

MERCADOLIBRE INC
Form 10-Q
November 05, 2012
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2012

-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 001-33647

MercadoLibre, Inc.

(Exact name of Registrant as specified in its Charter)

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Delaware
(State or other jurisdiction of
incorporation or organization)

98-0212790
(I.R.S. Employer
Identification Number)

Arias 3751, 7th Floor
Buenos Aires, C1430CRG, Argentina
(Address of registrant's principal executive offices)

(+5411) 4640-8000
(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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

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

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

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

44,150,920 shares of the issuer's common stock, \$0.001 par value, outstanding as of October 31, 2012.

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PART I. FINANCIAL INFORMATION

Item 1. Unaudited Condensed Consolidated Financial Statements

MercadoLibre, Inc.

Condensed Consolidated Financial Statements

as of September 30, 2012 and December 31, 2011

and for the three and nine-month periods

ended September 30, 2012 and 2011

Table of Contents**MercadoLibre, Inc.****Condensed Consolidated Balance Sheets**

As of September 30, 2012 and December 31, 2011

	September 30, 2012 (Unaudited)	December 31, 2011 (Audited)
Assets		
Current assets:		
Cash and cash equivalents	\$ 98,171,852	\$ 67,381,677
Short-term investments	79,390,492	74,928,620
Accounts receivable, net	16,447,126	16,815,087
Credits Cards Receivables	39,799,359	23,855,689
Prepaid expenses	2,232,034	1,269,594
Deferred tax assets	10,655,188	9,131,638
Other assets	8,215,671	6,863,250
Total current assets	254,911,722	200,245,555
Non-current assets:		
Long-term investments	59,418,012	43,933,316
Property and equipment, net	35,217,386	30,877,719
Goodwill, net	61,357,722	62,093,948
Intangible assets, net	7,535,276	6,494,857
Deferred tax assets	6,137,545	6,491,646
Other assets	6,046,889	5,794,395
Total non-current assets	175,712,830	155,685,881
Total assets	\$ 430,624,552	\$ 355,931,436
Liabilities and Equity		
Current liabilities:		
Accounts payable and accrued expenses	\$ 24,298,361	\$ 20,251,313
Funds payable to customers	83,559,610	69,216,185
Salaries and social security payable	18,022,393	13,525,293
Taxes payable	12,598,869	11,633,178
Loans payable and other financial liabilities	124,753	146,194
Dividends payable	4,812,036	3,531,362
Total current liabilities	143,416,022	118,303,525
Non-current liabilities:		
Salaries and social security payable	4,139,830	3,844,172
Loans payable and other financial liabilities	74,937	136,227
Deferred tax liabilities	8,367,423	8,670,606
Other liabilities	2,520,584	1,797,890
Total non-current liabilities	15,102,774	14,448,895
Total liabilities	\$ 158,518,796	\$ 132,752,420

Commitments and contingencies (Note 7)

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Redeemable noncontrolling interest	\$ 4,000,000	\$ 4,000,000
Equity:		
Common stock, \$0.001 par value, 110,000,000 shares authorized, 44,150,920 and 44,142,020 shares issued and outstanding at September 30, 2012 and December 31, 2011, respectively	\$ 44,151	\$ 44,142
Additional paid-in capital	120,468,759	120,452,032
Retained earnings	192,668,273	135,726,188
Accumulated other comprehensive loss	(45,075,427)	(37,043,346)
Total Equity	268,105,756	219,179,016
 Total liabilities, redeemable noncontrolling interest and equity	 \$ 430,624,552	 \$ 355,931,436

The accompanying notes are an integral part of these condensed consolidated financial statements.

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Weighted average shares	44,153,778	44,150,872	44,157,321	44,151,218
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The accompanying notes are an integral part of these condensed consolidated financial statements.

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MercadoLibre, Inc.

Condensed Consolidated Statements of Comprehensive Income**For the three and nine-month periods ended September 30, 2012 and 2011**

	Nine Months Ended September 30, 2012 (Unaudited)		Three Months Ended September 30, 2012 (Unaudited)	
	\$	\$	\$	\$
Net income	71,099,757	55,174,909	26,067,897	26,296,447
Other comprehensive income (loss), net of income tax:				
Currency traslation adjustment	(8,082,603)	(12,787,985)	(1,258,637)	(16,508,664)
Unrealized net gains on investments	975,179	928,179	104,883	546,745
Realized net gain on investments	(924,657)	(45,527)		
Net change in accumulated other comprehensive loss, net of income tax	(8,032,081)	(11,905,333)	(1,153,754)	(15,961,919)
Total Comprehensive income	\$ 63,067,676	\$ 43,269,576	\$ 24,914,143	\$ 10,334,528
Less: Comprehensive Income attributable to Noncontrolling Interest	325,499	522	76,368	522
Comprehensive income attributable to MercadoLibre, Inc.	\$ 62,742,177	\$ 43,269,054	\$ 24,837,775	\$ 10,334,006

The accompanying notes are an integral part of these condensed consolidated financial statements.

