UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2019

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: 001-38274

FUNKO, INC.

(Exact name of registrant as specified in its charter)

Delaware **(State or other jurisdiction of incorporation or organization)**	**35-2593276** **(I.R.S. Employer Identification No.)**
2802 Wetmore Avenue **Everett, Washington** **(Address of principal executive offices)**	**98201** **(Zip Code)**

(425) 783-3616
(Registrant's telephone number, including area code)
N/A
(Former name, former address and former fiscal year, if changed since last report)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Class A Common Stock, $0.0001 par value per share	FNKO	The Nasdaq Stock Market LLC

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

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

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

Large accelerated filer	☐	Accelerated filer	☒
Non-accelerated filer	☐	Smaller reporting company	☒
		Emerging growth company	☒

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

As of August 6, 2019, the registrant had 31,354,674 shares of Class A common stock, $0.0001 par value per share, and 17,690,314 shares of Class B common stock, $0.0001 par value per share, outstanding.

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. All statements contained in this Quarterly Report on Form 10-Q other than statements of historical fact, including statements regarding our future operating results and financial position, our business strategy and plans, potential acquisitions, market growth and trends, demand for our products, the remediation of our material weakness in internal control over financial reporting, the effectiveness of our preliminary prospectus on Form S-3, anticipated future expenses and payments, and our objectives for future operations, are forward-looking statements. The words "believe," "may," "will," "estimate," "continue," "anticipate," "intend," "expect," "could," "would," "project," "plan," "potentially," "preliminary," "likely," and similar expressions are intended to identify forward-looking statements. We have based these forward-looking statements largely on our current expectations and projections about future events and trends that we believe may affect our financial condition, results of operations, business strategy, short-term and long-term business operations and objectives, and financial needs. These forward-looking statements are subject to a number of risks, uncertainties, and assumptions, including the important factors described in this Quarterly Report on Form 10-Q under Part II. Item 1A. "Risk Factors," and in our other filings with the Securities and Exchange Commission, that may cause our actual results, performance or achievements to differ materially and adversely from those expressed or implied by the forward-looking statements.

Any forward-looking statements made herein speak only as of the date of this Quarterly Report on Form 10-Q, and you should not rely on forward-looking statements as predictions of future events. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee that the future results, performance, or achievements reflected in the forward-looking statements will be achieved or occur. We undertake no obligation to update any of these forward-looking statements for any reason after the date of this Quarterly Report on Form 10-Q or to conform these statements to actual results or revised expectations.

Part I – FINANCIAL INFORMATION

Item 1. Financial Statements

FUNKO, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
	(In thousands, except per share data)			
Net sales	$ 191,199	$ 138,723	$ 358,264	$ 275,934
Cost of sales (exclusive of depreciation and amortization shown separately below)	119,998	85,884	223,654	172,528
Selling, general, and administrative expenses	43,647	34,537	84,115	69,039
Acquisition transaction costs	—	—	—	28
Depreciation and amortization	10,425	9,650	20,655	18,951
Total operating expenses	174,070	130,071	328,424	260,546
Income from operations	17,129	8,652	29,840	15,388
Interest expense, net	3,763	5,584	7,835	11,480
Other (income) expense, net	(219)	2,602	(154)	1,160
Income before income taxes	13,585	466	22,159	2,748
Income tax expense	2,170	192	3,599	755
Net income	11,415	274	18,560	1,993
Less: net income attributable to non-controlling interests	6,283	204	11,233	1,326
Net income attributable to Funko, Inc.	$ 5,132	$ 70	$ 7,327	$ 667
	– —		– —	
Earnings per share of Class A common stock:	– —		– —	
Basic	$ 0.17	$ —	$ 0.26	$ 0.03
Diluted	$ 0.16	$ —	$ 0.24	$ 0.03
Weighted average shares of Class A common stock outstanding:				
Basic	29,910	23,344	28,284	23,341
Diluted	32,115	24,759	30,296	24,634

See accompanying notes to the unaudited condensed consolidated financial statements.

FUNKO, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
	(In thousands)			
Net income	$ 11,415	$ 274	$ 18,560	$ 1,993
Other comprehensive loss:				
Foreign currency translation loss, net of tax effect of $129 and $(61) for the three months ended June 30, 2019 and 2018, respectively, and $49 and $(61) for the six months ended June 30, 2019 and 2018, respectively	(824)	(2,272)	(171)	(1,189)
Comprehensive income (loss)	10,591	(1,998)	18,389	804
Less: Comprehensive income (loss) attributable to non-controlling interests	5,900	(971)	11,231	732
Comprehensive income attributable to Funko, Inc.	$ 4,691	$ (1,027)	$ 7,158	$ 72

See accompanying notes to the unaudited condensed consolidated financial statements.

FUNKO, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

	June 30, 2019	December 31, 2018
	(In thousands, except per share amounts)	
Assets		
Current assets:		
Cash and cash equivalents	$ 19,485	$ 13,486
Accounts receivable, net	131,646	148,627
Inventory	75,298	86,622
Prepaid expenses and other current assets	17,170	11,904
Total current assets	243,599	260,639
Property and equipment, net	43,331	44,296
Operating lease right-of-use assets	41,759	—
Goodwill	124,510	116,078
Intangible assets, net	229,316	233,645
Deferred tax asset	29,673	7,407
Other assets	3,986	4,275
Total assets	$ 716,174	$ 666,340
Liabilities and Stockholders' Equity		
Current liabilities:		
Line of credit	$ 19,329	$ 20,000
Current portion long-term debt, net of unamortized discount	10,619	10,593
Current portion of operating lease liabilities	8,602	—
Accounts payable	32,852	36,130
Income taxes payable	1,046	4,492
Accrued royalties	29,819	39,020
Accrued expenses and other current liabilities	26,931	33,015
Total current liabilities	129,198	143,250
Long-term debt, net of unamortized discount	211,383	216,704
Operating lease liabilities, net of current portion	40,401	—
Deferred tax liability	20	5
Liabilities under tax receivable agreement, net of current portion	33,019	6,504
Deferred rent and other long-term liabilities	5,788	6,623
Commitments and contingencies		
Stockholders' equity:		
Class A common stock, par value $0.0001 per share, 200,000 shares authorized; 30,214 and 24,960 shares issued and outstanding as of June 30, 2019 and December 31, 2018, respectively	3	2
Class B common stock, par value $0.0001 per share, 50,000 shares authorized; 18,740 and 23,584 shares issued and outstanding as of June 30, 2019 and December 31, 2018, respectively	2	2
Additional paid-in-capital	176,684	146,154
Accumulated other comprehensive loss	(336)	(167)
Retained earnings	16,044	8,717
Total stockholders' equity attributable to Funko, Inc.	192,397	154,708
Non-controlling interests	103,968	138,546
Total stockholders' equity	296,365	293,254
Total liabilities and stockholders' equity	$ 716,174	$ 666,340

See accompanying notes to the unaudited condensed consolidated financial statements.

FUNKO, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Six Months Ended June 30,	
	2019	2018
	(In thousands)	
Operating Activities		
Net income	$ 18,560	$ 1,993
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, amortization and other	21,054	18,951
Equity-based compensation	6,115	2,143
Accretion of discount on long-term debt	581	737
Amortization of debt issuance costs	130	291
Foreign currency gain (loss)	327	(129)
Changes in operating assets and liabilities:		
Accounts receivable, net	14,357	17,674
Inventory	11,342	14,516
Prepaid expenses and other assets	(191)	3,195
Accounts payable	(3,395)	(32,988)
Income taxes payable	(3,437)	(232)
Accrued royalties	(9,201)	(6,175)
Accrued expenses and other liabilities	(8,288)	2,165
Net cash provided by operating activities	47,954	22,141
Investing Activities		
Purchase of property and equipment	(11,730)	(14,117)
Acquisitions of businesses and related intangible assets, net of cash	(6,369)	(635)
Net cash used in investing activities	(18,099)	(14,752)
Financing Activities		
Borrowings on line of credit	22,543	161,571
Payments on line of credit	(23,383)	(130,049)
Debt issuance costs	(272)	—
Payment of long-term debt	(5,875)	(17,700)
Proceeds from exercise of equity-based options	1,387	—
Distribution to continuing equity owners	(18,121)	(18,885)
Net cash used in financing activities	(23,721)	(5,063)
Effect of exchange rates on cash and cash equivalents	(135)	838
Net increase in cash and cash equivalents	5,999	3,164
Cash and cash equivalents at beginning of period	13,486	7,728
Cash and cash equivalents at end of period	$ 19,485	$ 10,892

See accompanying notes to the unaudited condensed consolidated financial statements.

1. Organization and Operations

The unaudited condensed consolidated financial statements include Funko, Inc. and its subsidiaries (together with its subsidiaries, the “Company”) and have been prepared in accordance with U.S. generally accepted accounting principles (“U.S. GAAP”). All intercompany balances and transactions have been eliminated.

The Company was formed as a Delaware corporation on April 21, 2017. The Company was formed for the purpose of completing an initial public offering (“IPO”) of its Class A common stock and related transactions in order to carry on the business of Funko Acquisition Holdings, L.L.C. (“FAH, LLC”) and its subsidiaries. FAH, LLC, a holding company with no operating assets or operations, was formed on September 24, 2015. On October 30, 2015, ACON Funko Investors, L.L.C. (together with related entities, “ACON”), through FAH, LLC, acquired a controlling interest in Funko Holdings LLC (“FHL”) (the “ACON Acquisition”), a Delaware limited liability company formed on May 28, 2013, which is also a holding company with no operating assets or operations. FAH, LLC owns 100% of FHL and FHL owns 100% of Funko, LLC, a limited liability company formed in the state of Washington, which is its operating entity. Funko, LLC is headquartered in Everett, Washington and is a leading pop culture consumer products company. Funko, LLC designs, sources, and distributes licensed pop culture products.

On November 6, 2017, the Company completed an IPO of 10,416,666 shares of its Class A common stock at a public offering price of $12.00 per share, receiving approximately $117.3 million in net proceeds, after deducting underwriting discounts and commissions, which were used to purchase 10,416,666 of FAH, LLC’s newly-issued common units at a price per unit equal to the price per share of Class A common stock sold in the IPO, less underwriting discounts and commissions. The IPO and related reorganization transactions (the “Transactions”) resulted in the Company being the sole managing member of FAH, LLC. As the sole managing member of FAH, LLC, Funko, Inc. operates and controls all of FAH, LLC’s operations and, through FAH, LLC and its subsidiaries, conducts FAH, LLC’s business. Accordingly, the Company consolidates the financial results of FAH, LLC and reports a non-controlling interest in its unaudited condensed consolidated financial statements representing the FAH, LLC interests held by ACON Funko Investors, L.L.C., a Delaware limited liability company (“ACON Funko Investors”) and certain of its affiliates, Fundamental Capital, LLC and Funko International, LLC (collectively, “Fundamental”), and certain current and former executive officers, employees and directors, in each case, who held profits interests in FAH, LLC and who received common units of FAH, LLC in exchange for their profits interests in connection with the Transactions (as defined herein) (collectively, the “Original Equity Owners”) and the former holders of warrants to purchase ownership interests in FAH, LLC, which were converted into common units of FAH, LLC in connection with the Transactions, and, in each case, each of their permitted transferees that own common units in FAH, LLC and who may redeem at each of their options (subject in certain circumstances to time-based vesting requirements) their common units for, at the Company’s election, cash or newly-issued shares of the Company’s Class A common stock (collectively, the “Continuing Equity Owners”).

Consolidation and Interim Financial Information

In the opinion of management, all adjustments considered necessary for a fair presentation of the results as of the date of and for the interim periods presented have been included; such adjustments consist of normal recurring adjustments. The unaudited condensed consolidated results of operations for the current interim period are not necessarily indicative of the results for the entire year ending December 31, 2019, due to seasonality and other factors. These unaudited condensed consolidated financial statements should be read in conjunction with the Company’s audited consolidated financial statements and related notes included in its Annual Report on Form 10-K for the year ended December 31, 2018, filed with the Securities and Exchange Commission (“SEC”) on March 6, 2019.

Revision of Previously-Issued Financial Statements

During the three months ended June 30, 2019, the Company identified that its subsidiary, Loungefly, LLC (“Loungefly”), which was acquired on June 28, 2017, had been underpaying certain duties owed to U.S. Customs and Border Protection ("U.S. Customs"). In May 2019, the Company notified U.S. Customs of the potential underpayments and commenced an internal investigation to determine the cause of the underpayments and the proper amount of duties and fees owed for the applicable five-year statute of limitations period. The Company identified a total of approximately $7.8 million in underpayments to U.S. Customs during the period from May 24, 2014 through June 30, 2019, $6.3 million of which related to previously-issued consolidated financial statements. In July 2019, the Company submitted payment of $7.8 million to U.S. Customs along with a report detailing the nature of the underpayments.

The underpayment of the customs duties and fees led to certain errors in the Company's previously-issued consolidated financial statements. The Company has concluded that the errors identified were immaterial individually and, in the aggregate, to the Company's previously-issued quarterly and annual consolidated financial statements; however, the Company further concluded that correcting the errors cumulatively would have been material to its consolidated statement of operations for the three and six months ended June 30, 2019. Accordingly, prior period amounts have been revised to reflect the correction of these as well as other previously identified immaterial errors.

The following tables present the revised results for each quarterly period that was impacted, the adjustments made to each period and the previously reported amounts to summarize the effect of the revision on the previously-issued consolidated financial statements for the periods impacted.

(As reported)	**Three Months Ended**							
	Jun. 30, 2017	**Sep. 30, 2017**	**Dec. 31, 2017**	**Mar. 31, 2018**	**Jun. 30, 2018**	**Sep. 30, 2018**	**Dec. 31, 2018**	**Mar. 31, 2019**
	(In thousands, except per share data)							
Statement of Operations Data:								
Net sales	$104,746	$142,812	$ 169,474	$137,211	$138,723	$176,915	$ 233,224	$ 166,800
Cost of sales (exclusive of depreciation and amortization shown separately below)	$ 66,005	$ 84,387	$ 102,926	$ 85,921	$ 85,717	$108,898	$ 147,526	$ 103,268
Selling, general, and administrative expenses	$ 25,809	$ 32,511	$ 37,532	$ 34,810	$ 34,229	$ 41,267	$ 45,015	$ 40,818
Depreciation and amortization	$ 7,588	$ 8,433	$ 9,220	$ 9,301	$ 9,650	$ 9,961	$ 10,204	$ 10,093
Total operating expenses	$100,687	$125,467	$ 150,097	$130,060	$129,596	$160,126	$ 202,745	$ 154,179
Income from operations	$ 4,059	$ 17,345	$ 19,377	$ 7,151	$ 9,127	$ 16,789	$ 30,479	$ 12,621
Income (loss) before income taxes	$ (3,514)	$ 8,286	$ 7,995	$ 2,697	$ 941	$ 9,605	$ 19,935	$ 8,484
Income tax expense	$ 1,024	$ 22	$ 494	$ 460	$ 70	$ 1,519	$ 2,818	$ 1,414
Net income (loss)	$ (4,538)	$ 8,264	$ 7,501	$ 2,237	$ 871	$ 8,086	$ 17,117	$ 7,070
Net income attributable to non-controlling interests	$ -	$ -	$ 1,875	$ 1,338	$ 454	$ 6,056	$ 11,107	$ 4,910
Net income (loss) attributable to Funko, Inc.	$ (4,538)	$ 8,264	$ 5,626	$ 899	$ 417	$ 2,030	$ 6,010	$ 2,160
	- —	- —	- —	- —	- —	- —	- —	- —
Earnings per share of Class A common stock:	- —	- —	- —	- —	- —	- —	- —	- —
Basic			$ 0.04	$ 0.04	$ 0.02	$ 0.09	$ 0.24	$ 0.08
Diluted			$ 0.04	$ 0.04	$ 0.01	$ 0.08	$ 0.23	$ 0.08

(Adjustment)

	Three Months Ended							
	Jun. 30, 2017	Sep. 30, 2017	Dec. 31, 2017	Mar. 31, 2018	Jun. 30, 2018	Sep. 30, 2018	Dec. 31, 2018	Mar. 31, 2019
	(In thousands, except per share data)							
Statement of Operations Data:								
Net sales	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ 265
Cost of sales (exclusive of depreciation and amortization shown separately below)	$ -	$ 219	$ (331)	$ 723	$ 167	$ 148	$ 1,646	$ 388
Selling, general, and administrative expenses	$ -	$ -	$ -	$ (308)	$ 308	$ -	$ -	$ (350)
Depreciation and amortization	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ 137
Total operating expenses	$ -	$ 219	$ (331)	$ 415	$ 475	$ 148	$ 1,646	$ 175
Income from operations	$ -	$ (219)	$ 331	$ (415)	$ (475)	$ (148)	$ (1,646)	$ 90
Income (loss) before income taxes	$ -	$ (219)	$ 331	$ (415)	$ (475)	$ (148)	$ (1,646)	$ 90
Income tax expense	$ (435)	$ -	$ 161	$ 103	$ 122	$ 387	$ (48)	$ 15
Net income (loss)	$ 435	$ (219)	$ 170	$ (518)	$ (597)	$ (535)	$ (1,598)	$ 75
Net income attributable to non-controlling interests	$ -	$ -	$ 172	$ (216)	$ (250)	$ (75)	$ (815)	$ 40
Net income (loss) attributable to Funko, Inc.	$ 435	$ (219)	$ (2)	$ (302)	$ (347)	$ (460)	$ (783)	$ 35
	- —	- —	- —	- —	- —	- —	- —	- —
Earnings per share of Class A common stock:	- —	- —	- —	- —	- —	- —	- —	- —
Basic			$ -	$ (0.01)	$ (0.02)	$ (0.02)	$ (0.03)	$ -
Diluted			$ -	$ (0.02)	$ (0.01)	$ (0.02)	$ (0.03)	$ -

(Revised)

	Three Months Ended							
	Jun. 30, 2017	Sep. 30, 2017	Dec. 31, 2017	Mar. 31, 2018	Jun. 30, 2018	Sep. 30, 2018	Dec. 31, 2018	Mar. 31, 2019
	(In thousands, except per share data)							
Statement of Operations Data:								
Net sales	$ 104,746	$ 142,812	$ 169,474	$ 137,211	$ 138,723	$ 176,915	$ 233,224	$ 167,065
Cost of sales (exclusive of depreciation and amortization shown separately below)	$ 66,005	$ 84,606	$ 102,595	$ 86,644	$ 85,884	$ 109,046	$ 149,172	$ 103,656
Selling, general, and administrative expenses	$ 25,809	$ 32,511	$ 37,532	$ 34,502	$ 34,537	$ 41,267	$ 45,015	$ 40,468
Depreciation and amortization	$ 7,588	$ 8,433	$ 9,220	$ 9,301	$ 9,650	$ 9,961	$ 10,204	$ 10,230
Total operating expenses	$ 100,687	$ 125,686	$ 149,766	$ 130,475	$ 130,071	$ 160,274	$ 204,391	$ 154,354
Income from operations	$ 4,059	$ 17,126	$ 19,708	$ 6,736	$ 8,652	$ 16,641	$ 28,833	$ 12,711
Income (loss) before income taxes	$ (3,514)	$ 8,067	$ 8,326	$ 2,282	$ 466	$ 9,457	$ 18,289	$ 8,574
Income tax expense	$ 589	$ 22	$ 655	$ 563	$ 192	$ 1,906	$ 2,770	$ 1,429
Net income (loss)	$ (4,103)	$ 8,045	$ 7,671	$ 1,719	$ 274	$ 7,551	$ 15,519	$ 7,145
Net income attributable to non-controlling interests	$ -	$ -	$ 2,047	$ 1,122	$ 204	$ 5,981	$ 10,292	$ 4,950
Net income (loss) attributable to Funko, Inc.	$ (4,103)	$ 8,045	$ 5,624	$ 597	$ 70	$ 1,570	$ 5,227	$ 2,195
	- —	- —	- —	- —	- —	- —	- —	- —
Earnings per share of Class A common stock:	- —	- —	- —	- —	- —	- —	- —	- —
Basic			$ 0.04	$ 0.03	$ -	$ 0.07	$ 0.21	$ 0.08
Diluted			$ 0.04	$ 0.02	$ -	$ 0.06	$ 0.20	$ 0.08

(As reported)	Jun. 30, 2017	Sep. 30, 2017	Dec. 31, 2017	Mar. 31, 2018	Jun. 30, 2018	Sep. 30, 2018	Dec. 31, 2018	Mar. 31, 2019
Balance Sheet Data:				**(In thousands)**				
Assets:								
Accounts receivable, net	$ 81,629	$ 99,293	$115,478	$ 88,616	$ 96,474	$127,026	$148,627	$117,618
Inventory	$ 57,982	$ 78,836	$ 79,082	$ 73,950	$ 63,591	$ 81,206	$ 86,622	$ 75,396
Total current assets	$ 183,935	$ 217,112	$224,015	$193,686	$189,472	$244,110	$260,639	$232,495
Goodwill	$ 106,521	$ 107,265	$110,902	$113,498	$113,052	$112,977	$112,818	$121,892
Intangible assets, net	$ 257,991	$ 254,391	$250,649	$245,465	$241,337	$237,518	$233,645	$233,155
Deferred tax asset	$ —	$ —	$ 51	$ 82	$ 78	$ 5,795	$ 7,346	$ 21,081
Total assets	$ 588,380	$ 621,955	$630,313	$597,801	$590,994	$648,765	$663,019	$689,063
Liabilities:								
Accrued royalties	$ 16,297	$ 25,380	$ 25,969	$ 18,858	$ 19,351	$ 31,494	$ 39,020	$ 28,359
Accrued expenses and other current liabilities	$ 27,044	$ 32,871	$ 27,032	$ 29,726	$ 25,730	$ 31,066	$ 27,621	$ 19,647
Total current liabilities	$ 158,367	$ 204,912	$129,926	$118,496	$122,152	$165,281	$137,856	$120,100
Deferred tax liability	$ —	$ —	$ 588	$ 689	$ 259	$ 65	$ 5	$ 23
Deferred rent and other long-term liabilities	$ 3,464	$ 3,438	$ 3,474	$ 3,929	$ 4,027	$ 4,789	$ 5,583	$ 4,519
Stockholders' / Members' equity:								
Additional paid-in-capital / Members' equity	$ 291,460	$ 292,043	$129,320	$130,292	$131,624	$142,426	$146,408	$166,208
Accumulated other comprehensive (loss)	$ 771	$ 1,361	$ 802	$ 1,304	$ 207	$ 163	$ (171)	$ 100
Retained earnings	$(137,241)	$(128,976)	$ 1,041	$ 1,940	$ 2,357	$ 4,387	$ 10,397	$ 12,557
Total stockholders' equity attributable to Funko, Inc. / members' equity	$ 154,990	$ 164,428	$131,167	$133,540	$134,192	$146,980	$156,638	$178,870
Non-controlling interests	$ —	$ —	$149,988	$141,050	$132,149	$129,438	$139,728	$118,550
Total stockholders' / members' equity	$ 154,990	$ 164,428	$281,155	$274,590	$266,341	$276,418	$296,366	$297,420
Total liabilities and stockholders' equity	$ 588,380	$ 621,955	$630,313	$597,801	$590,994	$648,765	$663,019	$689,063

(Adjustment)	Jun. 30, 2017	Sep. 30, 2017	Dec. 31, 2017	Mar. 31, 2018	Jun. 30, 2018	Sep. 30, 2018	Dec. 31, 2018	Mar. 31, 2019
Balance Sheet Data:				**(In thousands)**				
Assets:								
Accounts receivable, net	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ 266
Inventory	$ 96	$ 520	$ 505	$ 451	$ 562	$ 1,048	$ —	$ 492
Total current assets	$ 96	$ 520	$ 505	$ 451	$ 562	$ 1,048	$ —	$ 758
Goodwill	$ 3,260	$ 3,260	$ 3,260	$ 3,260	$ 3,260	$ 3,260	$ 3,260	$ 3,260
Intangible assets, net	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ (137)
Deferred tax asset	$ —	$ —	$ —	$ —	$ —	$ 109	$ 61	$ 45
Total assets	$ 3,356	$ 3,780	$ 3,765	$ 3,711	$ 3,822	$ 4,417	$ 3,321	$ 3,926
Liabilities:								
Accrued royalties	$ —	$ 317	$ (423)	$ —	$ —	$ —	$ —	$ —
Accrued expenses and other current liabilities	$ 2,918	$ 3,244	$ 3,637	$ 3,573	$ 4,161	$ 4,796	$ 5,394	$ 5,925
Total current liabilities	$ 2,918	$ 3,561	$ 3,214	$ 3,573	$ 4,161	$ 4,796	$ 5,394	$ 5,925
Deferred tax liability	$ —	$ —	$ (76)	$ (101)	$ (136)	$ —	$ —	$ —
Deferred rent and other long-term liabilities	$ —	$ —	$ 490	$ 620	$ 775	$ 1,135	$ 1,040	$ 1,039
Stockholders' / Members' equity:								
Additional paid-in-capital / Members' equity	$ —	$ —	$ (254)	$ (254)	$ (254)	$ (254)	$ (254)	$ (254)
Accumulated other comprehensive (loss)	$ 4	$ 4	$ 4	$ 4	$ 4	$ 4	$ 4	$ 4
Retained earnings	$ 434	$ 215	$ 213	$ (89)	$ (436)	$ (897)	$ (1,680)	$ (1,645)
Total stockholders' equity attributable to Funko, Inc. / members' equity	$ 438	$ 219	$ (37)	$ (339)	$ (686)	$ (1,147)	$ (1,930)	$ (1,895)
Non-controlling interests	$ —	$ —	$ 174	$ (42)	$ (292)	$ (367)	$ (1,182)	$ (1,143)
Total stockholders' / members' equity	$ 438	$ 219	$ 137	$ (381)	$ (978)	$ (1,514)	$ (3,112)	$ (3,038)
Total liabilities and stockholders' equity	$ 3,356	$ 3,780	$ 3,765	$ 3,711	$ 3,822	$ 4,417	$ 3,321	$ 3,926

(Revised)	Jun. 30, 2017	Sep. 30, 2017	Dec. 31, 2017	Mar. 31, 2018	Jun. 30, 2018	Sep. 30, 2018	Dec. 31, 2018	Mar. 31, 2019
Balance Sheet Data:				(In thousands)				
Assets:								
Accounts receivable, net	$ 81,629	$ 99,293	$115,478	$ 88,616	$ 96,474	$127,026	$148,627	$117,884
Inventory	$ 58,078	$ 79,356	$ 79,587	$ 74,401	$ 64,153	$ 82,254	$ 86,622	$ 75,888
Total current assets	$ 184,031	$ 217,632	$224,520	$194,137	$190,034	$245,158	$260,639	$233,253
Goodwill	$ 109,781	$ 110,525	$114,162	$116,758	$116,312	$116,237	$116,078	$125,152
Intangible assets, net	$ 257,991	$ 254,391	$250,649	$245,465	$241,337	$237,518	$233,645	$233,018
Deferred tax asset	$ —	$ —	$ 51	$ 82	$ 78	$ 5,904	$ 7,407	$ 21,126
Total assets	$ 591,736	$ 625,735	$634,078	$601,512	$594,816	$653,182	$666,340	$692,989
Liabilities:								
Accrued royalties	$ 16,297	$ 25,697	$ 25,546	$ 18,858	$ 19,351	$ 31,494	$ 39,020	$ 28,359
Accrued expenses and other current liabilities	$ 29,962	$ 36,115	$ 30,669	$ 33,299	$ 29,891	$ 35,862	$ 33,015	$ 25,572
Total current liabilities	$ 161,285	$ 208,473	$133,140	$122,069	$126,313	$170,077	$143,250	$126,025
Deferred tax liability	$ —	$ —	$ 512	$ 588	$ 123	$ 65	$ 5	$ 23
Deferred rent and other long-term liabilities	$ 3,464	$ 3,438	$ 3,964	$ 4,549	$ 4,802	$ 5,924	$ 6,623	$ 5,558
Stockholders' / Members' equity:								
Additional paid-in-capital / Members' equity	$ 291,460	$ 292,043	$129,066	$130,038	$131,370	$142,172	$146,154	$165,954
Accumulated other comprehensive (loss)	$ 775	$ 1,365	$ 806	$ 1,308	$ 211	$ 167	$ (167)	$ 104
Retained earnings	$(136,807)	$(128,761)	$ 1,254	$ 1,851	$ 1,921	$ 3,490	$ 8,717	$ 10,912
Total stockholders' equity attributable to Funko, Inc. / members' equity	$ 155,428	$ 164,647	$131,130	$133,201	$133,506	$145,833	$154,708	$176,975
Non-controlling interests	$ —	$ —	$150,162	$141,008	$131,857	$129,071	$138,546	$117,407
Total stockholders' / members' equity	$ 155,428	$ 164,647	$281,292	$274,209	$265,363	$274,904	$293,254	$294,382
Total liabilities and stockholders' equity	$ 591,736	$ 625,735	$634,078	$601,512	$594,816	$653,182	$666,340	$692,989

The identified adjustments had no effect on previously reported total cash flows from operating, investing or financing activities for any of the periods reflected above.

