

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

FORM 10-K

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

For the fiscal year ended December 31, 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)
2802 Wetmore Avenue
Everett Washington
(Address of principal executive offices)

35-2593276
(I.R.S. Employer
Identification No.)

98201
(Zip Code)

(425) 783-3616
(Registrant's telephone number, including area code)

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

Title of each class
Class A Common Stock, \$0.0001 Par value

Trading Symbol(s)
FNKO

Name of exchange on which registered
Nasdaq

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

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

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

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

Indicate by check mark 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	<input type="checkbox"/>	Accelerated filer	<input checked="" type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>
Emerging growth company	<input checked="" type="checkbox"/>		

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 June 28, 2019, the last business day of the registrant's most recently completed second quarter, the approximate market value of the registrant's common stock held by non-affiliates was \$409.3 million.

As of March 3, 2020, the registrant had 34,944,941 shares of Class A common stock outstanding and 14,515,296 shares of Class B common stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive Proxy Statement relating to its 2020 Annual Meeting of Stockholders to be filed with the SEC within 120 days after the end of the fiscal year ended December 31, 2019 are incorporated herein by reference in Part III.

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BASIS OF PRESENTATION

As used in this Annual Report on Form 10-K (this “Form 10-K”), 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.
- “FHL” refers to Funko Holdings LLC, a Delaware limited liability company.
- “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”) and, together with the Term Loan A Facility, the “Former Senior Secured Credit Facilities”). 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 (as amended, 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” and together with the New Term Loan Facility, the “New Credit Facilities”).
- “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.
- “Tax Receivable Agreement” refers to a tax receivable agreement entered into between Funko, Inc., FAH, LLC and each of the Continuing Equity Owners as part of the Transactions, defined below.

- “*Transactions*” refers to certain organizational transactions that we effected in connection with our IPO in November 2017. See Note 18, Stockholders’ Equity of the notes to our consolidated financial statements for a description of the Transactions.
- “*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.

Presentation of Financial Information

FAH, LLC is the predecessor of the issuer, Funko, Inc., for financial reporting purposes. Funko, Inc. is the audited financial reporting entity. On October 30, 2015, ACON, through FAH, LLC, an entity formed in contemplation of the transaction, acquired a controlling interest in FHL and its subsidiary, Funko, LLC. We refer to this transaction as the “ACON Acquisition.” As a result of the ACON Acquisition, this Annual Report on Form 10-K presents certain financial information for two periods, Predecessor and Successor, which relate to the period preceding the ACON Acquisition on October 30, 2015 and the period succeeding the ACON Acquisition, respectively. References to the “Successor 2015 Period” refer to the period from October 31, 2015 through December 31, 2015 and references to the “Predecessor 2015 Period” refer to the period from January 1, 2015 through October 30, 2015. Financial information in the Predecessor 2015 Period principally relates to FHL and its subsidiary Funko, LLC.

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. All statements contained in this Annual Report on Form 10-K 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 remediation of our material weakness in internal control over financial reporting, 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 Annual Report on Form 10-K under Part II. Item 1A. “Risk Factors,” and in our other filings with the Securities and Exchange Commission (“SEC”), 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 Annual Report on Form 10-K, 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 Annual Report on Form 10-K or to conform these statements to actual results or revised expectations.

PART I

ITEM 1. BUSINESS

Funko: At the Nexus of Pop Culture

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 typically 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, handbags and homewares. With our unique style, expertise in pop culture, broad product distribution and highly accessible price points, we have developed a passionate following for our products that has underpinned our growth. We believe we sit at the nexus of pop culture—content providers value us for our broad network of retail customers, retailers value us for our broad portfolio of licensed pop culture products and pop culture insights, and consumers value us for our distinct, stylized products and the content they represent. We believe our innovative product design and market positioning have disrupted the licensed product markets and helped to define today’s pop culture products category.

Pop culture pervades modern life and almost everyone is a fan of something. In the past, pop culture fandom was often associated with stereotypical images of fans from narrow demographics, such as Star Trek fans attending conventions to speak Klingon to each other or friends getting together to play Dungeons & Dragons. Today, more quality content is available and technology innovation has made content accessible anytime, anywhere. As a result, the breadth and depth of pop culture fandom resembles, and in many cases exceeds, the type of fandom previously associated only with sports. Social media has further allowed for fans to share their love and form communities more easily than before. Everyday interactions at home, work or with friends, whether in person or through social media, are increasingly influenced by pop culture.

We have invested strategically in our relationships with key constituents in pop culture. Content providers value us for our broad network of retail customers and retailers value us for our broad portfolio of licensed pop culture products, pop culture insights and ability to drive consumer traffic. Consumers, who value us for our distinct, stylized products, remain at the center of everything we do.

- *Content Providers:* We have strong licensing relationships with many established content providers, such as Disney, HBO, LucasFilm, Marvel, Blizzard Entertainment, the National Football League and Warner Brothers. We have also recently entered into licensing relationships to develop products based on Fortnite and Pokémon. We strive to license every pop culture property that we believe is relevant to consumers. In 2019, we had license agreements with over 200 content providers covering over 800 active licensed properties. We believe our numerous licensing relationships have allowed us to build one of the largest portfolios in our industry, from which we can create multiple products based on each character within those properties. 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. For the year ended December 31, 2019, sales of our Pop! branded products grew 20% year-over-year in the United States, which is the most mature market for our Pop! branded products. We believe we have benefited from a trend of content providers consolidating their relationships to do more business with fewer licensees. We believe our track record of obtaining licenses from content providers, together with our proven ability to renew and extend the scope of our licenses, demonstrates the trust content providers place in us.
- *Retail Channels:* We sell our products through a diverse network of retail customers across multiple retail channels, including specialty retailers, mass-market retailers and e-commerce sites. We can provide our retail customers a customized product mix designed to appeal to their particular customer bases. Our current retail customers include GameStop, Amazon, Hot Topic, Target and Walmart in the United States, and Micromania, HEO, E.M.P. Merchandising and Smyths Toys, internationally. Additionally, for the year ended December 31, 2019, sales of our products on third party e-commerce websites increased 23% compared to the prior year. Retailers recognize the opportunity presented by the demand for pop culture products and are continuing to dedicate additional shelf space as well as increased presence on their e-commerce platforms to our products

and the pop culture category. Additionally, we believe some of our retail customers, such as Target and Walmart, view us as pop culture experts, and we help them manage their pop culture category. We believe we drive meaningful traffic to our retail customers' stores because our products have their own built-in fan base, are refreshed regularly creating a "treasure hunt" shopping experience for consumers, and are often supplemented with exclusive, limited-time products that are highlighted on social media. We believe these merchandising strategies create a sense of urgency with consumers that encourages repeat visits to our retail customers.

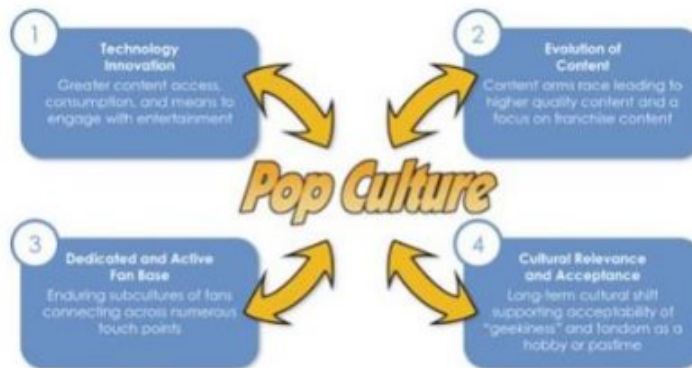
- **Consumers:** Fans are increasingly looking for ways to express their affinity for and engage with their favorite pop culture content. Over time, many of our consumers evolve from occasional buyers to more frequent purchasers, whom we categorize as enthusiasts or collectors. We estimate that enthusiasts, who are more engaged in pop culture, and collectors, who regularly purchase our products and self-identify as collectors, each make up approximately one-third of our customers. We create products to appeal to a broad array of fans across consumer demographic groups—men, women, boys and girls—not a single, narrow demographic. Most of our products are generally priced under \$10, excluding apparel and handbags, which allows our diverse consumer base to express their fandom frequently and impulsively. We continue to introduce innovative products designed to facilitate fan engagement across different price points and styles in different categories. In addition, our fans routinely express their passion for our products and brands through social media and live pop culture events, such as Comic-Con or Star Wars Celebration.

We have developed a nimble and low fixed-cost production model. The strength of our in-house creative team and relationships with content providers, retailers and third-party manufacturers allows us to move from product concept to pre-selling a new product in as few as 24 hours. We typically have a new figure on the store shelf between 110 and 200 days and can have it shipped from the factory in as few as 70 days in certain circumstances. As a result, we can dynamically manage our business to balance current content releases and pop culture trends with content based on classic evergreen properties, such as Harry Potter, Mickey Mouse or classic Batman. This has allowed us to deliver significant growth while lessening our dependence on individual content releases.

The Pop Culture Industry

Pop culture encompasses virtually everything that someone can be a fan of—movies, TV shows, video games, music and sports. The global licensed pop culture product industry in which we compete sits within the global licensed entertainment and character products market, which had \$122.7 billion in total sales in 2018 according to a Global Licensing Survey released by Licensing International. We believe that many retailers have seen traffic decline across traditional consumer categories. In contrast, demand for pop culture content, consumer products and experiences has grown rapidly.

The Forces At Work In The Pop Culture Industry



The pop culture industry is being driven by several major forces. Technology advances have made it easier to access, consume and engage with content. Content providers have produced more quality content to drive fan engagement, often with a focus on franchise properties. Dedicated, active and enduring fan bases have emerged across the pop culture landscape. These fans seek out opportunities to interact with their favorite content and with

like-minded fans through social media and content-centric experiences. At the same time, social norms have shifted, making fandom culturally accepted and mainstream. These trends reinforce one another leading to a substantial increase in pop culture fandom and to significant growth in the industry.

Technology Innovation

The proliferation of powerful mobile technology, such as tablets and smartphones, and the emergence of new content distribution services, such as Apple TV, Amazon Prime, Hulu and Netflix, have enabled fans to connect and engage with content anywhere, at any time, in larger “binge” quantities. More content and greater access have led to more fans spending more time per day consuming content. In addition, fans are able to develop a deeper affinity for content due to the increased prevalence of platforms and events where they can share their passion with other fans (such as through social media, blogs, YouTube, podcasts and online games). The accelerated pace of content discovery and sharing has created an environment where niche content can quickly become mainstream, resulting in more content becoming part of pop culture.

Evolution of Content

Content providers have increasingly focused on creating original scripted and franchise content that has broad global appeal and potential for sequels and brand extensions. During the 1990s, the top ten annual grossing movies included an average of 2.5 franchise films and from 2000 through 2018, the top ten annual grossing movies included an average of 6.6 franchise films. The growth of a healthy franchise ecosystem across content types has fostered fan loyalty and stimulated licensed product purchases. We expect the number of scripted original series to continue to grow, with content providers such as Amazon Prime, Hulu and Netflix spending or announcing the intention to spend substantial capital on new original content. For example, based on public filings, Netflix invested more than \$13 billion in content in 2018, compared to \$8.7 billion in 2016.

Dedicated and Active Fan Base

We believe pop culture fans possess distinguishing characteristics that make them highly valuable consumers. Like sports fans, fans of other forms of pop culture identify strongly with their favored properties, and have a natural tendency to form social communities around them. For context, in 2018, retail sales of licensed entertainment and character products totaled \$122.7 billion, compared to \$27.8 billion for retail sales of licensed sports products. Furthermore, as it becomes increasingly easy to access a large quantity of quality content, fans seek more ways to expand and express connectivity to their favored characters or properties as they share their passion with others. As a result, consumers are participating in the story of these properties via social media platforms and conventions, such as Comic-Con, AnimeExpo and Star Wars Celebration, rather than being solely consumers of content. By being a part of the conversation regarding their favored content, fans reinforce their love for it, thereby creating a cycle of fandom.

Growing Cultural Relevance and Acceptance

As pop culture engagement has increased, we believe it has become more culturally acceptable to be openly passionate about all forms of pop culture, not just sports. Social media is driving the importance of pop culture as fans increasingly want to engage with the content and their social communities to show affinity for pop culture content. Three of the top U.S. pop culture-related conventions, including New York Comic Con, Comic Con International: San Diego and Anime Expo 2018, drew close to half a million attendees in 2018, representing a sharp increase of over 82% from 2010. This represents a cultural shift supporting the acceptability of fan affinity for pop culture content across multiple demographic categories of fans, and the growth beyond the traditional narrow, male-dominated demographic.

Our Strategic Differentiation

Leading Design and Creative Capabilities

Our in-house creative team layers our own whimsical, fun and distinct stylization onto content providers' characters, creating unique products for which there is substantial consumer demand. With the help of our in-house creative team, we have also begun to develop our own proprietary intellectual property, including our Wetmore Forest line of characters. Our creative team also includes animators at Funko Animation Studios, who create video shorts that we have increasingly used to market our products in collaboration with some of our key licensors. In 2019 we also acquired Forrest-Pruzan Creative LLC ("FPC"), a leading board game development studio, which has enabled us to deliver a new pop culture product category to our fans. Our creative team is passionate about pop culture. We enjoy a strong pipeline of talent for our creative team given our culture and the opportunity we provide to work with the most relevant pop culture content. We believe content providers trust us with their properties, and consumers passionately engage with our products and brands because of our creativity. In addition, we reinvigorate classic evergreen or back catalog content by infusing a fresh, unique aesthetic and design into characters that enjoy enduring passion and nostalgia from fans. As a result of our creative capabilities and broad portfolio of licenses, we create a substantial number of new products each year, including approximately 5,000 new products introduced in 2019.

Diversity of Products and Accessible Price Points Create Broad Appeal

We create products to appeal to a broad array of fans across consumer demographic groups. We believe our broad appeal comes through our large selection of items, a large variety of licenses and properties and varied form factors across a number of product categories. We do not limit ourselves by targeting discrete demographics such as the stereotypical collector or the child seeking the latest (and often short-lived) toy craze. We estimate based on market and internal data that (1) occasional buyers, which we define as those consumers who are mainstream movie and TV fans, but do not self-identify as enthusiasts, (2) enthusiasts, who are more engaged in pop culture than occasional buyers but who do not self-identify as collectors, and (3) collectors each make up approximately one-third of our customers. To continue to broaden our offerings beyond figures, we have launched new or expanded categories such as plush, and accessories, and with the acquisition of FPC, we have expanded into the board game category. We believe we have one of the largest and most engaged fan bases in our industry, driven by their passion and love of our unique products and the properties we represent.