Table of Contents**MercadoLibre, Inc.****Condensed Consolidated Statements of Cash Flows****For the nine-month periods ended September 30, 2012 and 2011**

	Nine Months Ended September 30,	
	2012	2011
	(Unaudited)	
Cash flows from operations:		
Net income attributable to MercadoLibre, Inc.	\$ 71,056,893	\$ 55,174,387
Adjustments to reconcile net income to net cash provided by operating activities:		
Net Income attributable to Noncontrolling Interest	42,864	522
Depreciation and amortization	6,412,210	5,249,168
Accrued interest	(2,321,629)	(4,461,828)
LTRP accrued compensation	3,338,368	2,527,494
Deferred income taxes	(813,538)	1,174,177
Changes in assets and liabilities:		
Accounts receivable	(3,824,015)	(6,290,360)
Credit Card Receivables	(18,852,184)	(8,188,181)
Prepaid expenses	(1,022,894)	(276,976)
Other assets	(2,092,362)	(5,228,268)
Accounts payable and accrued expenses	10,869,830	6,288,050
Funds payable to customers	19,984,595	16,052,471
Other liabilities	930,000	273,016
Net cash provided by operating activities	83,708,138	62,293,672
Cash flows from investing activities:		
Purchase of investments	(344,739,785)	(297,570,336)
Proceeds from sale and maturity of investments	320,436,580	268,529,776
Payment for acquired businesses, net of cash acquired		(5,468,180)
Purchases of intangible assets	(1,341,789)	(119,262)
Purchases of property and equipment	(11,682,839)	(17,084,397)
Net cash used in investing activities	(37,327,833)	(51,712,399)
Cash flows from financing activities:		
Dividends paid	(13,155,438)	(7,061,847)
Stock options exercised	5,700	11,175
Net cash provided in financing activities	(13,149,738)	(7,050,672)
Effect of exchange rate changes on cash and cash equivalents	(2,440,392)	(1,277,650)
Net increase in cash and cash equivalents	30,790,175	2,252,951
Cash and cash equivalents, beginning of the period	67,381,677	56,830,466
Cash and cash equivalents, end of the period	\$ 98,171,852	\$ 59,083,417

The accompanying notes are an integral part of these condensed consolidated financial statements.

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MercadoLibre, Inc.

Notes to Condensed Consolidated Financial Statements (unaudited)

1. Nature of Business

MercadoLibre Inc. (the Company) is an e-commerce enabler whose mission is to build the necessary online and technology tools to allow practically anyone to trade almost anything in Latin America.

The Company developed a Web-based marketplace in which buyers and sellers are brought together to browse, buy and sell items such as computers, electronics, collectibles, automobiles, clothing and a host of practical and miscellaneous items. Additionally, the Company introduced MercadoPago in 2004, an integrated online payments solution. MercadoPago was designed to facilitate transactions on the MercadoLibre Marketplace by providing an escrow mechanism that enables users to send and receive payments online.

Since 2004, the Company introduced an online classifieds platform for motor vehicles, vessels and aircrafts and since 2006 the real estate online classifieds platform. In 2006, the Company launched eShops, a platform tailored to attract lower rotation items and increase the breadth of products offered, the introduction of user generated information guides for buyers that improve the shopping experience, and the expansion of the online classifieds model by adding the services category.

During 2007 the Company also launched a new and improved version of its MercadoPago payments platform in Chile and Colombia as well as in Argentina during 2008. The new MercadoPago, in addition to improving the ease of use and efficiency of payments for marketplace purchases, also allows for payments outside of the Company's marketplaces. Users are able to transfer money to other users with MercadoPago accounts and to incorporate MercadoPago as a means of payments in their independent commerce websites. In this way MercadoPago 3.0 as it has been called is designed to meet the growing demand for Internet based payments systems in Latin America. In 2010, the Company started processing off-MercadoLibre transactions through this new direct payments product to any website in Brazil which wants to adopt it and launched MercadoPago 3.0 in Brazil for all its marketplace transactions. In 2011, the Company started processing off-platform transactions using MercadoPago 3.0 in Mexico and Venezuela.

As of September 30, 2012, the Company, through its wholly-owned subsidiaries, operated online commerce platforms directed towards Argentina, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, Mexico, Panama, Peru, Portugal, Uruguay and Venezuela, and online payment solutions directed towards Argentina, Brazil, Mexico, Venezuela, Chile and Colombia. In addition, the Company operates a real estate classified platform that covers some areas of Florida, U.S.A.