2. Significant Accounting Policies

Use of Estimates

The preparation of the Company’s unaudited 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 the disclosure of contingent assets and liabilities at the date of the consolidated financial statements as well as the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates and assumptions.

Significant Accounting Policies

A description of the Company’s significant accounting policies is included in the audited consolidated financial statements within its Annual Report on Form 10–K for the year ended December 31, 2018.

Recently Adopted Accounting Standards

Lease Accounting. In February 2016, the FASB issued guidance related to lease accounting that requires the recognition of lease assets and lease liabilities on the balance sheet and disclosure of key information about leasing arrangements for leases with a term of more than 12 months. The Company adopted the standard on January 1, 2019 by recognizing and measuring leases at the adoption date with a cumulative effect of initially applying the guidance recognized at the date of initial application. Comparative information has not been restated and continues to be reported under the standards in effect for those periods.

The Company has elected the “package of practical expedients” and as a result is not required to reassess under the new standard its prior accounting conclusions about lease identification, lease classification and initial direct costs for lease contracts that exist as of the transition date. However, the Company has not elected the use of hindsight for determining the reasonably certain lease term.

The new lease standard also provides practical expedients and policy elections for an entity's ongoing accounting. The Company has elected the practical expedient to not separate lease and non-lease components for all of its leases. The Company has also elected the short-term lease recognition exemption, which results in no recognition of right-of-use assets and lease liabilities for existing short-term leases at transition.

Upon adoption on January 1, 2019, the Company recognized operating lease right-of-use assets and lease liabilities that have not previously been recorded. The lease liability for operating leases is based on the net present value of future minimum lease payments. The right-of-use asset for operating leases is based on the lease liability adjusted for the reclassification of certain balance sheet amounts such as deferred and prepaid rent. Deferred and prepaid rent will not be presented separately for periods subsequent to the adoption of the new lease standard.

The cumulative effect of initially applying the new lease accounting standard as of January 1, 2019 is as follows (in thousands):

	January 1, 2019		
	Beginning balance	**Cumulative Effect Adjustment**	**Beginning Balance, As Adjusted**
Assets:			
Operating lease right-of-use assets	$ —	$ 33,014	33,014
Liabilities and Stockholders' Equity:			
Current portion of operating lease liabilities	$ —	$ 7,380	$ 7,380
Accrued expenses and other current liabilities	$ 33,015	$ (429)	$ 32,586
Operating lease liabilities, net of current portion	$ —	$ 30,076	$ 30,076
Deferred rent and other long-term liabilities	$ 6,623	$ (4,013)	$ 2,610

The adoption of the standard did not result in any material changes to the recognition of operating lease expenses in the Company's unaudited condensed consolidated statements of operations.

Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income. In February 2018, the FASB issued new guidance that allows an entity to elect to reclassify "stranded" tax effects in accumulated other comprehensive income to retained earnings to address concerns related to accounting for certain provisions of the Tax Cuts and Jobs Act ("the Tax Act") enacted in December 2017. The adoption of this standard in the first quarter of 2019 had no impact on the Company's unaudited condensed consolidated financial statements.

3. Acquisitions

During the six months ended June 30, 2019, the Company completed one acquisition that was accounted for as a business combination by applying the acquisition method of accounting, where identifiable tangible and intangible assets acquired and liabilities assumed are recognized and measured as of the acquisition date at fair value and goodwill is calculated as the excess of the purchase price paid over the net assets acquired.

On February 11, 2019, the Company acquired 100% of the membership interests of Forrest-Pruzan Creative LLC (the "Forrest-Pruzan Acquisition"), a board game development studio in Seattle, WA, which now operates as Funko Games, LLC. This transaction represents an opportunity to expand the Company's product offerings into the board game category. The preliminary purchase consideration consists of $6.5 million in cash and 126,757 shares of the Company's Class A common stock with a fair value of $2.2 million paid at closing, $1.5 million cash holdback due to the sellers in 18 months, subject to certain conditions as per the agreement, and $2 million in cash due after a 24-month deferral period. The total purchase consideration of $11.9 million was allocated on a relative fair value basis between net assets acquired and liabilities assumed of $11.6 million and noncompetition agreements entered into contemporaneously with the acquisition of $0.3 million. The Company is still in the process of completing its analysis of the opening balance sheet balances and finalizing its analysis and assumptions over the fair value of assets and liabilities acquired and purchase consideration transferred, and the difference between the estimated and final values could be material.

Goodwill of $8.5 million is calculated as the excess of the purchase price paid over the net assets acquired. The goodwill recognized in connection with the Forrest-Pruzan Acquisition primarily reflects relevant skills and industry knowledge of the retained workforce, as well as intangible assets that do not qualify for separate recognition.

The activity of Funko Games, LLC included in the Company's condensed consolidated statements of operations from the acquisition date to June 30, 2019 was not material.

The purchase consideration allocated to the acquisition was as follows:

	Purchase Consideration at Fair Value (in thousands)
Cash paid	$ 6,500
Fair value of class A common stock issued	2,221
Cash holdback	1,400
Fair value of cash consideration due February 11, 2021	1,815
Total transaction price	$ 11,936
Less: Noncompetition agreements	(290)
Consideration transferred	$ 11,646

The following table shows the amounts recognized for each major class of assets acquired and liabilities assumed and the resultant purchase price allocation for the Forrest-Pruzan Acquisition as of February 11, 2019:

	Assets (Liabilities) Acquired (Assumed) at Fair Value (in thousands)
Cash and cash equivalents	$ 131
Property and equipment	14
Operating lease right-of-use assets	1,027
Goodwill	8,465
Intangible assets	3,300
Other assets	17
Current liabilities	(281)
Operating lease liabilities	(1,027)
Consideration transferred	$ 11,646

The following table summarizes the identifiable intangible assets acquired in connection with the transactions described above and their estimated useful lives as of February 11, 2019:

	Estimated Fair Value of Assets Acquired (in thousands)	Estimated Useful Life (Years)
Intangible asset type:		
Intellectual property	$ 720	3
Customer relationships	2,580	3
Intangible assets	$ 3,300	

4. Fair Value Measurements

The Company's financial instruments, other than those discussed below, include cash, accounts receivable, accounts payable, and accrued liabilities. The carrying amount of these financial instruments approximate fair value due to the short-term nature of these instruments. For financial instruments measured at fair value on a recurring basis, the Company prioritizes the inputs used in measuring fair value according to a three-tier fair value hierarchy defined by U.S. GAAP. For a description of the methods and assumptions that the Company uses to estimate the fair value and determine the classification according to the fair value hierarchy for each financial instrument, see the Company's audited consolidated financial statements and related notes included in its Annual Report on Form 10-K for the year ended December 31, 2018.

Debt. The estimated fair value of the Company's debt instruments, which are classified as Level 3 financial instruments, at June 30, 2019 and December 31, 2018, was approximately $245.5 million and $252.1 million, respectively. The carrying values of the Company's debt instruments at June 30, 2019 and December 31, 2018, were $241.3 million and $247.3 million, respectively. The estimated fair value of the Company's debt instruments primarily reflects assumptions regarding credit spreads for similar floating-rate instruments with similar terms and maturities and the Company's standalone credit risk.

5. Debt

Debt consists of the following (in thousands):

	June 30, 2019	December 31, 2018
New Revolving Credit Facility	$ 19,329	$ 20,000
New Term Loan Facility	$ 226,187	$ 232,063
Debt issuance costs	(4,185)	(4,766)
Total term debt	222,002	227,297
Less: current portion	10,619	10,593
Long-term debt, net	$ 211,383	$ 216,704

New Credit Facilities

On October 22, 2018 (the "Closing Date"), the Company entered into a new credit agreement providing for the New Term Loan Facility in the amount of $235.0 million and the New Revolving Credit Facility of $50.0 million (as amended, the "New Credit Facilities"). On February 11, 2019, the Company amended the New Credit Facilities to increase the New Revolving Credit Facility to $75.0 million.

Upon closing, proceeds from the New Credit Facilities were primarily used to repay all of the outstanding aggregate principal balance and accrued interest of $209.6 million on the previous Term Loan A Facility and $65.3 million on the previous Revolving Credit Facility. Upon repayment, both the previous Term Loan A Facility and the previous Revolving Credit Facility were terminated.

The New Term Loan Facility matures on October 22, 2023 (the "Maturity Date"). The New Term Loan Facility amortizes in quarterly installments in aggregate amounts equal to 5.00% of the original principal amount of the New Term Loan Facility in the first and second years of the New Term Loan Facility, 10.00% of the original principal amount of the New Term Loan Facility in the third and fourth years of the New Term Loan Facility and 12.50% of the original principal amount of the New Term Loan Facility in the fifth year of the New Term Loan Facility, with any outstanding balance due and payable on the Maturity Date. The first amortization payment was on December 31, 2018. The New Revolving Credit Facility terminates on the Maturity Date and loans thereunder may be borrowed, repaid, and reborrowed up to such date.

Loans under the New Credit Facilities bear interest, at the Company's option, at either the Euro-Rate (as defined in the Credit Agreement) plus 3.25% or the Base Rate (as defined in the Credit Agreement) plus 2.25%, with two 0.25% step-downs based on the achievement of certain leverage ratios following the Closing Date. The Euro-Rate is subject to a 0.00% floor. For loans based on the Euro-Rate, interest payments are due at the end of each applicable interest period. For loans based on the Base Rate, interest payments are due quarterly.

The New Credit Facilities are secured by substantially all of the assets of the Company and any of its existing or future material domestic subsidiaries, subject to customary exceptions. As of June 30, 2019 and December 31, 2018, the Company was in compliance with all of the covenants in its New Credit Facilities.

At June 30, 2019, the Company had $226.2 million and $19.3 million of borrowings outstanding under the New Term Loan Facility and New Revolving Credit Facility, respectively.   At December 31, 2018, the Company had $232.1 million and $20.0 million of borrowings outstanding under the New Term Loan Facility and New Revolving Credit Facility, respectively.

There were no outstanding letters of credit as of June 30, 2019 and December 31, 2018.

6. Leases

The Company has entered into non-cancellable operating leases for office, warehouse, and distribution facilities, with original lease periods expiring through 2030. Some operating leases also contain the option to renew for five-year periods at prevailing market rates at the time of renewal. In addition to minimum rent, certain of the leases require payment of real estate taxes, insurance, common area maintenance charges, and other executory costs. Differences between rent expense and rent paid are recognized as adjustments to operating lease right-of-use assets on the unaudited consolidated balance sheets. For certain leases the Company receives lease incentives, such as tenant improvement allowances, and records those as adjustments to operating lease right-of-use assets and operating leases liabilities on the unaudited condensed consolidated balance sheets and amortize the lease incentives on a straight-line basis over the lease term as an adjustment to rent expense. Rent expense was $3.5 million and $2.5 million for the three months ended June 30, 2019 and 2018, respectively, and $6.6 million and $4.7 million for the six months ended June 30, 2019 and 2018, respectively.

As of June 30, 2019, the Company had recorded operating lease liabilities of $49.0 million and operating lease right-of-use assets of $41.8 million. During the six months ended June 30, 2019, operating cash outflows relating to operating lease liabilities was $3.8 million and operating lease right-of-use assets obtained in exchange for new operating lease obligations was $7.9 million. As of June 30, 2019, the Company’s operating leases had a weighted-average remaining term of 7.3 years and weighted-average discount rate of 7.7%. Excluded from the measurement of operating lease liabilities and operating lease right-of-use assets were certain warehouse and distribution contracts that either qualify for the short-term lease recognition exception and/or do not give the Company the right to control the warehouse and/or distribution facilities underlying the contract.

The future payments on the Company’s operating lease liabilities as of June 30, 2019 were as follows (in thousands):

Remaining 2019	$	4,196
2020		9,815
2021		9,090
2022		7,842
2023		8,101
Thereafter		27,536
Total lease payments		66,580
Less: imputed interest		(17,577)
Total	$	49,003

7. Liabilities under Tax Receivable Agreement

On November 1, 2017, the Company entered into a tax receivable agreement with FAH, LLC (the “Tax Receivable Agreement”) and each of the Continuing Equity Owners that provides for the payment by the Company to the Continuing Equity Owners of 85% of the amount of tax benefits, if any, that it realizes, or in some circumstances, is deemed to realize, as a result of (i) future redemptions funded by the Company or exchanges, or deemed exchanges in certain circumstances, of common units for Class A common stock or cash, and (ii) certain additional tax benefits attributable to payments made under the Tax Receivable Agreement.

During the three and six months ended June 30, 2019, the Company recognized an additional liability related to the Tax Receivable Agreement in the amount of $10.6 million and $29.2 million, respectively, for the payments due to the redeeming members under the Tax Receivable Agreement, representing 85% of the aggregate tax benefits the Company expects to realize from the tax basis increases related to the redemption of FAH, LLC common units, after concluding it was probable that such Tax Receivable Agreement payments would be paid in the future based on the Company's estimate of future taxable income. The amount of Tax Receivable Agreement liabilities recognized during the three and six months ended June 30, 2018 was nominal.

There were no payments made pursuant to the Tax Receivable Agreement during the six months ended June 30, 2019 and 2018.

As of June 30, 2019, the Company's total obligation under the Tax Receivable Agreement, including accrued interest, was $35.9 million, of which $2.9 million was included in Accrued expenses and other current liabilities on the unaudited condensed consolidated balance sheets. There were no transactions subject to the Tax Receivable Agreement for which the Company did not recognize the related liability, as the Company concluded that it was probable that the Company would have sufficient future taxable income to utilize all of the related tax benefits. At December 31, 2018, the Company's total obligation under the Tax Receivable Agreement, including accrued interest, was $6.8 million, of which $0.3 million was included in Accrued expenses and other current liabilities on the condensed consolidated balance sheets.

8. Commitments and Contingencies

License Agreements

The Company enters into license agreements with various licensors of copyrighted and trademarked characters and design in connection with the products that it sells. The agreements generally require royalty payments based on product sales and in some cases may require minimum royalty and other related commitments.

In January 2019, the Company renewed its licensing agreements with Disney and its controlled affiliates, LucasFilm and Marvel. As of December 31, 2018, the Company recorded a $2.0 million consent fee under its existing licensing agreements with Disney, which was paid during the six months ended June 30, 2019.

Employment Agreements

The Company has employment agreements with certain officers. The agreements include, among other things, an annual bonus based on certain performance metrics of the Company, as defined by the board, and up to one year's severance pay beyond termination date.

Debt

The Company has entered into a credit agreement which includes a term loan facility and a revolving credit facility. See Note 5, Debt.

Tax Receivable Agreement

The Company is party to the Tax Receivable Agreement with FAH, LLC and each of the Continuing Equity Owners that provides for the payment by the Company to the Continuing Equity Owners under certain circumstances. See Note 7, Liabilities under Tax Receivable Agreement.

Legal Contingencies

The Company is involved in claims and litigation in the ordinary course of business, some of which seek monetary damages, including claims for punitive damages, which are not covered by insurance. For certain pending matters, accruals have not been established because such matters have not progressed sufficiently through discovery, and/or development of important factual information and legal information is insufficient to enable the Company to estimate a range of possible loss, if any. An adverse determination in one or more of these pending matters could have an adverse effect on the Company's condensed consolidated financial position, results of operations or cash flows.

The Company is, and may in the future become, subject to various legal proceedings and claims that arise in or outside the ordinary course of business. For example, on November 16, 2017, a purported stockholder of the Company filed a putative class action lawsuit in the Superior Court of Washington in and for King County against the Company, certain of its officers and directors, and the underwriters of its IPO, entitled *Robert Lowinger v. Funko, Inc., et. al*. In January and

March 2018, five additional putative class action lawsuits were filed in Washington state court, four in the Superior Court of Washington in and for King County and one in the Superior Court of Washington in and for Snohomish County. Two of the King County lawsuits, *Surratt v. Funko, Inc. et. al.* (filed on January 16, 2018) and *Baskin v. Funko, Inc. et. al.* (filed on January 30, 2018), were filed against the Company and certain of its officers and directors. The other two King County lawsuits, *The Ronald and Maxine Linde Foundation v. Funko, Inc. et. al.* (filed on January 18, 2018) and *Lovewell v. Funko, Inc. et. al* (filed on March 27, 2018), were filed against the Company, certain of its officers and directors, ACON, Fundamental and certain other defendants. The Snohomish County lawsuit, *Berkelhammer v. Funko, Inc. et. al.* (filed on March 13, 2018), was filed against us, certain of the Company's officers and directors, and ACON. On May 8, 2018, the *Berkelhammer* action was voluntarily dismissed, and on May 15, 2018 a substantially similar action was filed by the same plaintiff in the Superior Court of Washington in and for King County. On April 2, 2018, a putative class action lawsuit *Jacobs v. Funko, Inc. et. al* was filed in the United States District Court for the Western District of Washington against the Company, certain of its officers and directors, and certain other defendants. On May 21, 2018, the *Jacobs* action was voluntarily dismissed, and on June 12, 2018 a substantially similar action was filed by the same plaintiff in the Superior Court of Washington in and for King County.

On July 2, 2018, all of the above-referenced suits were ordered consolidated for all purposes into one action under the title *In re Funko, Inc. Securities Litigation* in the Superior Court of Washington in and for King County. On August 1, 2018, plaintiffs filed a consolidated complaint against the Company, certain of its officers and directors, ACON, Fundamental, and certain other defendants. On October 1, 2018, the Company moved to dismiss that action. Plaintiffs filed their opposition to the Company's motion to dismiss on October 31, 2018, and the Company filed its reply to plaintiffs' opposition on November 30, 2018. Oral arguments on the motions to dismiss were held on May 3, 2019. On August 2, 2019, the Superior Court of Washington in and for King County dismissed the consolidated action, allowing Plaintiffs leave to amend the complaint. The Court found, inter alia, that "Funko's statements regarding its financial disclosures were not materially false or misleading" and that "plaintiffs have not shown that Funko's 'opinion statements' were false or that such statements were not simply corporate optimism or puffery."
Additionally, on June 4, 2018, a putative class action lawsuit *Kanugonda v. Funko, et al.* was filed in the United States District Court for the Western District of Washington against the Company, certain of its officers and directors, and certain other defendants. On January 4, 2019, a lead plaintiff was appointed in that case. On April 30, 2019, the lead plaintiff filed an amended complaint against the previously named defendants.

The complaint in federal court alleges that the Company violated Sections 11, 12, and 15 of the Securities Act of 1933, as amended, by making allegedly materially misleading statements and by omitting material facts necessary to make the statements made therein not misleading. The lawsuit seeks, among other things, compensatory statutory damages and rescissory damages in account of the consideration paid for the Company's Class A common stock by the lead plaintiff and members of the putative class, as well as attorneys' fees and costs. The Company believes it has meritorious defenses to the claims of the plaintiff and members of the class and any liability for the alleged claims is not currently probable or reasonably estimable.

In connection with the Company's underpayment of customs duties at Loungefly described in Note 1, the Company's estimate of the range of probable loss for potential penalties that may be assessed by U.S. Customs is $0.2 million to $1.0 million at June 30, 2019, of which $0.5 million has been recorded as a contingent liability in the caption Accrued expenses and other current liabilities in its unaudited condensed consolidated balance sheet as of June 30, 2019.

9. Segments

The Company identifies its reportable segments according to how the business activities are managed and evaluated and for which discrete financial information is available and regularly reviewed by its Chief Operating Decision Maker (the "CODM") to allocate resources and assess performance. Because its CODM reviews financial performance and allocates resources at a consolidated level on a regular basis, it has one reportable segment. The following table is a summary of the Company's main product categories as a percent of net sales:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
Figures	83.5%	82.5%	82.6%	83.4%
Other	16.5%	17.5%	17.4%	16.6%

The following tables present summarized geographical information (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
Net sales:				
United States	$ 122,673	$ 97,108	$ 231,543	$ 185,958
International	68,526	41,615	126,721	89,976
Total net sales	$ 191,199	$ 138,723	$ 358,264	$ 275,934

	June 30, 2019	December 31, 2018
Long-lived assets:		
United States	$ 60,156	$ 23,781
China and Vietnam	20,480	20,662
United Kingdom	8,440	4,128
Total long-lived assets	$ 89,076	$ 48,571

10. Related Party Transactions

In June 2017, in connection with the acquisition of Loungefly, the Company assumed a lease for the Loungefly headquarters and warehouse operations with 20310 Plummer Street LLC and entered into a global sourcing agreement with Sure Star Development Ltd. Both entities are owned by certain former employees of the Company, who were also the former owners of Loungefly. For the three and six months ended June 30, 2018, the Company recorded $0.1 million and $0.2 million, respectively, in rental expense related to the lease, which was recorded in selling, general and administrative expenses in the Company's unaudited condensed consolidated statements of operations. The entities ceased to be related parties after July 12, 2018.

The Company sells products to Forbidden Planet, a U.K. retailer through its wholly owned subsidiary Funko UK, Ltd. One of the investors in Forbidden Planet is an employee of Funko UK. For the three and six months ended June 30, 2019 and 2018, the Company recorded approximately $0.5 million and $1.2 million, respectively, and $0.7 million and $1.9 million, respectively, in net sales to Forbidden Planet. At June 30, 2019 and December 31, 2018, accounts receivable from Forbidden Planet was $0.4 million and $0.8 million on the unaudited condensed consolidated balance sheets.

In February 2019, in connection with the Forrest-Pruzan Acquisition, the Company assumed two leases of office space with Roll and Move, LLC and Roll and Move II LLC, both of which are owned by certain former owners of Forrest-Pruzan Creative LLC, one of whom remains an employee of the Company. For the three and six months ended June 30, 2019, the Company recorded $0.1 million of rental expense related to the leases, which was recorded in selling, general and administrative expenses in the Company's unaudited condensed consolidated statements of operations. At June 30, 2019, the Company had recorded operating lease right-of-use assets and operating lease liabilities of $1.0 million related to the leases.

11. Income Taxes

Funko, Inc. is taxed as a corporation and pays corporate federal, state and local taxes on income allocated to it from FAH, LLC based upon Funko, Inc.'s economic interest held in FAH, LLC. FAH, LLC is treated as a pass-through partnership for income tax reporting purposes. FAH, LLC's members, including the Company, are liable for federal, state and local income taxes based on their share of FAH, LLC's pass-through taxable income.

The Company recorded $2.2 million and $0.2 million of income tax expense for the three months ended June 30, 2019 and 2018, respectively, and $3.6 million and $0.8 million for the six months ended June 30, 2019 and 2018, respectively. The Company's estimated annual effective tax rate for the six months ended June 30, 2019 was 16.7%. The Company's estimated annual effective tax rate is less than the statutory rate of 21% primarily because the Company is not liable for income taxes on the portion of FAH, LLC's earnings that are attributable to non-controlling interests.

During the three and six months ended June 30, 2019, the Company acquired an aggregate of 1.7 million and 5.0 million common units of FAH, LLC, respectively, in connection with the redemption of common units, which resulted in an increase in the tax basis of the Company's investment in FAH, LLC subject to the provisions of the Tax Receivable Agreement. As a result of these exchanges, during the three and six months ended June 30, 2019 the Company recognized an increase to its net deferred tax assets in the amount of $8.4 million and $22.3 million, respectively, and corresponding Tax Receivable Agreement liabilities of $10.6 million and $29.2 million, respectively, representing 85% of the tax benefits due to the Continuing Equity Owners. During the three and six months ended June 30, 2018, activity related to the redemption of FAH, LLC common units and the Tax Receivable Agreement was nominal.

12. Stockholders' Equity

The following is a reconciliation of changes in stockholders' equity for the three and six months ended June 30, 2019 and 2018:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
	(In thousands)			
Class A common stock				
Beginning balance	$ 3	$ 2	$ 2	$ 2
Shares issued	—	—	1	—
Ending balance	$ 3	$ 2	$ 3	$ 2
Class B common stock				
Beginning and ending balance	$ 2	$ 2	$ 2	$ 2
Additional paid-in capital				
Beginning balance	$ 165,954	$ 130,038	$ 146,154	$ 129,066
Equity-based compensation	3,367	1,171	6,115	2,143
Shares issued for equity-based compensation awards	277	—	1,426	—
Shares issued for purchase consideration	—	—	2,221	—
Redemption of common units of FAH, LLC	9,233	153	27,651	153
Establishment of liabilities under tax receivable agreement and related changes to deferred tax assets	(2,147)	8	(6,883)	8
Ending balance	$ 176,684	$ 131,370	$ 176,684	$ 131,370
Accumulated other comprehensive income (loss)				
Beginning balance	$ 104	$ 1,308	$ (167)	$ 806
Foreign currency translation loss, net of tax	(440)	(1,097)	(169)	(595)
Ending balance	$ (336)	$ 211	$ (336)	$ 211
Retained earnings				
Beginning balance	$ 10,912	$ 1,851	$ 8,717	$ 1,254
Net income attributable to Funko, Inc.	5,132	70	7,327	667
Ending balance	$ 16,044	$ 1,921	$ 16,044	$ 1,921
Non-controlling interests				
Beginning balance	$ 117,407	$ 141,008	$ 138,546	$ 150,162
Distributions to continuing equity owners	(10,069)	(8,027)	(18,121)	(18,884)
Redemption of common units of FAH, LLC	(9,270)	(153)	(27,688)	(153)
Foreign currency translation loss, net of tax	(383)	(1,175)	(2)	(594)
Net income attributable to non-controlling interests	6,283	204	11,233	1,326
Ending balance	$ 103,968	$ 131,857	$ 103,968	$ 131,857
Total stockholders' equity	$ 296,365	$ 265,363	$ 296,365	$ 265,363

The following is a reconciliation of changes in Class A and Class B common shares outstanding for the three and six months ended June 30, 2019 and 2018:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
	(In thousands)			
Class A common shares outstanding				
Beginning balance	28,522	23,338	24,960	23,338
Shares issued for equity-based compensation awards	22	—	131	—
Shares issued for purchase consideration	—	—	127	—
Redemption of common units of FAH, LLC	1,670	27	4,996	27
Ending balance	30,214	23,365	30,214	23,365
Class B common shares outstanding				
Beginning balance	20,281	24,976	23,584	24,976
Redemption of common units of FAH, LLC	(1,541)	(20)	(4,844)	(20)
Ending balance	18,740	24,956	18,740	24,956
Total Class A and Class B common shares outstanding	48,954	48,321	48,954	48,321

13. Non-controlling interests

Funko, Inc. is the sole managing member of FAH, LLC and as a result consolidates the financial results of FAH, LLC and reports a non-controlling interest representing the common units of FAH, LLC held by the Continuing Equity Owners. Changes in Funko, Inc.'s ownership interest in FAH, LLC while Funko, Inc. retains its controlling interest in FAH, LLC will be accounted for as equity transactions. As such, future redemptions or direct exchanges of common units of FAH, LLC by the Continuing Equity Owners will result in a change in ownership and reduce or increase the amount recorded as non-controlling interest and increase or decrease additional paid-in capital when FAH, LLC has positive or negative net assets, respectively.