Trusted Steward of the Most Important Pop Culture Content

We strive to license every pop culture property that we believe is relevant to our consumers. Over the last decade, we have built strong relationships with content providers and currently have a catalog of content licenses covering a large number of properties that we believe is one of the industry's largest. We believe there is a trend of content providers consolidating their relationships to do more business with fewer licensees. As a trusted steward with a strong retail distribution network and connection with the end user, we believe we have benefited from this trend. We often work collaboratively with content providers in advance of new content releases to create unique, stylized products to maximize the value of their properties. In some cases, the input we have provided has influenced the content provider's creative choices for its original content. We believe we are well positioned to continue to obtain licenses for new important movie franchises and other properties. Further, we have historically been able to renew productive licenses on commercially reasonable terms, which positions us to benefit from the ongoing desire of consumers to engage with and show affinity for their favorite pop culture content.

Deep, Mutually Beneficial Relationships with a Broad Network of Retail Customers

We partner with a diverse group of retail customers through which we sell our products. We believe many of our retail customers view us as experts in pop culture and in some cases, we help manage their pop culture category within their stores and can provide a curated experience by catering to their particular customer bases. We believe this enables us to enhance the productivity of the pop culture category for our retail customers, resulting in increased sales and expanded shelf space or online placement for our products—a major driver of our growth historically. Additionally, we believe our pop culture expertise and omnichannel sales model position us well to capture the industry shift from traditional brick and mortar to channel-agnostic content consumerism. In addition, we often release exclusive new products with a specific retail customer, which can drive traffic and sales for them.

Nimble Speed to Market Reflects “Fast Fashion” Product Development Process

Speed to market has become increasingly important as technological innovation has accelerated the pace of content discovery and sharing and the speed at which niche content can become mainstream. Our flexible and low-fixed cost production model enables us to go from product design of a figure to the store shelf between 110 and 200 days and we can have it shipped from the factory in as few as 70 days, with a minimal upfront investment for most figures of \$5,000 to \$7,500 in tooling, molds and internal design costs. Because of the strength of our in-house creative team, we are able to move from product design to pre-selling certain new products in as few as 24 hours. This ability, coupled with the valuable data insights we have developed over the past decade, and the increasing use of repeated franchise properties by content providers, reduces potential product risk to us while better positioning us to benefit from trends in content creation and consumption. As an example of our “fast fashion” product development process, we announced and were able to pre-sell a Baby Yoda figure, which was a surprise character in an episode of Disney’s Star Wars: The Mandalorian, within three weeks of the episode’s original release date on Disney+.

Dynamic Business Model Drives Revenue Visibility and Growth

Our business is diversified across content providers and properties, product categories, and sales channels. As a result, we can dynamically manage our business to capitalize on pop culture trends, which has allowed us to deliver significant growth while lessening our dependence on individual content releases. Our content provider relationships are highly diversified. For the years ended December 31, 2019, 2018 and 2017, no single property accounted for more than 6%, 6% and 5% of our sales, respectively, and the portion of our sales for the years ended December 31, 2019, 2018 and 2017 attributable to our top five properties was 23%, 20% and 16%, respectively. Our products are balanced across our licensed property categories. In 2019, we generated approximately 51% of sales from classic evergreen properties, approximately 20% from movie release properties, approximately 18% from current TV properties and approximately 11% from current video game properties. In 2018, we generated approximately 47% of sales from classic evergreen properties, approximately 20% from movie release properties, approximately 17% from current video game properties and approximately 16% from current TV properties. In 2017, we generated approximately 45% of sales from classic evergreen properties, approximately 21% from movie release properties, approximately 18% from current TV properties and approximately 15% from current video game properties.

We have visibility into the new release schedule of our content providers and our expansive license portfolio allows us to dynamically manage new product creation. This allows us to adjust the mix of products based on classic evergreen properties and new releases, depending on the media release cycle. In addition, we typically sell our products worldwide through a diverse group of sales channels, including specialty retailers, distributors, mass-market retailers, e-commerce sites and direct-to-consumer sales.

Visionary Management Team and Employees with Genuine Passion for Pop Culture

Our highly experienced management team is led by Brian Mariotti, an industry pioneer. A long-time pop culture fan, Brian recognized early on the impact that trends in media and entertainment would have on the pop culture industry and the value of having a diverse portfolio of licenses. Passion for pop culture pervades our company and our openness to new ideas from anywhere in the organization has resulted in some of our most innovative and differentiated products.

How We Plan to Grow

We are pursuing the following strategies that we believe will drive substantial future growth.

Increase Sales with Existing Retail Customers

We intend to continue to increase our sales by expanding our shelf space and deepening our relationships with our retail customers. Our products have driven traffic to our retail customers’ previously less productive square footage, which has resulted in increased shelf space for our products. In addition to designing unique, stylized products that resonate with pop culture fans and drive traffic, both online and in store, we intend to increase the number of retail customers for whom we curate pop culture selections. We believe doing so deepens our relationships with our retail customers and encourages them to allocate more shelf space to our products and pop culture products generally

and, in some cases, create pop culture departments where none existed before, which we believe will drive additional brand awareness and sales growth.

Add New Retail Customers and Expand Into New Channels

We regularly evaluate and add new retail customers as we believe consumers demand Funko products regardless of the retail channel through which they purchase them. While we believe we have opportunities to add new retailers within existing channels, we also plan to selectively target new or underdeveloped sales channels, such as dollar, drug, grocery and convenience stores. By adding new retail customers, we will increase the awareness and availability of our products to consumers, which we believe will increase sales.

Broaden Our Product Offerings

In addition to designing products to address new content that licensors continually produce, we plan to add new product categories, lines and brands to leverage our existing sales channels to continue to drive sales. For example, we have recently expanded our line of figures with our 5 Star line, which can be configured in different poses and allow collectors to creatively display their figures. We also continually evaluate product innovations and potential acquisition targets to complement our existing product categories, lines and brands. In June 2017, we completed the acquisition of Loungefly, LLC (“Loungefly”), a designer of a variety of licensed pop culture fashion handbags, small leather goods and accessories, to expand and diversify our product offerings in our accessories category (the “Loungefly Acquisition”). In February 2019, we acquired FPC, a leading board game development studio, to help us expand our product offerings into the board game category.

Expand Internationally

We believe that the forces at work first observed in the U.S. pop culture industry are global. We believe we are currently underpenetrated internationally, and we generate the majority of our net sales in the United States; however, we are also focused on growing our international business. Sales generated from customers outside of the United States accounted for approximately 34%, 32% and 27% of our sales for the years ended December 31, 2019, 2018 and 2017, respectively. We are continuing to invest in the growth of our international business, primarily in Europe, both directly and through third party distributors. In the future we may pursue similar acquisitions or expand our direct sales force or distributor relationships to further penetrate Asia Pacific, Latin America, Australia or other regions.

Leverage the Funko Brand Across Multiple Channels

We believe there is a significant opportunity to leverage our distinctive style and designs across numerous underserved channels such as digital content, as well as potentially movies and television. In March 2019, we launched a new mobile application, which allows Funko fans to track their collection, display their wish list and browse an expansive catalog of our products. Additionally, we are in the process of creating an online portal that will serve as an online destination for our consumers. This online community will allow consumers to create personal avatars, purchase digital products and interact with other consumers. We believe this opportunity will drive brand awareness with new audience segments, deepen consumer engagement to drive customer lifetime value, strengthen our direct connection with our consumers and grow our direct-to-consumer business, as well as support our retail customers.

Product Lines and Licenses

We sell a broad array of licensed pop culture consumer products featuring characters from an extensive range of media and entertainment content, including movies, TV shows, video games, music and sports. Our products combine our proprietary brands and distinct designs and aesthetic sensibilities into properties we license from content providers. We seek to license content that will allow us to capitalize on the popularity of current movies, TV shows, video games, music and other content releases, as well as classic evergreen properties, which are not tied to a current release, and which are less subject to pop culture trends. We also continue to develop our own content and intellectual property, such as our Wetmore Forest property.

Our Products

Our current products principally fall within the following product categories.

Figures. Our figures category includes figures that celebrate pop culture icons in the form of stylized vinyl, blind-packed miniatures and action figures. These figures combine the pop culture properties we license with our own distinctive designs to create pop culture figures that appeal to a broad range of consumers at an affordable price point, often under one of our proprietary brands, such as Pop!, Mystery Minis, 5 Star and Pint Size Heroes.

Other. Our other category includes plush products that are soft-sculpt figures that blend licensed content with our distinctive designs to create an array of product lines and are intended for consumers of all ages; accessories products that mix pop culture fandom with functionality, and feature everything from pens and pins to buttons and keychains, all based on pop culture icons; apparel (including t-shirts and hats); homewares (including drinkware, party lights and other home accessories); stylized bags, purses and wallets and board games.

Our Brands and Designs

Under the Funko brand, we have multiple proprietary brands under which we market most of our products. Currently, our principal proprietary brands include Pop! and Loungefly. Pop!, introduced in 2010, is our most well-recognized brand. The Pop! stylized design incorporates a rounded square head that typically consists of no mouth and a very simple nose. Pop! figures typically stand about four inches tall. The Pop! brand has also been applied across all of our other product categories, including games, plush, accessories, apparel and homewares. As a brand, Pop! represented 79%, 76% and 70% of our sales in 2019, 2018, and 2017, respectively.

Loungefly, acquired in June 2017, includes fashion focused stylized handbags, backpacks, clothing, small leather goods and accessories. Loungefly products currently are based on a limited set of licenses, however, we anticipate expanding the licenses and content used to create our Loungefly products in the future.

Other brands we market under include Mystery Minis, Paka Paka, 5 Star and SuperCute. In addition, we also develop product lines that we market under the broader Funko brand, rather than under any of our proprietary brands. We typically do so when we believe our speed to market or other competitive advantages uniquely position us to take advantage of certain opportunities. While these products may not initially be associated with one of our proprietary brands, they can still reflect our whimsical and creative style, and may develop into a distinct brand over time. We also continuously develop new product designs and lines, which may develop into proprietary brands in the future.

Our Licenses

Licensors. We have strong licensing relationships with many established content providers, such as Disney, HBO, LucasFilm, Marvel, the National Football League, Universal Studios and Warner Brothers. We also seek to establish licensing relationships with newer content providers in order to capitalize on new and emerging trends in pop culture. For example, in recent years, we have established relationships and entered into licensing arrangements with Netflix and Epic Games. We believe we provide value to content providers by maximizing the lifetime value of their content by extending its relevance to consumers through ongoing fan engagement.

License Agreements. Our license agreements permit us to use the intellectual property of our licensors in connection with the products we design and sell. These license agreements typically provide that our licensors own intellectual property rights in the products we design and sell under the license, and as a result, upon termination of the license, we no longer have the right to sell these products. A number of these license agreements relate to properties that are significant to our business and operations. Our license agreements typically have terms of between two and three years and are not automatically renewable. However, we believe we have strong relationships with our licensors, and have historically been able to renew productive licenses on commercially reasonable terms.

Our license agreements require us to make royalty payments to the licensor based on our sales of the licensed product and, in some cases, require us to incur other charges. For the years ended December 31, 2019, 2018 and 2017, the average royalty rate was 15.9%, 16.1% and 14.9%, respectively. Our royalty expense for any given year will vary depending on the mix of products sold during that year. For the years ended December 31, 2019, 2018 and 2017, we incurred royalty expenses of \$126.8 million, \$110.7 million and \$77.1 million, respectively. Our licenses are generally not exclusive. In addition, the rights that licensors grant to us are typically limited to specific properties,

product categories, territories and, in some cases, sales channels. In addition, our license agreements usually require us to obtain the licensor's approval of products we develop under the license prior to making any sales. They also typically provide for a minimum guarantee that covers all licensed properties under that license agreement, a portion of which is generally required to be paid in advance, and the amount of which is negotiated based on a variety of factors, including past and expected sales and the licensor's expected line-up of new releases. Historically, we have a strong track record for meeting minimum guarantees under our license agreements. For the years ended December 31, 2019, 2018 and 2017, we recorded reserves of \$2.4 million, \$5.5 million and \$2.9 million, respectively, related to prepaid royalties we estimated would not be recovered through sales. The increase in the reserves in 2018 was primarily due to our subscription box business, which we began phasing out in 2018. In addition, 2018 reflected higher reserves for minimum guarantees on international sales.

For the year ended December 31, 2019, 13%, 11% and 11% of sales were related to the Company's three largest license agreements with no other license agreements accounting for more than 10% of sales. For the year ended December 31, 2018, 15%, 11% and 10% of sales were related to the Company's three largest license agreements with no other license agreements accounting for more than 10% of sales. For the year ended December 31, 2017, there were no license agreements that accounted for more than 10% of sales.

Licensed Properties. We strive to license every pop culture property that we believe is relevant to consumers. What we consider to be a property will vary based on the terms of the underlying license agreement. In general, we consider each content title to constitute a single property. In some instances, however, a property may consist of an entire franchise or even a single character, particularly in our classic evergreen category. We divide our licensed properties into four main categories: classic evergreen, movie release, current TV and current video game. We also license certain properties that fall outside of these four main categories.

- *Classic Evergreen.* Properties in the classic evergreen category are based on movies, TV shows, video games, music, sports or other entertainment content that is not tied to a new or current release at the time we release the product. As a result, products that we design and sell based on these properties generally do not have a defined duration of market demand. Examples of our classic evergreen properties include Star Wars, Harry Potter, DC Comics, Marvel Comics and WWE.
- *Movie Release.* Properties in the movie release category are tied to new movie releases and are intended to capitalize on the excitement of fans surrounding these releases. Products that we design and sell based on these properties are expected to have a limited duration of market demand, depending on the popularity of the movie release. Examples of our movie release properties include Avengers: Endgame, Star Wars Episode IX, and Frozen 2.
- *Current TV.* Properties in the current TV category are tied to TV shows that are currently airing new content. These properties are expected to have a market demand depending on the popularity and longevity of the TV show, which is generally expected to be between three and seven years. Examples of our current TV properties include Stranger Things, Rick & Morty, The Walking Dead and Dragonball Z.
- *Current Video Game.* Properties in the current video game category are tied to new video game releases that are intended to capitalize on the excitement of fans surrounding these releases. Products that we design and sell based on these properties are expected to have a market demand depending on the popularity and longevity of the video game, which is generally expected to be three to seven years. Examples of our current video game properties include Fortnite and Overwatch.
- *Other.* We also occasionally license properties that do not fit within the four categories described above, including those associated with current events and limited-duration pop culture phenomena, which we are able to capitalize on due to our speed to market and low cost of production.

