges. The competition authorities in Germany and Australia have conducted investigations (now completed) of various actions taken by our businesses. Such claims and investigations, even if without foundation, typically are very expensive to defend, involve negative publicity and substantial diversion of management time and effort, and could result in significant judgments against us.

67

In several jurisdictions, we have taken actions designed to improve the security of transactions and the quality of the user experience on our websites. Beginning in June 2008, we have required users in the U.K. to offer PayPal as a payment alternative on most transactions on our localized U.K. website, and since October 2008, we have required sellers on eBay.com to accept one or more accepted payment methods (currently PayPal, credit or debit cards processed through Internet merchant accounts, ProPay, Skrill (formerly known as Moneybookers) and Paymate) and no longer allow any forms of paper payment, including checks and money orders, to be listed by sellers in the U.S. for most categories of items. While these initiatives are intended to improve and make safer our users' buying experience and/or increase activity on our sites, certain users may be negatively affected by or react negatively to these changes, and may allege that we have (and are abusing) market power. We have faced inquiries from government regulators in various jurisdictions related to such actions. For example, in 2008, both the Australian Competition and Consumer Commission and the Reserve Bank of Australia reviewed our policies requiring sellers to offer PayPal as a payment alternative on most transactions on our localized Australian website and precluding sellers from imposing a surcharge or any other fee for accepting PayPal or other payment methods. We may face similar inquiries from other government regulators in the future. Negative reactions to these changes by our users or government authorities could, among other things, force us to change our operating practices in ways that could harm our business, operating results and profitability.

Our business may be adversely affected by factors that cause our users to spend less time on our websites or mobile applications, including seasonal factors, national events and increased usage of other websites.

Anything that diverts our users from their customary level of usage of our websites or mobile applications could adversely affect our business. We would therefore be adversely affected by geopolitical events such as war, the threat of war, or terrorist activity, and natural disasters, such as hurricanes or earthquakes. Similarly, our results of operations historically have experienced seasonal fluctuations because many of our users reduce their activities on our websites with the onset of good weather during the summer months, and on and around national holidays. In particular, our GSI business is highly seasonal, with the fourth quarter holiday season accounting for a disproportionate amount of GSI's net revenues due to consumers increasing their purchases and businesses increasing their advertising to consumers during that period, and any factors that limit or dampen consumer spending during the fourth quarter holiday season could harm our GSI business. In addition, increased usage of social networking or other entertainment websites or mobile applications may decrease the amount of time users spend on our websites or mobile applications, which could adversely affect our financial results.

Our failure to cost-effectively manage certain aspects of our business could harm us.

We have expanded significantly our headcount, facilities and infrastructure in the U.S. and internationally, and anticipate that further expansion in certain areas will be required for some of our businesses. We are also increasing our product and service offerings across our businesses. This expansion has increased (and we expect will continue to increase), the complexity of our businesses and has placed (and we expect will continue to place) a significant strain on our management, operational, and financial resources. The areas that are put under strain by our growth include the following:

- Customer Account Billing. Our revenues depend on prompt and accurate billing processes. Our failure to grow our transaction-processing capabilities to accommodate the increasing number of transactions that must be billed on our and our subsidiaries' websites would harm our business and our ability to collect revenue.
- Customer Service. We continue to focus on providing better and more efficient customer support to our users. We intend to provide an increased level of support (including an increasing amount of telephone support) in a cost-effective manner. If we are unable to provide customer support in a cost-effective manner, users of our websites may have negative experiences, current and future revenues could suffer, our costs may increase and our operating margins may decrease.

We must continue to effectively hire, train and manage new employees. If our new hires perform poorly, if we are unsuccessful in hiring, training, managing and integrating new employees, or if we are unsuccessful in retaining our existing employees, our business may be harmed.

Our current and planned personnel, systems, procedures and controls may not be adequate to support our future operations. To effectively manage the expected growth of our operations and personnel, we will need to continue to improve our transaction processing, operational and financial systems, procedures and controls. This is a special challenge as we acquire new operations with different and incompatible systems. Any capital investments that we may make will increase our cost base, which will make it more difficult for us to offset any future revenue shortfalls by expense reductions in the short term. Failure to implement these improvements could limit our ability to manage our growth and adversely affect our operating results.
We may have exposure to greater than anticipated tax liabilities.