Net income and comprehensive income are attributed between Funko, Inc. and noncontrolling interest holders based on each party's relative economic ownership interest in FAH, LLC. As of June 30, 2019 and December 31, 2018, Funko, Inc. owned 30.2 million and 25.0 million of FAH, LLC common units, respectively, representing a 60.4% and 50.2% economic ownership interest in FAH, LLC, respectively.

Net income and comprehensive income of FAH, LLC excludes certain activity attributable to Funko, Inc., including $2.8 million and $5.0 million of equity-based compensation expense for share-based compensation awards issued by Funko, Inc. for the three and six months ended June 30, 2019, respectively, $0.4 million and $0.7 million of equity-based compensation expense for share-based compensation awards issued by Funko, Inc. for the three and six months ended June 30, 2018, respectively, $1.6 million and $2.5 million of income tax expense for corporate, federal, state and local taxes attributable to Funko, Inc. for the three and six months ended June 30, 2019, respectively, and $0.3 million and $0.1 million of income tax benefit for corporate, federal, state and local taxes attributable to Funko, Inc. for the three and six months ended June 30, 2018, respectively.

14. Earnings per Share

Basic earnings per share of Class A common stock is computed by dividing net income available to Funko, Inc. by the weighted-average number of shares of Class A common stock outstanding during the period. Diluted earnings per share of Class A common stock is computed by dividing net income available to Funko, Inc. by the weighted-average number of shares of Class A common stock outstanding adjusted to give effect to potentially dilutive securities.

The following table sets forth reconciliations of the numerators and denominators used to compute basic and diluted earnings per share of Class A common stock (in thousands, except shares and per share amounts):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
Numerator:				
Net income	$ 11,415	$ 274	$ 18,560	$ 1,993
Less: net income attributable to non-controlling interests	6,283	204	11,233	1,326
Net income attributable to Funko, Inc. — basic and diluted	$ 5,132	$ 70	$ 7,327	$ 667
Denominator:				
Weighted-average shares of Class A common stock outstanding — basic	29,909,518	23,344,429	28,283,578	23,341,086
Add: Effect of dilutive equity-based compensation awards and common units of FAH, LLC that are convertible into Class A common stock	2,205,901	1,414,619	2,012,075	1,292,798
Weighted-average shares of Class A common stock outstanding — diluted	32,115,419	24,759,048	30,295,653	24,633,884
Earnings per share of Class A common stock — basic	$ 0.17	$ —	$ 0.26	$ 0.03
Earnings per share of Class A common stock — diluted	$ 0.16	$ —	$ 0.24	$ 0.03

For the three and six months ended June 30, 2019 and 2018, an aggregate of 21.2 million and 22.4 million, respectively, and 26.5 million and 26.6 million, respectively, of potentially dilutive securities were excluded from the weighted-average in the computation of diluted earnings per share of Class A common stock because the effect would have been anti-dilutive. For the three and six months ended June 30, 2019, anti-dilutive securities included 20.0 million and 21.6 million, respectively, and 25.5 million for both the three and six months ended June 30, 2018, of common units of FAH, LLC that are convertible into Class A common stock, but were excluded from the computations of diluted earnings per share because the effect would have been anti-dilutive under the if-converted method.

Shares of the Company's Class B common stock do not participate in the earnings or losses of the Company and are therefore not participating securities. As such, separate presentation of basic and diluted earnings per share of Class B common stock under the two-class method has not been presented.

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

You should read the following discussion and analysis of our financial condition and results of operations together with our unaudited condensed consolidated financial statements and related notes included elsewhere in this Quarterly Report on Form 10-Q, as well as our audited consolidated financial statements and related notes as disclosed in our Annual Report on Form 10-K filed with the Securities and Exchange Commission ("SEC") on March 6, 2019. This discussion and analysis contains forward-looking statements based upon current plans, expectations and beliefs involving risks and uncertainties. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of various important factors, including those set forth under "Risk Factors" included in this Quarterly Report on Form 10-Q.

As used in this Quarterly Report on Form 10-Q, unless the context otherwise requires, references to:

- "*we,*" "*us,*" "*our,*" *the* "*Company,*" "*Funko*" and similar references refer: (1) following the consummation of the Transactions, to Funko, Inc., and, unless otherwise stated, all of its direct and indirect subsidiaries, including FAH, LLC and (2) prior to the completion of the Transactions, to FAH, LLC and, unless otherwise stated, all of its subsidiaries.

- "*ACON*" refers to ACON Funko Investors, L.L.C., a Delaware limited liability company, and certain funds affiliated with ACON Funko Investors, L.L.C. (including any such fund or entity formed to hold shares of Class A common stock for the Former Equity Owners).

- "*Continuing Equity Owners*" refers collectively to ACON, Fundamental, the Former Profits Interests Holders, the Warrant Holders and certain current and former executive officers, employees and directors and each of their permitted transferees that own common units in FAH, LLC after the Transactions and who may redeem at each of their options (subject in certain circumstances to time-based vesting requirements) their common units for, at our election, cash or newly-issued shares of Funko, Inc.'s Class A common stock.

- "*FAH, LLC*" refers to Funko Acquisition Holdings, L.L.C.

- "*FAH LLC Agreement*" refers to FAH, LLC's second amended and restated limited liability company agreement, as amended from time to time.

- "*Former Equity Owners*" refers to those Original Equity Owners affiliated with ACON who transferred their indirect ownership interests in common units of FAH, LLC for shares of Funko, Inc.'s Class A common stock (to be held by them either directly or indirectly) in connection with the consummation of the Transactions.

- "*Former Profits Interests Holders*" refers collectively to certain of our directors and certain current executive officers and employees, in each case, who, prior to the consummation of the Transactions, held existing vested and unvested profits interests in FAH, LLC pursuant to FAH, LLC's prior equity incentive plan and received common units of FAH, LLC in exchange for their profits interests (subject to any common units received in exchange for unvested profits interests remaining subject to their existing time-based vesting requirements) in connection with the Transactions.
- "*Former Senior Secured Credit Facilities*" refers to the Company's credit agreement, dated October 30, 2015, which provided for a $175.0 million term loan facility (the "Term Loan A Facility") and a revolving credit facility, including a $3.0 million sub-facility for the issuance of letters of credit (the "Revolving Credit Facility"). Among other amendments to the credit agreement, on January 17, 2017, the Company entered into an amendment which provided for, among other things, an additional $50.0 million term loan facility (the "Term Loan B Facility"), which was repaid in November 2017 in connection with our initial public offering ("IPO"). The Former Senior Secured Credit Facilities were terminated on October 22, 2018.

- "*Fundamental*" refers collectively to Fundamental Capital, LLC and Funko International, LLC.
- *"New Credit Facilities"* refers to the Company's credit agreement, dated October 22, 2018 (the "Credit Agreement"), providing for a term loan facility in the amount of $235.0 million (the "New Term Loan Facility") and a revolving credit facility of $50.0 million (which was increased to $75.0 million on February 11, 2019) (the "New Revolving Credit Facility").

- "*Original Equity Owners*" refers to the owners of ownership interests in FAH, LLC, collectively, prior to the Transactions, which include ACON, Fundamental, the Former Profits Interests Holders and certain current and former executive officers, employees and directors.

- "*Revolving Credit Facility*" refers to our former revolving credit facility, including a $3.0 million subfacility for the issuance of letters of credit.

- "*Transactions*" refers to certain organizational transactions that we effected in connection with our initial public offering ("IPO") in November 2017.
- "*Warrant Holders*" refers to lenders under our Former Senior Secured Credit Facilities (as defined herein) that previously held warrants to purchase ownership interests in FAH, LLC, which were converted into common units of FAH, LLC in connection with the consummation of the Transactions.

Overview

We are a leading pop culture consumer products company. Our business is built on the principle that almost everyone is a fan of something and the evolution of pop culture is leading to increasing opportunities for fan loyalty. We create whimsical, fun and unique products that enable fans to express their affinity for their favorite "something"—whether it is a movie, TV show, video game, musician or sports team. We infuse our distinct designs and aesthetic sensibility into one of the industry's largest portfolios of licensed content over a wide variety of product categories, including figures, plush, accessories, apparel and homewares.

We were founded in 1998 as a consumer products company focused on designing and selling nostalgic bobble head figures. In 2005, we were acquired by a small group of investors led by Brian Mariotti, who took over day-to-day operations and has served as our chief executive officer since that time. Under Brian's leadership, we have significantly broadened and deepened our relationships with content providers. Content providers trust us to create unique extensions of their intellectual property that extend the relevance of their content with consumers through ongoing engagement, helping to maximize the lifetime value of their content. We strive to license every pop culture property that we believe is relevant to consumers.

Domestically, we primarily sell our products to specialty retailers, mass-market retailers, and e-commerce sites. Internationally, we sell our products directly to similar retailers, primarily in Europe, through our subsidiary Funko UK, Ltd. We also sell our products to distributors for sale to small retailers in the United States and in certain countries internationally, typically where we do not have a direct presence. We also sell certain of our products directly to consumers through our e-commerce business and, to a lesser extent, at specialty licensing and comic book shows, conventions and exhibitions in cities throughout the United States, including at Comic-Con events.

On November 6, 2017, we completed our IPO of 10,416,666 shares of Class A common stock at an initial public offering price of $12.00 per share and received approximately $117.3 million in net proceeds after deducting underwriting discounts and commissions. We used the net proceeds to purchase 10,416,666 newly issued common units directly from FAH, LLC at a price per unit equal to the price per share of Class A common stock in the IPO less underwriting discounts and commissions. At June 30, 2019, we held 30.2 million common units, representing an approximately 60.4% interest in FAH, LLC.

Key Performance Indicators

We consider the following metrics to be key performance indicators to evaluate our business, develop financial forecasts, and make strategic decisions.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
	(amounts in thousands)			
Net sales	$ 191,199	$ 138,723	$ 358,264	$ 275,934
Net income	$ 11,415	$ 274	$ 18,560	$ 1,993
EBITDA (1)	$ 27,773	$ 15,700	$ 50,649	$ 33,179
Adjusted EBITDA (1)	$ 31,371	$ 19,473	$ 56,710	$ 36,510

(1) Earnings before interest, taxes, depreciation and amortization ("EBITDA") and Adjusted EBITDA are financial measures not calculated in accordance with U.S. GAAP, or non-GAAP financial measures. For a reconciliation of EBITDA and Adjusted EBITDA to net income (loss), the most closely comparable U.S. GAAP financial measure, see "Non-GAAP Financial Measures" below.

Results of Operations

The discussion in this Results of Operations gives effect to the correction of certain immaterial errors in our Consolidated Financial Statements for the three and six months ended June 30, 2018. Refer to Note 1 — Organization and Operations — Revision of Previously-issued Financial Statements in Part I, Item I of this Form 10-Q for further information.

Three Months Ended June 30, 2019 Compared to Three Months Ended June 30, 2018

The following table sets forth information comparing the components of net income for the three months ended June 30, 2019 and 2018:

	Three Months Ended June 30,		Period over Period Change	
	2019	2018	Dollar	Percentage
	(amounts in thousands, except percentages)			
Net sales	$ 191,199	$ 138,723	$ 52,476	37.8%
Cost of sales (exclusive of depreciation and amortization shown separately below)	119,998	85,884	34,114	39.7%
Selling, general, and administrative expenses	43,647	34,537	9,110	26.4%
Depreciation and amortization	10,425	9,650	775	8.0%
Total operating expenses	174,070	130,071	43,999	33.8%
Income from operations	17,129	8,652	8,477	98.0%
Interest expense, net	3,763	5,584	(1,821)	(32.6%)
Other (income) expense, net	(219)	2,602	(2,821)	(108.4%)
Income before income taxes	13,585	466	13,119	nm
Income tax expense	2,170	192	1,978	nm
Net income	11,415	274	11,141	nm
Less: net income attributable to non-controlling interests	6,283	204	6,079	nm
Net income attributable to Funko, Inc.	$ 5,132	$ 70	$ 5,062	nm

Net Sales

Net sales were $191.2 million for the three months ended June 30, 2019, an increase of 37.8%, compared to $138.7 million for the three months ended June 30, 2018. The increase in net sales was due primarily to an increase in the number of active properties and strong sales demand across all geographic regions and product categories, which generally contributes to higher net sales per active property.

For the three months ended June 30, 2019, the number of active properties increased 16.1% to 592 from 510 for the three months ended June 30, 2018, and the average net sales per active property increased 18.7% for the three months ended June 30, 2019 as compared to the three months ended June 30, 2018. An active property is a licensed property from which we generate sales of products during a given period. While we expect to see growth in the number of active properties and average sales per active property over time, we expect that the number of active properties and the average sales per active property will fluctuate from year to year or quarter to quarter based on what is relevant in pop culture at that time and the types of properties we are producing against.

On a geographical basis, net sales in the United States increased 26.3% to $122.7 million in the three months ended June 30, 2019 as compared to the three months ended June 30, 2018, and net sales internationally increased 64.7% to $68.5 million in the three months ended June 30, 2019 as compared to the three months ended June 30, 2018, driven by strong growth across all regions. On a product category basis, net sales of figures increased 39.4% to $159.7 million in the three months ended June 30, 2019 as compared to the three months ended June 30, 2018, and net sales of other products increased 30.2% to $31.5 million in the three months ended June 30, 2019 as compared to the three months ended June 30, 2018, driven primarily by continued growth of our Loungefly and other softline products.

Cost of Sales and Gross Margin (exclusive of depreciation and amortization)

Cost of sales (exclusive of depreciation and amortization) was $120.0 million for the three months ended June 30, 2019, an increase of 39.7%, compared to $85.9 million for the three months ended June 30, 2018. Cost of sales (exclusive of depreciation and amortization) increased primarily as a result of the continued growth in sales, as discussed above.
Gross margin (exclusive of depreciation and amortization), calculated as net sales less cost of sales as a percentage of net sales, was 37.2% for the three months ended June 30, 2019, compared to 38.1% for the three months ended June 30, 2018. The decrease in gross margin (exclusive of depreciation and amortization) for the three months ended June 30,

2019 compared to the three months ended June 30, 2018 was driven primarily by higher reserves on inventory, partially offset by improved product cost margins and lower license and royalty costs as a percentage of net sales.

Selling, General, and Administrative Expenses

Selling, general, and administrative expenses were $43.6 million for the three months ended June 30, 2019, an increase of 26.4%, compared to $34.5 million for the three months ended June 30, 2018. The increase was driven primarily by growth in the business, including a $4.9 million increase in personnel expenses and commissions, a $2.2 million increase in equity-based compensation expense, a $1.1 million increase in professional and consulting costs, and a $1.0 million increase in rent and related facilities costs. Selling, general and administrative expenses were 22.8% and 24.9% of net sales for the three months ended June 30, 2019 and 2018, respectively.

Depreciation and Amortization

Depreciation and amortization expense was $10.4 million for the three months ended June 30, 2019, an increase of 8.0%, compared to $9.7 million for the three months ended June 30, 2018, primarily related an increase in depreciation on tooling and molds as we continue to expand our product offerings.

Interest Expense, Net

Interest expense, net was $3.8 million for the three months ended June 30, 2019, a decrease of 32.6%, compared to $5.6 million for the three months ended June 30, 2018. The decrease in interest expense, net was due to lower interest rates on debt outstanding during the three months ended June 30, 2019 under the New Credit Facilities as compared to the interest rates on debt outstanding during the three months ended June 30, 2018 under the Former Senior Secured Credit Facilities.

Other (income) expense, net

Other (income) expense, net was $0.2 million of income for the three months ended June 30, 2019 and $2.6 million of expense for the three months ended June 30, 2018. Other (income) expense, net for the three months ended June 30, 2019 and 2018 was primarily related to foreign currency gains and losses relating to transactions denominated in currencies other than the US dollar.

Net income

Net income was $11.4 million for the three months ended June 30, 2019, compared to $0.3 million for the three months ended June 30, 2018. The increase in net income was primarily the result of the increase in net sales, the decrease in interest expense, net and the increase in other (income), net for the three months ended June 30, 2019 as compared to the three months ended June 30, 2018, as discussed above.

Six Months Ended June 30, 2019 Compared to Six Months Ended June 30, 2018

The following table sets forth information comparing the components of net income for the six months ended June 30, 2019 and 2018:

	Six Months Ended June 30,		Period over Period Change	
	2019	2018	Dollar	Percentage
	(amounts in thousands, except percentages)			
Net sales	$ 358,264	$ 275,934	$ 82,330	29.8%
Cost of sales (exclusive of depreciation and amortization shown separately below)	223,654	172,528	51,126	29.6%
Selling, general, and administrative expenses	84,115	69,039	15,076	21.8%
Acquisition transaction costs	-	28	(28)	(100.0%)
Depreciation and amortization	20,655	18,951	1,704	9.0%
Total operating expenses	328,424	260,546	67,878	26.1%
Income from operations	29,840	15,388	14,452	93.9%
Interest expense, net	7,835	11,480	(3,645)	(31.8%)
Other (income) expense, net	(154)	1,160	(1,314)	(113.3%)
Income before income taxes	22,159	2,748	19,411	706.4%
Income tax expense	3,599	755	2,844	376.7%
Net income	18,560	1,993	16,567	831.3%
Less: net income attributable to non-controlling interests	11,233	1,326	9,907	747.1%
Net income attributable to Funko, Inc.	$ 7,327	$ 667	$ 6,660	998.5%

Net Sales

Net sales were $358.3 million for the six months ended June 30, 2019, an increase of 29.8%, compared to $275.9 million for the six months ended June 30, 2018. The increase in net sales was due primarily to an increase in the number of active properties and strong sales demand across all geographic regions and product categories.

For the six months ended June 30, 2019, the number of active properties increased 23.5% to 663 from 537 for the six months ended June 30, 2018, and the average net sales per active property increased 5.2% for the six months ended June 30, 2019 as compared to the six months ended June 30, 2018. An active property is a licensed property from which we generate sales of products during a given period. While we expect to see growth in the number of active properties over time, we expect that the number of active properties and the average sales per active property will fluctuate from year to year or quarter to quarter based on what is relevant in pop culture at that time and the types of properties we are producing against.

On a geographical basis, net sales in the United States increased 24.5% to $231.5 million in the six months ended June 30, 2019 as compared to the six months ended June 30, 2018, and net sales internationally increased 40.8% to $126.7 million in the six months ended June 30, 2019 as compared to the six months ended June 30, 2018, driven by strong growth across all regions. On a product category basis, net sales of figures increased 28.6% to $295.8 million in the six months ended June 30, 2019 as compared to the six months ended June 30, 2018, and net sales of other products increased 36.1% to $62.4 million in the six months ended June 30, 2019 as compared to the six months ended June 30, 2018, driven primarily by continued growth of our Loungefly and other softline products.

Cost of Sales and Gross Margin (exclusive of depreciation and amortization)

Cost of sales (exclusive of depreciation and amortization) was $223.7 million for the six months ended June 30, 2019, an increase of 29.6%, compared to $172.5 million for the six months ended June 30, 2018. Cost of sales (exclusive of depreciation and amortization) increased primarily as a result of the continued growth in sales, as discussed above.
Gross margin (exclusive of depreciation and amortization), calculated as net sales less cost of sales as a percentage of net sales, was 37.6% for both the six months ended June 30, 2019 and 2018. Although stable overall, gross margin (exclusive of depreciation and amortization) for the six months ended June 30, 2019 reflected higher reserves on inventory, partially offset by improved product cost margins.Gross margin (exclusive of depreciation and amortization) for

the six months ended June 30, 2018 included approximately $1.8 million of costs related to Toys R Us shipments for which no revenue was recognized, a charge that did not recur in the six months ended June 30, 2019.

Selling, General, and Administrative Expenses

Selling, general, and administrative expenses were $84.1 million for the six months ended June 30, 2019, an increase of 21.8%, compared to $69.0 million for the six months ended June 30, 2018. The increase was driven primarily by growth in the business, including a $7.7 million increase in personnel expenses and commissions, a $4.0 million increase in equity-based compensation expense, a $2.4 million increase in rent and related facilities costs and a $1.2 million increase in other administrative costs. Selling, general and administrative expenses were 23.5% and 25.0% of net sales for the six months ended June 30, 2019 and 2018, respectively.

Depreciation and Amortization

Depreciation and amortization expense was $20.7 million for the six months ended June 30, 2019, an increase of 9.0%, compared to $19.0 million for the six months ended June 30, 2018, primarily related to an increase in depreciation on tooling and molds as we continue to expand our product offerings.

Interest Expense, Net

Interest expense, net was $7.8 million for the six months ended June 30, 2019, a decrease of 31.8%, compared to $11.5 million for the six months ended June 30, 2018. The decrease in interest expense, net was due to lower interest rates on debt outstanding during the six months ended June 30, 2019 under the New Credit Facilities as compared to the interest rates on debt outstanding during the six months ended June 30, 2018 under the Former Senior Secured Credit Facilities.

Other (income) expense, net

Other (income) expense, net was $0.2 million of income for the six months ended June 30, 2019 and $1.2 million of expense for the six months ended June 30, 2018. Other (income) expense, net for both the six months ended June 30, 2019 and 2018 was primarily related to foreign currency gains and losses relating to transactions denominated in currencies other than the US dollar.

Net income

Net income was $18.6 million for the six months ended June 30, 2019, compared to $2.0 million for the six months ended June 30, 2018. The increase in net income was primarily the result of the increase in net sales and the decrease in interest expense, net for the six months ended June 30, 2019 as compared to the six months ended June 30, 2018, as discussed above.

Non-GAAP Financial Measures

EBITDA, Adjusted EBITDA, Adjusted Net Income and Adjusted Earnings per Diluted Share (collectively the “Non-GAAP Financial Measures”) are supplemental measures of our performance that are not required by, or presented in accordance with, U.S. GAAP. The Non-GAAP Financial Measures are not measurements of our financial performance under U.S. GAAP and should not be considered as an alternative to net income (loss), earnings per share or any other performance measure derived in accordance with U.S. GAAP. We define EBITDA as net income (loss) before interest expense, net, income tax expense (benefit), depreciation and amortization. We define Adjusted EBITDA as EBITDA further adjusted for non-cash charges related to equity-based compensation programs, acquisition transaction costs and other expenses, foreign currency transaction gains and losses and other unusual or one-time items. We define Adjusted Net Income as net income attributable to Funko, Inc. adjusted for the reallocation of income attributable to non-controlling interests from the assumed exchange of all outstanding common units and options in FAH, LLC for newly issued-shares of Class A common stock of Funko, Inc. and further adjusted for the impact of certain non-cash charges and other items that we do not consider in our evaluation of ongoing operating performance. These items include, among other things, reallocation of net income attributable to non-controlling interests, non-cash charges related to equity-based compensation programs, acquisition transaction costs and other expenses, foreign currency transaction gains and losses and other unusual or one-time items, and the income tax expense (benefit) effect of these adjustments. We define Adjusted Earnings per Diluted Share as Adjusted Net Income divided by the weighted-average shares of Class A common stock outstanding, assuming (1) the full exchange of all outstanding common units and options in FAH, LLC for newly issued-shares of Class A common stock of Funko, Inc. and (2) the dilutive effect of stock options and unvested common units, if any. We caution investors that amounts presented in accordance with our definitions of the Non-GAAP Financial Measures may not be comparable to similar measures disclosed by our competitors, because not all companies and analysts calculate the Non-GAAP Financial Measures in the same manner. We present the Non-GAAP Financial Measures because we consider them to be important supplemental measures of our performance and believe they are frequently used by securities analysts, investors, and other interested parties in the evaluation of companies in our industry. Management believes that investors' understanding of our performance is enhanced by including these Non-GAAP Financial Measures as a reasonable basis for comparing our ongoing results of operations.

Management uses the Non-GAAP Financial Measures:

- as a measurement of operating performance because they assist us in comparing the operating performance of our business on a consistent basis, as they remove the impact of items not directly resulting from our core operations;
- for planning purposes, including the preparation of our internal annual operating budget and financial projections;
- as a consideration to assess incentive compensation for our employees;
- to evaluate the performance and effectiveness of our operational strategies; and
- to evaluate our capacity to expand our business.

By providing these Non-GAAP Financial Measures, together with reconciliations, we believe we are enhancing investors' understanding of our business and our results of operations, as well as assisting investors in evaluating how well we are executing our strategic initiatives. In addition, our New Secured Credit Facilities use Adjusted EBITDA to measure our compliance with covenants such as a senior leverage ratio. The Non-GAAP Financial Measures have limitations as analytical tools, and should not be considered in isolation, or as an alternative to, or a substitute for net income (loss) or other financial statement data presented in our unaudited condensed consolidated financial statements included elsewhere in this Quarterly Report on Form 10-Q as indicators of financial performance. Some of the limitations are:

- such measures do not reflect our cash expenditures, or future requirements for capital expenditures or contractual commitments;
- such measures do not reflect changes in, or cash requirements for, our working capital needs;
- such measures do not reflect the interest expense, or the cash requirements necessary to service interest or principal payments on our debt;
- although depreciation and amortization are non-cash charges, the assets being depreciated and amortized will often have to be replaced in the future and such measures do not reflect any cash requirements for such replacements; and
- other companies in our industry may calculate such measures differently than we do, limiting their usefulness as comparative measures.

Due to these limitations, Non-GAAP Financial Measures should not be considered as measures of discretionary cash available to us to invest in the growth of our business. We compensate for these limitations by relying primarily on our U.S. GAAP results and using these non-GAAP measures only supplementally. As noted in the table below, the Non-GAAP Financial Measures include adjustments for non-cash charges related to equity-based compensation programs, acquisition transaction costs and other expenses, foreign currency transaction gains and losses and other unusual or one-time items. It is reasonable to expect that these items will occur in future periods. However, we believe these adjustments are appropriate because the amounts recognized can vary significantly from period to period, do not directly relate to the ongoing operations of our business and complicate comparisons of our internal operating results and operating results of other companies over time. Each of the normal recurring adjustments and other adjustments described herein and in the reconciliation table below help management with a measure of our core operating performance over time by removing items that are not related to day-to-day operations.

The following tables reconcile the Non-GAAP Financial Measures to the most directly comparable U.S. GAAP financial performance measure, which is net income, for the periods presented:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
	(In thousands, except per share data)			
Net income attributable to Funko, Inc.	$ 5,132	$ 70	$ 7,327	$ 667
Reallocation of net income attributable to non-controlling interests from the assumed exchange of common units of FAH, LLC for Class A common stock (1)	6,283	204	11,233	1,326
Equity-based compensation (2)	3,367	1,171	6,115	2,143
Acquisition transaction costs and other expenses (3)	450	—	100	28
Foreign currency transaction (gain) loss (4)	(219)	2,602	(154)	1,160
Income tax expense (5)	(2,126)	(868)	(3,456)	(765)
Adjusted net income	$ 12,887	$ 3,179	$ 21,165	$ 4,559
Weighted-average shares of Class A common stock outstanding-basic	29,910	23,344	28,284	23,341
Equity-based compensation awards and common units of FAH, LLC that are convertible into Class A common stock	22,248	27,392	23,612	27,384
Adjusted weighted-average shares of Class A stock outstanding - diluted	52,158	50,736	51,896	50,725
Adjusted earnings per diluted share	$ 0.25	$ 0.06	$ 0.41	$ 0.09

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
	(amounts in thousands)			
Net income	$ 11,415	$ 274	$ 18,560	$ 1,993
Interest expense, net	3,763	5,584	7,835	11,480
Income tax expense	2,170	192	3,599	755
Depreciation and amortization	10,425	9,650	20,655	18,951
EBITDA	$ 27,773	$ 15,700	$ 50,649	$ 33,179
Adjustments:				
Equity-based compensation (2)	3,367	1,171	6,115	2,143
Acquisition transaction costs and other expenses (3)	450	—	100	28
Foreign currency transaction (gain) loss (4)	(219)	2,602	(154)	1,160
Adjusted EBITDA	$ 31,371	$ 19,473	$ 56,710	$ 36,510

(1) Represents the reallocation of net income attributable to non-controlling interests from the assumed exchange of common units of FAH, LLC for Class A common stock in periods in which income was attributable to non-controlling interests.