We expect these categories and the properties they encompass to evolve over time as current content becomes classic evergreen and as new forms of pop culture content emerge. In addition, while the percentage of sales attributable to our classic evergreen properties has been between approximately 51% and 45% over the past three years, it may fluctuate in any given year based on the number and popularity of new content releases.

Product Design and Development

We believe our creative product designs and nimble speed to market are key reasons why content providers trust us with their properties and consumers passionately engage with our brands and products. We leverage our creative, art and sculpting teams to design and develop products in-house from inception to production. Our creative team layers our whimsical, fun and unique style onto the content we license to create product designs that resonate with consumers. Our creative team is passionate about pop culture, and we have a strong pipeline of talent given our culture and the opportunity we provide to work with the most relevant pop culture content. Our designers often work collaboratively with content providers in advance of new content releases to create unique, stylized products to maximize the value of their properties and, in some cases, the input we have provided has influenced the content provider's creative choices for their original content.

Our product development team oversees all aspects of new product development in order to ensure a timely product design and development process, including submitting the initial design to the content provider for approval, developing the product prototype, receiving final content provider approval and coordinating manufacturing with our supply chain team and third-party manufacturer. Our flexible and low-fixed cost production model enables us to move from product design of a figure to shipping from the factory in as few as 70 days and typically between 110 and 200 days, with a minimal upfront investment for most figures of \$5,000 to \$7,500 in tooling, molds and internal design costs. Because of the strength of our in-house creative team, we are able to move from product design to pre-selling a new product in as few as 24 hours. This ability, coupled with the valuable data insights we have developed over the past decade and the increasing use of repeated franchise properties by content providers, reduces potential product risk to us.

Manufacturing and Materials

Our products are produced by third-party manufacturers primarily in Vietnam and China, which we choose on the basis of performance, capacity, capability and price. We also manufacture or assemble certain apparel and other products in the United States and Mexico. The use of third-party manufacturers enables us to avoid incurring fixed manufacturing costs, while maximizing flexibility, capacity and capability. Though our manufacturing base has diversified over time as we have grown our sales and expanded our product offerings, we have historically concentrated production with a small number of manufacturers and factories as part of a continuing effort to monitor quality, reduce manufacturing costs and ensure speed to market. In the case of most of the factories in which our products are manufactured, our products represent a significant percentage of each factory's total capacity, which we believe provides us greater flexibility in supply chain management. We do not have long-term contracts with our manufacturers. We believe that alternative sources of supply are available to us although we cannot be assured that we can obtain adequate supplies of manufactured products on a timely basis or at all.

We base our production schedules for products on our internal forecasts, taking into account historical trends of similar products and properties, current market information and communications with customers. The accuracy of our forecasts is affected by consumer acceptance of our products, which is based on the strength of the underlying licensed property, the strength of competing products, the marketing strategies of retailers, changes in buying patterns of both our retail customers and our consumers, and overall economic conditions. Unexpected changes in these factors could result in a lack of product availability or excess inventory of a particular product.

Although we do not conduct the day-to-day manufacturing of our products, we are responsible for designing both the product and the packaging. We seek to ensure quality control by actively reviewing the product, both in-house and via image at multiple stages in development and sample finished goods to validate the quality control process. In addition to quality control testing, safety testing of our products is done by independent third-party testing laboratories.

While we purchase finished products from our manufacturers, the cost of our products is impacted by the cost of labor, as well as the cost of the principal raw materials used in the production and sale of our products, including vinyl, fabric, ceramics and plastics. All of these materials are readily available but may be subject to significant fluctuations in price. Although we do not manufacture our products, we own most of the tools and molds used in the manufacturing process, and generally these are transferable among manufacturers if we choose to employ alternative manufacturers.

Sales

We sell our products to a diverse network of customers throughout the world. Domestically, we sell our products to specialty retailers, mass-market retailers and e-commerce sites. Our key retail partners in the United States include Amazon, GameStop, Hot Topic, Target and Walmart. We also plan to target new or underdeveloped sales channels, including dollar, drug, grocery and convenience stores. Internationally, we sell our products directly to similar retailers, primarily in Europe, through our subsidiary Funko UK, Ltd. Our key international retail customers include Micromania, HEO, E.M.P. Merchandising and Smyths Toys.

In addition to major retailers, 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 currently 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. Our direct-to-consumer sales accounted for approximately 4% of our sales for both 2019 and 2018 and 6% of our sales for 2017. Though our direct-to-consumer efforts have historically represented a small portion of our net sales, we intend to increase our focus on these efforts in the future.

We believe we have a diverse customer base, with our top ten customers representing approximately 44%, 46% and 45%, of our 2019, 2018 and 2017 sales, respectively. No single customer accounted for over 10% of revenues during these periods.

We maintain a full-time sales staff, many of whom make on-site visits to our customers for the purpose of showing products and soliciting orders. Many of our retail customers view us as experts in pop culture and, in some cases, we help manage their growing pop culture category within their stores, providing a curated experience by catering to their particular customer bases. For example, we have curated products based on Dr. Seuss and Harry Potter books for Barnes & Noble, and video game-based products, such as Fallout and Overwatch, for GameStop. We believe this creates a mutually beneficial relationship between us and our retail customers by providing us with an opportunity to enhance the productivity of the pop culture category within their stores, which may also result in expanded shelf space for our products. In addition to our full-time sales staff, we also retain a number of independent sales representatives to sell and promote our products both domestically and internationally.

We sell our products to our customers with payment terms typically varying from 30 to 90 days. As discussed above, we contract the manufacture of most of our products to third-party unaffiliated manufacturers primarily located in Vietnam, China and Mexico and ship those products to our warehouse facilities in the United States and the United Kingdom. While most of our sales originate in the United States and the United Kingdom from inventory we hold in our warehouses, certain of our customers may take title to our products upon shipment from the factory or at the port.

We establish reserves for sales allowances, including promotional and other allowances, at the time of sale. The reserves are determined as a percentage of sales based upon either historical experience or upon estimates or programs agreed upon by our customers and us. As of December 31, 2019 and 2018, we had reserves for sales allowances of \$22.6 million and \$13.0 million, respectively.

Marketing

We believe Funko's trendsetting and nostalgia-based product assortment is a unique voice in the pop culture marketplace. We have experienced significant growth in brand engagement as our product offerings continue their appeal to all ages. We believe that our expansive retailer presence, high engagement rates across our owned channels, and devout fan base create fervor for the Funko brand. Our ability to effectively engage with our customers has resulted in a deep affinity for Funko and our products.

Funko continues to acquire new fans through Facebook, Twitter, Instagram, Twitch and YouTube. In July of 2019 Funko's Twitter handle, @originalfunko, reached one million followers. In comparison, Mattel and Hasbro average approximately 150,000 followers. The quality of our owned content also resulted in a 140% year-over-year increase in YouTube subscribers to over 500,000 subscribers as of December 31, 2019. We continue to expand our reach globally through our engaging content, events and personal engagement with our fan base.

Connection to pop culture through a lifestyle product line that includes vinyl figures, action toys, plush, apparel, board games, housewares and accessories is our core business. Entertainment enthusiasts display their fandom through the lens of Funko products.

The desire to tap into this fandom has resulted in strategic collaborations with companies like Microsoft and NBCU. In August 2019, we collaborated with Microsoft to launch Gears Pop!, a mobile game that utilizes Funko's unique Pop! characters.

Our fan base has also demanded the attention of studio partners and retailers. In 2019, Funko served as an official press junket partner for Disney, appearing at notable Disney, Marvel & LucasFilm junkets to interact with influencers and talent whose characters appear in the Funko brand and product line.

The recent opening of a 40,000-square foot retail-tainment experience in the heart of Hollywood has further increased our brand presence.

Competition

We are a worldwide leader in the design, manufacture and marketing of licensed pop culture products, in a highly competitive industry. We compete with toy companies in many of our product categories, some of which have substantially more resources, stronger name recognition, and longer operating histories than us, and which benefit from greater economies of scale. We also increasingly compete with large toy companies for shelf space at leading mass market and other retailers. We also compete with numerous smaller domestic and foreign collectible product designers and manufacturers in each of our product categories. Our competitive advantage is based primarily on the creativity and quality of the design of our products and their perceived value, our price points, our license portfolio and our ability to bring new products to market quickly.

We produce most of our products under trademarks and copyrights that we own, utilizing the intellectual property of our licensors. Certain of our licensors have reserved the rights to manufacture, distribute and sell similar or identical products. Some of these products could directly compete with our products and could be sold to our customers or directly to consumers at lower prices than those at which our products are sold.

Although we believe we have one of the largest portfolios of licensed content in the pop culture industry, with strong relationships with many of our licensors, we must vigorously compete to obtain these licenses from leading content providers on commercially reasonable terms, and to expand our license rights into additional licensed product categories. This competition is based primarily on the creativity of our product designs, our ability to bring new products to market quickly, our ability to increase fan engagement, the breadth of our sales channels and the quality of our products. See Item 1A, "Risk Factors."

Intellectual Property

We believe that our trademarks, copyrights and other intellectual property rights have significant value and are important to the marketing of our brand and the favorable perception of our products. We track our trademark registrations to ensure that marks used in commerce are renewed and maintained to prevent expiration of trademark rights. As of December 31, 2019, we owned approximately 66 registered U.S. trademarks, 146 registered international trademarks, 55 pending U.S. trademark applications and 94 pending international trademark applications. Most of our products are produced and sold under trademarks owned by or licensed to us. We register many of our trademarks related to our brands and seek protection under the trademark and copyright laws of the United States and other countries where our products are produced or sold. These intellectual property rights can be significant assets. Accordingly, while we believe we are sufficiently protected, the failure to obtain or the loss of some of these rights could have an adverse effect on our business, financial condition and results of operations. See Item 1A, "Risk Factors."

Government Regulation

Our products sold in the United States are subject to the provisions of the Consumer Product Safety Act ("CPSA"), the Federal Hazardous Substances Act ("FHSA"), the Consumer Product Safety Improvement Act of 2008 ("CPSIA") and the Flammable Fabrics Act ("FFA"), and the regulations promulgated pursuant to such statutes. These statutes and the related regulations ban from the market any consumer products that fail to comply with applicable product safety laws, regulations, and standards. The Consumer Product Safety Commission may require the recall,

repurchase, replacement, or repair of any such banned products or products that otherwise create a substantial risk of injury and may seek penalties for regulatory noncompliance under certain circumstances. Similar laws exist in some U.S. states and our products sold worldwide are subject to the provisions of similar laws and regulations in many jurisdictions, including Canada, Australia, Europe and Asia.

We maintain a quality control program to help ensure compliance with applicable product safety requirements. We use independent third-party laboratories that employ testing and other procedures intended to maintain compliance with the CPSA, the FHSA, the CPSIA, the FFA, other applicable domestic and international product standards, as well as our own standards and those of some of our larger retail customers and licensors. Nonetheless, there can be no assurance that our products are or will be hazard free, and we may in the future experience issues in products that result in recalls, withdrawals, or replacements of products. A product recall could have a material adverse effect on our results of operations and financial condition, depending on the product affected by the recall and the extent of the recall efforts required. A product recall could also negatively affect our reputation and the sales of other Funko products. See Item 1A, "Risk Factors."

We are subject to various other federal, state, local and international laws and regulations applicable to our business, including export controls, and have established processes for compliance with these laws and regulations.

Employees

As of December 31, 2019, we employed 1,006 full-time employees. We employed 744 people in the United States, 252 people in Europe and 10 people in Asia. None of our employees are represented by a labor union or are party to a collective bargaining agreement, and we have had no labor-related work stoppages. We believe that we have good relationships with our employees.

Seasonality

While our customers in the retail industry, and many of our competitors, typically operate in highly seasonal businesses, we have historically experienced only moderate seasonality in our business. For the years ended December 31, 2019, 2018 and 2017 approximately 55%, 60% and 61%, respectively, of our net sales were made in the third and fourth quarters, as our customers build up their inventories in anticipation of the holiday season. In the fourth quarter of 2019, net sales were below expectations due to the challenging retail environment, which resulted in lower than expected purchases among Funko's top customers throughout the holiday season as well as softness in sales related to certain tentpole movie releases.

Generally, the first quarter of the year represents the lowest volume of shipments 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. See Item 1A, "Risk Factors."

Information about our Executive Officers and Board of Directors

The following table provides information regarding our executive officers and members of our board of directors (ages as of March 5, 2020):

Name	Age	Position(s)
Brian Mariotti	52	Chief Executive Officer, Director
Jennifer Fall Jung	49	Chief Financial Officer
Andrew Perlmutter	42	President
Tracy Daw	54	Senior Vice President, General Counsel and Secretary
Ken Brotman	54	Chairman of the Board of Directors
Gino Dellomo	41	Director
Charles Denson	63	Director
Diane Irvine	61	Director
Adam Kriger	53	Director
Sarah Kirshbaum Levy	49	Director
Michael Lunsford	52	Director

Executive Officers

Brian Mariotti has served as Funko, Inc.'s Chief Executive Officer and as a member of Funko, Inc.'s board of directors since its formation in April 2017, as the Chief Executive Officer of FAH, LLC and as a member of FAH, LLC's board of directors since October 2015, and as Chief Executive Officer of FHL and as a member of FHL's board of directors since May 2013. Mr. Mariotti has also served as Chief Executive Officer of Funko, LLC since he acquired the business with a small group of investors in 2005. We believe Mr. Mariotti's knowledge of the pop culture industry and many years of experience as our Chief Executive Officer make him well-qualified to serve as a member of our board of directors.

Jennifer Fall Jung has served as Funko, Inc.'s Chief Financial Officer since August 2019. Ms. Fall Jung previously served as Senior Vice President, Corporate Finance and Investor Relations of Gap, Inc. ("Gap"), a global clothing and accessories retailer, from January 2017 to March 2018. Prior to January 2017, Ms. Fall Jung served in various other roles at Gap, including Senior Vice President and Chief Financial Officer of Old Navy Global and Head of International from November 2012 to January 2017, Chief Financial Officer and Senior Vice President of Gap North America from February 2011 to November 2012, and Chief Financial Officer and Vice President of Strategy and Real Estate for Gap, Inc. Outlet from April 2007 to February 2011. Ms. Fall Jung received her B.B.A. in Finance and her M.B.A., with an emphasis in International Business from San Diego State University.