2. Summary of Significant Accounting Policies

Basis of presentation

The accompanying unaudited interim condensed consolidated financial statements are prepared in conformity with accounting principles generally accepted in the United States of America (U.S. GAAP) and include the accounts of the Company and its subsidiaries.

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MercadoLibre, Inc.

Notes to Condensed Consolidated Financial Statements (unaudited)

2. Summary of Significant Accounting Policies (Continued)

Basis of presentation (Continued)

These interim condensed consolidated financial statements are stated in US dollars. All intercompany transactions and balances have been eliminated.

Substantially all revenues and operating costs are generated in the Company's foreign operations, amounting to approximately 99.5% and 99.7% of the consolidated totals during the nine-month periods ended September 30, 2012 and 2011, respectively. Long-lived assets located in the foreign operations totaled \$97,722,978 and \$93,489,980 as of September 30, 2012 and December 31, 2011, respectively.

These interim condensed consolidated financial statements reflect the Company's consolidated financial position as of September 30, 2012 and December 31, 2011. These financial statements also show the Company's consolidated statements of income and of comprehensive income for the three and nine-month periods ended September 30, 2012 and 2011, its consolidated statement of cash flows for the nine-month periods ended September 30, 2012 and 2011. These interim condensed consolidated financial statements include all normal recurring adjustments that management believes are necessary to fairly state the Company's financial position, operating results and cash flows.

Because all of the disclosures required by U.S. GAAP for annual consolidated financial statements are not included herein, these unaudited interim condensed financial statements should be read in conjunction with the audited consolidated financial statements and the notes thereto for the year ended December 31, 2011, contained in the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission (SEC) on February 28, 2012. The condensed consolidated statements of income, of comprehensive income and of cash flows for the periods presented herein are not necessarily indicative of results expected for any future period.

Foreign Currency Translation

All of the Company's foreign operations have determined the local currency to be their functional currency, except for Venezuela since the year ended December 31, 2010. Accordingly, these foreign subsidiaries translate assets and liabilities from their local currencies into U.S. dollars using period/year-end exchange rates while income and expense accounts are translated at the average rates in effect during the period/year. The resulting translation adjustment is recorded as part of accumulated other comprehensive income (loss). Gains and losses resulting from transactions denominated in non-functional currencies are recognized in earnings.

According to US GAAP, the Company has transitioned its Venezuelan operations to highly inflationary status as from January 1, 2010 considering the U.S. dollar to be the functional currency for such operation.

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MercadoLibre, Inc.

Notes to Condensed Consolidated Financial Statements (unaudited)

**2. Summary of Significant Accounting Policies (Continued)
Foreign Currency Translation (Continued)**

As of September 30, 2012, the exchange rate used to re-measure transactions was 5.30 Bolivares Fuertes per U.S. dollar.

The following table sets forth the assets, liabilities and net assets of the Company's Venezuelan subsidiaries, before intercompany eliminations, as of September 30, 2012 and December 31, 2011 and net revenues for the nine-month periods ended September 30, 2012 and 2011.

	September 30, 2012	September 30, 2011
Venezuelan operations		
Net Revenues	\$ 37,872,351	\$ 23,051,176
	September 30, 2012	December 31, 2011
Assets	52,240,768	31,074,871
Liabilities	(18,491,056)	(10,414,881)
Net Assets	\$ 33,749,712	\$ 20,659,990

As of September 30, 2012, net assets (before intercompany eliminations) of the Venezuelan subsidiaries amounted to approximately 12.6% of our consolidated net assets, and cash and investments of the Venezuelan subsidiaries held in local currency in Venezuela amounted to approximately 14.3% of our consolidated cash and investments.

Although, the current mechanisms available to obtain U.S. dollars for dividends distributions to shareholders outside Venezuela imply increased restrictions, the Company does not expect that the current restrictions to purchase U.S. dollars have a significant adverse effect on its business plans with regard to its investment in Venezuela.

Income Tax Holiday in Argentina

From fiscal year 2008, the Company's Argentine subsidiary is beneficiary of a software development law. Part of the benefits obtained from being beneficiary of the aforementioned law is a relief of 60% of total income tax determined in each year, until fiscal year 2014. Aggregate tax benefit totaled \$2,530,901 and \$1,527,295 for the three-month periods ended September 30, 2012 and 2011, respectively, while for the nine-month periods ended at such dates amounted to \$6,656,141 and \$4,062,730, respectively. Aggregate per share effect of the Argentine tax holiday amounts to \$0.06 and \$0.03 for the three-month periods ended September 30, 2012 and 2011, respectively, while for the nine-month periods ended at such dates amounted to \$0.15 and \$0.09, respectively.

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MercadoLibre, Inc.