(2) Represents non-cash charges related to equity-based compensation programs, which vary from period to period depending on the timing of awards.

(3) Represents legal, accounting, and other related costs incurred in connection with acquisitions and other transactions. For the three and six months ended June 30, 2019, includes the accrual of a contingent liability of $0.5 million related to potential penalties that may be assessed by U.S. Customs in connection with the underpayment of customs duties at Loungefly. For the six months ended June 30, 2019, this accrual was partially offset by a $0.4 million reversal of a pre-acquisition contingent loss related to our Loungefly acquisition.

(4) Represents both unrealized and realized foreign currency (gains) losses on transactions other than in U.S. dollars.

(5) Represents the income tax expense effect of the above adjustments. This adjustment uses an effective tax rate of 25% for both the three and six months ended June 30, 2019 and 2018.

Liquidity and Financial Condition

Introduction

Our primary requirements for liquidity and capital are working capital, inventory management, capital expenditures, debt service and general corporate needs.

On March 7, 2018, we entered into an amendment to our former credit agreement which provided for, among other things, (i) a $13.0 million prepayment of the amounts owing under the Term Loan A Facility on the effective date of the amendment, with no changes in the amount of future amortization payments, (ii) a reduction in the interest rate margins (a) for the Term Loan A Facility, from 6.25% to 5.50% for base rate loans and 7.25% to 6.50% for London Inter-bank Offered Rate ("LIBOR") rate loans and (b) for the Revolving Credit Facility, from 2.50% to 1.75% for LIBOR rate loans, (iii) a 1% prepayment premium on prepayments under both the Term Loan A Facility and the Revolving Credit Facility for 180 days after the effective date of the amendment, and (iv) a $20.0 million increase to the borrowing base under the Revolving Credit Facility, so long as no loan party formed under the laws of England and Wales or Funko UK, Ltd. incurs secured indebtedness for borrowed money.

On October 22, 2018 (the "Closing Date"), Funko Acquisition Holdings, L.L.C., Funko Holdings LLC, Funko, LLC and Loungefly, LLC (each, a "Borrower" and collectively, the "Borrowers"), entered into a new Credit Agreement by and among each Borrower, certain financial institutions party thereto and PNC Bank, National Association, as administrative agent and collateral agent, providing for the New Term Loan Facility in the amount of $235.0 million and the New Revolving Credit Facility of $50.0 million. Proceeds from the New Credit Facilities were primarily used to repay the Former Senior Secured Credit Facilities.

The New Credit Facilities are secured by substantially all assets of the Borrowers and any of their existing or future material domestic subsidiaries, subject to customary exceptions. We are a holding company with no material assets and we do not conduct any business operations of our own. We have no independent means of generating revenue or cash flow, and our ability to pay dividends in the future, if any, is dependent upon the financial results and cash flows of FAH, LLC and its subsidiaries and distributions we receive from FAH, LLC. Under the terms of the New Credit Facilities, our operating subsidiaries are currently limited in their ability to pay cash dividends to the Company, subject to certain customary exceptions, including:

- the ability to pay, so long as there is no current or ongoing event of default, amounts required to be paid under the Tax Receivable Agreement, certain expenses associated with being a public company and reimbursement of expenses required by the LLC Agreement or the Registration Rights Agreement; and

- the ability to make other distributions of up to $10 million during any period of four fiscal quarters in order to pay dividends to the common unit holders of FAH, LLC (including the Company) as long as the funds received by the Company are used to pay dividends to the Company's stockholders, the Leverage Ratio (as defined in the New Credit Facilities) is not in excess of 2.00:1.00 and there is remaining Availability (as defined in the New Credit Facilities) under the New Credit Facilities of at least $25 million.

On February 11, 2019, the Company amended its New Credit Facilities to increase the New Revolving Credit Facility to $75.0 million, reflecting the incremental capacity of $25.0 million contemplated under the New Credit Facilities prior to such amendment.

On February 11, 2019, we acquired Forrest-Pruzan Creative LLC, a board game development studio in Seattle, WA. See Note 3, Acquisitions for further information.

On April 20, 2019, we filed a preliminary shelf registration statement on Form S-3 (as amended on May 13, 2019, the "Form S-3") with the SEC. If declared effective by the SEC, it will allow us to offer and sell from time-to-time up to $100.0 million of Class A common stock, preferred stock, debt securities, warrants, purchase contracts or units comprised of any combination of these securities for our own account and allows certain selling stockholders to offer and sell 31,884,185 shares of Class A common stock in one or more offerings. The shelf registration statement is intended to provide us flexibility to conduct registered sales of our securities, subject to market conditions and our future capital needs. The terms of any offering under the shelf registration statement will be established at the time of such offering and will be described in a prospectus supplement filed with the SEC prior to the completion of any such offering.

Liquidity and Capital Resources

The following table shows summary cash flow information for the six months ended June 30, 2019 and 2018 (in thousands):

	Six Months Ended June 30,	
	2019	2018
Net cash provided by operating activities	$ 47,954	$ 22,141
Net cash used in investing activities	(18,099)	(14,752)
Net cash used in financing activities	(23,721)	(5,063)
Effect of exchange rates on cash and cash equivalents	(135)	838
Net increase in cash and cash equivalents	$ 5,999	$ 3,164

Operating Activities. Net cash provided by operating activities was $48.0 million for the six months ended June 30, 2019, compared to $22.1 million for the six months ended June 30, 2018. Changes in net cash provided by (used in) operating activities result primarily from cash received from net sales and cash payments for product costs and royalty expenses paid to our licensors. Other drivers of the changes in net cash provided by operating activities include shipping and freight costs, selling, general and administrative expenses (including personnel expenses and commissions and rent and facilities costs) and interest payments made for our short-term borrowings and long-term debt. Our accounts receivable typically are short term and settle in approximately 30 to 90 days.

The increase for the six months ended June 30, 2019 compared to the six months ended June 30, 2018 was primarily due to an increase in net income, excluding non-cash adjustments, of $22.8 million, driven primarily by an increase in net sales and a decrease in interest expense, net (excluding the effect of a $0.3 million decrease in non-cash adjustments related to accretion of discount on long-term debt and amortization of debt issuance costs), primarily offset by an increase in cost of sales (exclusive of depreciation and amortization) and selling, general and administrative expenses. The increase in net cash provided by operating activities also reflected an increase due to changes in working capital. Changes in working capital increased net cash provided by operating activities by $3.0 million and were primarily due to an increase in accounts payable of $29.6 million, partially offset by increases in prepaid expenses and other assets, inventory and accounts receivable, net of $3.4 million, $3.2 million, and $3.3 million, respectively, and decreases to accrued expenses and other liabilities, income taxes payable and accrued royalties of $10.5 million, $3.2 million and $3.0 million, respectively.

Investing Activities. Our net cash used in investing activities primarily consists of acquisitions, net of cash, and purchase of property and equipment. For the six months ended June 30, 2019, net cash used in investing activities was $18.1 million and was primarily comprised of $11.7 million for purchases of property and equipment primarily relating to tooling and molds and initial cash consideration, net of cash acquired of $6.4 million for the Forrest-Pruzan Acquisition.

For the six months ended June 30, 2018, net cash used in investing activities was $14.8 million and was primarily comprised of purchases of property and equipment primarily relating to tooling and molds.

Financing Activities. Our financing activities primarily consist of proceeds from the issuance of long-term debt, net of debt issuance costs, the repayment of long-term debt, payments and borrowings under our line of credit facility, contributions from, and distributions to, the Continuing Equity Owners and proceeds from the exercise of equity-based options. We do not anticipate any future financing activity related to contributions from the Continuing Equity Owners.

For the six months ended June 30, 2019, net cash used in financing activities was $23.7 million, primarily related to distributions to the Continuing Equity Owners of $18.1 million, payments on the New Term Loan Facility of $5.9 million, and net payments on the New Revolving Credit Facility of $0.8 million, partially offset by proceeds from the exercise of equity based options of $1.4 million.

For the six months ended June 30, 2018, net cash used in financing activities was $5.1 million, primarily related to payments on the Term Loan A Facility of $17.7 million and $18.9 million in distributions to FAH, LLC members, partially offset by net borrowings on the Revolving Credit Facility of $31.5 million.

Financial Condition

Notwithstanding our obligations under the Tax Receivable Agreement between Funko, Inc., FAH, LLC and each of the Continuing Equity Owners (the “Tax Receivable Agreement”), we believe that our sources of liquidity and capital will be sufficient to finance our continued operations, growth strategy, our planned capital expenditures and the additional expenses we expect to incur as a public company for at least the next 12 months. However, we cannot assure you that our cash provided by operating activities, cash and cash equivalents or cash available under our New Revolving Credit Facility will be sufficient to meet our future needs. If we are unable to generate sufficient cash flows from operations in the future, and if availability under our New Revolving Credit Facility is not sufficient, we may have to obtain additional financing. If we obtain additional capital by issuing equity, the interests of our existing stockholders will be diluted. If we incur additional indebtedness, that indebtedness may contain significant financial and other covenants that may significantly restrict our operations. We cannot assure you that we could obtain refinancing or additional financing on favorable terms or at all.

As noted above, on October 22, 2018, we entered into the New Credit Facilities and repaid in full our Former Senior Secured Credit Facilities. The New Credit Facilities are secured by substantially all assets of the Borrowers and any of their existing or future material domestic subsidiaries, subject to customary exceptions.

The Borrowers and any of their existing or future material domestic subsidiaries guarantee repayment of the New Credit Facilities. The New Term Loan Facility matures on October 22, 2023 (the "Maturity Date"). The New Term Loan Facility amortizes in quarterly installments in aggregate amounts equal to 5.00% of the original principal amount of the New Term Loan Facility in the first and second years of the New Term Loan Facility, 10.00% of the original principal amount of the New Term Loan Facility in the third and fourth years of the New Term Loan Facility and 12.50% of the original principal amount of the New Term Loan Facility in the fifth year of the New Term Loan Facility, with any outstanding balance due and payable on the Maturity Date. The New Revolving Credit Facility terminates on the Maturity Date and loans thereunder may be borrowed, repaid, and reborrowed up to such date.

Loans under the New Credit Facilities will, at the Borrowers' option, bear interest at either the Euro-Rate (as defined in the Credit Agreement) plus 3.25% or the Base Rate (as defined in the Credit Agreement) plus 2.25%, with two 0.25% step-downs based on the achievement of certain leverage ratios following the Closing Date. The Euro-Rate is subject to a 0.00% floor. For loans based on the Euro-Rate, interest payments are due at the end of each applicable interest period. For loans based on the Base Rate, interest payments are due quarterly.

The Credit Agreement governing the New Credit Facilities contains a number of covenants that, among other things and subject to certain exceptions, restrict our ability to:

- incur additional indebtedness;
- incur certain liens;
- consolidate, merge or sell or otherwise dispose of our assets;
- alter the business conducted by us and our subsidiaries;
- make investments, loans, advances, guarantees and acquisitions;
- pay dividends or make other distributions on equity interests, or redeem, repurchase or retire equity interests;
- enter into transactions with affiliates;
- enter into agreements restricting our subsidiaries' ability to pay dividends;
- issue or sell equity interests or securities convertible into or exchangeable for equity interests;
- redeem, repurchase or refinance other indebtedness; and
- amend or modify our governing documents.

In addition, the Credit Agreement requires FAH, LLC and its subsidiaries to comply on a quarterly basis with a maximum senior leverage ratio and a minimum fixed charge coverage ratio (in each case, measured on a trailing four-quarter basis). The maximum senior leverage ratio is currently 3.00:1.00. As of June 30, 2019 and December 31, 2018, we were in compliance with all covenants in our New Credit Facilities.

The Credit Agreement also contains certain customary representations and warranties and affirmative covenants, and certain reporting obligations. In addition, the lenders under the New Credit Facilities will be permitted to accelerate all outstanding borrowings and other obligations, terminate outstanding commitments and exercise other specified remedies upon the occurrence of certain events of default (subject to certain grace periods and exceptions), which include, among other things, payment defaults, breaches of representations and warranties, covenant defaults, certain cross-defaults and cross-accelerations to other indebtedness, certain events of bankruptcy and insolvency, certain judgments and changes of control. The Credit Agreement defines "change of control" to include, among other things, any person or group other than ACON and its affiliates becoming the beneficial owner of more than 35% of the voting power of the equity interests of Funko, Inc.

As of June 30, 2019, we had $19.5 million of cash and cash equivalents and $114.4 million of working capital, compared with $13.5 million of cash and cash equivalents and $117.4 million of working capital as of December 31, 2018. Working capital is impacted by the seasonal trends of our business and the timing of new product releases, as well as our current portion of long-term debt and draw downs on our line of credit.

Future Sources and Uses of Liquidity

Sources

As noted above, historically, our primary sources of cash flows have been cash flows from operating activities and borrowings under our Former Senior Secured Credit Facilities and New Credit Facilities.

On October 22, 2018, the Company entered into the New Credit Facilities. Upon closing, proceeds from the New Credit Facilities were primarily used to repay all of the outstanding aggregate principal balance and accrued interest of $209.6 million on the previous Term Loan A Facility and $65.3 million on the previous Revolving Credit Facility. Upon repayment, both the previous Term Loan A Facility and the previous Revolving Credit Facility were terminated. On February 11, 2019, the Company amended the New Credit Facilities to increase the New Revolving Credit Facility to $75.0 million, of which $19.3 million was outstanding as of June 30, 2019. For a discussion of our New Credit Facilities, see Note 5, Debt of our unaudited condensed consolidated financial statements. For a discussion of our Former Senior Secured Credit Facilities, see Note 10, Debt in the Company's Annual Report on Form 10-K for the year ended December 31, 2018.

As described above, on April 20, 2019, we filed a preliminary shelf registration statement on Form S-3 with the SEC. If declared effective by the SEC, it will allow us to offer and sell from time-to-time up to $100.0 million of Class A common stock, preferred stock, debt securities, warrants, purchase contracts or units comprised of any combination of these securities for our own account. The terms of any offering under the shelf registration statement will be established at the time of such offering and will be described in a prospectus supplement filed with the SEC prior to the completion of any such offering.

Uses

Additional future liquidity needs may include public company costs, tax distributions, the redemption right held by the Continuing Equity Owners that they may exercise from time to time (should we elect to exchange their common units for a cash payment), payments under the Tax Receivable Agreement and general cash requirements for operations and capital expenditures. The Continuing Equity Owners may exercise their redemption right for as long as their common units remain outstanding. Although the actual timing and amount of any payments that may be made under the Tax Receivable Agreement will vary, we expect that the payments we will be required to make to the Continuing Equity Owners will be significant. Any payments made by us to the Continuing Equity Owners under the Tax Receivable Agreement will generally reduce the amount of overall cash flow that might have otherwise have been available to us or to FAH, LLC and, to the extent that we are unable to make payments under the Tax Receivable Agreement for any reason, the unpaid amounts generally will be deferred and will accrue interest until paid by us; provided however, that nonpayment for a specified period may constitute a material breach under the Tax Receivable Agreement and therefore may accelerate payments due under the Tax Receivable Agreement.

Seasonality

While our customers in the retail industry typically operate in highly seasonal businesses, we have historically experienced only moderate seasonality in our business. Historically, over 50% of our net sales are made in the third and fourth quarters, primarily in the period from August through November, as our customers build up their inventories in anticipation of the holiday season. Historically, the first quarter of the year has represented the lowest volume of shipment and sales in our business and in the retail and toy industries generally and it is also the least profitable quarter due to the various fixed costs of the business. However, the rapid growth we have experienced in recent years may have masked the full effects of seasonal factors on our business to date, and as such, seasonality may have a greater effect on our results of operations in future periods.

Contractual Obligations

Other than the changes in lease obligations disclosed in Note 2, Leases, there were no material changes in our commitments during the six months ended June 30, 2019 under contractual obligations as disclosed in our Annual Report on Form 10-K for the year ended December 31, 2018 outside the course of normal business.

Off-Balance Sheet Arrangements

As of June 30, 2019, we did not have any off-balance sheet arrangements.

Critical Accounting Policies and Estimates

Discussion and analysis of our financial condition and results of operations are based on our unaudited condensed consolidated financial statements which have been prepared in accordance with U.S. GAAP. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets and liabilities and related disclosures of contingent assets and liabilities, revenue and expenses at the date of the unaudited condensed consolidated financial statements. We base our estimates on historical experience and on various other assumptions in accordance with U.S. GAAP that we believe to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions.

Critical accounting policies and estimates are those that we consider the most important to the portrayal of our financial condition and operating results and require management’s most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain. Our critical accounting policies and estimates include those related to revenue recognition and sales allowances, royalties, inventory, goodwill and intangible assets, equity-based compensation and income taxes. Changes to these policies and estimates could have a material adverse effect on our results of operations and financial condition.

There have been no significant changes to our critical accounting policies to our disclosure reported in “Critical Accounting Policies and Estimates” in our Annual Report on Form 10-K for the year ended December 31, 2018 except as disclosed in Note 2, Significant Accounting Policies.

Item 3. Quantitative and Qualitative Disclosures about Market Risk.

We are primarily exposed to market risk from changes in interest rates and foreign currency. These market risks arise in the normal course of business, as we do not engage in speculative trading activities. There have been no material changes in our market risk from the disclosure included under “Quantitative and Qualitative Disclosures of Market Risk” in the Annual Report on Form 10-K for the year ended December 31, 2018.

Item 4. Controls and Procedures.

Limitations on Effectiveness of Disclosure Controls and Procedures.

In designing and evaluating our disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. In addition, the design of disclosure controls and procedures must reflect that there are resource constraints and that management is required to apply judgment in evaluating the benefits of possible controls and procedures relative to their costs.

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our chief executive officer and chief financial officer, has concluded, based on its evaluation as of June 30, 2019, that our “disclosure controls and procedures” (as such term is defined in Rules 13a–15(e) and 15d–15(e) under the Securities and Exchange Act of 1934, as amended (the Exchange Act”)), were not effective at the reasonable assurance level due to the material weakness in the Company’s internal control over financial reporting described below.

Based on the effects of the underpayment of certain duties and fees owed to U.S. Customs and Border Protection ("U.S. Customs") as described in Note 1 to our unaudited condensed consolidated financial statements included in this Quarterly Report on Form 10-Q, management has concluded that a material weakness in the Company's internal control over financial reporting existed as of June 30, 2019 related to the Company's absence of controls to ensure the completeness and accuracy of the information used in the calculation of duties payable to U.S. Customs at our Loungefly subsidiary.

This control deficiency did not result in a material misstatement of our prior period consolidated annual or interim financial statements. However, the control deficiency could have resulted in material misstatements to the annual or interim consolidated financial statements that would not have been prevented or detected. Accordingly, management has concluded that this control deficiency constitutes a material weakness.

We intend to implement a plan to remediate the material weakness, which we expect will include identifying key stakeholders across the relevant departments, providing training and education from outside experts, formalizing a customs policy and procedures manual which will include, among other things, a process for reviewing customs entry forms, and implementing a semi-annual review of compliance with our customs policy and procedures and, if necessary, allocation of additional resources, including personnel, to our compliance functions.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting during the quarter ended June 30, 2019 identified in management's evaluation pursuant to Rules 13a-15(d) or 15d-15(d) of the Exchange Act that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II – OTHER INFORMATION

Item 1. Legal Proceedings.

We are, and may in the future become, subject to various legal proceedings and claims that arise in or outside the ordinary course of business. For example, on November 16, 2017, a purported stockholder of the Company filed a putative class action lawsuit in the Superior Court of Washington in and for King County against us, certain of our officers and directors, and the underwriters of our IPO, entitled Robert Lowinger v. Funko, Inc., et. al. In January and March 2018, five additional putative class action lawsuits were filed in Washington state court, four in the Superior Court of Washington in and for King County and one in the Superior Court of Washington in and for Snohomish County. Two of the King County lawsuits, *Surratt v. Funko, Inc. et. al.* (filed on January 16, 2018) and *Baskin v. Funko, Inc. et. al.* (filed on January 30, 2018), were filed against us and certain of our officers and directors. The other two King County lawsuits, *The Ronald and Maxine Linde Foundation v. Funko, Inc. et. al.* (filed on January 18, 2018) and *Lovewell v. Funko, Inc. et. al* (filed on March 27, 2018), were filed against us, certain of our officers and directors, ACON, Fundamental and certain other defendants. The Snohomish County lawsuit, *Berkelhammer v. Funko, Inc. et. al.* (filed on March 13, 2018), was filed against us, certain of our officers and directors, and ACON.

On May 8, 2018, the *Berkelhammer* action was voluntarily dismissed, and on May 15, 2018 a substantially similar action was filed by the same plaintiff in the Superior Court of Washington in and for King County. On April 2, 2018, a putative class action lawsuit *Jacobs v. Funko, Inc. et. al* was filed in the United States District Court for the Western District of Washington against us, certain of our officers and directors, and certain other defendants. On May 21, 2018 the *Jacobs* action was voluntarily dismissed, and on June 12, 2018 a substantially similar action was filed by the same plaintiff in the Superior Court of Washington in and for King County.

On July 2, 2018, all of the above-referenced suits were ordered consolidated for all purposes into one action under the title *In re Funko, Inc. Securities Litigation* in the Superior Court of Washington in and for King County. On August 1, 2018, plaintiffs filed a consolidated complaint against us, certain of our officers and directors, ACON, Fundamental, and certain other defendants. On October 1, 2018, we moved to dismiss that action. Plaintiffs filed their opposition to our motion to dismiss on October 31, 2018, and we filed our reply to plaintiffs' opposition on November 30, 2018. Oral arguments on the motions to dismiss were held on May 3, 2019. A ruling on the motions to dismiss has not yet been issued. On August 2, 2019, the Court granted our motion to dismiss the consolidated state litigation, allowing Plaintiffs leave to amend the complaint. The Court found, inter alia, that "Funko's statements regarding its financial disclosures were not materially false or misleading" and that "plaintiffs have not shown that Funko's 'opinion statements' were false or that such statements were not simply corporate optimism or puffery."

Additionally, on June 4, 2018, a putative class action lawsuit *Kanugonda v. Funko, Inc., et al.* was filed in the United States District Court for the Western District of Washington against us, certain of our officers and directors, and certain other defendants. On January 4, 2019, a lead plaintiff was appointed in that case. On April 30, 2019, the lead plaintiff filed an amended complaint against the previously named defendants.

The complaint in federal court alleges that we violated Sections 11, 12, and 15 of the Securities Act of 1933, as amended, by making allegedly materially misleading statements and by omitting material facts necessary to make the statements made therein not misleading. The lawsuit seeks, among other things, compensatory statutory damages and rescissory damages in account of the consideration paid for our Class A common stock by the lead plaintiff and members of the putative class, as well as attorneys' fees and costs.

We are party to additional legal proceedings incidental to our business. While the outcome of these additional matters could differ from management's expectations, we do not believe that the resolution of such matters is reasonably likely to have a material effect on our results of operations or financial condition.

Item 1A. Risk Factors.

Our business faces significant risks and uncertainties. Certain important factors may have a material adverse effect on our business prospects, financial condition and results of operations, and they should be carefully considered. Accordingly, in evaluating our business, we encourage you to consider the following discussion of risk factors in its entirety, in addition to other information contained in or incorporated by reference into this Quarterly Report on Form 10-Q and our other public filings with the Securities and Exchange Commission ("SEC"). Other events that we do not currently anticipate or that we currently deem immaterial may also affect our business, prospects, financial condition and results of operations.

Risks Related to Our Business

Our success depends on our ability to execute our business strategy.

Our net sales and profitability have grown rapidly in recent periods; however, this should not be considered indicative of our future performance. Our future growth, profitability and cash flows depend upon our ability to successfully execute our business strategy, which is dependent upon a number of factors, including our ability to:

- expand our market presence in existing sales channels and enter additional sales channels;
- anticipate, gauge and respond to rapidly changing consumer preferences and pop culture trends;
- acquire or enter into new licenses in existing product categories or in new product categories and renew existing licenses;
- expand our geographic presence to take advantage of opportunities outside of the United States;
- enhance and maintain favorable brand recognition for our Company and product offerings;
- maintain and expand margins through sales growth and efficiency initiatives;
- effectively manage our relationships with third-party manufacturers;
- effectively manage our debt, working capital and capital investments to maintain and improve the generation of cash flow; and
- execute any acquisitions quickly and efficiently and integrate businesses successfully.

There can be no assurance that we can successfully execute our business strategy in the manner or time period that we expect. Further, achieving these objectives will require investments which may result in short-term costs without generating any current sales or countervailing cost savings and, therefore, may be dilutive to our earnings, at least in the short term. In addition, we may decide to divest or discontinue certain brands or products or streamline operations and incur other costs or special charges in doing so. We may also decide to discontinue certain programs or sales to certain retailers based on anticipated strategic benefits. The failure to realize the anticipated benefits from our business strategy could have a material adverse effect on our prospects, business, financial condition and results of operations.

Our business is dependent upon our license agreements, which involve certain risks.

Products from which we generate substantially all of our net sales are produced under license agreements which grant us the right to use certain intellectual property in such products. These license agreements typically have short terms (between two and three years), are not automatically renewable, and, in some cases, give the licensor the right to terminate the license agreement at will. Our license agreements typically provide that our licensors own the intellectual property rights in the products we design and sell under the license, and as a result, upon termination of the license, we would no longer have the right to sell these products, while our licensors could engage a competitor to do so. We believe our ability to retain our license agreements depends, in large part, on the strength of our relationships with our licensors.

Any events or developments adversely affecting those relationships, or the loss of one or more members of our management team, particularly our chief executive officer, could adversely affect our ability to maintain and renew our license agreements on similar terms or at all. Our top ten licensors collectively accounted for approximately 73% and 72% of our sales for the six months ended June 30, 2019 and 2018, respectively. Moreover, while we have separate licensing arrangements with Disney, LucasFilm and Marvel, these parties are all under common ownership by Disney and collectively these licensors accounted for approximately 36% and 35% of our sales for the six months ended June 30, 2019 and 2018, respectively. The termination or lack of renewal of one or more of our license agreements, or the renewal of a license agreement on less favorable terms, could have a material adverse effect on our business, financial condition and results of operations. For example, in January 2019 we renewed our licensing agreements with Disney, LucasFilm and Marvel. In connection with such renewals, we were required to provide Disney certain benefits and fees in addition to paying Disney approximately $2.0 million as a consent fee under our previous licensing agreements. While we may enter into additional license agreements in the future, the terms of such license agreements may be less favorable than the terms of our existing license agreements.

Our license agreements are complex, and typically grant our licensors the right to audit our compliance with the terms and conditions of such agreements. Any such audit could result in a dispute over whether we have paid the proper royalties, which could require us to pay additional royalties, and the amounts involved could be material. For example, as of June 30, 2019, we had a reserve of $7.7 million on our balance sheet related to ongoing and future royalty audits. In addition to royalty payments, these agreements as a whole impose numerous other obligations on us, including obligations to, among other things:

- maintain the integrity of the applicable intellectual property;
- obtain the licensor's approval of the products we develop under the license prior to making any sales;
- permit the licensor's involvement in, or obtain the licensor's approval of, advertising, packaging and marketing plans;
- maintain minimum sales levels or make minimum guaranteed royalty payments;
- actively promote the sale of the licensed product and maintain the availability of the licensed product throughout the license term;
- spend a certain percentage of our sales of the licensed product on marketing and advertising for the licensed product;
- sell the products we develop under the license only within a specified territory or within specified sales channels;
- indemnify the licensor in the event of product liability or other claims related to the licensed product and advertising or other materials used to promote the licensed product;
- obtain the licensor's approval of the retail price of the licensed products;
- sell the licensed products to the licensor at a discounted price or at the lowest price charged to our customers;
- obtain the licensor's consent prior to assigning or sub-licensing to third parties; and
- provide notice to, obtain approval from, or, in limited circumstances, make certain payments to the licensor in connection with certain changes in control.