Andrew Perlmutter has served as the President of Funko, Inc. and FAH, LLC since October 2017. Mr. Perlmutter was the Senior Vice President of Sales of FAH, LLC from June 2013 until October 2017. Prior to joining FAH, LLC, he was a co-founder of Bottle Rocket Collective, a board and travel games company, where he oversaw product manufacturing and sales from December 2012 until December 2013. Prior to his time at Bottle Rocket Collective, he was a National Account Manager at The Wilko Group from August 2001 until December 2012, where he managed sales to a variety of major mass-market, specialty and online retailers. Mr. Perlmutter received a B.A. in Interpersonal Communications from Southern Illinois University.

Tracy Daw has served as Funko, Inc.'s Senior Vice President, General Counsel and Secretary since its formation in April 2017, and as the Senior Vice President and General Counsel of FAH, LLC since July 2016. Mr. Daw served as the General Counsel of INRIX, Inc. from April 2012 until July 2016, where he was responsible for global legal affairs, with emphasis on corporate and intellectual property matters. He also previously served in various roles at RealNetworks, Inc. from February 2000 until April 2012, including as Senior Vice President, Chief Legal Officer and Corporate Secretary, where he managed the company's global legal affairs and corporate development efforts. From 1990 to 2000, Mr. Daw was a member of the law firm of Sidley Austin LLP, where he was a partner. Mr. Daw received a J.D. from the University of Michigan Law School and a B.S. in Industrial and Labor Relations from Cornell University.

Directors

Ken Brotman has served on the board of directors of Funko, Inc. since its formation in April 2017, and on the board of directors of FAH, LLC since October 2015. Mr. Brotman is a Founder and Managing Partner at ACON Investments, which he co-founded in 1996. Before that, Mr. Brotman was a partner at Veritas Capital, Inc. from 1993 until 1996, and, between 1987 and 1993, held positions at various private equity firms including Bain Capital and Wasserstein Perella Management Partners. Mr. Brotman has served on the board of directors of various ACON Investments portfolio companies since 1997 including several in the retail and consumer products sectors. Mr. Brotman received an M.B.A. from Harvard Business School and a B.S. in Economics from The Wharton School of the University of Pennsylvania. We believe Mr. Brotman's extensive private equity investment and company strategy and oversight experience and background with respect to acquisitions, debt financings and equity financings makes him well-qualified to serve as a member and as the chairman of our board of directors.

Gino Dellomo has served on the board of directors of Funko, Inc. since its formation in April 2017, and on the board of directors of FAH, LLC since October 2015. Mr. Dellomo is a Director at ACON Investments, which he joined in October 2006. Since October 2006, he has also served on the board of directors of various ACON Investments portfolio companies. Between 2001 and 2006, Mr. Dellomo held various positions at various investment banks, including Deutsche Bank Securities, Inc., FBR Capital Markets & Co. and MCG Capital Corp. Mr. Dellomo received a B.S. in Finance from Georgetown University. We believe Mr. Dellomo's private equity investment and company oversight experience and background with respect to acquisitions, debt financings and equity financings makes him well-qualified to serve as a member of our board of directors.

Charles Denson has served on the board of directors of Funko, Inc. since its formation in April 2017, and on the board of directors of FAH, LLC since June 2016. Mr. Denson has served as the President and Chief Executive Officer of Anini Vista Advisors, an advisory and consulting firm, since March 2014. From February 1979 until January 2014, Mr. Denson held various positions at NIKE, Inc., where he was appointed to several management roles, including, in 2001, President of the NIKE Brand, a position he held until January 2014. Mr. Denson also serves on the board of directors of several privately held organizations. Mr. Denson received a B.A. in Business from Utah State University. We believe Mr. Denson's extensive experience in brand building, brand management and organizational leadership in the public company context makes him well-qualified to serve on our board of directors.

Diane Irvine has served on the board of directors of Funko, Inc. and FAH, LLC since August 2017. Ms. Irvine previously served as Chief Executive Officer of Blue Nile, Inc., an online retailer of diamonds and fine jewelry, from February 2008 until November 2011, as President from February 2007 until November 2011, and as Chief Financial Officer from December 1999 until September 2007. From February 1994 until May 1999, Ms. Irvine served as Vice President and Chief Financial Officer of Plum Creek Timber Company, Inc., and from September 1981 until February 1994, she worked at accounting firm Coopers & Lybrand LLP in various capacities, most recently as partner. Ms. Irvine currently serves on the boards of directors of Casper Sleep Inc. (on whose board she has served since August 2019), Yelp Inc. (on whose board she has served since September 2011), and D.A. Davidson & Co. (on whose board she has served since January 2018), and previously served on the boards of directors of XO Group Inc. from November 2014 to December 21, 2018, Rightside Group Ltd. from August 2014 until July 2017, CafePress, Inc. from July 2012 until May 2015, and Blue Nile, Inc. from May 2001 until November 2011. Ms. Irvine received an M.S. in Taxation and a Doctor of Humane Letters from Golden Gate University, and a B.S. in Accounting from Illinois State University. We believe Ms. Irvine's extensive public company management experience and financial expertise make her well-qualified to serve on our board of directors.

Adam Kriger has served on the board of directors of Funko, Inc. since its formation in April 2017, and on the board of directors of FAH, LLC since June 2016. Mr. Kriger is an Executive Partner at ACON Investments, which he joined in August 2017. Before that, Mr. Kriger served as the Senior Vice President of Global Strategy for McDonald's Corporation from December 2001 until March 2015. He also previously served as the Senior Vice President of Global Strategy for Starwood Hotels & Resorts Worldwide from 1998 until 1999, and as the Vice President of Strategy and Development for The Walt Disney Company from 1988 until 1990, and then again from 1992 until 1998. Mr. Kriger serves on the boards of several non-profit organizations and private companies. Mr. Kriger received an M.B.A. from Harvard Business School and a B.A. in Quantitative Economics from Stanford University. We believe Mr. Kriger's extensive strategic, risk management and organizational leadership experience in the public company context make him well-qualified to serve on our board of directors.

Sarah Kirshbaum Levy has served on the board of directors of Funko, Inc. since September 2019. Ms. Levy served as the Chief Operating Officer of Viacom Media Networks, a division of the entertainment and media company, ViacomCBS, from 2016 through 2019, where she was responsible for overseeing global strategy, finance and operations for the division. Prior to her appointment at Viacom Media Networks, Ms. Levy was Chief Operating Officer at Nickelodeon from 2005 to 2016. She also currently sits on the board of the Lucius Littauer Foundation, which makes grants in the areas of education, social welfare, health care, and Jewish studies. Ms. Levy received an M.B.A. and B.A. in Economics from Harvard University. We believe Ms. Levy's extensive experience in entertainment and media, in particular her familiarity with consumer products licensing, make her well-qualified to serve on our board of directors.

Michael Lunsford has served on the board of directors of Funko, Inc. since October 2018. Mr. Lunsford previously served as the Chief Executive Officer of SK Planet, Inc. from 2013 until 2018 and as interim Chief Executive Officer of shopkick, Inc. in 2016. From 2008 to 2013, Mr. Lunsford held various management roles with RealNetworks, Inc., including interim Chief Executive Officer and Executive Vice President and General Manager of RealNetworks' Core Business and Chief Executive Officer of Rhapsody. Mr. Lunsford also served on the board of directors of shopkick, Inc. from 2013 to 2018, and on the boards of directors of various portfolio companies owned by SK Planet, Inc. from 2013 to 2018. Since 2014, Mr. Lunsford has served on the board of directors of the University of North Carolina Board of Visitors and IslandWood. Mr. Lunsford received an M.B.A. and a B.A. in Economics from The University of North Carolina. We believe Mr. Lunsford's broad management, retail and e-commerce experience make him well-qualified to serve on our board of directors.

Segment Information

We identify our reportable segments according to how the business activities are managed and evaluated, for which discrete financial information is available and is regularly reviewed by our Chief Operating Decision Maker ("CODM") to allocate resources and assess performance. Because our CODM reviews financial performance and allocates resources at a consolidated level on a regular basis, we have one reportable segment.

Our History

Funko, Inc. was formed as a Delaware corporation on April 21, 2017 for the purpose of completing our IPO. 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., through FAH, LLC and the ACON Acquisition, acquired a controlling interest in FHL, 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, which is the operating entity.

Available Information

Our Internet address is www.funko.com. At our Investor Relations website, investor.funko.com, we make available free of charge a variety of information for investors, including:

- our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and any amendments to those reports, as soon as reasonably practicable after we electronically file that material with or furnish it to the SEC;
- press releases on quarterly earnings, product and service announcements, events and legal developments;
- corporate governance information including our corporate governance guidelines, codes of conduct and ethics and committee charters;
- other news and announcements that we may post from time to time that investors might find useful or interesting; and
- opportunities to sign up for email alerts and RSS feeds to have information pushed in real time.

The information found on our website is not part of this or any other report we file with, or furnish to, the SEC.

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 Annual Report on Form 10-K 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. 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%, 72% and 72% of our sales for the years ended December 31, 2019, 2018 and 2017, 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 38%, 34% and 33% of our sales for the

years ended December 31, 2019, 2018 and 2017, 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 and a requirement that we pay additional royalties, the amounts of which could be material. As of December 31, 2019, we had a reserve of \$7.8 million on our balance sheet related to ongoing and future royalty audits, based on estimates of the costs we expect to incur. 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, the goodwill associated with their intellectual property, and their ability 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 may not be able to design and develop products that will be popular with consumers, and we may not 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 79%, 76% and 70% of our sales for the years ended December 31, 2019, 2018 and 2017, 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, trends and changes in the retail industry can negatively impact our business, financial condition and results of operations. For example, the retail industry, and in particular the toys sector, experienced softness during the 2019 holiday season, which adversely impacted our sales.

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 44%, 46% and 45% of our sales for the years ended December 31, 2019, 2018 and 2017, 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.

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 1,006 as of December 31, 2019. As a result of our acquisition of Underground Toys Limited in January 2017, 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 depends 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 years ended December 31, 2019, 2018 and 2017, our gross margins (exclusive of depreciation and amortization) were 35.5%, 37.2% and 38.5%, 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 such as 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 their 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. For the years ended December 31, 2019, 2018 and 2017, we recorded reserves of \$2.4 million, \$5.5 million and \$2.9 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. For example, in the fourth quarter of 2019, we wrote-down \$16.8 million of inventory due to our decision to dispose of slower moving inventory to increase operational capacity which contributed to the Company's net loss for the period.

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 December 31, 2019, we owned approximately 66 registered U.S. trademarks, 146 registered international trademarks, 55 pending U.S. trademark applications and 94 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, our products 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 in 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 planned management transitions, 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 of Seattle 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 and popularity 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 55%, 60% and 61%, of our net sales for the

years ended December 31, 2019, 2018 and 2017, 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. During the 2019 holiday season, for example, we experienced lower than expected purchases by our top customers as well as softness in sales related to certain tentpole movie releases, both of which adversely affected our financial results. 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.

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. 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.

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 Vietnam, China 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.”

The novel coronavirus outbreak could adversely impact our business, financial condition and results of operations.

In January 2020, the World Health Organization declared the novel coronavirus outbreak originating in Wuhan, China to be a public health emergency. Certain of our suppliers and the manufacturers of certain of our products have been and may continue to be adversely impacted by the novel coronavirus outbreak. As a result, we have faced and may continue to face delays or difficulty sourcing products, which could negatively affect our business and financial results. Even if we are able to find alternate sources for such products, they may cost more, which could adversely impact our profitability and financial condition.

At this time, there is significant uncertainty relating to the potential effect of the novel coronavirus on our business. Infections may become more widespread, including to other countries where we source products or have operations, which may worsen the supply shortage or force us to restrict our third-party manufacturing or other operations. In addition, because the outbreak has spread to the greater Seattle, Washington area, where our headquarters and primary warehouse facility are located, we may need to restrict access to our facilities, which could negatively impact productivity. The outbreak may also reduce foot traffic in the stores where our products are sold or temporarily reduce demand for our products. Any of these occurrences may have a negative impact on our business, financial condition or results of 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 Coventry, England; London, England; Maldon, England; Bath, England; Burbank, California; Chatsworth, California; and Puyallup, Washington. In addition, the factories that produce most of our products are located in Vietnam, China 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 or the West Coast in general, or in 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 34%, 32% and 27% of our sales for the years ended December 31, 2019, 2018 and 2017, 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 Vietnam, China 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 pandemics, including related to the 2019 coronavirus outbreak, 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, and other countries have been escalating in recent years. U.S. tariff impositions against Chinese exports have been followed by retaliatory Chinese tariffs on U.S. exports to

China. Certain of the products we purchase from manufacturers in China have been or may in the future be 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.

Following a national referendum and enactment of legislation by the government of the United Kingdom, the United Kingdom withdrew from the European Union ("Brexit") on January 31, 2020 and entered into a transition period during which it will continue its ongoing and complex negotiations with the European Union relating to the future trading relationship between the parties. Significant political and economic uncertainty remains about whether the terms of the relationship will differ materially from the terms before withdrawal, as well as about the possibility that a so-called "no deal" separation will occur if negotiations are not completed by the end of the transition period.

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, 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.

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 2020 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, in 2019 we identified that our subsidiary, Loungefly, historically underpaid certain duties owed to U.S. Customs. In May 2019, we 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. We 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, we 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. Pursuant to the applicable statute, for an importer that meets all of the requirements for self-reporting underpayments, the maximum civil potential penalty is 100% of the lawful duties, taxes, and fees due to U.S. Customs and the civil penalty for an importer who fails to meet the self-reporting requirements is up to the value of the merchandise associated with underpayment. 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 consolidated balance sheet, as of December 31, 2019. As of the date of this Annual Report on Form 10-K, we are not aware of any investigation that has been initiated by U.S. Customs or any other governmental body. If U.S. Customs or any other governmental body elects to investigate us and decides to impose penalties, the imposition of penalties could be in excess of the contingent liability that we have recorded in our consolidated balance sheet. 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.

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 front-end 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.

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, 2015, 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 entitled *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 argument on the motion to dismiss was 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." On October 3, 2019, plaintiffs filed a first amended consolidated complaint. We moved to dismiss that complaint on December 5, 2019. We anticipate that the motion will be fully briefed by March 11, 2020, and that oral argument on the motion will take place March 27, 2020.

Additionally, on June 4, 2018, a putative class action lawsuit entitled *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 parties to the federal action, now captioned *Berkelhammer v. Funko, Inc. et al.* have agreed to a stay of that action pending developments in the state case.

The complaints in both state and federal court allege 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 lawsuits seek, among other things, compensatory statutory damages and rescissory damages in account of the consideration paid for our Class A common stock by the plaintiffs 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, the realization of such benefits may be delayed or reduced or our acquisitions or investments may have unexpected costs.