Notes to Condensed Consolidated Financial Statements (unaudited)

2. Summary of Significant Accounting Policies (Continued) **Income Tax Holiday in Argentina (Continued)**

If the Company had not been granted the Argentine tax holiday, the Company would have pursued an alternative tax planning strategy and, therefore, the impact of not having this particular benefit would not necessarily be the abovementioned U.S. dollar and per share effect.

On August 17, 2011, the Argentine government issued a new software development Law which is still pending for the regulatory decree. If the Argentine operation qualifies under the new software development law, the current income tax relief could slightly decrease but will extend its tax holiday, which would otherwise finish in 2014, for an additional five year period, to 2019 and would obtain some other fiscal benefits.

Use of estimates

The preparation of interim condensed consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Estimates are used for, but not limited to accounting for allowance for doubtful accounts, depreciation, amortization, impairment and useful lives of long-lived assets, compensation cost related to cash and share-based compensation, recognition of current and deferred income taxes and contingencies. Actual results could differ from those estimates.

Recent Accounting Pronouncements

On July 27, 2012, the Financial Accounting Standards Board issued Accounting Standards Update No. 2012-02 Testing Indefinite-Lived Intangible Assets for Impairment. The objective of the amendments in this update is to reduce the cost and complexity of performing an impairment test for indefinite-lived intangible assets by simplifying how an entity tests those assets for impairment and to improve consistency in impairment testing guidance among long-lived asset categories. The amendments permit an entity first to assess qualitative factors to determine whether it is more likely than not that an indefinite-lived intangible asset is impaired as a basis for determining whether it is necessary to perform the quantitative impairment test in accordance with Subtopic 350-30, Intangibles Goodwill and Other General Intangibles Other than Goodwill. The more-likely-than-not threshold is defined as having a likelihood of more than 50 percent. The amendments are effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012. Early adoption is permitted, including for annual and interim impairment tests performed as of a date before July 27, 2012, if a public entity's financial statements for the most recent annual or interim period have not yet been issued or, for nonpublic entities, have not yet been made available for issuance. The Company will adopt this accounting standard in the fourth quarter of 2012 and it does not anticipate that this adoption will have a significant impact on its financial position, results of operations or cash flows.

Table of Contents**MercadoLibre, Inc.****Notes to Condensed Consolidated Financial Statements (unaudited)****3. Net income per share**

Basic earnings per share for the Company's common stock is computed by dividing net income available to common shareholders attributable to common stock for the period by the weighted average number of common shares outstanding during the period.

Diluted earnings per share for the Company's common stock assume the exercise of outstanding stock options under the Company's stock based employee compensation plan.

The following table shows how net income available to common shareholders is allocated using the two-class method, for the three and nine-month periods ended September 30, 2012 and 2011:

	Three Months Ended September 30,			
	2012		2011	
	Basic	Diluted	Basic	Diluted
Net income	\$ 26,067,897	\$ 26,067,897	\$ 26,296,447	\$ 26,296,447
Net income attributable to noncontrolling interests	(24,804)	(24,804)	(522)	(522)
Change in redeemable amount of noncontrolling interest	184,100	184,100		
Net income attributable to MercadoLibre, Inc. corresponding to common stock	\$ 26,227,193	\$ 26,227,193	\$ 26,295,925	\$ 26,295,925

	Nine Months Ended September 30,			
	2012		2011	
	Basic	Diluted	Basic	Diluted
Net income	\$ 71,099,757	\$ 71,099,757	\$ 55,174,909	\$ 55,174,909
Net income attributable to noncontrolling interests	(42,864)	(42,864)	(522)	(522)
Change in redeemable amount of noncontrolling interest	321,300	321,300		
Net income attributable to MercadoLibre, Inc. corresponding to common stock	\$ 71,378,193	\$ 71,378,193	\$ 55,174,387	\$ 55,174,387

Table of Contents**MercadoLibre, Inc.****Notes to Condensed Consolidated Financial Statements (unaudited)****3. Net income per share (Continued)**

Net income per share of common stock is as follows for the three and nine-month periods ended September 30, 2012 and 2011:

	Three Months Ended September 30,			
	2012		2011	
	Basic	Diluted	Basic	Diluted
Net income attributable to MercadoLibre, Inc. per common share	\$ 0.59	\$ 0.59	\$ 0.60	\$ 0.60
Numerator:				
Net income attributable to MercadoLibre, Inc.	\$ 26,227,193	\$ 26,227,193	\$ 26,295,925	\$ 26,295,925
Denominator:				
Weighted average of common stock outstanding for Basic earnings per share	44,150,387	44,150,387	44,141,925	44,141,925
Adjustment for stock options		1,975		4,513
Adjustment for shares granted under LTRP		4,959		4,780
Adjusted weighted average of common stock outstanding for Diluted earnings per share	44,150,387	44,157,321	44,141,925	44,151,218
	Nine Months Ended September 30,			
	2012		2011	
	Basic	Diluted	Basic	Diluted
Net income attributable to MercadoLibre, Inc. per common share	\$ 1.62	\$ 1.62	\$ 1.25	\$ 1.25
Numerator:				
Net income attributable to MercadoLibre, Inc.	\$ 71,378,193	\$ 71,378,193	\$ 55,174,387	\$ 55,174,387
Denominator:				
Weighted average of common stock outstanding for Basic earnings per share	44,146,834	44,146,834	44,137,176	44,137,176
Adjustment for stock options		1,977		8,894
Adjustment for shares granted under LTRP		4,967		4,802
Adjusted weighted average of common stock outstanding for Diluted earnings per share	44,146,834	44,153,778	44,137,176	44,150,872

The calculation of diluted net income per share excludes all anti-dilutive shares. During the three and nine-month periods ended September 30, 2012 and 2011, there were no anti-dilutive shares.

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MercadoLibre, Inc.

Notes to Condensed Consolidated Financial Statements (unaudited)**4. Goodwill and Intangible Assets**

The composition of goodwill and intangible assets is as follows:

	September 30, 2012	December 31, 2011
Goodwill	\$ 61,357,722	\$ 62,093,948
Intangible assets with indefinite lives		
- Trademarks	5,333,319	5,068,147
Amortizable intangible assets		
- Licenses and others	3,959,090	2,798,112
- Non-compete agreement	1,212,085	1,270,807
- Customer list	1,739,596	1,742,087
Total intangible assets	\$ 12,244,090	\$ 10,879,153
Accumulated amortization	(4,708,814)	(4,384,296)
Total intangible assets, net	\$ 7,535,276	\$ 6,494,857

Goodwill

The changes in the carrying amount of goodwill for the nine-month period ended September 30, 2012 and the year ended December 31, 2011, are as follows:

	Period ended September 30, 2012							
	Brazil	Argentina	Chile	Mexico	Venezuela	Colombia	Other Countries	Total
Balance, beginning of year	\$ 11,663,443	\$ 21,583,774	\$ 6,577,459	\$ 10,621,839	\$ 4,846,030	\$ 5,367,526	\$ 1,433,877	\$ 62,093,948
- Effect of exchange rates change	(889,147)	(1,805,923)	630,715	865,861		431,712	30,556	(736,226)
Balance, end of the period	\$ 10,774,296	\$ 19,777,851	\$ 7,208,174	\$ 11,487,700	\$ 4,846,030	\$ 5,799,238	\$ 1,464,433	\$ 61,357,722

	Year ended December 31, 2011							
	Brazil	Argentina	Chile	Mexico	Venezuela	Colombia	Other Countries	Total
Balance, beginning of year	\$ 13,130,649	\$ 23,364,326	\$ 7,296,888	\$ 5,025,623	\$ 4,846,030	\$ 5,448,068	\$ 1,384,730	\$ 60,496,314
- Purchase of Autoplaza.com				6,663,045				6,663,045
- Effect of exchange rates change	(1,467,206)	(1,780,552)	(719,429)	(1,066,829)		(80,542)	49,147	(5,065,411)
Balance, end of the year	\$ 11,663,443	\$ 21,583,774	\$ 6,577,459	\$ 10,621,839	\$ 4,846,030	\$ 5,367,526	\$ 1,433,877	\$ 62,093,948

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MercadoLibre, Inc.

Notes to Condensed Consolidated Financial Statements (unaudited)**4. Goodwill and Intangible Assets (Continued)**Amortizable intangible assets

Amortizable intangible assets are comprised of customer lists and user base, trademarks and trade names, non-compete agreements, acquired software licenses and other acquired intangible assets including developed technologies. Aggregate amortization expense for intangible assets totaled \$207,374 and \$252,293 for the three-month periods ended September 30, 2012 and 2011, respectively, while for the nine-month periods ended at such dates amounted to \$669,850 and \$730,815, respectively.

Expected future intangible asset amortization completed as of September 30, 2012 is as follows:

For year ended 12/31/2012	\$ 99,249
For year ended 12/31/2013	905,346
For year ended 12/31/2014	648,325
For year ended 12/31/2015	488,022
Thereafter	61,015
	\$ 2,201,957

5. Segment reporting

Reporting segments are based upon the Company's internal organizational structure, the manner in which the Company's operations are managed, the criteria used by management to evaluate the Company's performance, the availability of separate financial information, and overall materiality considerations.

Segment reporting is based on geography as the main basis of segment breakdown to reflect the evaluation of the Company's performance defined by the management. The Company's segments include Brazil, Argentina, Mexico, Venezuela and other countries (such as Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, Panama, Peru, Portugal and Uruguay).