The determination of our worldwide provision for income taxes and other tax liabilities requires estimation and significant judgment, and there are many transactions and calculations where the ultimate tax determination is uncertain. Like many other multinational corporations, we are subject to tax in multiple U.S. and foreign tax jurisdictions and have structured our operations to reduce our effective tax rate. Our determination of our tax liability is always subject to audit and review by applicable domestic and foreign tax authorities, and we are currently undergoing a number of investigations, audits and reviews by taxing authorities throughout the world, including with respect to our tax structure. Any adverse outcome of any such audit or review could have a negative effect on our business, operating results and financial condition, and the ultimate tax outcome may differ from the amounts recorded in our financial statements and may materially affect our financial results in the period or periods for which such determination is made. While we have established reserves based on assumptions and estimates that we believe are reasonable to cover such eventualities, these reserves may prove to be insufficient in the event that any taxing authority is successful in asserting tax positions that are contrary to our positions.

In addition, the economic downturn reduced tax revenues for U.S. federal and state governments, and a number of proposals to increase taxes from corporate entities are being considered at various levels of government. Among the options have been a range of proposals included in the tax and budget policies recommended to the U.S. Congress by the U.S. Department of the Treasury to modify the federal tax rules related to the imposition of U.S. federal corporate income taxes for companies operating in multiple U.S. and foreign tax jurisdictions. If such proposals are enacted into law, this could increase our effective tax rate. A number of U.S. states have likewise attempted to increase corporate tax revenues by taking an expansive view of corporate presence to attempt to impose corporate income taxes and other direct business taxes on companies that have no physical presence in their state. Many U.S. states are also altering their apportionment formulas to increase the amount of taxable income/loss attributable to their state from certain out-of-state businesses. Companies that operate over the Internet, such as eBay, are a target of some of these state efforts. If more states are successful in applying direct taxes to Internet companies that do not have a physical presence in the state, this could increase our effective tax rate.

Our integrated X.commerce platform, which is open to third-party developers, subjects us to additional risks.

In 2009, we launched the PayPal Developer Platform to enable third-party developers to access a wide variety of PayPal product and programming code specifications and to connect to select PayPal payment application programming interfaces (APIs). We also began providing a software tool kit for building mobile payments applications, and enabling third-party developers to access certain APIs with respect to our Marketplaces platforms. In June 2011, we launched X.commerce, our integrated open commerce platform initiative, which includes our eBay Developer Program, the PayPal Developer Network and Magento, which provides open source ecommerce platforms and which we acquired in August 2011. There can be no assurance that merchants and third-party developers will develop and maintain applications and services on our open commerce platforms on a timely basis or at all, and a number of factors could cause such third-party developers to curtail or stop development for our platforms. In addition, our business is subject to many regulatory restrictions, which may be contravened by such third party applications. If this were to occur, we could be liable for the regulatory failure and our business could be adversely affected.

There are risks associated with our indebtedness.

At June 30, 2012, we had approximately $12 million in secured indebtedness outstanding, $550 million of senior unsecured indebtedness outstanding under our $2.0 billion commercial paper program, and approximately $1.5 billion of other senior unsecured indebtedness outstanding. We also have a $3.0 billion revolving credit facility, under which we maintain $2.0 billion of available borrowing capacity in order to repay commercial paper borrowings in the event we are unable to repay those borrowings from other sources when they come due. As of June 30, 2012, no borrowings or letters of credit were outstanding under this revolving credit facility and, accordingly, $1.0 billion of borrowing capacity was available for other purposes permitted by this credit facility.

We may incur additional indebtedness in the future, including under our commercial paper program and revolving credit facility or through public or private offerings of debt securities. Our outstanding indebtedness and any additional indebtedness we incur may have important consequences, including, without limitation, the following:

- we will be required to use cash to pay the principal of and interest on our indebtedness;

- our indebtedness and leverage may increase our vulnerability to adverse changes in general economic and industry conditions, as well as to competitive pressure;
- our ability to obtain additional financing for working capital, capital expenditures, acquisitions, share repurchases and other general corporate and other purposes may be limited; and
- our flexibility in planning for, or reacting to, changes in our business and our industry may be limited.