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.

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. For example, our operations are subject to the European Union's General Data Protection Regulation, which imposes data privacy and security requirements on companies doing business in the European Union, including substantial penalties for non-compliance. The California Consumer Privacy Act (the "CCPA"), which went into effect on January 1, 2020, imposes similar requirements on companies handling data of California residents and creates a new and potentially severe statutory damages framework for (i) violations of the CCPA and (ii) businesses that fail to implement reasonable security procedures and practices to prevent data breaches. 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 \$75.0 million on February 11, 2019). Proceeds from the New Credit Facilities were primarily used to repay the Former Senior Secured Credit Facilities. As of December 31, 2019, we had \$242.3 million of indebtedness outstanding under our New Credit Facilities, consisting of \$216.5 million outstanding under our New Term Loan Facility (net of unamortized discount of \$3.8 million) and \$25.8 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 March 3, 2020, ACON holds approximately 40.1% of the combined voting power of our common stock through its ownership of 10,934,606 shares of our Class A common stock and 8,882,120 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 March 3, 2020, collectively hold approximately 51.5% 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 34,917,582 common units of FAH, LLC as of December 31, 2019, representing approximately 68.7% 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 the 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 March 3, 2020, we had an aggregate of 165,055,059 shares of Class A common stock authorized but unissued, as well as approximately 15,927,938 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 Incentive Award Plan (the "2017 Plan"), including, as of December 31, 2019, 2,683,024 shares of Class A common stock underlying stock options we granted to certain of our directors, executive officers and other employees and 1,548,029 shares of Class A common stock underlying restricted stock units we granted to certain of our executive officers and other employees. We have also reserved for issuance an aggregate number of shares under the Company's 2019 Incentive Award Plan (the "2019 Plan") equal to the sum of (i) 3,000,000 shares of our Class A common stock and (ii) an annual increase on the first day of each calendar year beginning on January 1, 2020 and ending on and including January 1, 2029, equal to the lesser of (A) 2% of the shares of Class A Common Stock outstanding as of the last day of the immediately preceding fiscal year on a fully-diluted basis and (B) such lesser number of shares of Class A common stock as determined by our board of directors. Any shares of Class A common stock that we issue, including under our 2017 Plan, our 2019 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 and August 30, 2019, the "Form S-3") with the SEC. The Form S-3 was declared effective by the SEC on September 16, 2019. The Form

S-3 allows 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, following the secondary underwritten public offering which was completed on September 19, 2019, allows certain Original Equity Owners to sell 27,934,185 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;
- 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^{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 Securities Exchange Act of 1934, as amended (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 Consumer 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, prior to the completion of our IPO, most of our management team, including our chief executive officer and chief financial officer, had 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 prior to the completion of our IPO. 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.

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 our 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 have devoted, and will need to continue 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. Any 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 report our financial results or report them in a timely manner.

We are a public reporting company subject to the rules and regulations established from time to time by the SEC and The Nasdaq Stock Market. These rules and regulations require, among other things, that we have and periodically evaluate procedures with respect to our internal control over financial reporting. Reporting obligations as a public company are likely to continue to place a considerable strain on our financial and management systems, processes and controls, as well as on our personnel.

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 to 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 December 31, 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 was and may in the future be unable to conclude that we have effective internal control over financial reporting, and 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 litigation from investors and stockholders, any of 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 the price of our Class A common stock and adversely affect our results of operations and financial condition.

In addition to taking remediation measures in response to the material weakness we identified 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, 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 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

As of December 31, 2019, our leased properties primarily consist of office space, warehouses and distribution facilities. The table below sets forth certain information regarding our material properties, all of which are leased.

Property	Location	Approximate Square Footage	Lease Expiration Date
Corporate Headquarters and Retail Store	Everett, Washington	99,000	January 31, 2027
Offices, Main Warehouse and Distribution Facility	Everett, Washington	201,000	January 31, 2026
Warehouse and Distribution Facility	Everett, Washington	119,000	July 31, 2021
Warehouse and Distribution Facility	Everett, Washington	83,000	July 31, 2021
Administrative Offices	Everett, Washington	25,000	January 31, 2032
Warehouse and Distribution Facility	Puyallup, Washington	142,000	July 31, 2021
Administrative Offices, Licensing and Apparel Sales	Burbank, California	15,000	December 31, 2024
Warehouse	Chatsworth, California	46,000	June 28, 2020
Retail Store	Hollywood, California	40,000	March 31, 2030
Warehouse and Administrative Offices	Coventry, England	349,000	July 7, 2029
Warehouse and Administrative Offices	Maldon, Essex, United Kingdom	90,000	July 12, 2021
Sales and Administrative Offices	London, United Kingdom	11,000	June 5, 2028
Offices and Animation Studio	Bath, United Kingdom	9,000	March 12, 2028

For leases that are scheduled to expire during the next 12 months, we may negotiate new lease agreements, renew existing lease agreements or use alternate facilities. We believe that our facilities are adequate for our needs and believe that we should be able to renew any of the above leases or secure similar property without an adverse impact on our operations.

ITEM 3. 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 entitled *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 argument on the motion to dismiss was 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." On October 3, 2019, plaintiffs filed a first amended consolidated complaint. We moved to dismiss that complaint on December 5, 2019. We anticipate that the motion will be fully briefed by March 11, 2020, and that oral argument on the motion will take place March 27, 2020.

Additionally, on June 4, 2018, a putative class action lawsuit entitled *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 parties to the federal action, now captioned *Berkelhammer v. Funko, Inc. et al.*, have agreed to a stay of that action pending developments in the state case.

The complaints in both state and federal court allege 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 lawsuits seek, among other things, compensatory statutory damages and rescissory damages in account of the consideration paid for our Class A common stock by the plaintiffs 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 4. MINE SAFETY DISCLOSURES

Not applicable.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF SECURITIES

Market Information

On November 2, 2017, our Class A common stock began trading on the Nasdaq Global Market under the symbol "FNKO." Prior to that time, there was no public market for our stock. There is no established public trading market for our Class B common stock.

Holders of Record

As of March 3, 2020, there were 13 stockholders of record of our Class A common stock. As of March 3, 2020, there were 16 stockholders of record of our Class B common stock.

Issuer Purchases of Equity Securities

There were no share repurchases during the fourth quarter of the fiscal year ended December 31, 2019.

Dividend Policy

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, and therefore we do not anticipate declaring or paying any cash dividends on our Class A common stock in the foreseeable future. Holders of our Class B common stock are not entitled to participate in any dividends declared by our board of directors. Additionally, our ability to pay any cash dividends on our Class A common stock is limited by restrictions on the ability of FAH, LLC and our other subsidiaries to pay dividends or make distributions under the terms of our New Credit Facilities. Furthermore, because we are a holding company, our ability to pay cash 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. Any future determination as to the declaration and payment of dividends, if any, will be at the discretion of our board of directors, subject to compliance with contractual restrictions and covenants in the agreements governing our current and future indebtedness. Any such determination will also depend upon our business prospects, results of operations, financial condition, cash requirements and availability and other factors that our board of directors may deem relevant.

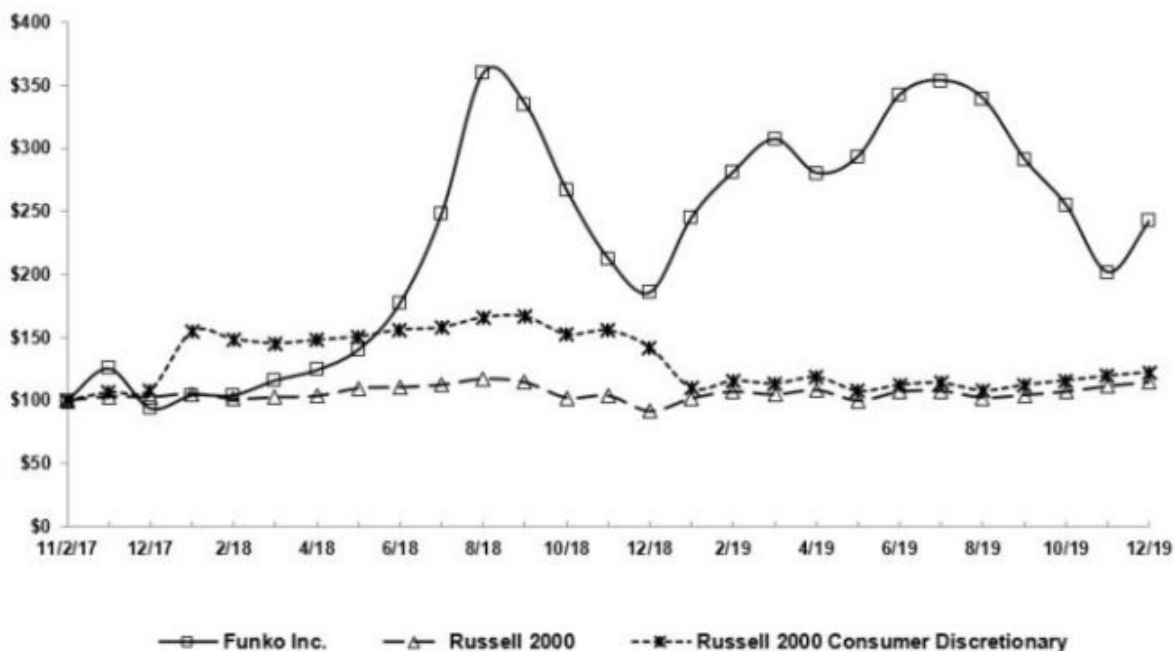
FAH, LLC paid cash tax distributions to its members during the years ended December 31, 2019, 2018 and 2017 of \$53.8 million (of which \$29.9 million was paid to Funko, Inc. and \$23.9 million was paid to continuing equity owners), \$26.9 million (of which \$6.5 million was paid to Funko, Inc. and \$20.4 million was paid to continuing equity owners) and \$23.7 million, respectively. Additionally, FAH, LLC paid a special distribution to its members during the year ended December 31, 2017 of \$49.2 million (of which \$49.0 million consisted of cash and \$0.2 million consisted of a reduction in interest and principal under loans to certain members of management).

Stock Performance Graph

The following graph and table illustrate the total return from November 2, 2017 through December 31, 2019, for (i) our Class A common stock, (ii) the Russell 2000 Index, and (iii) the Russell 2000 Consumer Discretionary Index. The graph and the table assume that \$100 was invested on November 2, 2017 in each of our Class A common stock, the Russell 2000 Index, and the Russell 2000 Consumer Discretionary Index, and that any dividends were reinvested. The comparisons reflected in the graph and table are not intended to forecast the future performance of our stock and may not be indicative of our future performance.

COMPARISON OF 26 MONTH CUMULATIVE TOTAL RETURN*

Among Funko Inc., the Russell 2000 Index,
and the Russell 2000 Consumer Discretionary Index



*\$100 invested on 11/2/17 in stock or index, including reinvestment of dividends.
Fiscal year ending December 31.

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	11/2/2017	12/29/2017	12/31/2018	12/31/2019
Funko, Inc.	100.00	94.06	186.00	242.72
Russell 2000	100.00	102.89	91.56	114.93
Russell 2000 Consumer Discretionary	100.00	108.40	141.97	122.60

ITEM 6. SELECTED FINANCIAL DATA

The following tables present the selected historical consolidated financial and other data for Funko, Inc. The selected consolidated statements of operations and cash flows data for the years ended December 31, 2019, 2018 and 2017 and the selected consolidated balance sheets data as of December 31, 2019 and 2018 are derived from the audited consolidated financial statements contained in Part II, Item 8 of this Annual Report on Form 10-K. Our selected consolidated balance sheet data as of December 31, 2017 and 2016 our selected consolidated financial data set forth below for the period from October 31, 2015 through December 31, 2015 (Successor 2015 Period) and the period from January 1, 2015 through October 30, 2015 (Predecessor 2015 Period) are derived from our consolidated financial statements not included elsewhere herein.

Subsequent to the IPO and related reorganization transactions, Funko, Inc. has been a holding company whose principal asset is its equity interest in FAH, LLC. As the sole managing member of FAH, LLC, Funko, Inc. operates and controls all of the business and affairs of FAH, LLC, and through FAH, LLC, conducts its business. As a result, the Company consolidates FAH, LLC's financial results and reports a non-controlling interest related to the common units not owned by Funko, Inc. Such consolidation has been reflected for all periods presented. Our selected historical consolidated financial and other data does not reflect what our financial position and results of operations would have been had we been a separate, stand-alone public company during those periods.

Our selected historical consolidated financial and other data may not be indicative of our future results of operations or future cash flows. You should read the information set forth below in conjunction with our historical consolidated financial statements and the notes to those statements, Item 1A. – “Risk Factors” and Item 7. – “Management’s Discussion and Analysis of Financial Condition and Results of Operations” included elsewhere in this Form 10-K.