Direct contribution consists of net revenues from external customers less direct costs. Direct costs include specific costs of net revenues, sales and marketing expenses, and general and administrative expenses over which segment managers have direct discretionary control, such as advertising and marketing programs, customer support expenses, allowances for doubtful accounts, headcount compensation, third party fees. All corporate related costs have been excluded from the Company's direct contribution.

Expenses over which segment managers do not currently have discretionary control, such as certain technology and general and administrative costs are monitored by management through shared cost centers and are not evaluated in the measurement of segment performance.

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MercadoLibre, Inc.

Notes to Condensed Consolidated Financial Statements (unaudited)**5. Segment reporting (Continued)**

The following tables summarize the financial performance of the Company's reporting segments:

	Three Months Ended September 30, 2012					Total
	Brazil	Argentina	Mexico	Venezuela	Other Countries	
Net revenues	\$ 46,202,033	\$ 24,122,810	\$ 6,736,106	\$ 14,213,460	\$ 5,992,375	\$ 97,266,784
Direct costs	(27,296,613)	(11,291,054)	(4,251,146)	(4,058,735)	(2,857,274)	(49,754,822)
Direct contribution	18,905,420	12,831,756	2,484,960	10,154,725	3,135,101	47,511,962
Operating expenses and indirect costs of net revenues						(13,798,275)
Income from operations						33,713,687
Other income (expenses):						
Interest income and other financial gains						2,925,913
Interest expense and other financial results						(312,860)
Foreign currency loss						(193,529)
Other losses, net						(179,707)
Net income before income / asset tax expense						\$ 35,953,504

	Three Months Ended September 30, 2011					Total
	Brazil	Argentina	Mexico	Venezuela	Other Countries	
Net revenues	\$ 46,003,915	\$ 15,828,272	\$ 5,608,572	\$ 9,045,783	\$ 5,141,602	\$ 81,628,144
Direct costs	(25,709,957)	(6,264,769)	(3,183,432)	(3,180,061)	(2,636,836)	(40,975,055)
Direct contribution	20,293,958	9,563,503	2,425,140	5,865,722	2,504,766	40,653,089
Operating expenses and indirect costs of net revenues						(10,689,366)
Income from operations						29,963,723
Other income (expenses):						
Interest income and other financial gains						2,913,596
Interest expense and other financial results						(1,052,865)
Foreign currency gain						3,284,190
Other loss, net						(7,292)
Net income before income / asset tax expense						\$ 35,101,352

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MercadoLibre, Inc.

Notes to Condensed Consolidated Financial Statements (unaudited)

5. Segment reporting (Continued)

	Nine Months Ended September 30, 2012					Total
	Brazil	Argentina	Mexico	Venezuela	Other Countries	
Net revenues	\$ 132,572,544	\$ 62,800,492	\$ 19,366,784	\$ 37,872,351	\$ 17,234,677	\$ 269,846,848
Direct costs	(78,106,262)	(28,957,465)	(11,167,356)	(12,634,983)	(8,569,958)	(139,436,024)
Direct contribution	54,466,282	33,843,027	8,199,428	25,237,368	8,664,719	130,410,824
Operating expenses and indirect costs of net revenues						(39,881,473)
Income from operations						90,529,351
Other income (expenses):						
Interest income and other financial gains						8,996,775
Interest expense and other financial results						(864,477)
Foreign currency loss						(477,499)
Other losses, net						(190,968)
Net income before income / asset tax expense						\$ 97,993,182

	Nine Months Ended September 30, 2011					Total
	Brazil	Argentina	Mexico	Venezuela	Other Countries	
Net revenues	\$ 120,659,242	\$ 38,800,077	\$ 16,212,999	\$ 23,051,176	\$ 13,742,478	\$ 212,465,972
Direct costs	(69,712,512)	(15,845,674)	(8,881,811)	(9,096,997)	(7,230,721)	(110,767,715)
Direct contribution	50,946,730	22,954,403	7,331,188	13,954,179	6,511,757	101,698,257
Operating expenses and indirect costs of net revenues						(30,891,982)
Income from operations						70,806,275
Other income (expenses):						
Interest income and other financial gains						7,037,264
Interest expense and other financial results						(2,562,633)
Foreign currency gain						2,080,822
Other income, net						253,148
Net income before income / asset tax expense						77,614,876

The following table summarizes the allocation of the long-lived tangible assets based on geography:

	September 30, 2012	December 31, 2011
US long-lived tangible assets	\$ 6,363,775	\$ 5,976,544

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Other countries long-lived tangible assets		
Argentina	16,400,362	14,316,612
Brazil	2,071,442	2,528,378
Mexico	353,922	409,707
Venezuela	8,243,064	7,192,073
Other countries	1,784,821	454,405
	\$ 28,853,611	\$ 24,901,175
Total long-lived tangible assets	\$ 35,217,386	\$ 30,877,719

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MercadoLibre, Inc.