If we breach any of these obligations or any other obligations set forth in any of our license agreements, we could be subject to monetary penalties and our rights under such license agreements could be terminated, either of which could have a material adverse effect on our business, financial condition and results of operations.

Our success is also partially dependent on the reputation of our licensors and the goodwill associated with their intellectual property, and the ability of our licensors to protect and maintain the intellectual property rights that we use in connection with our products, all of which may be harmed by factors outside our control. See also "If we are unable to obtain, maintain and protect our intellectual property rights, in particular trademarks and copyrights, or if our licensors are unable to maintain and protect their intellectual property rights that we use in connection with our products, our ability to compete could be negatively impacted."

As a purveyor of licensed pop culture consumer products, we cannot assure you that we will be able to design and develop products that will be popular with consumers, or that we will be able to maintain the popularity of successful products.

The interests of consumers evolve extremely quickly and can change dramatically from year to year. To be successful we must correctly anticipate both the products and the movies, TV shows, video games, music, sports and other content releases (including the related characters), that will appeal to consumers and quickly develop and introduce products that can compete successfully for consumers' limited time, attention and spending. Evolving consumer tastes and shifting interests, coupled with an ever changing and expanding pipeline of products and content that compete for consumers' interest and acceptance, create an environment in which some products and content can fail to achieve consumer acceptance, while others can be popular during a certain period of time but then be rapidly replaced. As a result, consumer products, particularly those based on pop culture such as ours, can have short life cycles. In addition, given the growing market for digital products and the increasingly digital nature of pop culture, there is also a risk that consumer demand for physical products may decrease over time. If we devote time and resources to developing and marketing products that consumers do not find appealing enough to buy in sufficient quantities, our sales and profits may decline, and our business performance may be damaged. Similarly, if our product offerings fail to correctly anticipate consumer interests, our sales and earnings will be adversely affected.

Additionally, our business is increasingly global and depends on interest in and acceptance of our products and our licensors' brands by consumers in diverse markets around the world with different tastes and preferences. As such, our success depends on our ability to successfully predict and adapt to changing consumer tastes and preferences in multiple markets and geographies and to design products that can achieve popularity globally over a broad and diverse consumer audience. There is no guarantee that we will be able to successfully develop and market products with global appeal.

Consumer demand for pop culture products can and does shift rapidly and without warning. As a result, even if our product offerings are initially successful, there can be no guarantee that we will be able to maintain their popularity with consumers. Accordingly, our success will depend, in part, on our ability to continually design and introduce new products that consumers find appealing. To the extent we are unable to do so, our sales and profitability will be adversely affected. This is particularly true given the concentration of our sales under certain of our brands, particularly Pop!. Sales of our Pop! branded products accounted for approximately 82% and 77% of our sales for the six months ended June 30, 2019 and 2018, respectively. If consumer demand for our Pop! branded products were to decrease, our business, financial condition and results of operations could be adversely affected unless we were able to develop and market additional products that generated an equivalent amount of net sales at a comparable gross margin, which there is no guarantee we would be able to do.

Changes in the retail industry and markets for consumer products affecting our retail customers or retailing practices could negatively impact our business, financial condition and results of operations.

Our products are primarily sold to consumers through retailers that are our direct customers or customers of our distributors. As such, changes in the retail industry can negatively impact our business, financial condition and results of operations.

Due to the challenging environment for traditional "brick-and-mortar" retail locations caused by declining in-store traffic, many retailers are closing physical stores, and some traditional retailers are engaging in significant reorganizations, filing for bankruptcy and going out of business. For example, in September 2017, Toys "R" Us, Inc. and certain of its subsidiaries filed voluntary petitions for relief under Chapter 11 of Title 11 of the United States Bankruptcy Code, and in March 2018, Toys "R" Us, Inc. announced the wind down of its U.S. operations and the potential insolvency proceedings of certain of its subsidiaries. Toys "R" Us, Inc. accounted for approximately 3.4% of our sales for the year ended December 31, 2017. In addition to furthering consolidation in the retail industry, such a trend could have a negative effect on the financial health of our retail customers and distributors, potentially causing them to experience difficulties in fulfilling their payment obligations to us or our distributors, reduce the amount of their purchases, seek extended credit terms or otherwise change their purchasing patterns, alter the manner in which they promote our products or the resources they devote to promoting and selling our products or cease doing business with us or our distributors. If any of our retail customers were to file for bankruptcy, we could be unable to collect amounts owed to us and could even be required to repay certain amounts paid to us prior to the bankruptcy filing. The occurrence of any of these events would have an adverse effect on our business, cash flows, financial condition and results of operations.

If we do not effectively maintain and further develop our relationships with retail customers and distributors, our growth prospects, business and results of operations could be harmed.

Historically, substantially all of our net sales have been derived from our retail customers and distributors, upon which we rely to reach the consumers who are the ultimate purchasers of our products. In the United States, we primarily sell our products directly to specialty retailers, mass-market retailers and e-commerce sites. In international markets, we sell our products directly to similar retailers, primarily in Europe, through our subsidiary Funko UK, Ltd. We also sell our products to distributors for sale to retailers in the United States and in certain countries internationally, typically in those countries in which we do not currently have a direct presence. Our top ten customers represented approximately 43% and 40% of our sales for the six months ended June 30, 2019 and 2018, respectively.

We depend on retailers to provide adequate and attractive space for our products and point of purchase displays in their stores. We further depend on our retail customers to employ, educate and motivate their sales personnel to effectively sell our products. If our retail customers do not adequately display our products or choose to promote competitors' products over ours, our sales could decrease, and our business could be harmed. Similarly, we depend on our distributors to reach retailers in certain market segments in the United States and to reach international retailers in countries where we do not have a direct presence. Our distributors generally offer products from several different companies, including our competitors. Accordingly, we are at risk that these distributors may give higher priority to selling other companies' products. If we were to lose the services of a distributor, we might need to find another distributor in that area, and there can be no assurance of our ability to do so in a timely manner or on favorable terms.

In addition, our business could be adversely affected if any of our retail customers or distributors were to reduce purchases of our products. Our retail customers and distributors generally build inventories in anticipation of future sales and will decrease the size of their future product orders if sales do not occur as rapidly as they anticipate. Our customers make no long-term commitments to us regarding purchase volumes and can therefore freely reduce their purchases of our products. Any reduction in purchases of our products by our retail customers and distributors, or the loss of any key retailer or distributor, could adversely affect our net sales, operating results and financial condition.

Furthermore, consumer preferences have shifted, and may continue to shift in the future, to sales channels other than traditional retail, including e-commerce, in which we have more limited experience, presence and development. Consumer demand for our products may be lower in these channels than in traditional retail channels. In addition, our entry into new product categories and geographies has exposed, and may continue to expose, us to new sales channels in which we have less expertise. If we are not successful in developing our e-commerce channel and other new sales channels, our net sales and profitability may be adversely affected.

Our industry is highly competitive and the barriers to entry are low. If we are unable to compete effectively with existing or new competitors, our sales, market share and profitability could decline.

Our industry is, and will continue to be, highly competitive. We compete with toy companies in many of our product categories, some of which have substantially more resources than us, stronger name recognition, longer operating histories and greater economies of scale. We also compete with numerous smaller domestic and foreign collectible product designers and manufacturers. Across our business, we face competitors who are constantly monitoring and attempting to anticipate consumer tastes and trends, seeking ideas that will appeal to consumers and introducing new products that compete with our products for consumer acceptance and purchase.

In addition to existing competitors, the barriers to entry for new participants in our industry are low, and the increasing use of digital technology, social media and the internet to spark consumer interest has further increased the ability for new participants to enter our markets and has broadened the array of companies against which we compete. New participants can gain access to retail customers and consumers and become a significant source of competition for our products in a very short period of time. Additionally, since we do not have exclusive rights to any of the properties we license or the related entertainment brands, our competitors, including those with more resources and greater economies of scale, can obtain licenses to design and sell products based on the same properties that we license, potentially on more favorable terms. Any of these competitors may be able to bring new products to market more quickly, respond more rapidly than us to changes in consumer preferences and produce products of higher quality or that can be sold at more accessible price points. To the extent our competitors' products achieve greater market acceptance than our products, our business, financial condition and results of operations will be adversely affected.

In addition, certain of our licensors have reserved the rights to manufacture, distribute and sell identical or similar products to those we design and sell under our license agreements. These products could directly compete with our products and could be sold at lower prices than those at which our products are sold, resulting in higher margins for our customers compared to our products, potentially lessening our customers' demand for our products and adversely affecting our sales and profitability.

Furthermore, competition for access to the properties we license is intense, and we must vigorously compete to obtain licenses to the intellectual property we need to produce our products. This competition could lessen our ability to secure, maintain, and renew our existing licenses, or require us to pay licensors higher royalties and higher minimum guaranteed payments in order to obtain new licenses or retain our existing licenses. To the extent we are unable to license properties on commercially reasonable terms, or on terms at least as favorable as our competitors, our competitive position and demand for our products will suffer. Because our ability to compete for licensed properties is based largely on our ability to increase fan engagement and generate royalty revenues for our licensors, any reduction in the demand for and sales of our products will further inhibit our ability to obtain licenses on commercially reasonable terms or at all. As a result, any such reduction in the demand for and sales of our products could have a material adverse effect on our business, financial condition and results of operations.

We also increasingly compete with toy companies and other product designers for shelf space at specialty, mass-market and other retailers. Our retail customers will allocate shelf space and promotional resources based on the margins of our products for our customers, as well as their sales volumes. If toy companies or other competitors produce higher margin or more popular merchandise than our products, our retail customers may reduce purchases of our products and, in turn, devote less shelf space and resources to the sale of our products, which could have a material adverse effect on our sales and profitability.

We have experienced rapid growth in recent periods. If we fail to manage our growth effectively, our financial performance may suffer.

We have experienced rapid growth over the last several years, which has placed a strain on our managerial, operational, product design and development, sales and marketing, administrative and financial infrastructure. For example, we increased our total number of full-time employees from 66 as of December 31, 2013 to 845 as of June 30, 2019. As a result of our acquisition of Underground Toys Limited in January 2017 (the "Underground Toys Acquisition"), we now have distribution operations in the United Kingdom, our first distribution center outside of our headquarters in Everett, Washington. In June 2017, with the acquisition of Loungefly, LLC, we added an additional distribution center in Chatsworth, California. Our success will depend in part upon our ability to manage our growth effectively. To do so, we must continue to increase the productivity of our existing employees and to hire, train and manage new employees as needed, which we may not be able to do successfully or without compromising our corporate culture. See "Our success is critically dependent on the efforts and dedication of our officers and other employees, and the loss of any one or more key employees, or our inability to attract and retain qualified personnel and maintain our corporate culture, could adversely affect our business." To manage domestic and international growth of our operations and personnel, we will need to continue to improve our product development, supply chain, financial and management controls and our reporting processes and procedures and implement more extensive and integrated financial and business information systems. These additional investments will increase our operating costs, which will make it more difficult for us to offset any future revenue shortfalls by reducing expenses in the short term. Moreover, if we fail to scale our operations or manage our growth successfully, our business, financial condition and operating results could be adversely affected.

Our gross margin may not be sustainable and may fluctuate over time.

Our gross margin has historically fluctuated, primarily as a result of changes in product mix, changes in our costs, price competition and acquisitions. For the six months ended June 30, 2019 and 2018, our gross margins (exclusive of depreciation and amortization) were 37.6% and 37.5%, respectively. Our current gross margin may not be sustainable, and our gross margin may decrease over time. A decrease in gross margin can be the result of numerous factors, including, but not limited to:

- changes in customer, geographic, or product mix;
- introduction of new products, including our expansion into additional product categories;
- increases in the royalty rates under our license agreements;
- inability to meet minimum guaranteed royalties;
- increases in, or our inability to reduce, our costs;
- entry into new markets or growth in lower margin markets;
- increases in raw materials, labor or other manufacturing- and inventory-related costs;

- increases in transportation costs, including the cost of fuel, and increased shipping costs to meet customer demand;
- increased price competition;
- changes in the dynamics of our sales channels, including those affecting the retail industry and the financial health of our customers;
- increases in sales discounts and allowances provided to our customers;
- acquisitions of companies with a lower gross margin than ours; and
- overall execution of our business strategy and operating plan.

If any of these factors, or other factors unknown to us at this time, occur, then our gross margin could be adversely affected, which could have a material adverse effect on our business, financial condition and results of operations.

Our business is largely dependent on content development and creation by third parties.

We spend considerable resources in designing and developing products in conjunction with planned movie, television, video game, music and other content releases by various third-party content providers. The timing of the development and release, and the ultimate consumer interest in and success of, such content depends on the efforts of these third parties, as well as conditions in the media and entertainment industry generally. We do not control when or if any particular project will be greenlit, developed or released, and the creators of such projects may change their plans with respect to release dates or cancel development altogether. This can make it difficult for us to successfully develop and market products in conjunction with a given content release, given the lead times involved in product development and successful marketing efforts. Additionally, unforeseen factors in the media and entertainment industry, including labor strikes and unforeseen developments with talent, including accusations of a star's wrongdoing, may also delay or cancel the release of such projects. Any such delay or cancellation may decrease the number of products we sell and harm our business.

We may not realize the full benefit of our licenses if the properties we license have less market appeal than expected or if sales from the products that use those properties are not sufficient to satisfy the minimum guaranteed royalties.

We seek to fulfill consumer preferences and interests by designing and selling products primarily based on properties owned by third parties and licensed to us. The popularity of the properties we license can significantly affect our sales and profitability. If we produce products based on a particular movie, TV show or video game, the success of the underlying content has a critical impact on the level of consumer interest in the associated products we are offering. Although we license a wide variety of properties, sales of products tied to major movie franchises have been significant contributors to our business. In addition, the theatrical duration of movie releases has decreased over time and we expect this trend to continue with the increase of content made available on video streaming services. This may make it increasingly difficult for us to sell products based on such properties or lead our customers to reduce demand for our products to minimize inventory risk. If the performance of one or more of such movie franchises failed to meet expectations or if there was a shift in consumer tastes away from such franchises generally, our results of operations could be adversely affected. In addition, competition in our industry for access to licensed properties can lessen our ability to secure, maintain, and renew our existing licenses on commercially reasonable terms, if at all, and to attract and retain the talented employees necessary to design, develop and market successful products based on these properties.

Our license agreements usually also require us to pay minimum royalty guarantees, which may in some cases be greater than what we are ultimately able to recoup from actual sales. When our licensing agreements require minimum royalty guarantees, we accrue a royalty liability based on the contractually required percentage, as revenues are earned. In the case that a minimum royalty guarantee is not expected to be met through sales, we will accrue up to the minimum amount required to be paid. As of June 30, 2019 and December 31, 2018, we recorded reserves of $0.7 million and $5.5 million, respectively, related to prepaid royalties we estimated would not be recovered through sales. Acquiring or renewing licenses may require the payment of minimum guaranteed royalties that we consider to be too high to be profitable, which may result in losing licenses that we currently hold when they become available for renewal, or missing business opportunities for new licenses. Additionally, we have no guarantee that any particular property we license will translate into a successful product. Products tied to a particular content release may be developed and released before demand for the underlying content is known. The underperformance of any such product may result in reduced sales and operating profit for us.

Our success depends, in part, on our ability to successfully manage our inventories.

We must maintain sufficient inventory levels to operate our business successfully, but we must also avoid accumulating excess inventory, which increases working capital needs and lowers gross margin. We obtain substantially all of our inventory from third-party manufacturers located outside the United States and must typically order products well in advance of the time these products will be offered for sale to our customers. As a result, it may be difficult to respond to changes in consumer preferences and market conditions, which, for pop culture products, can change rapidly. If we do not accurately anticipate the popularity of certain products, then we may not have sufficient inventory to meet demand. Alternatively, if demand or future sales do not reach forecasted levels, we could have excess inventory that we may need to hold for a long period of time, write down, sell at prices lower than expected or discard. If we are not successful in managing our inventory, our business, financial condition and results of operations could be adversely affected.

We may also be negatively affected by changes in retailers' inventory policies and practices. As a result of the desire of retailers to more closely manage inventory levels, there is a growing trend to make purchases on a "just-in-time" basis. This requires us to more closely anticipate demand and could require us to carry additional inventory. Policies and practices of individual retailers may adversely affect us as well, including those relating to access to and time on shelf space, price demands, payment terms and favoring the products of our competitors. Our retail customers make no binding long-term commitments to us regarding purchase volumes and make all purchases by delivering purchase orders. Any retailer can therefore freely reduce its overall purchase of our products, including the number and variety of our products that it carries, and reduce the shelf space allotted for our products. If demand or future sales do not reach forecasted levels, we could have excess inventory that we may need to hold for a long period of time, write down, sell at prices lower than expected or discard. If we are not successful in managing our inventory, our business, financial condition and results of operations could be adversely affected.

An inability to develop and introduce products in a timely and cost-effective manner may damage our business.

Our sales and profitability depend on our ability to bring products to market to meet customer demands and before consumers begin to lose interest in a given property. There is no guarantee that we will be able to manufacture, source and ship new or continuing products in a timely manner or on a cost-effective basis to meet constantly changing consumer demands. This risk is heightened by our customers' increasingly compressed shipping schedules and the seasonality of our business. Furthermore, our license agreements typically require us to obtain the licensor's approval of the products we develop under a particular license prior to making any sales, which can have the effect of delaying our product releases. Additionally, for products based on properties in our movie, TV show and video game categories, this risk may also be exacerbated by our need to introduce new products on a timeframe that corresponds with a particular content release. These time constraints may lead our customers to reduce their demand for these products in order to minimize their inventory risk. Moreover, unforeseen delays or difficulties in the development process, significant increases in the planned cost of development, manufacturing or distribution delays or changes in anticipated consumer demand for our products and new brands, or the related third party content, may cause the introduction date for products to be later than anticipated, may reduce or eliminate the profitability of such products or, in some situations, may cause a product or new brand introduction to be discontinued.

If we are unable to obtain, maintain and protect our intellectual property rights, in particular trademarks and copyrights, or if our licensors are unable to maintain and protect their intellectual property rights that we use in connection with our products, our ability to compete could be negatively impacted.

Our intellectual property is a valuable asset of our business. As of June 30, 2019, we owned approximately 51 registered U.S. trademarks, 122 registered international trademarks, 38 pending U.S. trademark applications and 51 pending international trademark applications. The market for our products depends to a significant extent upon the value associated with our product design, our proprietary brands and the properties we license. Although certain of our intellectual property is registered in the United States and in several of the foreign countries in which we operate, there can be no assurances with respect to the rights associated with such intellectual property in those countries, including our ability to register, use, maintain or defend key trademarks and copyrights. We rely on a combination of trademark, trade dress, copyright and trade secret laws, as well as confidentiality procedures and contractual restrictions, to establish and protect our intellectual property or other proprietary rights. However, these laws, procedures and restrictions provide only limited and uncertain protection and any of our intellectual property rights may be challenged, invalidated, circumvented, infringed or misappropriated, including by counterfeiters and parallel importers. In addition, our intellectual property portfolio in many foreign countries is less extensive than our portfolio in the United States, and the laws of foreign countries, including many emerging markets in which our products are produced or sold, may not protect our intellectual property rights to the same extent as the laws of the United States. The costs required to protect our trademarks and copyrights may be substantial.

In addition, we may fail to apply for, or be unable to obtain, protection for certain aspects of the intellectual property used in or beneficial to our business. Further, we cannot provide assurance that our applications for trademarks, copyrights and other intellectual property rights will be granted, or, if granted, will provide meaningful protection. In addition, third parties have in the past and could in the future bring infringement, invalidity or similar claims with respect to any of our current trademarks and copyrights, or any trademarks or copyrights that we may seek to obtain in the future. Any such claims, whether or not successful, could be extremely costly to defend, divert management's attention and resources, damage our reputation and brands, and substantially harm our business and results of operations.

In order to protect or enforce our intellectual property and other proprietary rights, or to determine the enforceability, scope or validity of the intellectual or proprietary rights of others, we may initiate litigation or other proceedings against third parties. Any lawsuits or proceedings that we initiate could be expensive, take significant time and divert management's attention from other business concerns. Litigation and other proceedings also put our intellectual property at risk of being invalidated, or if not invalidated, may result in the scope of our intellectual property rights being narrowed. In addition, our efforts to try to protect and defend our trademarks and copyrights may be ineffective. Additionally, we may provoke third parties to assert claims against us. We may not prevail in any lawsuits or other proceedings that we initiate, and the damages or other remedies awarded, if any, may not be commercially valuable. The occurrence of any of these events may have a material adverse effect on our business, financial condition and results of operations.

In addition, most of our products bear the trademarks and other intellectual property rights of our licensors, and the value of our products is affected by the value of those rights. Our licensors' ability to maintain and protect their trademarks and other intellectual property rights is subject to risks similar to those described above with respect to our intellectual property. We do not control the protection of the trademarks and other intellectual property rights of our licensors and cannot ensure that our licensors will be able to secure or protect their trademarks and other intellectual property rights. The loss of any of our significant owned or licensed trademarks, copyrights or other intellectual property could have a material adverse effect on our business, financial condition and results of operations. In addition, our licensors may engage in activities or otherwise be subject to negative publicity that could harm their reputation and impair the value of the intellectual property rights we license from them, which could reduce consumer demand for our products and adversely affect our business financial condition and results of operations.

Our success depends on our ability to operate our business without infringing, misappropriating or otherwise violating the trademarks, copyrights and proprietary rights of other parties.

Our commercial success depends at least in part on our ability to operate without infringing, misappropriating or otherwise violating the trademarks, copyrights and other proprietary rights of others. However, we cannot be certain that the conduct of our business does not and will not infringe, misappropriate or otherwise violate such rights. Many companies have employed intellectual property litigation as a way to gain a competitive advantage, and to the extent we gain greater visibility and market exposure as a public company, we may also face a greater risk of being the subject of such litigation. For these and other reasons, third parties may allege that our products or activities, including products we make under license, infringe, misappropriate or otherwise violate their trademark, copyright or other proprietary rights. While we typically receive intellectual property infringement indemnities from our licensors, the indemnities are often limited to third-party copyright infringement claims to the extent arising from our use of the licensed material. Defending against allegations and litigation could be expensive, take significant time, divert management's attention from other business concerns, and delay getting our products to market. In addition, if we are found to be infringing, misappropriating or otherwise violating third-party trademark, copyright or other proprietary rights, we may need to obtain a license, which may not be available on commercially reasonable terms or at all, or may need to redesign or rebrand our products, which may not be possible. We may also be required to pay substantial damages or be subject to a court order prohibiting us and our customers from selling certain products or engaging in certain activities. Any claims of violating others' intellectual property, even those without merit, could therefore have a material adverse effect on our business, financial condition and results of operations.

Our operating results may be adversely affected and damage to our reputation may occur due to production and sale of counterfeit versions of our products.

As we have expanded internationally, and the global popularity of our products has increased, we are increasingly subject to efforts by third parties to produce counterfeit versions of our products. There can be no guarantee that our efforts, including our work with customs officials and law enforcement authorities, to block the manufacture of counterfeit goods, prevent their entry into end markets, and detect counterfeit products in customer networks will be successful or result in any material reduction in the availability of counterfeit goods. Any such counterfeit sales, to the extent they replace otherwise legitimate sales, could adversely affect our operating results and damage our reputation.

Our success is critically dependent on the efforts and dedication of our officers and other employees, and the loss of one or more key employees, or our inability to attract and retain qualified personnel and maintain our corporate culture, could adversely affect our business.

Our officers and employees are at the heart of all of our efforts. It is their skill, creativity and hard work that drive our success. In particular, our success depends to a significant extent on the continued service and performance of our senior management team, including our chief executive officer, Brian Mariotti. We are dependent on his talents and believe he is integral to our relationships with our licensors and certain of our key retail customers. The loss of any member of our senior management team, or of any other key employees, or the inability to successfully complete a planned transition related to our chief financial officer, could impair our ability to execute our business plan and could therefore have a material adverse effect on our business, financial condition and results of operations. We do not currently maintain key man life insurance policies on any member of our senior management team or on our other key employees.

In addition, competition for qualified personnel is intense. We compete with many other potential employers in recruiting, hiring and retaining our senior management team and our many other skilled officers and other employees around the world. Our headquarters is located near Seattle and competition in the Seattle area for qualified personnel, particularly those with technology-related skills and experience, is intense due to the increasing number of technology and e-commerce companies with a large or growing presence in Seattle, some of whom have greater resources than us and may be located closer to the city than we are.

Furthermore, as we continue to grow our business and hire new employees, it may become increasingly challenging to hire people who will maintain our corporate culture. We believe our corporate culture, which fosters speed, teamwork and creativity, is one of our key competitive strengths. As we continue to grow, we may be unable to identify, hire or retain enough people who will maintain our corporate culture, including those in management and other key positions. Our corporate culture could also be adversely affected by the increasingly global distribution of our employees, as well as their increasingly diverse skill sets. If we are unable to maintain the strength of our corporate culture, our competitive ability and our business may be adversely affected.

Our operating results may fluctuate from quarter to quarter and year to year due to the seasonality of our business, as well as due to the timing of new product releases.

The businesses of our retail customers are highly seasonal, with a majority of retail sales occurring during the period from October through December in anticipation of the holiday season. As a consequence, we have experienced moderate seasonality in our business. Approximately 59.8%, 60.5% and 58.7% of our net sales for the years ended December 31, 2018, 2017 and 2016, respectively, were made in the third and fourth quarters, as our customers build up their inventories in anticipation of the holiday season.

This seasonal pattern requires significant use of working capital, mainly to manufacture inventory during the portion of the year prior to the holiday season and requires accurate forecasting of demand for products during the holiday season in order to avoid losing potential sales of highly popular products or producing excess inventory of less popular products. In addition, as a result of the seasonal nature of our business, we would be significantly and adversely affected, in a manner disproportionate to the impact on a company with sales spread more evenly throughout the year, by unforeseen events such as a terrorist attack or economic shock that harm the retail environment or consumer buying patterns during our key selling season, or by events such as strikes or port delays that interfere with the shipment of goods during the critical months leading up to the holiday shopping season.

In addition, our results of operations may fluctuate significantly from quarter to quarter or year to year depending on the timing of new product releases and related content releases. Sales of a certain product or group of products tied to a particular content release can dramatically increase our net sales in any given quarter or year. The timing and mix of products we sell in any given year will depend on various factors, including the timing and popularity of new releases by third-party content providers and our ability to license properties based on these releases.

Our results of operations may also fluctuate as a result of factors such as the delivery schedules set by our customers and holiday shut down schedules set by our third-party manufacturers. Additionally, the rapid growth we have experienced in recent years may have masked the full effects of seasonal factors on our business to date, and as such, these factors may have a greater effect on our results of operations in future periods.

Our use of third-party manufacturers to produce our products presents risks to our business.

We use third-party manufacturers to manufacture all of our products and have historically concentrated production with a small number of manufacturers and factories. As a result, the loss or unavailability of one of our manufacturers or one of the factories in which our products are produced, even on a temporary basis, could have a negative impact on our business, financial condition and results of operations. This risk is exacerbated by the fact that we do not have written contracts with certain of our manufacturers. While we believe our external sources of manufacturing could be shifted, if necessary, to alternative sources of supply, we would require a significant period of time to make such a shift. Because we believe our products represent a significant percentage of the total capacity of each factory in which they are produced, such a shift may require us to establish relationships with new manufacturers, which we may not be able to do on a timely basis, on similar terms, or at all. We may also be required to seek out additional manufacturers in response to increased demand for our products, as our current manufacturers may not have the capacity to increase production. If we were prevented from or delayed in obtaining a material portion of the products produced by our manufacturers, or if we were required to shift manufacturers (assuming we would be able to do so), our sales and profitability could be significantly reduced.