	Year Ended December 31,				Successor	Predecessor
	2019	2018	2017	2016	Period from October 31, 2015 through December 31, 2015	Period from January 1, 2015 through October 30, 2015
(In thousands, except per share amounts)						
Consolidated Statements of Operations Data:						
Net sales	\$ 795,122	\$ 686,073	\$ 516,084	\$ 426,717	\$ 56,565	\$ 217,491
Cost of sales (exclusive of depreciation and amortization shown separately below)	512,580	430,746	317,267	280,396	44,485	131,621
Selling, general, and administrative expenses	193,803	155,321	120,944	77,525	13,894	37,145
Acquisition transaction costs	—	28	3,641	1,140	7,559	13,301
Depreciation and amortization	42,126	39,116	31,975	23,509	3,370	5,723
Total operating expenses	748,509	625,211	473,827	382,570	69,308	187,790
Income (loss) from operations	46,613	60,862	42,257	44,147	(12,743)	29,701
Interest expense, net	14,342	21,739	30,636	17,267	2,818	2,202
Loss on extinguishment of debt	—	4,547	5,103	—	—	—
Other expense (income), net	(25)	4,082	(734)	—	—	—
Income (loss) before income taxes	32,296	30,494	7,252	26,880	(15,561)	27,499
Income tax expense	4,476	5,432	1,266	—	—	—
Net income (loss)	27,820	25,062	5,986	26,880	(15,561)	27,499
Less: net income attributable to non-controlling interests	16,095	17,599	2,047	—	—	—
Net income (loss) attributable to Funko, Inc.	\$ 11,725	\$ 7,463	\$ 3,939	\$ 26,880	\$ (15,561)	\$ 27,499
Earnings per share of Class A common stock						
⁽¹⁾ :						
Basic	\$ 0.38	\$ 0.31	\$ 0.04			
Diluted	\$ 0.36	\$ 0.29	\$ 0.04			
Consolidated Statements of Cash Flows Data:						
Net cash provided by operating activities	\$ 90,765	\$ 49,991	\$ 23,837	\$ 49,468	\$ 14,110	\$ 8,538
Net cash used in investing activities	\$ (48,633)	\$ (27,501)	\$ (65,215)	\$ (22,105)	\$ (244,421)	\$ (10,043)
Net cash provided by (used in) financing activities	\$ (28,340)	\$ (15,046)	\$ 43,012	\$ (45,613)	\$ 244,456	\$ 11,390
Selected Other Data:						
EBITDA ⁽²⁾	\$ 88,764	\$ 91,349	\$ 69,863	\$ 67,656	\$ (9,373)	\$ 35,424
Adjusted EBITDA ⁽²⁾	\$ 123,037	\$ 113,540	\$ 90,031	\$ 96,960	\$ 13,170	\$ 61,996

	December 31,				
	2019	2018	2017	2016	2015
Consolidated Balance Sheets Data:	(In thousands)				
Cash and cash equivalents	\$ 25,229	\$ 13,486	\$ 7,728	\$ 6,161	\$ 24,411
Total assets	\$ 796,467	\$ 666,340	\$ 634,078	\$ 522,237	\$ 505,330
Total debt ⁽³⁾	\$ 242,323	\$ 247,297	\$ 233,899	\$ 217,753	\$ 169,846
Total operating lease liabilities ⁽⁴⁾	\$ 72,936	\$ —	\$ —	\$ —	\$ —
Total members' / stockholders' equity	\$ 305,144	\$ 293,254	\$ 281,292	\$ 217,377	\$ 243,556

- (1) Basic and diluted earnings per share of Class A common stock is applicable only for periods after the Company's IPO. See Note 20, Earnings per Share of the notes to our consolidated financial statements.
- (2) EBITDA and Adjusted EBITDA are supplemental measures of our performance that are not required by, or presented in accordance with, U.S. GAAP. EBITDA and Adjusted EBITDA are not measurements of our financial performance under U.S. GAAP and should not be considered as an alternative to net income (loss) or any other performance measure derived in accordance with U.S. GAAP. See "Non-GAAP Financial Measures" in Part II, Item 7 of this Form 10-K for additional information and a reconciliation to the most directly comparable U.S. GAAP financial measure.
- (3) Total debt consists of borrowing under our Former Senior Secured Credit Facilities and New Credit Facilities, as applicable, net of unamortized discount costs as of December 31, 2019, 2018, 2017, 2016 and 2015 of \$3.8 million, \$4.8 million, \$5.3 million, \$6.4 million and \$5.2 million, respectively.
- (4) The Company adopted Accounting Standards Codification Topic 842, *Leases* 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. See Note 2, Significant Accounting Policies of the notes to our consolidated financial statements.

ITEM 7. 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 audited consolidated financial statements and related notes included elsewhere in this Annual Report on Form 10-K. 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 Annual Report on Form 10-K.

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.

Summary

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. As of December 31, 2019, we held 34,917,582 common units, representing an approximately 68.7% 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.

	Year Ended December 31,		
	2019	2018	2017
	(amounts in thousands)		
Net sales	\$ 795,122	\$ 686,073	\$ 516,084
Net income	\$ 27,820	\$ 25,062	\$ 5,986
EBITDA ⁽¹⁾	\$ 88,764	\$ 91,349	\$ 69,863
Adjusted EBITDA ⁽¹⁾	\$ 123,037	\$ 113,540	\$ 90,031

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

Factors Affecting our Business

Growth in the Market for Pop Culture Consumer Products

Our operating results and prospects will be impacted by developments in the market for pop culture consumer products. Our business has benefitted from pop culture trends including (1) technological innovation that has facilitated content consumption and engagement, (2) creation of more quality content, (3) greater cultural prevalence and acceptance of pop culture fandom and (4) increased engagement by fans with pop culture content beyond mere consumption driven by social media and demonstrated by fan-centric experiences, such as Comic-Con events around the world. These trends have contributed to significant recent growth in the demand for pop culture products like ours in recent years; however, consumer demand for pop culture products and pop culture trends can and does shift rapidly and without warning. To the extent we are unable to offer products that appeal to consumers, our operating results will be adversely affected. This is particularly true given the concentration of our sales of products under certain of our brands, particularly our Pop! brand, which represented approximately 79%,

76% and 70% of our sales for the years ended December 31, 2019, 2018 and 2017, respectively, and which is sold across multiple product categories.

Relationships with Content Providers

We generate substantially all of our net sales from products based on intellectual property we license from others. We have strong relationships with many established content providers and seek to establish licensing relationships with newer content providers. Our content provider relationships are highly diversified, allowing us to license a wide array of properties and thereby reduce our exposure to any individual property or license.

We believe there is a trend of content providers consolidating their relationships to do more business with fewer licensees. We believe our ability to help maximize the value and extend the relevance of our content providers' properties has allowed us to benefit from this trend. Although we have a successful track record of renewing and extending the scope of licenses, our 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. In addition, the efforts of our senior management team have been integral to our relationships with our licensors. Inability to license newer pop culture properties, 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 adversely affect our business.

Retail Industry Dynamics; Relationships with Retail Customers

Historically, substantially all of our 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. Our top ten customers represented approximately 44%, 46% and 45% of our sales for the years ended December 2019, 2018 and 2017, respectively. In the fourth quarter of 2019, net sales were below expectations due to the challenging retail environment, which resulted in lower than expected purchases among Funko's top customers throughout the holiday season as well as softness in sales related to certain tentpole movie releases.

We depend on retailers to provide adequate and attractive space for our products and point of purchase displays in their stores. In recent years, traditional retailers have been affected by a shift in consumer preferences towards other channels, particularly e-commerce. We believe that this shift may have benefited our business in recent periods as brick and mortar retailers dedicated additional shelf space to our products and pop culture consumer products generally to drive additional traffic to their stores and improve sales in previously less productive shelf space. In addition, we have seen an increase in sales for our product on retailers' e-commerce platforms.

Our customers do not make long-term commitments to us regarding purchase volumes and can therefore easily 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 for any reason could adversely affect our business. In addition, our future growth depends upon our ability to successfully execute our business strategy. See Item 1A, "Risk Factors."

Content Mix

The timing and mix of products we sell in any given quarter or 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. We have diversified our product offerings across property categories. We have visibility into the new release schedule of many of our content providers and our expansive license portfolio allows us to dynamically manage new product creation. This insight allows us to adjust the mix of products based on classic evergreen properties and new releases, depending on the media release cycle. In addition, over time, we have continued to increase our number of active properties. An active property is a property from which we generate sales of products during a given period. For the years ended December 31, 2019, 2018 and 2017, we had sales of our products across 804, 672 and 500 properties, respectively.

Our results of operations may also fluctuate significantly from quarter to quarter or year to year depending on the timing and popularity of new product releases and related content releases. Sales of a certain product or group of products tied to a particular property can dramatically increase our net sales in any given quarter or year. While we expect to see growth in the number of properties and products over time, we expect that the number of active properties and the sales per active property will fluctuate from quarter to quarter or year over year based on what is relevant in pop culture at that time and the types of properties we are producing against. In addition, despite our

efforts to diversify the properties on which we base our products, if the performance of one or more of these properties fails to meet expectations or are delayed in their release, our operating results could be adversely affected. For example, in the fourth quarter of 2019, sales related to certain movie releases failed to meet expectations, which had an adverse effect on our operating results.

Taxation and Expenses

After consummation of our IPO on November 6, 2017, we became subject to U.S. federal, state and local income taxes with respect to our allocable share of any taxable income of FAH, LLC, and we are taxed at the prevailing corporate tax rates. In addition to tax expenses, we also will incur expenses related to our operations, as well as payments under the Tax Receivable Agreement, which we expect to be significant. We intend to cause FAH, LLC to make distributions in an amount sufficient to allow us to pay our tax obligations and operating expenses, including distributions to fund any ordinary course payments due under the Tax Receivable Agreement.

In addition, as a public company, we have incurred, and will continue to incur, additional annual expenses related to operating as a public company, including, among other things, additional directors' and officers' liability insurance, director fees, reporting requirements of the SEC, transfer agent fees, hiring additional accounting, legal and administrative personnel, increased auditing and legal fees and similar expenses. We also incurred non-recurring costs as part of our transition to a publicly traded company, consisting of professional fees and other expenses.

Components of our Results of Operations

Net Sales

We sell a broad array of licensed pop culture consumer products across a variety of categories, including figures, plush, accessories, apparel and homewares, primarily to retail customers and distributors. We also sell our products directly to consumers through our e-commerce operations and, to a lesser extent, at specialty licensing and comic book conventions and exhibitions.

Revenue from the sale of our products is recognized when control of the goods is transferred to the customer, which is upon shipment or upon receipt of finished goods by the customer, depending on the contract terms. The majority of revenue is recognized upon shipment of products to the customer. We routinely enter into arrangements with our customers to provide sales incentives, support customer promotions, and provide allowances for returns and defective merchandise. The estimated costs of these programs reduce gross sales in the period the related sale is recognized. Sales terms typically do not allow for a right of return except in relation to a manufacturing defect. Shipping costs billed to our customers are included in net sales, while shipping and handling costs, which include inbound freight costs and the cost to ship products to our customers, are included in cost of sales.

Cost of Sales

Cost of sales consists primarily of product costs, royalty expenses paid to our licensors and the cost to ship our products, including both inbound freight and outbound products to our customers. Our cost of sales excludes depreciation and amortization.

Our products are produced by third-party manufacturers primarily in Vietnam, China and Mexico. The use of third-party manufacturers enables us to avoid incurring fixed product costs, while maximizing flexibility, capacity and capability. As part of a continuing effort to reduce manufacturing costs and ensure speed to market, we have historically kept our production concentrated with a small number of manufacturers and factories even as we have grown and diversified. In recent years, we have worked to improve the efficiency of our supply chain to improve our gross margins.

Our product costs and gross margins will be impacted from period to period based on the product mix in any given period. Our plush products tend to have a higher product cost and lower gross margins than our figures.

Our royalty costs and gross margins will also be impacted from period to period based on our mix of licensed products sold, as well as a variety of other factors including reserves for minimum guarantees and ongoing and future royalty audits.

Our shipping costs, both inbound and outbound, will fluctuate from period to period based on customer mix due to varying shipping terms and other factors.

Selling, General and Administrative Expenses

Selling, general and administrative expenses are primarily driven by wages, commissions and benefits, warehouse, fulfillment (internal and external), rent and facilities costs, infrastructure and technology costs, advertising and marketing expenses, including the costs to participate at specialty licensing and comic book conventions and exhibitions, as well as costs to develop promotional video and other online content created for advertising purposes. Credit card fees, insurance, legal expenses, other professional expenses and other miscellaneous operating costs are also included in selling, general and administrative expenses. Selling costs generally correlate to revenue timing and therefore experience similar moderate seasonal trends. We expect general and administrative costs to increase as our business evolves.

We have invested considerably in general and administrative costs to support the growth and anticipated growth of our business and anticipate continuing to do so in the future. Since our IPO, we have experienced a significant increase in accounting, legal and professional fees associated with being a public company as further described above under “—Factors Affecting Our Business—Taxation and Expenses.”

Acquisition Transaction Costs

Acquisition transaction costs represent costs incurred for potential and completed acquisitions. In 2017, we incurred costs related to the Underground Toys Acquisition, the Loungefly Acquisition, and A Large Evil Corporation Acquisition.

Depreciation and Amortization

Depreciation expense is recognized on a straight-line basis over the estimated useful lives of our property and equipment. Amortization relates to definite-lived intangible assets that are expensed on a straight-line basis over the estimated useful lives. Our intangible assets, which are being amortized over a range of two to 20 years, are mainly comprised of trade names, customer relationships and intellectual property we recognized as part of the ACON Acquisition and, to a lesser extent, the Underground Toys Acquisition and the Loungefly Acquisition.

Interest Expense, Net

Interest expense, net includes the cost of our short-term borrowings and long-term debt, including the amortization of debt issuance costs and original issue discounts, net of any interest income earned.

Results of Operations

Year Ended December 31, 2019 Compared to Year Ended December 31, 2018

The following table sets forth information comparing the components of net income for the years ended December 31, 2019 and 2018:

	Year Ended December 31,		Period over Period Change	
	2019	2018	Dollar	Percentage
	<i>(amounts in thousands, except percentages)</i>			
Net sales	\$ 795,122	\$ 686,073	\$ 109,049	15.9 %
Cost of sales (exclusive of depreciation and amortization shown separately below)	512,580	430,746	81,834	19.0 %
Selling, general, and administrative expenses	193,803	155,321	38,482	24.8 %
Acquisition transaction costs	—	28	(28)	(100.0) %
Depreciation and amortization	42,126	39,116	3,010	7.7 %
Total operating expenses	748,509	625,211	123,298	19.7 %
Income from operations	46,613	60,862	(14,249)	(23.4) %
Interest expense, net	14,342	21,739	(7,397)	(34.0) %
Loss on extinguishment of debt	—	4,547	(4,547)	(100.0) %
Other expense (income), net	(25)	4,082	(4,107)	(100.6) %
Income before income taxes	32,296	30,494	1,802	5.9 %
Income tax expense	4,476	5,432	(956)	(17.6) %
Net income	27,820	25,062	2,758	11.0 %
Less: net income attributable to non-controlling interests	16,095	17,599	(1,504)	(8.5) %
Net income attributable to Funko, Inc.	\$ 11,725	\$ 7,463	\$ 4,262	57.1 %

Net Sales

Net sales were \$795.1 million for the year ended December 31, 2019, an increase of 15.9% compared to \$686.1 million for the year ended December 31, 2018. The increase in net sales was due primarily to the continued expansion of products and properties in our portfolio, as well as enhanced distribution and product placement with our retail partners, partially offset by a more challenging retail environment, which resulted in lower than expected purchases among Funko's top customers throughout the 2019 holiday season as well as softness in sales related to certain tentpole movie releases in the year ended December 31, 2019 as compared to the year ended December 31, 2018.

In the year ended December 31, 2019, the number of active properties increased 20% to 804 from 672 in the year ended December 31, 2018, and average net sales per active property remained stable at \$1.0 million for both the years ended December 31, 2019 and 2018. While we expect to see growth in the number of active properties over time, we expect that 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 12.4% to \$523.9 million in the year ended December 31, 2019 as compared to \$466.0 million in the year ended December 31, 2018, and net sales internationally increased 23.3% to \$271.2 million in the year ended December 31, 2019 from \$220.0 million in the year ended December 31, 2018, primarily as a result of our growth in Europe. On a product category basis, net sales of figures increased 14.7% to \$642.5 million in the year ended December 31, 2019 as compared to the year ended December 31, 2018 and net sales of other products increased 21.4% to \$152.6 million in the year ended December 31, 2019 as compared to the year ended December 31, 2018.