Notes to Condensed Consolidated Financial Statements (unaudited)**5. Segment reporting (Continued)**

The following table summarizes the allocation of the goodwill and intangible assets based on geography:

	September 30, 2012	December 31, 2011
US intangible assets	\$ 23,631	\$
Other countries goodwill and intangible assets		
Argentina	21,425,412	22,407,558
Brazil	10,794,457	11,686,315
Mexico	14,763,732	13,709,353
Venezuela	6,595,117	6,599,584
Other countries	15,290,649	14,185,995
	\$ 68,869,367	\$ 68,588,805
Total goodwill and intangible assets	\$ 68,892,998	\$ 68,588,805

6. Fair Value Measurement of Assets and Liabilities

The following table summarizes the Company's financial assets and liabilities measured at fair value on a recurring basis as of September 30, 2012 and December 31, 2011:

Description	Balances as of September 30, 2012	Quoted Prices in active markets for identical Assets (Level 1)	Balances as of December 31, 2011	Quoted Prices in active markets for identical Assets (Level 1)
Assets				
Cash and Cash Equivalents:				
Money Market Funds	\$ 25,178,383	\$ 25,178,383	\$ 20,836,617	\$ 20,836,617
Investments:				
Asset backed securities	17,250,864	17,250,864	18,309,316	18,309,316
Sovereign Debt Securities	15,113,399	15,113,399	10,708,563	10,708,563
Corporate Debt Securities	32,016,324	32,016,324	17,824,331	17,824,331
Total financial Assets	\$ 89,558,970	\$ 89,558,970	\$ 67,678,827	\$ 67,678,827

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MercadoLibre, Inc.

Notes to Condensed Consolidated Financial Statements (unaudited)

6. Fair Value Measurement of Assets and Liabilities (Continued)

The Company's financial assets are valued using market prices on active markets (level 1). Level 1 instrument valuations are obtained from real-time quotes for transactions in active exchange markets involving identical assets. As of September 30, 2012 and December 31, 2011, the Company did not have any assets obtained from readily-available pricing sources for comparable instruments (level 2) or without observable market values that would require a high level of judgment to determine fair value (level 3).

The unrealized net gains on short term and long term investments are reported as a component of accumulated other comprehensive income. The Company does not anticipate any significant realized losses associated with those investments in excess of the Company's historical cost.

In addition, as of September 30, 2012 and December 31, 2011, the Company had \$74,427,916 and \$72,019,726 of short-term investments, which consisted of time deposits. Those investments are accounted for at amortized cost which, as of September 30, 2012 and December 31, 2011, approximates their fair values.

As of September 30, 2012 and December 31, 2011, the carrying value of the Company's cash and cash equivalents approximated their fair value which was held primarily in money markets funds and bank deposits. In addition, the carrying value of accounts receivables, credit card receivables, funds payable to customers, other receivables, other assets, accounts payables, social security payables, taxes payables, loans and provisions and other liabilities approximates their fair values because of its short term maturity.

For the three and nine-month periods ended September 30, 2012 and 2011, the Company held no direct investments in auction rate securities, collateralized debt obligations, structured investment vehicles. As of September 30, 2012 and December 31, 2011, the Company does not have any non-financial assets or liabilities measured at fair value.

As of September 30, 2012 and December 31, 2011, the fair value of short and long-term investments classified as available for sale securities are as follows:

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MercadoLibre, Inc.

Notes to Condensed Consolidated Financial Statements (unaudited)

6. Fair Value Measurement of Assets and Liabilities (Continued)

	September 30, 2012			
	Gross Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses (1)	Estimated Fair Value
Short-term investments				
Sovereign Debt Securities	\$ 39,946	\$ 26	\$	\$ 39,972
Corporate Debt Securities	4,914,703	7,901		4,922,604
Total Short-term investments	\$ 4,954,649	\$ 7,927	\$	\$ 4,962,576
Long-term investments				
Sovereign Debt Securities	\$ 14,734,664	\$ 338,763	\$	\$ 15,073,427
Corporate Debt Securities	26,457,314	640,130	(3,724)	27,093,720
Asset Backed Securities (2)	16,767,501	491,305	(7,942)	17,250,864
Total Long-term investments	\$ 57,959,479	\$ 1,470,198	\$ (11,666)	\$ 59,418,011
Total	\$ 62,914,128	\$ 1,478,125	\$ (11,666)	\$ 64,380,587
	December 31, 2011			
	Gross Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses (1)	Estimated Fair Value
Short-term investments				
Sovereign Debt Securities	\$ 1,554,448	\$ 322	\$	\$ 1,554,770
Corporate Debt Securities	1,375,006		(20,882)	1,354,124
Total Short-term investments	\$ 2,929,454	\$ 322	\$ (20,882)	\$ 2,908,894
Long-term investments				
Sovereign Debt Securities	\$ 8,483,883	\$ 669,910	\$	\$ 9,153,793
Corporate Debt Securities	16,386,974	187,946	(104,713)	16,470,207
Asset Backed Securities (2)	17,647,012	715,749	(53,445)	18,309,316
Total Long-term investments	\$ 42,517,869	\$ 1,573,605	\$ (158,158)	\$ 43,933,316
Total	\$ 45,447,323	\$ 1,573,927	\$ (179,040)	\$ 46,842,210