In addition, while we require that our products supplied by third-party manufacturers be produced in compliance with all applicable laws and regulations, and we have the right to monitor compliance by our third-party manufacturers with our manufacturing requirements and to oversee the quality control process at our manufacturers' factories, there is always a risk that one or more of our third-party manufacturers will not comply with our requirements, and that we will not immediately discover such non-compliance. For example, the Consumer Product Safety Improvement Act of 2008, or the CPSIA, limits the amounts of lead and phthalates that are permissible in certain products and requires that our products be tested to ensure that they do not contain these substances in amounts that exceed permissible levels. In the past, products manufactured by certain of our third-party manufacturers have tested positive for phthalates. Though the amount was not in excess of the amount permissible under the CPSIA, we cannot guarantee that products made by our third-party manufacturers will not in the future contain phthalates in excess of permissible amounts, or will not otherwise violate the CPSIA, other consumer or product safety requirements, or labor or other applicable requirements. Any failure of our third-party manufacturers to comply with such requirements in manufacturing products for us could result in damage to our reputation, harm our brand image and sales of our products and potentially create liability for us.

Monitoring compliance by independent manufacturers is complicated by the fact that expectations of ethical business practices continually evolve, may be substantially more demanding than applicable legal requirements and are driven in part by legal developments and by diverse groups active in publicizing and organizing public responses to perceived ethical shortcomings. Accordingly, we cannot predict how such expectations might develop in the future and cannot be certain that our manufacturing requirements, even if complied with, would satisfy all parties who are active in monitoring and publicizing perceived shortcomings in labor and other business practices worldwide.

Additionally, the third-party manufacturers that produce most of our products are located in China, Vietnam and Mexico. As a result, we are subject to various risks resulting from our international operations. See "Our substantial sales and manufacturing operations outside the United States subject us to risks associated with international operations."

Our operations, including our corporate headquarters, primary distribution facilities and third-party manufacturers, are concentrated in certain geographic regions, which makes us susceptible to adverse conditions in those regions.

Our corporate headquarters and primary distribution facilities are located in Everett, Washington. We also have additional warehouse facilities and/or offices located in Maldon, England; Bath, England; and Chatsworth, California. In addition, the factories that produce most of our products are located in China, Vietnam and Mexico. As a result, our business may be more susceptible to adverse conditions in these regions than the operations of more geographically diverse competitors.

Such conditions could include, among others, adverse economic and labor conditions, as well as demographic trends. Furthermore, Everett is the location from which most of the products we sell are received, stored and shipped to our customers. We depend heavily on ocean container delivery to receive products from our third-party manufacturers located in Asia and contracted third-party delivery service providers to deliver our products to our distribution facilities. Any disruption to or failures in these delivery services, whether as a result of extreme or severe weather conditions, natural disasters, labor unrest or otherwise, affecting western Washington in particular, the West Coast in general, or other areas in which we operate, could significantly disrupt our operations, damage or destroy our equipment and inventory and cause us to incur additional expenses, any of which could have a material adverse effect on our business, financial condition and results of operations. For example, in the fall of 2014, longshoreman work stoppages created a significant backlog of cargo containers at ports. We experienced delays in the shipment of our products as a result of this backlog and were unable to meet our planned inventory allocations for a limited period of time. Although we possess insurance for damage to our property and the disruption of our business, this insurance, and in particular earthquake insurance, which is subject to various limitations and requires large deductibles or co-payments, may not be sufficient to cover all of our potential losses, and may be cancelled by us in the future or otherwise cease to be available to us on reasonable terms or at all. Similarly, natural disasters and other adverse events or conditions affecting east or southeast Asia, where most of our products are produced, could halt or disrupt the production of our products, impair the movement of finished products out of those regions, damage or destroy the molds and tooling necessary to make our products and otherwise cause us to incur additional costs and expenses, any of which could also have a material adverse effect on our business, financial condition and results of operations.

Our substantial sales and manufacturing operations outside the United States subject us to risks associated with international operations.

We operate facilities and sell products in numerous countries outside the United States. Sales to our international customers comprised approximately 35.4% and 32.6% of our sales for the six months ended June 30, 2019 and 2018, respectively. We expect sales to our international customers to account for an increasing portion of our sales in future fiscal years, including as a result of the Underground Toys Acquisition and the formation of our subsidiary Funko UK, Ltd., through which we now sell directly to certain of our customers in Europe, the Middle East and Africa. In fact, over time, we expect our international sales and operations to continue to grow both in dollars and as a percentage of our overall business as a result of a key business strategy to expand our presence in emerging and underserved international markets. Additionally, as discussed above, we use third-party manufacturers located in China, Vietnam and Mexico to produce most of our products. These international sales and manufacturing operations, including operations in emerging markets, are subject to risks that may significantly harm our sales, increase our costs or otherwise damage our business, including:

- currency conversion risks and currency fluctuations;
- limitations on the repatriation of earnings;
- potential challenges to our transfer pricing determinations and other aspects of our cross-border transactions, which can materially increase our taxes and other costs of doing business; political instability, civil unrest and economic instability;
- greater difficulty enforcing intellectual property rights and weaker laws protecting such rights;
- complications in complying with different laws and regulations in varying jurisdictions, including the U.S. Foreign Corrupt Practices Act (“FCPA”), the U.K. Bribery Act of 2010, similar anti-bribery and anti-corruption laws and local and international environmental, labor, health and safety laws, and in dealing with changes in governmental policies and the evolution of laws and regulations and related enforcement;
- difficulties understanding the retail climate, consumer trends, local customs and competitive conditions in foreign markets which may be quite different from the United States;
- changes in international labor costs and other costs of doing business internationally;
- the imposition of and changes in tariffs, quotas, border adjustment taxes or other protectionist measures by any major country or market in which we operate, which could make it significantly more expensive and difficult to import products into that country or market, raise the cost of such products, decrease our sales of such products or decrease our profitability.
- proper payment of customs duties and/or excise taxes;
- natural disasters and the greater difficulty and cost in recovering therefrom;
- transportation delays and interruptions;

- difficulties in moving materials and products from one country to another, including port congestion, strikes or other labor disruptions and other transportation delays and interruptions; and
- increased investment and operational complexity to make our products compatible with systems in various countries and compliant with local laws.

Because of the importance of international sales, sourcing and manufacturing to our business, our financial condition and results of operations could be significantly harmed if any of the risks described above were to occur or if we are otherwise unsuccessful in managing our increasingly global business.

Increases in tariffs, trade restrictions or taxes on our products could have an adverse impact on our operations.

The commerce we conduct in the international marketplace makes us subject to tariffs, trade restrictions and other taxes when the raw materials or components we purchase, and the products we ship, cross international borders. Trade tensions between the United States and China, as well as those between the United States and Canada, Mexico and other countries have been escalating in recent months. Most notably, three rounds of U.S. tariffs were placed on Chinese goods being exported to the United States, with such tariffs taking effect in July, August and September 2018. Each of these U.S. tariff impositions against Chinese exports were followed by a round of retaliatory Chinese tariffs on U.S. exports to China. Certain of the products we purchase from manufacturers in China are subject to these tariffs, which could make our products less competitive than those of our competitors whose inputs are not subject to these tariffs. In addition, the U.S. administration has threatened to impose tariffs on all products imported from China, which would impact all of our products and supplies imported from China to the United States. If this were to occur, we may not be able to mitigate the impacts of these tariffs, and our business, results of operations and financial position would be materially adversely affected. Products we sell into certain foreign markets could also become subject to similar retaliatory tariffs, making the products we sell uncompetitive compared to similar products not subjected to such import tariffs. Further changes in U.S. trade policies, tariffs, taxes, export restrictions or other trade barriers, or restrictions on raw materials or components may limit our ability to produce products, increase our manufacturing costs, decrease our profit margins, reduce the competitiveness of our products, or inhibit our ability to sell products or purchase raw materials or components, which would have a material adverse effect on our business, results of operations and financial condition.

The results of the United Kingdom's referendum on withdrawal from the European Union may have a negative effect on global economic conditions, financial markets and our business.

In June 2016, a majority of voters in the United Kingdom elected to withdraw from the European Union in a national referendum known as "Brexit" and, in March 2017, the government of the United Kingdom formally initiated the withdrawal process. These events have created significant uncertainty about the future relationship between the United Kingdom and the European Union and have given rise to calls for certain regions within the United Kingdom to preserve their place in the European Union by separating from the United Kingdom, as well as for the governments of other European Union member states to consider withdrawal.

These developments, or the perception that any of them could occur, have had and may continue to have a material adverse effect on global economic conditions and the stability of global financial markets, and may significantly reduce global market liquidity and restrict the ability of key market participants to operate in certain financial markets. Asset valuations, currency exchange rates and credit ratings may be especially subject to increased market volatility. Lack of clarity about future United Kingdom laws and regulations as the United Kingdom determines which European Union laws to replace or replicate in the event of a withdrawal, including financial laws and regulations, tax and free trade agreements, intellectual property rights, privacy and data protection, environmental, health and safety laws and regulations and employment laws, could increase costs and depress economic activity. If the United Kingdom and the European Union are unable to negotiate acceptable withdrawal terms or if other European Union member states pursue withdrawal, barrier-free access between the United Kingdom and other European Union member states or among the European economic area overall could be diminished or eliminated.

Any of these factors could have a material adverse effect on our business, financial condition and results of operations. Our operations in the United Kingdom subject us to revenue risk with respect to our customers in the United Kingdom and adverse movements in foreign currency exchange rates, in addition to risks related to the general economic and legal uncertainty related to Brexit described above.

U.S. tax legislation significantly changed U.S. federal income tax rules and may materially adversely affect our financial condition, results of operations and cash flows.

The Tax Cuts and Jobs Act (the "Tax Act") enacted in December 2017 has significantly changed U.S. federal income taxation, including reducing the U.S. corporate income tax rate, limiting certain interest deductions, imposing a one-time transition tax on all undistributed earnings and profits of certain non-U.S. entities and other additional taxes with respect to certain non-U.S. earnings, permitting full expensing of certain capital expenditures, adopting elements of a territorial tax system, revising the rules governing net operating losses and the rules governing foreign tax credits, and introducing new anti-base erosion provisions. Many of these changes became effective immediately, without any transition periods or grandfathering for existing transactions. The legislation is unclear in many respects and could be subject to potential amendments and technical corrections, as well as interpretations and implementing regulations by the Treasury and Internal Revenue Service, any of which could lessen or increase certain adverse impacts of the legislation. In addition, it is unclear how these U.S. federal income tax changes may affect state and local taxation.

Any of these above factors could potentially impact the measurement of our tax balances and reduce any anticipated benefits of the Tax Act.

Unanticipated changes in effective tax rates or adverse outcomes resulting from examination of our income or other tax returns could adversely affect our operating results and financial condition.

We are subject to income taxes in the United States and the United Kingdom, and our tax liabilities will be subject to the allocation of expenses in differing jurisdictions. Our future effective tax rates could be subject to volatility or adversely affected by a number of factors, including:

- changes in the valuation of our deferred tax assets and liabilities;
- expected timing and amount of the release of any tax valuation allowances;
- tax effects of equity-based compensation;
- costs related to intercompany restructurings; or
- changes in tax laws, regulations or interpretations thereof.

In addition, we may be subject to audits of our income, sales and other transaction taxes by the U.K., U.S. federal and state authorities. Outcomes from these audits could have an adverse effect on our operating results and financial condition.

Changes in foreign currency exchange rates can significantly impact our reported financial performance.

Our increasingly global operations mean we produce, buy, and sell products in many different markets with many different currencies. As a result, if the exchange rate between the U.S. dollar and a local currency for an international market in which we have significant sales or operations changes, our financial results as reported in U.S. dollars may be meaningfully impacted even if our business in the local currency is not significantly affected. Similarly, our expenses can be significantly impacted, in U.S. dollar terms, by exchange rates, meaning the profitability of our business in U.S. dollar terms can be negatively impacted by exchange rate movements which we do not control. In recent years, certain key currencies, such as the euro and the British pound sterling, depreciated significantly compared to the U.S. dollar. Depreciation in key currencies during 2019 and beyond may have a significant negative impact on our sales and earnings as they are reported in U.S. dollars.

Global and regional economic downturns that negatively impact the retail and credit markets, or that otherwise damage the financial health of our retail customers and consumers, can harm our business and financial performance.

We design, manufacture and market a wide variety of consumer products worldwide for sale to our retail customers and directly to consumers. Our financial performance is impacted by the level of discretionary consumer spending in the markets in which we operate. Recessions, credit crises and other economic downturns, or disruptions in credit markets, in the United States and in other markets in which our products are sold can result in lower levels of economic activity, lower employment levels, less consumer disposable income, and lower consumer confidence. The retail industry is subject to volatility, especially during uncertain economic conditions. A downturn in the retail industry in particular may disproportionately affect us because a substantial majority of our net sales are to retail customers. Significant increases in the costs of other products which are required by consumers, such as gasoline, home heating fuels, or groceries, may reduce household spending on our products. Such cost increases and weakened economic conditions may result from any number of factors, including terrorist attacks, wars and other conflicts, natural disasters, increases in critical commodity prices or labor costs, or the prospect of such events. Such a weakened economic and business climate, as well as consumer uncertainty created by such a climate, could harm our sales and profitability. Similarly, reductions in the value of key assets held by consumers, such as their homes or stock market investments, can lower consumer confidence and consumer spending power. Any of these factors can reduce the amount which consumers spend on the purchase of our products. This in turn can reduce our sales and harm our financial performance and profitability.

In addition to experiencing potentially lower sales of our products during times of economic difficulty, in an effort to maintain sales during such times, we may need to reduce the price of our products, increase our promotional spending or sales allowances, or take other steps to encourage retailer and consumer purchases of our products. Those steps may lower our net sales or increase our costs, thereby decreasing our operating margins and lowering our profitability.

Our business depends in large part on our vendors and outsourcers, and our reputation and ability to effectively operate our business may be harmed by actions taken by these third parties outside of our control.

We rely significantly on vendor and outsourcing relationships with third parties for services and systems including manufacturing, transportation, logistics and information technology. In 2018, we initiated a relationship with a third party logistics company to process and fulfill customer orders in Europe. Any shortcoming of one of our vendors or outsourcers, including our third party logistics provider in Europe, particularly one affecting the quality of these services or systems, may be attributed by customers to us, thus damaging our reputation and brand value, and potentially affecting our results of operations. In addition, problems with transitioning these services and systems to, or operating failures with, these vendors and outsourcers could cause delays in product sales, reduce the efficiency of our operations and require significant capital investments to remediate.

We are subject to various government regulations and may be subject to additional regulations in the future, violation of which could subject us to sanctions or otherwise harm our business.

As a company that designs and sells consumer products, we are subject to significant government regulation, including, in the United States, under the CPSA, the FHSA, the CPSIA and the FFA, as well as under product safety and consumer protection statutes in our international markets. There can be no assurance that we will be in compliance, and failure to comply with these acts could result in sanctions which could have a negative impact on our business, financial condition and results of operations. This risk is exacerbated by our reliance on third parties to manufacture our products. See “Our use of third-party manufacturers to produce our products presents risks to our business.”

Governments and regulatory agencies in the markets in which we manufacture and sell products may enact additional regulations relating to product safety and consumer protection in the future and may also increase the penalties for failing to comply with such regulations. In addition, one or more of our customers might require changes in our products, such as the non-use of certain materials, in the future. Complying with any such additional regulations or requirements could impose increased costs on our business. Similarly, increased penalties for non-compliance could subject us to greater expense in the event any of our products were found to not comply with such regulations. Such increased costs or penalties could harm our business.

As discussed above, our international operations subject us to a host of other governmental regulations throughout the world, including antitrust, customs and tax requirements, anti-boycott regulations, environmental regulations and the FCPA. Complying with these regulations imposes costs on us which can reduce our profitability, and our failure to successfully comply with any such legal requirements could subject us to monetary liabilities and other sanctions that could further harm our business and financial condition. For example, as discussed in Note 1 to our unaudited condensed consolidated financial statements included in this Quarterly Report on Form 10-Q, we identified that our subsidiary, Loungefly, historically underpaid certain duties owed to U.S. Customs. In May 2019, the Company notified U.S. Customs of potential underpayments of customs duties and commenced an internal investigation to determine the cause of the underpayments and the proper amount of duties owed for the applicable five-year statute of limitations period. The Company identified a total of approximately \$7.8 million in underpayments to U.S. Customs during the period from May 24, 2014 through June 30, 2019, \$6.3 million of which related to previously issued financial statements. In July 2019, the Company submitted payment of \$7.8 million to U.S. Customs along with a report explaining the nature of the underpayments. The fact that such underpayments occurred could lead to government investigation or litigation, which could result in additional payments and potential penalties. We have recorded a contingent liability of \$0.5 million related to potential penalties that may be assessed by U.S. Customs in this matter. This amount is recorded under the caption “Accrued expenses and other current liabilities” in our condensed consolidated balance sheet, as of June 30, 2019. The imposition of any penalties or other remedial measures could have a material adverse effect on our business, results of operations, and financial condition. We could also incur additional expenses related to remedial measures, including those that we are implementing in response to our conclusion that we have a material weakness in our internal control over financial reporting.

We could be subject to future product liability suits or product recalls which could have a significant adverse effect on our financial condition and results of operations.

As a company that designs and sells consumer products, we may be subject to product liability suits or involuntary product recalls or may choose to voluntarily conduct a product recall. While costs associated with product liability claims and product recalls have generally not been material to our business, the costs associated with future product liability claims or product recalls in any given fiscal year, individually or in the aggregate, could be significant. In addition, any product recall, regardless of the direct costs of the recall, could harm consumer perceptions of our products, subject us to additional government scrutiny, divert development and management resources, adversely affect our business operations and otherwise put us at a competitive disadvantage compared to other companies in our industry, any of which could have a significant adverse effect on our financial condition and results of operations.

We are currently subject to securities class action litigation and may be subject to similar or other litigation in the future, all of which will require significant management time and attention, result in significant legal expenses and may result in unfavorable outcomes, which may have a material adverse effect on our business, operating results and financial condition, and negatively affect the price of our Class A common stock.

We are, and may in the future become, subject to various legal proceedings and claims that arise in or outside the ordinary course of business. For example, on November 16, 2017, a purported stockholder of the Company filed a putative class action lawsuit in the Superior Court of Washington in and for King County against us, certain of our officers and directors, and the underwriters of our IPO, entitled *Robert Lowinger v. Funko, Inc., et. al.* In January and March 2018, five additional putative class action lawsuits were filed in Washington state court, four in the Superior Court of Washington in and for King County and one in the Superior Court of Washington in and for Snohomish County. Two of the King County lawsuits, *Surratt v. Funko, Inc. et. al.* (filed on January 16, 2018) and *Baskin v. Funko, Inc. et. al.* (filed on January 30, 2018), were filed against us and certain of our officers and directors. The other two King County lawsuits, *The Ronald and Maxine Linde Foundation v. Funko, Inc. et. al.* (filed on January 18, 2018) and *Lovewell v. Funko, Inc. et. al* (filed on March 27, 2018), were filed against us, certain of our officers and directors, ACON, Fundamental and certain other defendants. The Snohomish County lawsuit, *Berkelhammer v. Funko, Inc. et. al.* (filed on March 13, 2018), was filed against us, certain of our officers and directors, and ACON. On May 8, 2018, the *Berkelhammer* action was voluntarily dismissed, and on May 15, 2018 a substantially similar action was filed by the same plaintiff in the Superior Court of Washington in and for King County. On April 2, 2018, a putative class action lawsuit *Jacobs v. Funko, Inc. et. al* was filed in the United States District Court for the Western District of Washington against us, certain of our officers and directors, and certain other defendants. On May 21, 2018 the *Jacobs* action was voluntarily dismissed, and on June 12, 2018 a substantially similar action was filed by the same plaintiff in the Superior Court of Washington in and for King County.

On July 2, 2018, all of the above-referenced suits were ordered consolidated for all purposes into one action under the title *In re Funko, Inc. Securities Litigation* in the Superior Court of Washington in and for King County. On August 1, 2018, plaintiffs filed a consolidated complaint against us, certain of our officers and directors, ACON, Fundamental, and certain other defendants. On October 1, 2018, we moved to dismiss that action. Plaintiffs filed their opposition to our motion to dismiss on October 31, 2018, and we filed our reply to plaintiffs' opposition on November 30, 2018. Oral arguments on the motions to dismiss were held on May 3, 2019. On August 2, 2019, the Court granted our motion to dismiss the consolidated state litigation, allowing Plaintiffs leave to amend the complaint. The Court found, inter alia, that "Funko's statements regarding its financial disclosures were not materially false or misleading" and that "plaintiffs have not shown that Funko's 'opinion statements' were false or that such statements were not simply corporate optimism or puffery."

Additionally, on June 4, 2018, a putative class action lawsuit *Kanugonda v. Funko, et al.* was filed in the United States District Court for the Western District of Washington against us, certain of our officers and directors, and certain other defendants. On January 4, 2019, a lead plaintiff was appointed in that case. On April 30, 2019, the lead plaintiff filed an amended complaint against the previously named defendants.

The complaint in federal court alleges that we violated Sections 11, 12, and 15 of the Securities Act of 1933, as amended, by making allegedly materially misleading statements and by omitting material facts necessary to make the statements made therein not misleading. The lawsuit seeks, among other things, compensatory statutory damages and rescissory damages in account of the consideration paid for our Class A common stock by the lead plaintiff and members of the putative class, as well as attorneys' fees and costs.

The results of the securities class action lawsuit and any future legal proceedings cannot be predicted with certainty. Also, our insurance coverage may be insufficient, our assets may be insufficient to cover any amounts that exceed our insurance coverage, and we may have to pay damage awards or otherwise may enter into settlement arrangements in connection with such claims. Any such payments or settlement arrangements in current or future litigation could have a material adverse effect on our business, operating results or financial condition. Even if the plaintiffs' claims are not successful, current or future litigation could result in substantial costs and significantly and adversely impact our reputation and divert management's attention and resources, which could have a material adverse effect on our business, operating results and financial condition, and negatively affect the price of our Class A common stock. In addition, such lawsuits may make it more difficult to finance our operations.

Failure to comply with anti-corruption and anti-bribery laws could result in fines, criminal penalties and materially adversely affect our business, financial condition and results of operations.

A significant risk resulting from our global operations is compliance with a wide variety of U.S. federal and state and non-U.S. laws, regulations and policies, including laws related to anti-corruption, anti-bribery and laundering. The FCPA, the U.K. Bribery Act of 2010 and similar anti-corruption and anti-bribery laws in other jurisdictions generally prohibit companies, their officers, directors, employees and third-party intermediaries, business partners, and agents from making improper payments or other improper things of value to government officials or other persons. There has been an increase in anti-bribery and anti-corruption law enforcement activity in recent years, with more frequent and aggressive investigations and enforcement proceedings by both the U.S. Department of Justice and the SEC, increased enforcement activity by non-U.S. regulators, and increases in criminal and civil proceedings brought against companies and individuals. We operate in parts of the world that are considered high-risk from an anti-bribery and anti-corruption perspective, and strict compliance with anti-bribery and anti-corruption laws may conflict with local customs and practices. We cannot assure you that our internal controls, policies and procedures will protect us from improper conduct by our officers, directors, employees, third-party intermediaries, business partners or agents. To the extent that we learn that any of these parties do not adhere to our internal control policies, we are committed to taking appropriate remedial action. In the event that we believe or have reason to believe that any such party has or may have violated such laws, we may be required to investigate or have outside counsel investigate the relevant facts and circumstances, and detecting, investigating and resolving actual or alleged violations can be expensive and require a significant diversion of time, resources and attention from senior management. Any violation of U.S. federal and state and non-U.S. anti-bribery and anti-corruption laws, regulations and policies could result in substantial fines, sanctions, civil or criminal penalties, and curtailment of operations in the U.S. or other applicable jurisdictions. In addition, actual or alleged violations could damage our reputation and ability to do business. Any of the foregoing could materially adversely affect our business, financial condition and results of operations.

We are subject to governmental economic sanctions requirements and export and import controls that could impair our ability to compete in international markets or subject us to liability if we are not in compliance with applicable laws.

As a U.S. company, we are subject to U.S. export control and economic sanctions laws and regulations, and we are required to export our products in compliance with those laws and regulations, including the U.S. Export Administration Regulations and economic and trade sanctions programs administered by the Treasury Department's Office of Foreign Assets Control. U.S. economic sanctions and export control laws and regulations prohibit the shipment of specified products and services to countries, governments and persons that are the subject of U.S. sanctions. While we take precautions against doing any business, directly or indirectly, in or with countries, governments and persons subject to U.S. sanctions, such measures may be circumvented. There can be no assurance that we will be in compliance with U.S. export control or economic sanctions laws and regulations in the future. Any such violation could result in criminal or civil fines, penalties or other sanctions and repercussions, including reputational harm that could materially adversely affect our business.

We may not realize the anticipated benefits of acquisitions or investments, or those benefits may be delayed or reduced in their realization.

Acquisitions have been a component of our growth and the development of our business and are likely to continue to be in the future. Acquisitions can broaden and diversify our brand holdings and product offerings, expand our distribution capabilities and allow us to build additional capabilities and competencies. For example, in the case of the Underground Toys Acquisition, we looked to strengthen our ability to sell our products directly to international retailers, primarily those located in Europe, and reduce our reliance on third-party distributors in Europe and certain other international jurisdictions. However, we cannot be certain that the products and offerings of companies we may acquire, or acquire an interest in, will achieve or maintain popularity with consumers in the future or that any such acquired companies or investments will allow us to more effectively distribute our products, market our products, develop our competencies or to grow our business.

In some cases, we expect that the integration of the companies that we may acquire into our operations will create production, distribution, marketing and other operating synergies which will produce greater sales growth and profitability and, where applicable, cost savings, operating efficiencies and other advantages. However, we cannot be certain that these synergies, efficiencies and cost savings will be realized. Even if achieved, these benefits may be delayed or reduced in their realization. In other cases, we may acquire or invest in companies that we believe have strong and creative management, in which case we may plan to operate them more autonomously rather than fully integrating them into our operations. We cannot be certain that the key talented individuals at these companies would continue to work for us after the acquisition or that they would develop popular and profitable products, in the future. There is no guarantee that any acquisition or investment we may make will be successful or beneficial or that we will be able to manage the integration process successfully, and acquisitions can consume significant amounts of management attention and other resources, which may negatively impact other aspects of our business.

Our e-commerce business is subject to numerous risks that could have an adverse effect on our business and results of operations.

Although sales through our websites have constituted a small portion of our net sales historically, we expect to continue to grow our e-commerce business in the future. Though sales through our websites generally have higher profit margins and provide us useful insight on the sales impact of certain of our marketing campaigns, further development of our e-commerce business also subjects us to a number of risks. Our online sales may negatively impact our relationships with our retail customers and distributors if they perceive that we are competing with them. In addition, online commerce is subject to increasing regulation by states, the federal government and various foreign jurisdictions. Compliance with these laws will increase our costs of doing business, and our failure to comply with these laws could also subject us to potential fines, claims for damages and other remedies, any of which would have an adverse effect on our business, financial condition and results of operations.