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

Cost of sales (exclusive of depreciation and amortization) was \$512.6 million for the year ended December 31, 2019, an increase of 19.0%, compared to \$430.7 million for the year ended December 31, 2018. Cost of sales (exclusive of depreciation and amortization) increased primarily as a result of the continued growth in sales, which drove a \$27.5 million increase in product costs, a \$16.1 million increase in royalty expenses and a \$8.1 million increase in shipping and freight costs. In addition to the increase as a result of sales growth, cost of sales for the year ended December 31, 2019 include a one-time \$16.8 million charge related to the write-down of inventory as a result of the Company's decision to dispose of slower moving inventory to increase operational capacity. This charge is incremental to normal course reserves.

Gross margin (exclusive of depreciation and amortization), calculated as net sales less cost of sales as a percentage of sales, was 35.5% for the year ended December 31, 2019, compared to 37.2% for the year ended December 31, 2018. Gross margin (exclusive of depreciation and amortization) decreased 170 basis points for the year ended December 31, 2019 compared to the year ended December 31, 2018, due primarily to a one-time \$16.8 million charge related to the write-down of inventory as a result of the Company's decision to dispose of slower moving inventory to increase operational capacity and higher duties as a percentage of net sales related to our Loungefly products, partially offset by lower product costs as a percentage of net sales and a decrease in shipping and freight costs as a percentage of net sales for the year ended December 31, 2019 compared to the year ended December 31, 2018.

Selling, General, and Administrative Expenses

Selling, general, and administrative expenses were \$193.8 million for the year ended December 31, 2019, an increase of 24.8%, compared to \$155.3 million for the year ended December 31, 2018. The increase was driven primarily by a \$20.1 million increase in personnel expenses and commissions, a \$3.9 million increase in equity-based compensation, a \$3.8 million increase in rent and related facilities costs and a \$3.7 million increase in warehouse and office support costs. These increases primarily reflect increased headcount, warehouse costs and marketing to support new product launches as well as new office, retail and warehouse facilities.

Selling, general, and administrative expenses were 24.4% of sales for the year ended December 31, 2019, compared to 22.6% of sales for the year ended December 31, 2018 primarily due to higher personnel expenses and commissions, equity-based compensation and warehouse and office support costs as a percentage of net sales.

Depreciation and Amortization

Depreciation and amortization expense was \$42.1 million for the year ended December 31, 2019, compared to \$39.1 million for the year ended December 31, 2018, primarily driven by an increase in depreciation on tooling and molds as we continue to expand our product offerings and an increase in amortization of intangible assets acquired from the Forrest-Pruzan Acquisition in February 2019.

Interest Expense, Net

Interest expense, net was \$14.3 million for the year ended December 31, 2019, a decrease of 34.0%, compared to \$21.7 million for the year ended December 31, 2018. The decrease in interest expense, net was due to lower interest rates and lower average balances of debt outstanding during the year ended December 31, 2019 under the New Credit Facilities as compared to the interest rates and average balances of debt outstanding during the year ended December 31, 2018 primarily under the Former Senior Secured Credit Facilities.

Loss on extinguishment of debt

There was no loss on extinguishment of debt for the year ended December 31, 2019, compared to \$4.5 million for the year ended December 31, 2018. Loss on extinguishment of debt for the year ended December 31, 2018 represented the write-off of \$4.1 million of unamortized debt issuance costs on our previous Term Loan A Facility and \$0.4 million of unamortized debt issuance costs on our previous Revolving Credit Facility, each of which were repaid in full on October 22, 2018 in connection with the Company entering 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.

Income Tax Expense

Income tax expense was \$4.5 million for the year ended December 31, 2019, a decrease of 17.6%, compared to \$5.4 million for the year ended December 31, 2018. The decrease was primarily due to lower non-deductible expenses and tax benefits related to share-based compensation awards for the year ended December 31, 2019 as compared to the year ended December 31, 2018, partially offset by an increase in income before income taxes of \$1.8 million for the year ended December 31, 2019 as compared to the year ended December 31, 2018.

Net Income

Net income was \$27.8 million for the year ended December 31, 2019, compared to \$25.1 million for the year ended December 31, 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 year ended December 31, 2019 as compared to the year ended December 31, 2018, as discussed above.

Year Ended December 31, 2018 Compared to Year Ended December 31, 2017

The following table sets forth information comparing the components of net income for the years ended December 31, 2018 and 2017:

	Year Ended December 31,		Period over Period Change	
	2018	2017	Dollar	Percentage
<i>(amounts in thousands, except percentages)</i>				
Net sales	\$ 686,073	\$ 516,084	\$ 169,989	32.9 %
Cost of sales (exclusive of depreciation and amortization shown separately below)	430,746	317,267	113,479	35.8 %
Selling, general, and administrative expenses	155,321	120,944	34,377	28.4 %
Acquisition transaction costs	28	3,641	(3,613)	(99.2) %
Depreciation and amortization	39,116	31,975	7,141	22.3 %
Total operating expenses	625,211	473,827	151,384	31.9 %
Income from operations	60,862	42,257	18,605	44.0 %
Interest expense, net	21,739	30,636	(8,897)	(29.0) %
Loss on extinguishment of debt	4,547	5,103	(556)	(10.9) %
Other expense (income), net	4,082	(734)	4,816	(656.1) %
Income before income taxes	30,494	7,252	23,242	320.5 %
Income tax expense	5,432	1,266	4,166	329.1 %
Net income	25,062	5,986	19,076	318.7 %
Less: net income attributable to non-controlling interests	17,599	2,047	15,552	759.7 %
Net income attributable to Funko, Inc.	\$ 7,463	\$ 3,939	\$ 3,524	89.5 %

Net Sales

Net sales were \$686.1 million for the year ended December 31, 2018, an increase of 32.9% compared to \$516.1 million for the year ended December 31, 2017. The increase in net sales was due primarily to the continued expansion of products and properties in our portfolio, as well as enhanced distribution and product placement with our retail partners.

In the year ended December 31, 2018, the number of active properties increased 34% to 672 from 500 in the year ended December 31, 2017, and average net sales per active property remained stable at \$1.0 million for both the years ended December 31, 2018 and 2017. While we expect to see growth in the number of active properties over time, we expect that 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 23.9% to \$466.0 million in the year ended December 31, 2018 as compared to \$376.1 million in the year ended December 31, 2017, and net sales internationally increased 57.2% to \$220.0 million in the year ended December 31, 2018 from \$140.0 million in the year ended December 31, 2017, primarily as a result of our growth in Europe. On a product category basis, net sales of figures increased 32.7% to \$560.1 million in the year ended December 31, 2018 as compared to the year ended December 31, 2017 and net sales of other products increased 34.0% to \$126.0 million in the year ended December 31, 2018 as compared to the year ended December 31, 2017.

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

Cost of sales (exclusive of depreciation and amortization) was \$430.7 million for the year ended December 31, 2018, an increase of 35.8%, compared to \$317.3 million for the year ended December 31, 2017. Cost of sales (exclusive of depreciation and amortization) increased primarily as a result of the continued growth in sales, which drove both higher product costs and royalty expenses. In 2018, in addition to the increase as a result of sales growth, cost of sales included \$2.0 million of incremental packaging and display costs, a \$1.8 million increase from donating inventory to charitable organizations and a \$1.4 million increase for inventory reserves and adjustments. In 2017, cost of sales included \$3.2 million related to the application of purchase accounting in connection with the Underground Toys Acquisition and the Loungefly Acquisition, which required inventory to be recorded at estimated fair value at the time of acquisition. This step-up in value resulted in an increase to inventory of \$2.6 million and \$0.6 million based on the estimated fair value as of the date of the Underground Toys Acquisition and Loungefly Acquisition, respectively.

Gross margin (exclusive of depreciation and amortization), calculated as net sales less cost of sales as a percentage of sales, was 37.2% for the year ended December 31, 2018, compared to 38.5% for the year ended December 31, 2017. Gross margin (exclusive of depreciation and amortization) decreased 130 basis points for the year ended December 31, 2018 compared to the year ended December 31, 2017, due primarily to the increase in our average royalty rate to 16.1% for the year ended December 31, 2018 compared to 14.9% for the year ended December 31, 2017 (primarily reflecting higher reserves for minimum guarantees, due in part to our subscription box business, which we began phasing out in 2018, and higher reserves for minimum guarantees on international sales, as well as ongoing and future royalty audits), higher compliance chargebacks received from our customers and an increase in inventory reserves, partially offset by inventory step up costs in 2017 related to our Underground Toys and Loungefly Acquisitions.

Selling, General, and Administrative Expenses

Selling, general, and administrative expenses were \$155.3 million for the year ended December 31, 2018, an increase of 28.4%, compared to \$120.9 million for the year ended December 31, 2017. The increase was driven primarily by growth in the business, including incremental expenses associated with our direct distribution model in Europe, our Loungefly operations and growth in the staffing at Funko Animation Studios. More specifically, the increase in expenses primarily resulted from a \$20.3 million increase in personnel expenses and commissions (which included \$1.0 million of certain severance costs incurred during the year ended December 31, 2018 in connection with the departure of certain members of senior management, including the founders of Loungefly), a \$7.5 million increase in rent and related facilities costs, which is a result of our continued expanded operations, and a \$3.6 million increase in equity-based compensation expense. These increases were partially offset by a decrease in bad debt expense of \$3.5 million due primarily to the bad debt expense recorded in 2017 related to the Toys 'R Us bankruptcy, which was partially offset by \$0.8 million in additional bad debt expense related to the bankruptcy of a European customer in 2018.

Selling, general, and administrative expenses were 22.6% of sales for the year ended December 31, 2018, compared to 23.4% of sales for the year ended December 31, 2017. While we have invested considerably in general and administrative costs to support the growth and anticipated growth of our business and anticipate continuing to do so in the future, our growth in sales more than offset the growth of our selling, general and administrative expenses in the year ended December 31, 2018.

Acquisition Transaction Costs

Transaction costs related to acquisitions were nominal for the year ended December 31, 2018 and \$3.6 million for the year ended December 31, 2017. Transaction costs for the year ended December 31, 2017 were primarily related to the Underground Toys and Loungefly Acquisitions.

Depreciation and Amortization

Depreciation and amortization expense was \$39.1 million for the year ended December 31, 2018, compared to \$32.0 million for the year ended December 31, 2017. Depreciation increased \$6.5 million, primarily related to the increase in depreciation on tooling and molds as a result of the expansion of our product lines, leasehold improvements at our corporate offices and warehouse facilities, and amortization increased \$0.6 million as a result of the Underground Toys Acquisition and the Loungefly Acquisition.

Interest Expense, Net

Interest expense, net was \$21.7 million for the year ended December 31, 2018, a decrease of 29.0%, compared to \$30.6 million for the year ended December 31, 2017. The decrease in interest expense, net was primarily related to the paydown of the Term Loan B Facility and Revolving Credit Facility with proceeds from our IPO in November 2017 and lower interest rates on our New Term Loan Facility and New Revolving Credit Facility as compared to our previous Term Loan A Facility and previous Revolving Credit Facility.

Loss on extinguishment of debt

Loss on extinguishment of debt was \$4.5 million for the year ended December 31, 2018, a decrease of 10.9%, compared to \$5.1 million for the year ended December 31, 2017. Loss on extinguishment of debt for the year ended December 31, 2018 represented the write-off of \$4.1 million of unamortized debt issuance costs on our previous Term Loan A Facility and \$0.4 million of unamortized debt issuance costs on our previous Revolving Credit Facility, each of which were repaid in full on October 22, 2018 in connection with the Company entering 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. Loss on extinguishment of debt for the year ended December 31, 2017 represented the write-off of unamortized discount costs on our Term Loan B Facility which was repaid in full in November 2017 in connection with the IPO.

Income Tax Expense

Income tax expense was \$5.4 million for the year ended December 31, 2018, an increase of 329.1%, compared to \$1.3 million for the year ended December 31, 2017. The increase was primarily due to the increase in income before income taxes of \$23.2 million, or 320.5%, for the year ended December 31, 2018 as compared to the year ended December 31, 2017. Additionally, in 2017, the LLC flow-through structure of FAH, LLC benefited our income tax expense as, prior to the IPO, we were subject to certain LLC entity-level taxes and foreign taxes but generally not subject to entity-level U.S. federal income taxes. Partially offsetting the increase in income tax expense was a decrease in the statutory U.S. federal corporate tax rate to 21% for the year ended December 31, 2018 as compared to a statutory rate of 34% for the year ended December 31, 2017.