69

Our ability to make payments of principal of and interest on our indebtedness depends upon our future performance, which will be subject to general economic conditions, industry cycles and financial, business and other factors affecting our consolidated results of operations and financial condition, many of which are beyond our control. If we are unable to generate sufficient cash flow from operations in the future to service our debt, we may be required to, among other things:

- repatriate funds at substantial tax cost;
- seek additional financing in the debt or equity markets;
- refinance or restructure all or a portion of our indebtedness;
- sell selected assets;
- reduce or delay planned capital expenditures; or
- reduce or delay planned operating expenditures.

Such measures might not be sufficient to enable us to service our debt. In addition, any such financing, refinancing or sale of assets might not be available on economically favorable terms or at all.

We depend on the continued growth of online and mobile commerce.

The business of selling goods over the Internet and mobile networks, particularly through online trading, is dynamic and relatively new. Concerns about fraud, privacy and other problems may discourage additional consumers from adopting the Internet or mobile devices as modes of commerce, or may prompt consumers to offline channels. In countries such as the U.S., Germany, Korea and the U.K., where our services and online commerce generally have been available for some time and the level of market penetration of our services is high, acquiring new users for our services may be more difficult and costly than it has been in the past. Moreover, the growth rates of Internet users is slowing in many countries where we have a significant presence. In order to expand our user base, we must appeal to and acquire consumers who historically have used traditional means of commerce to purchase goods and may prefer Internet analogues to such traditional retail means, such as the retailer's own website, to our offerings. If these consumers prove to be less active than our earlier users due to lower levels of willingness to use the Internet or mobile devices for commerce for any reason, including lack of access to high-speed communications equipment, congestion of traffic on the Internet, Internet or mobile network outages or delays, disruptions or other damage to users' computers or mobile devices, and we are unable to gain efficiencies in our operating costs, including our cost of acquiring new customers, our business could be adversely impacted.

Our businesses depend on continued and unimpeded access to the Internet, as well as access to mobile networks. Internet service providers may be able to block, degrade, or charge us or our users additional fees for our offerings, which could harm our business.

Our customers rely on access to the Internet or mobile networks to use our products and services. In many cases, that access is provided by companies that compete with at least some of our offerings, including incumbent telephone companies, cable companies, mobile communications companies and large Internet service providers. Some of these providers have stated that they may take measures that could degrade, disrupt, or increase the cost of customers' use of our offerings by restricting or prohibiting the use of their infrastructure to support or facilitate our offerings, or by charging increased fees to us or our users to provide our offerings. Mobile operators or operating system providers could block or place onerous restrictions on our ability to offer our mobile applications in their mobile application stores. Internet service providers or mobile networks could attempt to charge us each time our customers use our offerings. Worldwide, a number of companies have announced plans to take such actions or are selling products designed to facilitate such actions. The United States Federal Communications Commission enacted rules in December 2010 (Preserving the Open Internet Broadband Industry Practices [FCC-10-201]) establishing baseline restrictions that would regulate the ability of Internet access companies to interfere with Internet traffic transported over wired and wireless networks. These FCC rules are expected to be reviewed by the Federal courts in 2012. Pending greater regulatory and judicial clarity, any interference with our offerings or higher charges for access to our offerings, whether paid by us or by our customers, could cause us to lose existing customers, impair our ability to attract new customers and harm our revenue and growth.

Our business depends on the development and maintenance of the Internet infrastructure.

The success of our services will depend largely on the development and maintenance of the Internet infrastructure. This includes maintenance of a reliable network backbone with the necessary speed, data capacity, and security, as well as timely development of complementary products, for providing reliable Internet access and services. The Internet has experienced, and is likely to continue to experience, significant growth in the numbers of users and amount of traffic. The Internet infrastructure may be unable to support such demands. In addition, increasing numbers of users, increasing bandwidth requirements, or problems caused by "viruses," "worms," malware and similar programs may harm the performance of the Internet. The backbone computers of the Internet have been the targets of such programs. From time to time, the Internet has experienced, and is likely to continue to experience, a variety of outages and other delays as a result of damage to portions of its infrastructure. Any such outages and delays could reduce the level of Internet usage generally as well as the level of usage of our services, which could adversely impact our business.