- (1) Unrealized losses from securities are primarily attributable to market price movements. Management does not believe any remaining unrealized losses represent other-than-temporary impairments based on our evaluation of available evidence including the credit rating of the investments, as of September 30, 2012 and December 31, 2011.

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(2) Asset backed securities have investment grade credit ratings.

As of September 30, 2012, the estimated fair values of short-term and long-term investments classified by its contractual maturities are as follows:

One year or less	\$ 4,962,576
One year to two years	9,327,280
Two years to three years	18,027,929
Three years to four years	9,465,330
Four years to five years	7,525,512
More than five years	15,071,960
Total	\$ 64,380,587

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MercadoLibre, Inc.

Notes to Condensed Consolidated Financial Statements (unaudited)

7. Commitments and Contingencies

Litigation and Other Legal Matters

The Company is subject to certain contingent liabilities with respect to existing or potential claims, lawsuits and other proceedings. The Company accrues liabilities when it considers probable that future costs will be incurred and such costs can be reasonably estimated. The proceeding-related reserve is based on developments to date and historical information related to actions filed against the Company. As of September 30, 2012, the Company had established reserves for proceeding-related contingencies of \$2,486,669 to cover legal actions against the Company. In addition, as of September 30, 2012 the Company and its subsidiaries are subject to certain legal actions considered by the Company's management and its legal counsels to be reasonably possible for an aggregate amount up to \$4,699,800.

No loss amount has been accrued for such possible legal actions of which most significant (individually or in the aggregate) are described below.

As of September 30, 2012, 499 legal actions were pending in the Brazilian ordinary courts. In addition, as of September 30, 2012, there were 2,894 cases still pending in Brazilian consumer courts. Filing and pursuing of an action before Brazilian consumer courts do not require the assistance of a lawyer. In most of the cases filed against the Company, the plaintiffs asserted that the Company was responsible for fraud committed against them, or responsible for damages suffered when purchasing an item on the Company's website, when using MercadoPago, or when the Company invoiced them.

On March 17, 2006, Vintage Denim Ltda., or Vintage, sued the Company's Brazilian subsidiaries MercadoLivre.com Atividades de Internet Ltda. and eBazar.com.br Ltda. in the 29th Civil Court of the County of São Paulo, State of São Paulo, Brazil. Vintage requested a preliminary injunction alleging that these subsidiaries were infringing Diesel trademarks and their right of exclusive distribution as a result of sellers listing allegedly counterfeit and original imported Diesel branded clothing through the Brazilian page of the Company's website, based on Brazilian Industrial Property Law (Law 9,279/96). Vintage sought an order enjoining the sale of Diesel-branded clothing on the Company's platform. A preliminary injunction was granted on April 11, 2006 to prohibit the offer of Diesel-branded products, and a fine for non-compliance was imposed in the approximate amount of \$5,300 per defendant per day of non-compliance. The Company appealed that fine and obtained its suspension in 2006. Because the appeal of the preliminary injunction failed, in March of 2007, Vintage presented petitions alleging the Company's non-compliance with the preliminary injunction granted to Vintage and requested a fine of approximately \$3.3 million against the Company's subsidiaries, which represents approximately \$5,300 per defendant per day of alleged non-compliance since April 2006. In July 2007, the judge ordered the payment of the fine mandated in the preliminary injunction, without specifying the amount. In September 2007, the judge decided that (i) the Brazilian subsidiaries were not responsible for alleged infringement of intellectual property rights by its users; and that (ii) the plaintiffs did not prove the alleged infringement of its intellectual property rights. However, the decision maintained the injunction until such ruling is non-appealable. The plaintiff appealed the judge's ruling regarding the subsidiary's non-responsibility and the Company appealed the decision that maintained the preliminary injunction. On July 26, 2011 the State Court of Appeals of the State of São Paulo confirmed the judge's ruling regarding our subsidiary's non-responsibility. The decision on the appeal regarding the decision that maintained the preliminary injunction is still pending. In the opinion of the Company's leg