Additionally, some jurisdictions have implemented, or may implement, laws that require remote sellers of goods and services to collect and remit taxes on sales to customers located within the jurisdiction. In particular, the Streamlined Sales Tax Project (an ongoing, multi-year effort by U.S. state and local governments to pursue federal legislation that would require collection and remittance of sales tax by out-of-state sellers) could allow states that meet certain simplification and other criteria to require out-of-state sellers to collect and remit sales taxes on goods purchased by in-state residents. Furthermore, in June 2018, the U.S. Supreme Court ruled in *South Dakota v. Wayfair* that a U.S. state may require an online retailer with no in-state property or personnel to collect and remit sales taxes on sales made to the state's residents, which may permit wider enforcement of sales tax collection requirements. These collection responsibilities and the complexity associated with tax collection, remittance and audit requirements would also increase the costs associated with our e-commerce business.

Furthermore, our e-commerce operations subject us to risks related to the computer systems that operate our websites and related support systems, such as system failures, viruses, computer hackers and similar disruptions. If we are unable to continually add software and hardware, effectively upgrade our systems and network infrastructure and take other steps to improve the efficiency of our systems, system interruptions or delays could occur that adversely affect our operating results and harm our brand. While we depend on our technology vendors to manage "up-time" of the frontend e-commerce store, manage the intake of our orders, and export orders for fulfillment, we could begin to run all or a greater portion of these components ourselves in the future. Any failure on the part of our third-party e-commerce vendors or in our ability to transition third-party services effectively could result in lost sales and harm our brand. There is a risk that consumer demand for our products online may not generate sufficient sales to make our e-commerce business profitable, as consumer demand for physical products online may be less than in traditional retail sales channels. To the extent our e-commerce business does not generate more net sales than costs, our business, financial condition and results of operations will be adversely affected.

Use of social media may materially and adversely affect our reputation or subject us to fines or other penalties.

We rely to a large extent on our online presence to reach consumers and use third-party social media platforms as marketing tools. For example, we maintain Facebook, Twitter, Instagram and YouTube accounts. As e-commerce and social media platforms continue to rapidly evolve, we must continue to maintain a presence on these platforms and establish presences on new or emerging popular social media platforms. If we are unable to cost-effectively use social media platforms as marketing tools, our ability to acquire new consumers and our financial condition may suffer. Furthermore, as laws and regulations rapidly evolve to govern the use of these platforms, the failure by us, our employees or third parties acting at our direction to abide by applicable laws and regulations in the use of these platforms could subject us to regulatory investigations, class action lawsuits, liability, fines or other penalties and have a material adverse effect on our business, financial condition and result of operations.

Failure to successfully operate our information systems and implement new technology effectively could disrupt our business or reduce our sales or profitability.

We rely extensively on various information technology systems and software applications, including our enterprise resource planning software, to manage many aspects of our business, including product development, management of our supply chain, sale and delivery of our products, financial reporting and various other processes and transactions. We are critically dependent on the integrity, security and consistent operations of these systems and related back-up systems. These systems are subject to damage or interruption from power outages, computer and telecommunications failures, computer viruses, malware and other security breaches, catastrophic events such as hurricanes, fires, floods, earthquakes, tornadoes, acts of war or terrorism and usage errors by our employees. The efficient operation and successful growth of our business depends on these information systems, including our ability to operate and upgrade them effectively and to select and implement adequate disaster recovery systems successfully. The failure of these information systems to perform as designed, our failure to operate them effectively, or a security breach or disruption in operation of our information systems could disrupt our business, require significant capital investments to remediate a problem or subject us to liability. In 2018, we upgraded the enterprise resource planning software used by our United Kingdom operations. This upgrade resulted in certain delays in our operations in the first few months of implementation. We are also considering upgrades to our enterprise resource planning software at our other locations, including in the United States. If the potential upgrades are not successful or result in delays, our business could be disrupted or harmed.

In addition, we have recently implemented, and expect to continue to invest in and implement, modifications and upgrades to our information technology systems and procedures to support our growth and the development of our e-commerce business. These modifications and upgrades could require substantial investment and may not improve our profitability at a level that outweighs their costs, or at all. In addition, the process of implementing any new technology systems involves inherent costs and risks, including potential delays and system failures, the potential disruption of our internal control structure, the diversion of management’s time and attention, and the need to re-train or hire new employees, any of which could disrupt our business operations and have a material adverse effect on our business, financial condition and results of operations.

If our electronic data is compromised our business could be significantly harmed.

We maintain significant amounts of data electronically. This data relates to all aspects of our business, including current and future products and entertainment under development, and also contains certain customer, consumer, supplier, partner and employee data. We maintain systems and processes designed to protect the data within our control, but notwithstanding such protective measures, there is a risk of intrusion or tampering that could compromise the integrity and privacy of this data. In addition, we provide confidential and proprietary information to our third-party business partners in certain cases where doing so is necessary or appropriate to conduct our business. While we obtain assurances from those parties that they have systems and processes in place to protect such data, and where applicable, that they will take steps to assure the protections of such data by third parties, nonetheless those partners may also be subject to data intrusion or otherwise compromise the protection of such data. Any compromise of the confidential data of our customers, consumers, suppliers, partners, employees or ourselves, or failure to prevent or mitigate the loss of or damage to this data through breach of our information technology systems or other means could substantially disrupt our operations, harm our customers, consumers and other business partners, damage our reputation, violate applicable laws and regulations and subject us to additional costs and liabilities and loss of business that could be material.

A failure to comply with laws and regulations relating to privacy and the protection of data relating to individuals may result in negative publicity, claims, investigations and litigation, and adversely affect our financial performance.

We are subject to laws, rules, and regulations in the United States, the European Union, and other jurisdictions relating to the collection, use, and security of personal information and data. Such data privacy laws, regulations, and other obligations may require us to change our business practices and may negatively impact our ability to expand our business and pursue business opportunities. We may incur significant expenses to comply with the laws, regulations and other obligations that apply to us. Additionally, the privacy- and data protection-related laws, rules, and regulations applicable to us are subject to significant change. Several jurisdictions have passed new laws and regulations in this area, and other jurisdictions are considering imposing additional restrictions. In particular, our operations are subject to the European Union's new General Data Protection Regulation, which became effective in May 2018 and imposed a host of new data privacy and security requirements on companies doing business in the European Union, including substantial penalties for non-compliance. Privacy- and data protection-related laws and regulations also may be interpreted and enforced inconsistently over time and from jurisdiction to jurisdiction. In addition to government regulation, privacy advocates and industry groups may propose new and different self-regulatory standards that either legally or contractually apply to us. One example of such self-regulatory standards to which we may be contractually bound is the Payment Card Industry Data Security Standard, or PCI DSS. Though we currently use third-party vendors to process and store credit card data in connection with our e-commerce business, to the extent we process or store such data ourselves in the future, we may be subject to various aspects of the PCI DSS, and fines, penalties, and a loss of the ability to process credit card payments could result from any failure to comply with the PCI DSS. Any actual or perceived inability to comply with applicable privacy or data protection laws, regulations, or other obligations could result in significant cost and liability, litigation or governmental investigations, damage our reputation, and adversely affect our business.

Our indebtedness could adversely affect our financial health and competitive position.

On October 22, 2018, we entered into the Credit Agreement providing for the New Term Loan Facility in the amount of $235.0 million and the New Revolving Credit Facility in the amount of $50.0 million (which was increased to $75 million on February 11, 2019). Proceeds from the New Credit Facilities were primarily used to repay the Former Senior Secured Credit Facilities. As of June 30, 2019, we had $241.3 million of indebtedness outstanding under our New Credit Facilities, consisting of $222.0 million outstanding under our New Term Loan Facility (net of unamortized discount of $4.2 million) and $19.3 million outstanding under our New Revolving Credit Facility.

In order to service this indebtedness and any additional indebtedness we may incur in the future, we need to generate cash. Our ability to generate cash is subject, to a certain extent, to our ability to successfully execute our business strategy, as well as general economic, financial, competitive, regulatory and other factors beyond our control. We cannot assure you that our business will be able to generate sufficient cash flow from operations or that future borrowings or other financing will be available to us in an amount sufficient to enable us to service our indebtedness and fund our other liquidity needs. To the extent we are required to use our cash flow from operations or the proceeds of any future financing to service our indebtedness instead of funding working capital, capital expenditures or other general corporate purposes, we will be less able to plan for, or react to, changes in our business, industry and in the economy generally. This will place us at a competitive disadvantage compared to our competitors that have less indebtedness.

In addition, the Credit Agreement contains, and any agreements evidencing or governing other future indebtedness may contain, certain restrictive covenants that limit our ability, among other things, to engage in certain activities that are in our long-term best interests, including our ability to:

- incur additional indebtedness;
- incur certain liens;
- consolidate, merge or sell or otherwise dispose of our assets;
- alter the business conducted by us and our subsidiaries;
- make investments, loans, advances, guarantees and acquisitions;
- pay dividends or make other distributions on equity interests, or redeem, repurchase or retire equity interests;

- enter into transactions with our affiliates;
- enter into agreements restricting our subsidiaries' ability to pay dividends;
- issue or sell equity interests or securities convertible into or exchangeable for equity interests;
- redeem, repurchase or refinance our other indebtedness; and
- amend or modify our governing documents.

The restrictive covenants in the Credit Agreement also require us to maintain specified financial ratios. While we have not previously breached and are not in breach of any of these covenants, there can be no guarantee that we will not breach these covenants in the future. Our ability to comply with these covenants and restrictions may be affected by events and factors beyond our control. Our failure to comply with any of these covenants or restrictions could result in an event of default under our credit facilities. This would permit the lending banks under such facilities to take certain actions, including terminating all outstanding commitments and declaring all amounts due under our credit agreement to be immediately due and payable, including all outstanding borrowings, accrued and unpaid interest thereon, and prepayment premiums with respect to such borrowings and any terminated commitments. In addition, the lenders would have the right to proceed against the collateral we granted to them, which includes substantially all of our assets. The occurrence of any of these events could have a material adverse effect on our business, financial condition and results of operations.

We may not be able to secure additional financing on favorable terms, or at all, to meet our future capital needs.

In the future, we may require additional capital to respond to business opportunities, challenges, acquisitions or unforeseen circumstances, and may determine to engage in equity or debt financings or enter into credit facilities or refinance existing indebtedness for other reasons. We may not be able to timely secure additional debt or equity financing on favorable terms, or at all. As discussed above, the Credit Agreement contains restrictive covenants that limit our ability to incur additional indebtedness and engage in other capital-raising activities. Any debt financing obtained by us in the future could involve covenants that further restrict our capital raising activities and other financial and operational matters, which may make it more difficult for us to operate our business, obtain additional capital and pursue business opportunities, including potential acquisitions. Furthermore, if we raise additional funds through the issuance of equity or convertible debt or other equity-linked securities, our existing stockholders could suffer significant dilution. If we are unable to obtain adequate financing or financing on terms satisfactory to us, when we require it, our ability to continue to grow or support our business and to respond to business challenges could be significantly limited.

Uncertainty relating to the LIBOR calculation process and potential phasing out of LIBOR after 2021 may adversely affect the market value of our current or future debt obligations.

The London Inter-bank Offered Rate ("LIBOR") and certain other interest "benchmarks" may be subject to regulatory guidance and/or reform that could cause interest rates under our current or future debt agreements to perform differently than in the past or cause other unanticipated consequences. The United Kingdom's Financial Conduct Authority, which regulates LIBOR, has announced that it intends to stop encouraging or requiring banks to submit LIBOR rates after 2021, and it is unclear if LIBOR will cease to exist or if new methods of calculating LIBOR will evolve. If LIBOR ceases to exist or if the methods of calculating LIBOR change from their current form, interest rates on our debt obligations under our New Credit Facilities may be adversely affected.

Any impairment in the value of our goodwill or other assets would adversely affect our financial condition and results of operations.

We are required, at least annually, or as facts and circumstances warrant, to test goodwill and other assets to determine if impairment has occurred. Impairment may result from any number of factors, including adverse changes in assumptions used for valuation purposes, such as actual or projected net sales growth rates, profitability or discount rates, or other variables. If the testing indicates that impairment has occurred, we are required to record a non-cash impairment charge for the difference between the carrying value of the goodwill or other assets and the implied fair value of the goodwill or the fair value of other assets in the period the determination is made. We cannot always predict the amount and timing of any impairment of assets. Should the value of goodwill or other assets become impaired, it would have an adverse effect on our financial condition and results of operations.

Risks Relating to Our Organizational Structure

ACON has significant influence over us, including over decisions that require the approval of stockholders, and its interests, along with the interests of our other Continuing Equity Owners, in our business may conflict with the interests of our other stockholders.

Each share of our Class A common stock and Class B common stock entitles its holders to one vote per share on all matters presented to our stockholders. As of August 6, 2019, ACON holds approximately 47.7% of the combined voting power of our common stock through its ownership of 12,921,039 shares of our Class A common stock and 10,495,687 shares of our Class B common stock. Accordingly, ACON will have significant influence over substantially all transactions and other matters submitted to a vote of our stockholders, such as a merger, consolidation, dissolution or sale of all or substantially all of our assets, the issuance or redemption of certain additional equity interests, and the election of directors. This influence may increase the likelihood that we will consummate transactions that are not in the best interests of holders of our Class A common stock or, conversely, prevent the consummation of transactions that are in the best interests of holders of our Class A common stock.

Additionally, the Continuing Equity Owners who, as of August 6, 2019, collectively hold approximately 64.7% of the combined voting power of our common stock, may receive payments from us under the Tax Receivable Agreement in connection with our purchase of common units of FAH, LLC directly from certain of the Continuing Equity Owners upon a redemption or exchange of their common units in FAH, LLC, including the issuance of shares of our Class A common stock upon any such redemption or exchange. As a result, the interests of the Continuing Equity Owners may conflict with the interests of holders of our Class A common stock. For example, the Continuing Equity Owners may have different tax positions from us which could influence their decisions regarding whether and when to dispose of assets, whether and when to incur new or refinance existing indebtedness, and whether and when we should terminate the Tax Receivable Agreement and accelerate our obligations thereunder. In addition, the structuring of future transactions may take into consideration tax or other considerations of the Continuing Equity Owners even in situations where no similar considerations are relevant to us.

In addition, pursuant to the Stockholders Agreement between Funko, Inc., ACON, Fundamental and Brian Mariotti, our chief executive officer (the “Stockholders Agreement”), ACON has the right to designate certain of our directors, which we refer to as the ACON Directors, which will be three ACON Directors for as long as ACON directly or indirectly, beneficially owns, in the aggregate 35% or more of our Class A common stock, two ACON Directors for so long as ACON, directly or indirectly, beneficially owns, in the aggregate, less than 35% but at least 25% or more of our Class A common stock and one ACON Director for as long as ACON, directly or indirectly, beneficially owns, in the aggregate, less than 25% but at least 15% or more of our Class A common stock (assuming in each such case that all outstanding common units in FAH, LLC are redeemed for newly issued shares of our Class A common stock on a one-for-one basis). Each of ACON, Fundamental, and Brian Mariotti, our chief executive officer, will also agree to vote, or cause to vote, all of their outstanding shares of our Class A common stock and Class B common stock at any annual or special meeting of stockholders in which directors are elected, so as to cause the election of the ACON Directors and Mr. Mariotti for as long as he is our chief executive officer. Additionally, pursuant to the Stockholders Agreement, we shall take all commercially reasonable action to cause (1) the board of directors to be comprised of at least seven directors or such other number of directors as our board of directors may determine; (2) the individuals designated in accordance with the terms of the Stockholders Agreement to be included in the slate of nominees to be elected to the board of directors at the next annual or special meeting of our stockholders at which directors are to be elected and at each annual meeting of our stockholders thereafter at which a director’s term expires; (3) the individuals designated in accordance with the terms of the Stockholders Agreement to fill the applicable vacancies on the board of directors; and (4) an ACON Director to be the chairperson of the board of directors (as defined in the amended and restated bylaws).

In addition, the Stockholders Agreement provides that for as long as ACON or certain related parties, as defined in the Stockholders Agreement (the "ACON Related Parties"), beneficially own, directly or indirectly, in the aggregate, 30% or more of all issued and outstanding shares of our Class A common stock (assuming that all outstanding common units in FAH, LLC are redeemed for newly issued shares of our Class A common stock on a one-for-one basis), we will not take, and will cause our subsidiaries not to take, certain actions or enter into certain transactions (whether by merger, consolidation, or otherwise) without the prior written approval of ACON and each of its affiliated funds that hold common units of FAH, LLC or our Class A common stock, including:

- entering into any transaction or series of related transactions in which any person or group (other than the ACON Related Parties and any group that includes the ACON Related Parties, Fundamental (or certain of its affiliates or permitted transferees) or Mr. Mariotti) acquires, directly or indirectly, in excess of 50% of the then outstanding shares of any class of our or our subsidiaries' capital stock, or following which any such person or group has the direct or indirect power to elect a majority of the members of our board of directors or to replace us as the sole manager of FAH, LLC (or to add another person as co-manager of FAH, LLC);
- the reorganization, recapitalization, voluntary bankruptcy, liquidation, dissolution or winding up of us or any of our subsidiaries;
- the sale, lease or exchange of all or substantially all of our and our subsidiaries' property and assets;
- the resignation, replacement or removal of us as the sole manager of FAH, LLC, or the appointment of any additional person as a manager of FAH, LLC;
- any acquisition or disposition of our or any of our subsidiaries' assets for aggregate consideration in excess of $10.0 million in a single transaction or series of related transactions (other than transactions solely between or among us and our direct or indirect wholly owned subsidiaries);
- the creation of a new class or series of capital stock or other equity securities of us or any of our subsidiaries;
- the issuance of additional shares of Class A common stock, Class B common stock, preferred stock or other equity securities of us or any of our subsidiaries other than (1) under any stock option or other equity compensation plan approved by our board of directors or the compensation committee, (2) pursuant to the exercise or conversion of any options, warrants or other securities existing as of the date of the Stockholders Agreement and (3) in connection with any redemption of common units of FAH, LLC pursuant to the FAH LLC Agreement;
- any amendment or modification of our or any of our subsidiaries' organizational documents, other than the FAH LLC Agreement, which shall be subject to amendment or modification solely in accordance with the terms set forth herein; and
- any increase or decrease of the size of our board of directors.

We are a "controlled company" within the meaning of the Nasdaq rules and, as a result, will qualify for, and intend to rely on, exemptions from certain corporate governance requirements. You will not have the same protections afforded to stockholders of companies that are subject to such corporate governance requirements.

Pursuant to the terms of the Stockholders Agreement, ACON, Fundamental and Brian Mariotti, our chief executive officer, in the aggregate, have more than 50% of the voting power for the election of directors, and, as a result, we are considered a "controlled company" for the purposes of the Nasdaq rules. As such, we qualify for, and may rely on, exemptions from certain corporate governance requirements, including the requirements to have a majority of "independent directors" as defined under the Nasdaq rules on our board of directors, an entirely independent nominating and corporate governance committee with a written charter addressing the committee's purpose and responsibilities, and an entirely independent compensation committee with a written charter addressing the committee's purpose and responsibilities.

The corporate governance requirements and specifically the independence standards are intended to ensure that directors who are considered independent are free of any conflicting interest that could influence their actions as directors. As a result of our reliance on the foregoing "controlled company" exemptions, you may not have the same protections afforded to stockholders of companies that are subject to all of the corporate governance requirements of the Nasdaq rules.

Our amended and restated certificate of incorporation provides that the doctrine of "corporate opportunity" does not apply with respect to any director or stockholder who is not employed by us or our subsidiaries.

The doctrine of corporate opportunity generally provides that a corporate fiduciary may not develop an opportunity using corporate resources, acquire an interest adverse to that of the corporation or acquire property that is reasonably incident to the present or prospective business of the corporation or in which the corporation has a present or expectancy interest, unless that opportunity is first presented to the corporation and the corporation chooses not to pursue that opportunity. The doctrine of corporate opportunity is intended to preclude officers or directors or other fiduciaries from personally benefiting from opportunities that belong to the corporation. Our amended and restated certificate of incorporation provides that the doctrine of "corporate opportunity" does not apply with respect to any director or stockholder who is not employed by us or our subsidiaries. Any director or stockholder who is not employed by us or our subsidiaries therefore has no duty to communicate or present corporate opportunities to us, and has the right to either hold any corporate opportunity for their (and their affiliates') own account and benefit or to recommend, assign or otherwise transfer such corporate opportunity to persons other than us, including to any director or stockholder who is not employed by us or our subsidiaries.

As a result, certain of our stockholders, directors and their respective affiliates are not prohibited from operating or investing in competing businesses. We therefore may find ourselves in competition with certain of our stockholders, directors or their respective affiliates, and we may not have knowledge of, or be able to pursue, transactions that could potentially be beneficial to us. Accordingly, we may lose a corporate opportunity or suffer competitive harm, which could negatively impact our business or prospects.

Our principal asset consists of our interest in FAH, LLC, and accordingly, we depend on distributions from FAH, LLC to pay taxes and expenses, including payments under the Tax Receivable Agreement. FAH, LLC's ability to make such distributions may be subject to various limitations and restrictions.

Upon consummation of the IPO, we became a holding company and have no material assets other than our ownership of 30.2 million common units of FAH, LLC as of June 30, 2019, representing approximately 60.4% of the economic interest in FAH, LLC. We have no independent means of generating revenue or cash flow, and our ability to pay dividends in the future, if any, is dependent upon the financial results and cash flows of FAH, LLC and its subsidiaries and distributions we receive from FAH, LLC. There can be no assurance that our subsidiaries will generate sufficient cash flow to dividend or distribute funds to us or that applicable local law and contractual restrictions, including negative covenants in our debt instruments, will permit such dividends or distributions.

FAH, LLC is treated as a partnership for U.S. federal income tax purposes and, as such, generally is not subject to entity-level U.S. federal income tax. Instead, taxable income is allocated to holders of its common units, including us. As a result, we incur income taxes on our allocable share of net taxable income of FAH, LLC. Under the terms of the FAH LLC Agreement, FAH, LLC is obligated to make tax distributions to its members, including us, except to the extent such distributions would render FAH, LLC insolvent or are otherwise prohibited by law or any limitations or restrictions in our debt agreements. The amount of such tax distribution is calculated based on the highest combined federal, state and local tax rate that may potentially apply to any one of FAH, LLC's members, regardless of the actual final tax liability of any such member. As a result of the foregoing, FAH, LLC may be obligated to make tax distributions in excess of some or all of its members' actual tax liability, which could reduce its cash available for its business operations. In addition to tax expenses, we also incur expenses related to our operations, our interests in FAH, LLC and related party agreements, including payment obligations under the Tax Receivable Agreement and expenses and costs of being a public company, all of which could be significant. We intend, as its managing member, to cause FAH, LLC to make distributions in an amount sufficient to allow us to pay our taxes and operating expenses, including any ordinary course payments due under the Tax Receivable Agreement. However, FAH, LLC's ability to make such distributions may be subject to various limitations and restrictions including, but not limited to, restrictions on distributions that would either violate any contract or agreement to which FAH, LLC is then a party, including debt agreements, or any applicable law, or that would have the effect of rendering FAH, LLC insolvent. If FAH, LLC does not have sufficient funds to pay tax distributions or other liabilities to fund our operations, we may have to borrow funds, which could materially adversely affect our liquidity and financial condition and subject us to various restrictions imposed by any such lenders. To the extent that we are unable to make payments under the Tax Receivable Agreement for any reason, such payments will be deferred and will accrue interest until paid; provided, however, that nonpayment for a specified period may constitute a material breach of a material obligation under the Tax Receivable Agreement and therefore may accelerate payments due under the Tax Receivable Agreement. If FAH, LLC does not have sufficient funds to make distributions, our ability to declare and pay cash dividends may also be restricted or impaired. See "Risks Relating to Ownership of Our Class A Common Stock."

In certain circumstances, FAH, LLC will be required to make distributions to us and the Continuing Equity Owners, and the distributions that FAH, LLC will be required to make may be substantial.

As discussed above, under the terms of the FAH LLC Agreement, FAH, LLC is obligated to make tax distributions to us and the Continuing Equity Owners based on the highest combined federal, state and local tax rates that may potentially apply to any one member of FAH, LLC. As a result of potential differences in the amount of net taxable income allocable to us and to the Continuing Equity Holders, as well as the use of an assumed tax rate in calculating FAH, LLC's distribution obligations, we may receive distributions significantly in excess of our tax liabilities and obligations to make payments under the Tax Receivable Agreement between FAH, LLC, the Continuing Equity Owners and us. Funds we receive from FAH, LLC to satisfy its tax distribution obligations will not be available for reinvestment in our business. To the extent we do not distribute such cash balances as dividends on our Class A common stock and instead, for example, hold such cash balances or lend them to FAH, LLC, the Continuing Equity Owners would benefit from any value attributable to such accumulated cash balances as a result of their ownership of Class A common stock following an exchange of their common units for Class A common stock.

Our Tax Receivable Agreement with the Continuing Equity Owners requires us to make cash payments to them in respect of certain tax benefits to which we may become entitled, the amounts that we may be required to pay could be significant, and we may not realize such tax benefits.

In connection with the consummation of the IPO, we entered into a Tax Receivable Agreement with FAH, LLC and each of the Continuing Equity Owners. Pursuant to the Tax Receivable Agreement, we will be required to make cash payments to the Continuing Equity Owners equal to 85% of the tax benefits, if any, that we realize, or in some circumstances are deemed to realize as a result of (1) any future redemptions funded by us or exchanges (or deemed exchanges in certain circumstances) of common units for Class A common stock or cash, and (2) certain additional tax benefits attributable to payments under the Tax Receivable Agreement. The amount of the cash payments that we may be required to make under the Tax Receivable Agreement could be significant. Payments under the Tax Receivable Agreement will generally be based on the tax reporting positions that we determine, which are subject to challenge by taxing authorities. Payments made under the Tax Receivable Agreement will not be returned upon a successful challenge by a taxing authority to our reporting positions. Any payments made by us to the Continuing Equity Owners under the Tax Receivable Agreement will generally reduce the amount of overall cash flow that might have otherwise been available to us. To the extent that we are unable to make timely payments under the Tax Receivable Agreement for any reason, the unpaid amounts will be deferred and will accrue interest until paid by us. Nonpayment for a specified period may constitute a material breach of a material obligation under the Tax Receivable Agreement and therefore may accelerate payments due under the Tax Receivable Agreement. Furthermore, our future obligation to make payments under the Tax Receivable Agreement could make us a less attractive target for an acquisition, particularly in the case of an acquirer that cannot use some or all of the tax benefits that may be deemed realized under the Tax Receivable Agreement upon a change of control. The payments under the Tax Receivable Agreement are also not conditioned upon the Continuing Equity Owners maintaining a continued ownership interest in FAH, LLC.

The amounts that we may be required to pay to the Continuing Equity Owners under the Tax Receivable Agreement may be accelerated in certain circumstances and may also significantly exceed the actual tax benefits that we ultimately realize.

The Tax Receivable Agreement provides that if certain mergers, asset sales, other forms of business combination, or other changes of control were to occur, if we materially breach any of our material obligations under the Tax Receivable Agreement or if, at any time, we elect an early termination of the Tax Receivable Agreement, then the Tax Receivable Agreement will terminate and our obligations, or our successor's obligations, to make future payments under the Tax Receivable Agreement would accelerate and become immediately due and payable. In those circumstances members of FAH, LLC would be deemed to exchange any remaining outstanding common units of FAH, LLC for Class A common stock and would generally be entitled to payments under the Tax Receivable Agreement resulting from such deemed exchange. The amount due and payable in those circumstances is determined based on certain assumptions, including an assumption that we would have sufficient taxable income to fully utilize all potential future tax benefits that are subject to the Tax Receivable Agreement. We may need to incur debt to finance payments under the Tax Receivable Agreement to the extent our cash resources are insufficient to meet our obligations under the Tax Receivable Agreement.

As a result of the foregoing, we would be required to make an immediate cash payment equal to the present value of the anticipated future tax benefits that are the subject of the Tax Receivable Agreement, which payment may be made significantly in advance of the actual realization, if any, of such future tax benefits. We could also be required to make cash payments to the Continuing Equity Owners that are greater than the specified percentage of the actual benefits we ultimately realize in respect of the tax benefits that are subject to the Tax Receivable Agreement. Our obligations under the Tax Receivable Agreement could have a substantial negative impact on our liquidity and could have the effect of delaying, deferring or preventing certain mergers, asset sales, other forms of business combination, or other changes of control. There can be no assurance that we will be able to finance our obligations under the Tax Receivable Agreement.