We may be unable to protect or enforce our own intellectual property rights adequately.

We regard the protection of our intellectual property, including our trademarks (particularly those covering the eBay and PayPal names), patents, copyrights, domain names, trade dress and trade secrets as critical to our success. We aggressively protect our intellectual property rights by relying on federal, state and common law rights in the U.S. and internationally, as well as a variety of administrative procedures. We also rely on contractual restrictions to protect our proprietary rights in products and services. We have entered into confidentiality and invention assignment agreements with our employees and contractors and confidentiality agreements with parties with whom we conduct business in order to limit access to and disclosure of our proprietary information. Effective intellectual property protection may not be available in every country in which our products and services are made available, and contractual arrangements and the other steps we have taken to protect our intellectual property may not prevent third parties from infringing or misappropriating our technology or deter independent development of equivalent or superior technologies or other intellectual property rights by others.

We pursue the registration of our domain names, trademarks and service marks in the U.S. and internationally. Additionally, we have filed U.S. and international patent applications covering certain aspects of our proprietary technology. Effective trademark, copyright, patent, domain name, trade dress and trade secret protection is very expensive to maintain and may require litigation. We must protect our intellectual property rights and other proprietary rights in an increasing number of jurisdictions, a process that is expensive and time consuming and may not be successful in every location. We may not be able to discover or determine the extent of any unauthorized use of our proprietary rights. We have licensed in the past, and expect to license in the future, certain of our proprietary rights, such as trademarks or copyrighted material, to others. These licensees may take actions that diminish the value of our proprietary rights or harm our reputation.

We are subject to the risks of owning real property.

We own real property, including land and buildings related to our operations. We have little experience in managing real property. Ownership of this property subjects us to a number of additional risks, including:

- the possibility of environmental contamination and the costs associated with fixing any environmental problems;
- disruptions to our operations resulting from possible natural disasters, interruptions in utilities and similar events;
- adverse changes in the value of these properties due to interest rate changes, changes in the commercial property markets, or other factors;
- the possible need for structural improvements in order to comply with zoning, seismic, disability law, or other requirements; and
- possible disputes with tenants, neighboring owners, or others.

Some anti-takeover provisions may affect the price of our common stock.

Our Board of Directors has the authority to issue up to 10,000,000 shares of preferred stock and to determine the preferences, rights and privileges of those shares without any further vote or action by the stockholders. The rights of the holders of common stock may be harmed by rights granted to the holders of any preferred stock that may be issued in the future. Some provisions of our certificate of incorporation and bylaws could have the effect of making it more difficult for a potential acquirer to acquire a majority of our outstanding voting stock or take control of our board of directors. These include provisions that provide for a classified board of directors through our annual meeting of stockholders in 2015, prohibit stockholders from taking action by written consent and restrict the ability of stockholders to call special meetings. We are also subject to provisions of Delaware law that prohibit us from engaging in any business combination with any interested stockholder (as defined by Delaware law) for a period of three years from the date the person became an interested stockholder, unless certain conditions are met. This restriction could have the effect of delaying or preventing a change of control.

71

Item 2: Unregistered Sales of Equity Securities and Use of Proceeds

Stock repurchase activity during the three months ended June 30, 2012 was as follows:

Period Ended	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Programs	Maximum Dollar Value that May Yet be Purchased Under the Programs (1)
April 30, 2012	1,188,300	$39.64	1,188,300	$593,507,940
May 31, 2012	6,404,090	$39.49	6,404,090	$340,611,522
June 30, 2012	1,407,610	$38.82	1,407,610	$2,285,961,949
	9,000,000		9,000,000	

(1) In September 2010, our Board of Directors authorized a stock repurchase program that provides for the repurchase of up to $2 billion of our common stock, with no expiration from the date of authorization. In June 2012, our Board authorized an additional stock repurchase program that provides for the repurchase of up to an additional $2 billion of our common stock, with no expiration from the date of authorization. These stock repurchase programs are intended to offset the impact of dilution from our equity compensation programs. During the six months ended June 30, 2012, we repurchased approximately $595 million of our common stock under our stock repurchase programs at an average price of $37.16 per share. As of June 30, 2012, approximately $2.3 billion remained available for further purchases of our common stock under our stock repurchase programs.

Item 3: Defaults Upon Senior Securities

Not applicable.

Item 4: Mine Safety Disclosures

Not applicable.

Item 5: Other Information

Not applicable.

Item 6: Exhibits

Exhibit 3.01*	Amended and Restated Certificate of Incorporation of Registrant.
Exhibit 3.02*	Amended and Restated Bylaws of Registrant.
Exhibit 10.01+	Amendment to Registrant's 2003 Deferred Stock Unit Plan, effective April 2, 2012.
Exhibit 10.02+	Amendment to GSI Commerce, Inc. 2010 Equity Incentive Plan, effective April 2, 2012.
Exhibit 10.03+	Amendment to eBay Incentive Plan, effective April 2, 2012.
Exhibit 10.04+	Amendment to GSI Commerce, Inc. Leadership Team Incentive Plan, effective April 2, 2012.
Exhibit 10.05+	Form of Restricted Stock Unit Award Agreement (and Performance-Based Restricted Stock Unit Award Agreement) under Registrant's 2003 Deferred Stock Unit Plan, Registrant's 2008 Equity Incentive Award Plan and GSI Commerce, Inc. 2010 Equity Incentive Plan.
Exhibit 10.06+	Form of Restricted Stock Unit Award Agreement (with Modified Vesting) under Registrant's 2008 Equity Incentive Award Plan.
Exhibit 10.07+	Form of Restricted Stock Unit Award Agreement GSI Commerce, Inc. 2010 Equity Incentive Plan.
Exhibit 10.08+	Form of Stock Option Agreement under Registrant's 2008 Equity Incentive Award Plan.
Exhibit 10.09+	Form of Stock Option Agreement (with Modified Vesting) under Registrant's 2008 Equity Incentive Award Plan.
Exhibit 10.10+	Form of Performance Share Unit Award Agreement under Registrant's 2008 Equity Incentive Award Plan.
Exhibit 10.11+	Form of Director Award Agreement under Registrant's 2003 Deferred Stock Unit Plan.
Exhibit 10.12+	Form of Electing Director Award Agreement under Registrant's 2003 Deferred Stock Unit Plan.
Exhibit 10.13+	Form of New Director Award Agreement under Registrant's 2003 Deferred Stock Unit Plan.
Exhibit 10.14+	Form of Director Deferred Stock Unit Award Agreement under Registrant's 2008 Equity Incentive Award Plan.
Exhibit 12.01	Statement regarding computation of ratio of earnings to fixed charges.
Exhibit 31.01	Certification of Registrant's Chief Executive Officer, as required by Section 302 of the Sarbanes-Oxley Act of 2002.
Exhibit 31.02	Certification of Registrant's Chief Financial Officer, as required by Section 302 of the Sarbanes-Oxley Act of 2002.
Exhibit 32.01	Certification of Registrant's Chief Executive Officer, as required by Section 906 of the Sarbanes-Oxley Act of 2002.
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101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

* Filed as an exhibit to Registrant's Current Report on Form 8-K filed with the Securities and Exchange Commission on April 27, 2012 and incorporated herein by reference.
+ Indicates a management contract or compensatory plan or arrangement.

73

SIGNATURES

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.

eBay Inc.
Principal Executive Officer:

By: /s/ John J. Donahoe
John J. Donahoe
President and Chief Executive Officer

Date: July 18, 2012

Principal Financial Officer:

By: /s/ Robert H. Swan
Robert H. Swan
Senior Vice President, Finance and Chief Financial Officer

Date: July 18, 2012

Principal Accounting Officer:

By: /s/ Brian J. Doerger
Brian J. Doerger
Vice President, Chief Accounting Officer

Date: July 18, 2012

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75