We will not be reimbursed for any payments made to the Continuing Equity Owners under the Tax Receivable Agreement in the event that any tax benefits are disallowed.

We will not be reimbursed for any cash payments previously made to the Continuing Equity Owners pursuant to the Tax Receivable Agreement if any tax benefits initially claimed by us are subsequently challenged by a taxing authority and are ultimately disallowed. Instead, any excess cash payments made by us to a Continuing Equity Owner will be netted against any future cash payments that we might otherwise be required to make under the terms of the Tax Receivable Agreement. However, a challenge to any tax benefits initially claimed by us may not arise for a number of years following the initial time of such payment or, even if challenged early, such excess cash payment may be greater than the amount of future cash payments that we might otherwise be required to make under the terms of the Tax Receivable Agreement and, as a result, there might not be future cash payments from which to net against. The applicable U.S. federal income tax rules are complex and factual in nature, and there can be no assurance that the IRS or a court will not disagree with our tax reporting positions. As a result, it is possible that we could make cash payments under the Tax Receivable Agreement that are substantially greater than our actual cash tax savings.

If we were deemed to be an investment company under the Investment Company Act of 1940, as amended, or the 1940 Act, as a result of our ownership of FAH, LLC, applicable restrictions could make it impractical for us to continue our business as contemplated and could have a material adverse effect on our business, financial condition and results of operations.

Under Sections 3(a)(1)(A) and (C) of the 1940 Act, a company generally will be deemed to be an “investment company” for purposes of the 1940 Act if (1) it is, or holds itself out as being, engaged primarily, or proposes to engage primarily, in the business of investing, reinvesting or trading in securities or (2) it engages, or proposes to engage, in the business of investing, reinvesting, owning, holding or trading in securities and it owns or proposes to acquire investment securities having a value exceeding 40% of the value of its total assets (exclusive of U.S. government securities and cash items) on an unconsolidated basis. We do not believe that we are an “investment company,” as such term is defined in either of those sections of the 1940 Act.

As the sole managing member of FAH, LLC, we control and operate FAH, LLC. On that basis, we believe that our interest in FAH, LLC is not an “investment security” as that term is used in the 1940 Act. However, if we were to cease participation in the management of FAH, LLC, our interest in FAH, LLC could be deemed an “investment security” for purposes of the 1940 Act.

We and FAH, LLC intend to conduct our operations so that we will not be deemed an investment company. However, if we were to be deemed an investment company, restrictions imposed by the 1940 Act, including limitations on our capital structure and our ability to transact with affiliates, could make it impractical for us to continue our business as contemplated and could have a material adverse effect on our business, financial condition and results of operations.

Our organizational structure, including the Tax Receivable Agreement, confers certain benefits upon the Continuing Equity Owners that will not benefit Class A common stockholders to the same extent as it will benefit the Continuing Equity Owners.

Our organizational structure, including the Tax Receivable Agreement, confers certain benefits upon the Continuing Equity Owners that will not benefit the holders of our Class A common stock to the same extent as it will benefit such Continuing Equity Owners. We have entered into the Tax Receivable Agreement with FAH, LLC and the Continuing Equity Owners and it provides for the payment by us to the Continuing Equity Owners of 85% of the amount of tax benefits, if any, that we realize, or in some circumstances are deemed to realize, as a result of (1) any future redemptions funded by us or exchanges (or deemed exchanges in certain circumstances) of common units for Class A common stock or cash and (2) certain additional tax benefits attributable to payments under the Tax Receivable Agreement. This and other aspects of our organizational structure may adversely impact the future trading market for our Class A common stock.

Risks Relating to Ownership of Our Class A Common Stock

The Continuing Equity Owners own common units in FAH, LLC, and the Continuing Equity Owners will have the right to redeem their common units in FAH, LLC pursuant to the terms of the FAH LLC Agreement for shares of Class A common stock or cash.

As of August 6, 2019, we had an aggregate of 168,645,326 shares of Class A common stock authorized but unissued, as well as approximately 18,737,808 shares of Class A common stock issuable, at our election, upon redemption of FAH, LLC common units held by the Continuing Equity Owners. FAH, LLC has entered into the FAH LLC Agreement, and subject to certain restrictions set forth in such agreement, the Continuing Equity Owners are entitled to have their common units redeemed from time to time at each of their options (subject in certain circumstances to time-based vesting requirements) for, at our election, newly-issued shares of our Class A common stock on a one-for-one basis or a cash payment equal to a volume weighted average market price of one share of Class A common stock for each common unit redeemed, in each case, in accordance with the terms of the FAH LLC Agreement; provided that, at our election, we may effect a direct exchange by us of such Class A common stock or such cash, as applicable, for such common units. The Continuing Equity Owners may exercise such redemption right for as long as their common units remain outstanding. We also entered into a Registration Rights Agreement pursuant to which the shares of Class A common stock issued to certain of the Continuing Equity Owners (including each of our executive officers) upon such redemption and the shares of Class A common stock issued to the Former Equity Owners in connection with the Transactions will be eligible for resale, subject to certain limitations set forth in the Registration Rights Agreement.

We cannot predict the size of future issuances of our Class A common stock or the effect, if any, that future issuances and sales of shares of our Class A common stock may have on the market price of our Class A common stock. Sales or distributions of substantial amounts of our Class A common stock, including shares issued in connection with an acquisition, or the perception that such sales or distributions could occur, may cause the market price of our Class A common stock to decline.

You may be diluted by future issuances of additional Class A common stock or common units in connection with our incentive plans, acquisitions or otherwise; future sales of such shares in the public market, or the expectations that such sales may occur, could lower our stock price.

Our amended and restated certificate of incorporation authorizes us to issue shares of our Class A common stock and options, rights, warrants and appreciation rights relating to our Class A common stock for the consideration and on the terms and conditions established by our board of directors in its sole discretion, whether in connection with acquisitions or otherwise. In addition, we, FAH, LLC and the Continuing Equity Owners are party to the FAH LLC Agreement under which the Continuing Equity Owners (or certain permitted transferees thereof) have the right (subject to the terms of the FAH LLC Agreement) to have their common units redeemed from time to time at each of their options (subject in certain circumstances to time-based vesting requirements) by FAH, LLC in exchange for, at our election, newly-issued shares of our Class A common stock on a one-for-one basis or a cash payment equal to a volume-weighted average market price of one share of Class A common stock for each common unit redeemed, in each case, in accordance with the terms of the FAH LLC Agreement; provided that, at our election, we may effect a direct exchange by us of such Class A common stock or such cash, as applicable, for such common units. The Continuing Equity Owners may exercise such redemption right for as long as their common units remain outstanding. The market price of shares of our Class A common stock could decline as a result of these redemptions or exchanges or the perception that a redemption or exchange could occur. These redemptions or exchanges, or the possibility that these redemptions or exchanges may occur, also might make it more difficult for holders of our Class A common stock to sell such stock in the future at a time and at a price that they deem appropriate. We have reserved for issuance 5,518,518 shares of Class A common stock under our 2017 Plan, including, as of June 30, 2019, 2,655,507 shares of Class A common stock underlying stock options we granted to certain of our directors, executive officers and other employees and 1,697,694 shares of Class A common stock underlying restricted stock units we granted to certain of our executive officers and other employees. Any shares of Class A common stock that we issue, including under our 2017 Plan or other equity incentive plans that we may adopt in the future, would dilute the percentage ownership held by the holders of our Class A common stock.

In the future, we may also issue additional securities if we need to raise capital, including, but not limited to, in connection with acquisitions, which could constitute a material portion of our then-outstanding shares of Class A common stock. Further, in connection with the completion of the IPO, we entered into a Registration Rights Agreement with certain of the Original Equity Owners (including each of our executive officers). On April 20, 2019, we filed a preliminary shelf registration statement on Form S-3 (as amended on May 13, 2019, the "Form S-3") with the SEC. If declared effective by the SEC, it will allow us to sell from time-to-time up to $100.0 million of Class A common stock, preferred stock, debt securities, warrants, purchase contracts or units comprised of any combination of these securities for our own account and will allow certain Original Equity Owners to sell 31,934,185 shares of Class A common stock in one or more offerings.

If we offer and sell Class A common stock under the Form S-3, it would dilute the percentage ownership held by the existing holders of our Class A common stock. Any sales in connection with the Registration Rights Agreement, or the prospect of any such sales, could materially impact the market price of our Class A common stock and could impair our ability to raise capital through future sales of equity securities.

Our Class A common stock price may be volatile or may decline regardless of our operating performance and you may not be able to resell your shares at or above the price you paid for them.

Volatility in the market price of our Class A common stock may prevent you from being able to sell your shares at or above the price you paid for them. Many factors, which are outside our control, may cause the market price of our Class A common stock to fluctuate significantly, including those described elsewhere in this "Risk Factors" section, as well as the following:

- our operating and financial performance and prospects;
- our quarterly or annual earnings or those of other companies in our industry compared to market expectations;
- conditions that impact demand for our products;
- future announcements concerning our business, our customers' businesses or our competitors' businesses;
- the public's reaction to our press releases, other public announcements and filings with the SEC;
- the market's reaction to our reduced disclosure and other requirements as a result of being an "emerging growth company" under the Jumpstart Our Business Startups Act ("JOBS Act");
- the size of our public float;
- coverage by or changes in financial estimates by securities analysts or failure to meet their expectations;
- market and industry perception of our success, or lack thereof, in pursuing our growth strategy;
- strategic actions by us or our competitors, such as acquisitions or restructurings;
- changes in laws or regulations which adversely affect our industry, our licensors or us;
- changes in accounting standards, policies, guidance, interpretations or principles;
- changes in senior management or key personnel;
- issuances, exchanges or sales, or expected issuances, exchanges or sales of our capital stock;
- changes in our dividend policy;
- adverse resolution of new or pending litigation against us, and the imposition of fines or other remedial measures as a result of the underpayment of customs duties at Loungefly; and
- changes in general market, economic and political conditions in the United States and global economies or financial markets, including those resulting from natural disasters, terrorist attacks, acts of war and responses to such events.

As a result, volatility in the market price of our Class A common stock may prevent investors from being able to sell their Class A common stock at or above the price they paid for them or at all. These broad market and industry factors may materially reduce the market price of our Class A common stock, regardless of our operating performance. In addition, price volatility may be greater if the public float and trading volume of our Class A common stock is low. As a result, you may suffer a loss on your investment.

We do not intend to pay dividends on our Class A common stock for the foreseeable future.

We currently intend to retain all available funds and any future earnings to fund the development and growth of our business and to repay indebtedness. As a result, we do not anticipate declaring or paying any cash dividends on our Class A common stock in the foreseeable future. Any decision to declare and pay dividends in the future will be made at the discretion of our board of directors and will depend on, among other things, our business prospects, results of operations, financial condition, cash requirements and availability, industry trends and other factors that our board of directors may deem relevant. Any such decision will also be subject to compliance with contractual restrictions and covenants in the agreements governing our current and future indebtedness. Our New Credit Facilities contain certain covenants that restrict the ability of FAH, LLC and its subsidiaries to pay dividends or make distributions. Because we are a holding company, our ability to pay dividends on our Class A common stock depends on our receipt of cash distributions from FAH, LLC and, through FAH, LLC, cash distributions and dividends from our other direct and indirect wholly owned subsidiaries. In addition, we may incur additional indebtedness, the terms of which may further restrict or prevent us from paying dividends on our Class A common stock. As a result, you may have to sell some or all of your Class A common stock after price appreciation in order to generate cash flow from your investment, which you may not be able to do. Our inability or decision not to pay dividends, particularly when others in our industry have elected to do so, could also adversely affect the market price of our Class A common stock.

Delaware law and certain provisions in our amended and restated certificate of incorporation and our amended and restated bylaws may prevent efforts by our stockholders to change the direction or management of our company.

We are a Delaware corporation, and the anti-takeover provisions of Delaware law impose various impediments to the ability of a third party to acquire control of us, even if a change of control would be beneficial to our existing stockholders. In addition, our amended and restated certificate of incorporation and our amended and restated bylaws contain provisions that may make the acquisition of our company more difficult without the approval of our board of directors, including, but not limited to, the following:

- our board of directors is classified into three classes, each of which serves for a staggered three-year term;
- only the chairperson of our board of directors or a majority of our board of directors may call special meetings of our stockholders, except that at such time as ACON, certain of its affiliates and their permitted transferees, which we collectively refer to as the ACON Related Parties, directly or indirectly, beneficially own in the aggregate, 35% or more of all shares of Class A common stock (including for this purpose all shares of Class A common stock issuable upon redemption of common units, assuming all such common units are redeemed for Class A common stock on a one-for-one basis) issued and outstanding, the holders of a majority in voting power of the outstanding shares of our capital stock may also call special meetings of our stockholders;
- we have authorized undesignated preferred stock, the terms of which may be established and shares of which may be issued without stockholder approval;
- any action required or permitted to be taken by our stockholders at an annual meeting or special meeting of stockholders may be taken without a meeting, without prior notice and without a vote, if a written consent is signed by the holders of our outstanding shares of common stock representing not less than the minimum number of votes that would be necessary to authorize such action at a meeting at which all outstanding shares of common stock entitled to vote thereon were present and voted, provided that at such time as the ACON Related Parties, directly or indirectly, beneficially own in the aggregate, less than 35% of all shares of Class A common stock (including for this purpose all shares of Class A common stock issuable upon redemption of common units, assuming all such common units are redeemed for Class A common stock on a one-for-one basis) issued and outstanding, any action required or permitted to be taken by our stockholders at an annual meeting or special meeting of stockholders may not be taken by written consent in lieu of a meeting;
- our amended and restated certificate of incorporation may be amended or repealed by the affirmative vote of a majority of the votes which all our stockholders would be eligible to cast in an election of directors and our amended and restated bylaws may be amended or repealed by a majority vote of our board of directors or by the affirmative vote of a majority of the votes which all our stockholders would be eligible to cast in an election of directors, provided that at such time as the ACON Related Parties, directly or indirectly, beneficially own in the aggregate, less than 35% of all shares of Class A common stock (including for this purpose all shares of Class A common stock issuable upon redemption of common units, assuming all such common units are redeemed for Class A common stock on a one-for-one basis) issued and outstanding, our amended and restated certificate of incorporation and our amended and restated bylaws may be amended or repealed by the affirmative vote of the holders of at least $66\frac{2}{3}\%$ of the votes which all our stockholders would be entitled to cast in any annual election of directors and our amended and restated bylaws may also be amended or repealed by a majority vote of our board of directors;
- we require advance notice and duration of ownership requirements for stockholder proposals; and
- we have opted out of Section 203 of the Delaware General Corporation Law of the State of Delaware, or the DGCL, however, our amended and restated certificate of incorporation will contain provisions that are similar to Section 203 of the DGCL (except with respect to ACON and Fundamental and any of their respective affiliates and any of their respective direct or indirect transferees of Class B common stock).

These provisions could discourage, delay or prevent a transaction involving a change in control of our company. These provisions could also discourage proxy contests and make it more difficult for you and other stockholders to elect directors of your choosing and cause us to take other corporate actions you desire, including actions that you may deem advantageous, or negatively affect the trading price of our Class A common stock. In addition, because our board of directors is responsible for appointing the members of our management team, these provisions could in turn affect any attempt by our stockholders to replace current members of our management team.

Please see “Risks Relating to Our Organizational Structure—ACON has significant influence over us, including over decisions that require the approval of stockholders, and its interests, along with the interests of our other Continuing Equity Owners, in our business may conflict with the interests of our other stockholders.”

Our amended and restated certificate of incorporation provides, subject to certain exceptions, that the Court of Chancery of the State of Delaware will be the sole and exclusive forum for certain stockholder litigation matters, which could limit our stockholders’ ability to obtain a favorable judicial forum for disputes with us or our directors, officers, employees or stockholders.

Our amended and restated certificate of incorporation provides, subject to limited exceptions, that the Court of Chancery of the State of Delaware will, to the fullest extent permitted by law, be the sole and exclusive forum for (1) any derivative action or proceeding brought on our behalf; (2) any action asserting a claim of breach of a fiduciary duty owed by any of our directors, officers or other employees to us or our stockholders; (3) any action asserting a claim against us, any director or our officers and employees arising pursuant to any provision of the DGCL, our amended and restated certificate of incorporation or our amended and restated bylaws, or as to which the DGCL confers exclusive jurisdiction on the Court of Chancery; or (4) any action asserting a claim against us, any director or our officers or employees that is governed by the internal affairs doctrine. This provision would not apply to suits brought to enforce a duty or liability created by the Exchange Act, Securities Act, or, in each case, the rules and regulations thereunder, or any other claim for which the U.S. federal courts have exclusive jurisdiction. Any person or entity purchasing or otherwise acquiring any interest in shares of our capital stock shall be deemed to have notice of and to have consented to the provisions of our amended and restated certificate of incorporation described above. This choice of forum provision may limit a stockholder’s ability to bring a claim in a judicial forum that it finds favorable for disputes with us or any of our directors, officers, other employees or stockholders which may discourage lawsuits with respect to such claims. Alternatively, if a court were to find the choice of forum provision that will be contained in our amended and restated certificate of incorporation to be inapplicable or unenforceable in an action, we may incur additional costs associated with resolving such action in other jurisdictions, which could materially adversely affect our business, financial condition and results of operations.

We may issue shares of preferred stock in the future, which could make it difficult for another company to acquire us or could otherwise adversely affect holders of our Class A common stock, which could depress the price of our Class A common stock.

Our amended and restated certificate of incorporation authorizes us to issue one or more series of preferred stock. Our board of directors has the authority to determine the preferences, limitations and relative rights of the shares of preferred stock and to fix the number of shares constituting any series and the designation of such series, without any further vote or action by our stockholders. Our preferred stock could be issued with voting, liquidation, dividend and other rights superior to the rights of our Class A common stock. The potential issuance of preferred stock may delay or prevent a change in control of us, discouraging bids for our Class A common stock at a premium to the market price, and materially and adversely affect the market price and the voting and other rights of the holders of our Class A common stock.

Taking advantage of the reduced disclosure requirements applicable to “emerging growth companies” may make our Class A common stock less attractive to investors.

The JOBS Act provides that, for so long as a company qualifies as an “emerging growth company,” it will, among other things:

- be exempt from the provisions of Section 404(b) of the Sarbanes-Oxley Act of 2002, as amended, or the Sarbanes-Oxley Act, requiring that its independent registered public accounting firm provide an attestation report on the effectiveness of its internal control over financial reporting;
- be exempt from the “say on pay” and “say on golden parachute” advisory vote requirements of the Dodd-Frank Wall Street Reform and Customer Protection Act, or the Dodd-Frank Act;

- be exempt from certain disclosure requirements of the Dodd-Frank Act relating to compensation of its executive officers and be permitted to omit the detailed compensation discussion and analysis from the proxy statements and reports it files under the Securities Exchange Act of 1934, as amended (the “Exchange Act”); and
- be exempt from any rules that may be adopted by the Public Company Accounting Oversight Board requiring mandatory audit firm rotations or a supplement to the auditor’s report on our financial statements.

We currently have chosen to take advantage of each of the exemptions described above. We have irrevocably elected not to take advantage of the extension of time to comply with new or revised financial accounting standards available under Section 107(b) of the JOBS Act. We could be an emerging growth company until December 31, 2022. We cannot predict if investors will find our Class A common stock less attractive if we elect to rely on these exemptions, or if taking advantage of these exemptions would result in less active trading or more volatility in the price of our Class A common stock.

The obligations associated with being a public company require significant resources and management attention, which may divert from our business operations.

As a result of our IPO, we became subject to the reporting requirements of the Exchange Act and the Sarbanes-Oxley Act. The Exchange Act requires that we file annual, quarterly and current reports with respect to our business and financial condition. The Sarbanes-Oxley Act requires, among other things, that we establish and maintain effective internal control over financial reporting. As a result, we now incur significant legal, accounting and other expenses that we did not previously incur. Additionally, most of our management team, including our chief executive officer and chief financial officer, have not previously managed a publicly traded company, and as a result, have little experience in complying with the increasingly complex and changing legal and regulatory landscape in which public companies operate. Furthermore, while certain members of our board of directors have been officers and other employees of public companies, only one of our directors has previously served on the board of directors of a public company. Our entire management team and many of our other employees now need to devote substantial time to compliance and may not be able to effectively or efficiently manage us our transition into a public company.

In addition, establishing and maintaining the corporate infrastructure demanded of a public company may also divert management’s attention from implementing our business strategy, which could prevent us from improving our business, results of operations and financial condition. We have made, and will continue to make, changes to our internal control over financial reporting, including information technology controls, and procedures for financial reporting and accounting systems to meet our reporting obligations as a public company. However, the measures we take may not be sufficient to satisfy our obligations as a public company. If we do not continue to develop and implement the right processes and tools to manage our changing enterprise and maintain our culture, our ability to compete successfully and achieve our business objectives could be impaired, which could negatively impact our business, financial condition and results of operations. In addition, we cannot predict or estimate the amount of additional costs we may incur to comply with these requirements. We anticipate that these costs will materially increase our general and administrative expenses.

Furthermore, as a public company, we have incurred and will continue to incur additional legal, accounting and other expenses that have not been reflected in historical financial statements. In addition, rules implemented by the SEC have imposed various requirements on public companies, including establishment and maintenance of effective disclosure and financial controls and changes in corporate governance practices. Our management and other personnel will need to devote a substantial amount of time to these compliance initiatives. These rules and regulations result in our incurring legal and financial compliance costs and will make some activities more time-consuming and costly. For example, we expect these rules and regulations to make it more difficult and more expensive for us to obtain director and officer liability insurance, and we may be required to accept reduced policy limits and coverage or incur substantially higher costs to obtain the same or similar coverage. As a result, it may be more difficult for us to attract and retain qualified people to serve on our board of directors and our board committees or as executive officers.

As a public reporting company, we are subject to rules and regulations established from time to time by the SEC regarding our internal control over financial reporting. The failure to establish and maintain effective internal control over financial reporting and disclosure controls and procedures may cause us to not be able to accurately or timely report our financial results.

Under Section 404(a) of the Sarbanes-Oxley Act our management is required to assess and report annually on the effectiveness of our internal control over financial reporting and identify any material weaknesses in our internal control over financial reporting. Once we are no longer an emerging growth company, Section 404(b) of the Sarbanes-Oxley Act will require our independent registered public accounting firm to issue an annual report that addresses the effectiveness of our internal control over financial reporting.

As of June 30, 2019, we have identified a material weakness in our internal control over financial reporting based on the effects of the underpayment of customs duties at Loungefly. As a result of this material weakness or any other material weakness that may be identified in the future, our senior management may be unable to conclude that we have effective internal control over financial reporting or our independent registered public accounting firm may not be able to render an unqualified opinion on management's assessment and the effectiveness of our internal control over financial reporting at such time as it is required to do so. In addition, we could be subject to sanctions or investigations by the SEC, the Nasdaq Stock Market or other regulatory authorities, a loss of public and investor confidence, and to litigation from investors and stockholders, which could have a material adverse effect on our business and our stock price. If our remedial measures are insufficient to address this material weakness, or if further material weaknesses are discovered, we may not be able to manage our business effectively or accurately report our financial performance on a timely basis, which could cause a decline in our Class A common stock price and adversely affect our results of operations and financial condition.

In addition to the remediation measures we plan to take in response to our material weakness relating to the underpayment of customs duties at Loungefly, we may need to expend additional resources and provide additional management oversight in order to establish effective disclosure controls and procedures and internal control over financial reporting. Implementing any appropriate changes to our internal controls may require specific compliance training of our employees, could entail substantial costs, take a significant period of time to complete or divert management's attention from other business concerns. These changes may not, however, ultimately be effective to achieve and maintain adequate internal controls.

We may fail to meet analyst expectations, or analysts may issue unfavorable commentary about us or our industry or downgrade our Class A common stock, which could cause the price of our Class A common stock to decline.

Our Class A common stock is traded publicly, and various securities analysts follow our company and issue reports on us. These reports include information about our historical financial results as well as the analysts' estimates of our future performance. The analysts' estimates are based upon their own independent opinions and may be different from our own estimates or expectations. If our operating results are below the estimates or expectations of public market analysts and investors, the trading price of our Class A common stock could decline. In addition, one or more analysts could cease to cover our company, which could cause us to lose visibility in the market, and one or more analysts could downgrade our Class A common stock or issue other negative commentary about our company or our industry. As a result of one or more of these factors, the trading price of our Class A common stock could decline.

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

None.

Item 5. Other Information

As described in Part I, Item 4. Controls and Procedures, we have identified a material weakness in our internal control over financial reporting as of June 30, 2019. We have concluded that this material weakness also existed as of December 31, 2018 and March 31, 2019. Accordingly, the previous conclusions included in Item 9A of our Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 6, 2019 that our disclosure controls and procedures and internal control over financial reporting were effective are hereby updated to conclude that our disclosure controls and procedures and internal control over financial reporting as of December 31, 2018 were ineffective. Also, the previous conclusion included in Item 4 of our Quarterly Report on Form 10-Q filed with the Securities and Exchange Commission on May 3, 2019 that our disclosure controls and procedures were effective is hereby updated to conclude that our disclosure controls and procedures as of March 31, 2019 were ineffective.

Item 6. Exhibits

EXHIBIT INDEX

Exhibit Number	Exhibit Description	Incorporated by Reference				Filed/ Furnished Herewith
		Form	File No.	Exhibit	Filing Date	
3.1	Amended and Restated Certificate of Incorporation of Funko, Inc.	S-8	333-221390	4.1	11/7/17	
3.2	Amended and Restated Bylaws of Funko, Inc.	S-8	333-221390	4.2	11/7/17	
10.1	Funko, Inc. 2019 Incentive Award Plan.	8-K	001-38724	10.1	6/27/2019	
31.1	Certification of Chief Executive Officer pursuant to Rules 13a-14(a)/15d-14(a) under the Securities Exchange Act of 1934, as amended.					*
31.2	Certification of Chief Financial Officer pursuant to Rules 13a-14(a)/15d-14(a) under the Securities Exchange Act of 1934, as amended.					*
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.					**
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.					**
101.INS	XBRL Instance Document.					***
101.SCH	XBRL Taxonomy Extension Schema Document.					***
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.					***
101.DEF	XBRL Taxonomy Definition Linkbase Document.					***
101.LAB	XBRL Taxonomy Label Linkbase Document.					***
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.					***

* Filed herewith
** Furnished herewith
*** Submitted electronically herewith

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.

FUNKO, INC.
(Registrant)

Date: August 8th, 2019

By: /s/ Russell Nickel

Russell Nickel

Chief Financial Officer (Principal Financial Officer)

EXHIBIT 31.1

CERTIFICATION

I, Brian Mariotti, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Funko, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 8, 2019

/s/ Brian Mariotti
Brian Mariotti
Chief Executive Officer

EXHIBIT 31.2

CERTIFICATION

I, Russell Nickel, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Funko, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: August 8, 2019

/s/ Russell Nickel
Russell Nickel
Chief Financial Officer

EXHIBIT 32.1

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350

In connection with this Quarterly Report on Form 10-Q of Funko, Inc. (the “Company”) for the period ended June 30, 2019 (the “Report”), I, Brian Mariotti, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of my knowledge:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: August 8, 2019

/s/ Brian Mariotti
Brian Mariotti
Chief Executive Officer

EXHIBIT 32.2

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350

In connection with this Quarterly Report on Form 10-Q of Funko, Inc. (the “Company”) for the period ended June 30, 2019 (the “Report”), I, Russell Nickel, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of my knowledge:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: August 8, 2019

/s/ Russell Nickel
Russell Nickel
Chief Financial Officer