Net income

Net income was \$25.1 million for the year ended December 31, 2018, compared to \$6.0 million for the year ended December 31, 2017. The increase in net income was primarily the result of the increase in net sales for the year ended December 31, 2018 as compared to the year ended December 31, 2017, 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 monitoring fees, non-cash charges related to equity-based compensation programs, earnout fair market value adjustments, inventory step-ups, loss on extinguishment of debt, acquisition transaction costs and other expenses, the Loungefly customs investigation and related costs, certain severance, relocation and other costs, foreign currency transaction gains and losses, Tax Receivable Agreement liability adjustments 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 (or the common unit equivalent of profit interests in FAH, LLC for periods prior to the IPO) 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, monitoring fees, non-cash charges related to equity-based compensation programs, loss on extinguishment of debt, earnout fair market value adjustments, inventory step-ups, acquisition transaction costs and other expenses, the Loungefly customs investigation and related costs, certain severance, relocation and related costs, foreign currency transaction gains and losses, Tax Receivable Agreement liability adjustments and other unusual or one-time items, and the income tax expense (benefit) effect of (1) these adjustments and (2) the pass-through entity taxable income as if the parent company was a subchapter C corporation in periods prior to the IPO. 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 (or the common unit equivalent of profit interest in FAH, LLC for periods prior to the IPO) 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 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 consolidated financial statements included elsewhere in this Annual Report on Form 10-K 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, earnout fair market value adjustments, inventory step-ups, loss on extinguishment of debt, acquisition transaction costs and other expenses, the Loungefly customs investigation and related costs, certain severance, relocation and related costs, foreign currency transaction gains and losses, Tax Receivable Agreement liability adjustments 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. In addition, the Non-GAAP Financial Measures include adjustments for other items, such as monitoring fees, that we do not expect to regularly record in the future. 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 (loss), for the periods presented:

	Year Ended December 31,		
	2019	2018	2017
Net income attributable to Funko, Inc.	\$ 11,725	\$ 7,463	\$ 3,939
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⁾	16,095	17,599	2,047
Monitoring fees ⁽²⁾	—	—	1,676
Equity-based compensation ⁽³⁾	13,044	9,140	5,574
Loss on extinguishment of debt	—	4,547	5,103
Earnout fair market value adjustment ⁽⁴⁾	—	—	30
Inventory step-up ⁽⁵⁾	—	—	3,182
Acquisition transaction costs and other expenses ⁽⁶⁾	383	3,391	5,336
Customs investigation and related costs ⁽⁷⁾	3,357	—	—
Certain severance, relocation and related costs ⁽⁸⁾	739	1,031	—
Foreign currency transaction loss (gain) ⁽⁹⁾	(177)	4,082	(733)
Tax receivable agreement liability adjustments	152	—	—
One-time inventory write-down ⁽¹⁰⁾	16,775	—	—
Income tax expense ⁽¹¹⁾	(12,166)	(7,739)	(8,660)
Adjusted net income	\$ 49,927	\$ 39,514	\$ 17,494
Weighted-average shares of Class A common stock outstanding-basic	30,898	23,821	23,338
Equity-based compensation awards and common units of FAH, LLC that are convertible into Class A common stock	21,167	26,858	27,297
Adjusted weighted-average shares of Class A stock outstanding - diluted	52,065	50,679	50,635
Adjusted earnings per diluted share	\$ 0.96	\$ 0.78	\$ 0.35

	Year Ended December 31,				Successor	Predecessor
	2019	2018	2017	2016	Period from October 31, 2015 through December 31, 2015	Period from January 1, 2015 through October 30, 2015
	(amounts in thousands)					
Net income (loss)	\$ 27,820	\$ 25,062	\$ 5,986	\$ 26,880	\$ (15,561)	\$ 27,499
Interest expense, net	14,342	21,739	30,636	17,267	2,818	2,202
Income tax expense	4,476	5,432	1,266	—	—	—
Depreciation and amortization	42,126	39,116	31,975	23,509	3,370	5,723
EBITDA	\$ 88,764	\$ 91,349	\$ 69,863	\$ 67,656	\$ (9,373)	\$ 35,424
Adjustments:						
Monitoring fees ⁽²⁾	—	—	1,676	1,498	272	3,346
Equity-based compensation ⁽³⁾	13,044	9,140	5,574	2,369	4,484	9,925
Loss on extinguishment of debt	—	4,547	5,103	—	—	—
Earnout fair market value adjustment ⁽⁴⁾	—	—	30	8,561	1,540	—
Inventory step-up ⁽⁵⁾	—	—	3,182	13,434	8,688	—
Acquisition transaction costs and other expenses ⁽⁶⁾	383	3,391	5,336	3,442	7,559	13,301
Customs investigation and related costs ⁽⁷⁾	3,357	—	—	—	—	—
Certain severance, relocation and related costs ⁽⁸⁾	739	1,031	—	—	—	—
Foreign currency transaction loss (gain) ⁽⁹⁾	(177)	4,082	(733)	—	—	—
Tax receivable agreement liability adjustments	152	—	—	—	—	—
One-time inventory write-down ⁽¹⁰⁾	16,775	—	—	—	—	—
Adjusted EBITDA	\$ 123,037	\$ 113,540	\$ 90,031	\$ 96,960	\$ 13,170	\$ 61,996

- (1) Represents the reallocation of net income attributable to non-controlling interests from the assumed exchange of common units of FAH, LLC in periods in which income was attributable to non-controlling interests.
- (2) Represents monitoring fees paid pursuant to a management services agreement with ACON that was entered into in connection with the ACON Acquisition, which terminated upon the consummation of the IPO in November 2017.
- (3) Represents non-cash charges related to equity-based compensation programs, which vary from period to period depending on timing of awards.
- (4) Reflects the increase in the fair value of contingent liabilities incurred in connection with the Underground Toys Acquisition.
- (5) Represents a non-cash adjustment to cost of sales resulting from acquisitions.
- (6) Represents legal, accounting, and other related costs incurred in connection with the IPO, acquisitions and other transactions. Included for the year ended December 31, 2018 is a one-time \$2.0 million consent fee related to certain existing license agreements which we expect to pay in connection with the renewal of such licensing agreements and \$0.7 million for the recognition of a pre-acquisition contingency related to our Loungefly acquisition.

- (7) Represents legal, accounting and other related costs incurred in connection with the Company's investigation of the underpayment of customs duties at Loungefly. For the year ended December 31, 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.
- (8) Represents certain severance, relocation and related costs. For the year ended December 31, 2019, includes \$0.4 million of severance costs incurred in connection with the departure of our former Chief Financial Officer and \$0.3 million of severance, relocation and related costs associated with the consolidation of our warehouse facilities in the United Kingdom. For the year ended December 31, 2018, includes severance costs incurred in connection with the departure of certain members of senior management, including the founders of Loungefly.
- (9) Represents both unrealized and realized foreign currency losses (gains) on transactions other than in U.S. dollars.
- (10) Represents a one-time \$16.8 million charge for the year ended December 31, 2019 to cost of goods sold for additional inventory reserves to dispose of certain inventory items. This charge is incremental to normal course inventory reserves and was recorded as a result of the Company's decision to dispose of slower moving inventory to increase operational capacity.
- (11) Represents the income tax expense (benefit) effect of (i) the above adjustments and (ii) the pass-through entity taxable income as if the parent company was a subchapter C corporation in periods prior to the IPO. This adjustment uses an effective tax rate of 25% for the years ended December 31, 2019 and 2018 and 36.2% for the year ended December 31, 2017, respectively.

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. In the year ended December 31, 2017 we also received contributions from members of FAH, LLC as further described below under "Liquidity;" however, we do not anticipate receiving any additional contributions from members of FAH, LLC.

On October 22, 2018 (the "Closing Date"), Funko Acquisition Holdings, L.L.C., Funko Holdings LLC, Funko, LLC and Loungefly, LLC (each, an "Original Borrower" and collectively, the "Original Borrowers"), entered into a 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.

On February 11, 2019, the Company amended the Credit Agreement 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 September 23, 2019, the Original Borrowers and Funko Games, LLC (collectively, the "Borrowers") entered into a second amendment to the Credit Agreement (the "Amendment"). The Amendment, among other things, extends the maturity date of the New Credit Facilities to September 23, 2024, reduces the interest margin applicable to all loans under the credit agreement by 0.75% and reduces certain fees incurred under the credit agreement. The Amendment also allows the Company to request that the New Term Loan Facility be increased by an additional \$25.0 million.

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 \$25.0 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 Credit Agreement) is not greater than a ratio that is 0.50:1.00 less than the Leverage Ratio (as defined in the Credit Agreement) for the applicable fiscal quarter and there is remaining Availability (as defined in the Credit Agreement) under the New Credit Facilities of at least \$25.0 million.

We expect these limitations to continue in the future under the terms of the New Credit Facilities and that they may continue under the terms of any future credit agreement or any future debt or preferred equity securities of ours or of our subsidiaries.

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 and August 30, 2019, the "Form S-3") with the SEC. The Form S-3 was declared effective by the SEC on September 16, 2019. The Form S-3 allows 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 27,884,185 shares of

Class A common stock in one or more offerings. On September 19, 2019, certain selling stockholders completed a secondary underwritten public offering of 4,000,000 shares of Class A common stock under our Form S-3.

The Form S-3 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 future 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 years ended December 31, 2019, 2018 and 2017 (in thousands):

	Year Ended December 31,		
	2019	2018	2017
Net cash provided by operating activities	\$ 90,765	\$ 49,991	\$ 23,837
Net cash used in investing activities	(48,633)	(27,501)	(65,215)
Net cash provided by (used in) financing activities	(28,340)	(15,046)	43,012
Effect of exchange rates on cash and cash equivalents	(2,049)	(1,686)	(67)
Net increase in cash and cash equivalents	\$ 11,743	\$ 5,758	\$ 1,567

Operating Activities. Our net cash provided by operating activities consists of net income adjusted for certain non-cash items, including depreciation and amortization, equity-based compensation and fair value adjustments to contingent consideration, accretion of discount on long-term debt, as well as the effect of changes in working capital and other activities.

Net cash provided by operating activities was \$90.8 million for the year ended December 31, 2019, compared to \$50.0 million for the year ended December 31, 2018. Changes in net cash provided by 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 year ended December 31, 2019 compared to the year ended December 31, 2018 was primarily due to changes in working capital, which increased net cash provided by operating activities by \$39.2 million and were primarily due to decreases in inventory and accounts receivable, net of \$34.3 million and \$32.2 million, respectively, and an increase in accounts payable of \$21.0 million, partially offset by decreases to accrued royalties, accrued expenses and other liabilities and income taxes payable of \$17.9 million, \$10.0 million and \$5.8 million, respectively, and an increase in prepaid expenses and other assets of \$14.6 million. The increase in net cash provided by operating activities also reflected an increase in net income, excluding non-cash adjustments, of \$1.6 million, driven primarily by an increase in net sales and a decrease in interest expense, net (excluding the effect of a \$0.9 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.

Net cash provided by operating activities was \$50.0 million for the year ended December 31, 2018, compared to \$23.8 million for the year ended December 31, 2017. The increase was primarily due to an increase in net income, excluding non-cash adjustments, of \$30.9 million, driven primarily by an increase in net sales and a decrease in interest expense, net (excluding the effect of a \$2.3 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 was partially offset by a decrease due to changes in working capital. Changes in working capital decreased net cash provided by operating activities by \$4.8 million and were primarily due a decrease in accounts payable of \$35.4 million and an increase in accounts receivable, net of \$7.7 million, partially offset by a decrease in prepaid expenses and other assets of \$18.5 million, an increase in accrued royalties of \$10.8 million and a decrease in inventory of \$8.3 million.

Investing Activities. Our net cash used in investing activities primarily relates to the purchase of property and equipment and acquisitions, net of cash acquired. For the year ended December 31, 2019, net cash used in investing activities was \$48.6 million and was comprised of \$42.3 million used for the purchase of property and equipment, primarily related to tooling and molds used for the expansion of product lines, and cash consideration, net of cash acquired of \$6.4 million for the Forrest-Pruzan Acquisition.

For the year ended December 31, 2018, net cash used in investing activities was \$27.5 million and was comprised of \$26.9 million used for the purchase of property and equipment, primarily related to tooling and molds used for the expansion of product lines, and \$0.6 million used for acquisitions, specifically an increase in cash used to acquire Loungefly as a result of certain working capital adjustments.

For the year ended December 31, 2017, net cash used in investing activities was \$65.2 million and was primarily comprised of initial cash consideration of \$12.6 million, \$16.1 million and \$3.9 million for the Underground Toys Acquisition, the Loungefly Acquisition and A Large Evil Corporation Acquisition, respectively. Additionally, \$33.6 million of net cash used in investing activities was for the purchase of property and equipment and primarily consisted of \$21.1 million for the purchase of property and equipment related to tooling and molds for the expansion of product lines and \$6.6 million for leasehold improvements related to the build-out of our new headquarters.

Financing Activities. Our financing activities primarily consist of proceeds from stock issuances, 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, members and the payment of contingent consideration. We do not anticipate any financing activity related to contributions from members going forward.

For the year ended December 31, 2019, net cash used in financing activities was \$28.3 million, primarily related to distributions to the Continuing Equity Owners of \$23.9 million and payments on the New Term Loan Facility of \$11.8 million, partially offset by net borrowings on the New Revolving Credit Facility of \$5.7 million and proceeds from the exercise of equity based options of \$2.2 million.

For the year ended December 31, 2018, net cash used in financing activities was \$15.0 million, primarily related to payments on the New Term Loan Facility and Term Loan A Facility of \$231.3 million and \$20.4 million in distributions to members of FAH, LLC, partially offset by proceeds from the New Term Loan Facility of \$230.0 million, and net borrowings on the revolving lines of credit of \$9.2 million.

For the year ended December 31, 2017, net cash provided by financing activities was \$43.0 million, primarily related to proceeds from the issuance of Class A common stock sold in the IPO net of underwriter's discounts and commissions of \$117.3 million, proceeds from the Term Loan A Facility, Term Loan B Facility and Subordinated Promissory Notes of \$86.3 million, and contribution from members of FAH, LLC of \$5.0 million, partially offset by payments on the Term Loan B Facility and Subordinated Promissory Notes of \$79.0 million, \$72.8 million in distributions to members of FAH, LLC and payments for contingent consideration of \$18.0 million. During 2017, we also had net borrowings on the Revolving Credit Facility of \$4.1 million.

Financial Condition

Notwithstanding our obligations under the Tax Receivable Agreement between Funko, Inc., FAH, LLC and each of the Continuing Equity Owners, 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 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, subject to customary exceptions, guarantee repayment of the New Credit Facilities. The New Term Loan Facility matures on September 23, 2024 (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 and sixth 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) or, in the case of swing loans, the Swing Rate (as defined in the Credit Agreement), plus 2.50% or the Base Rate (as defined in the Credit Agreement) plus 1.50%, with two 0.25% step-downs based on the achievement of certain leverage ratios. 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 Borrowers may request that the New Term Loan Facility be increased by an additional \$25.0 million.

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 of 1.25:1.00 (in each case, measured on a trailing four-quarter basis). The maximum senior leverage ratio is currently 2.75:1.00, which will step down to 2.50:1.00 on December 31, 2020 and to 2.25:1.00 on December 31, 2021. As of December 31, 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 December 31, 2019, we had \$25.2 million of cash and cash equivalents and \$101.6 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 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. For further discussion of changes in our debt, see below, and Note 10, Debt of the notes to our consolidated financial statements.

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 Subordinated Promissory Notes, Former Senior Secured Credit Facilities and New Credit Facilities. We expect these sources of liquidity to continue to be our primary sources of liquidity.

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. For a discussion of our New Credit Facilities, see Note 10, Debt of the notes to our consolidated financial statements.

Former Senior Secured Credit Facilities. For a discussion of our Former Senior Secured Credit Facilities, see Note 10, Debt of the notes to our consolidated financial statements.

Subordinated Promissory Notes. For a discussion of our former Subordinated Promissory Notes, see Note 10, Debt of the notes to our consolidated financial statements.

Offerings of Registered Securities. In addition, as described above, on April 20, 2019, we filed a preliminary shelf registration statement on Form S-3 with the SEC, which was declared effective by the SEC on September 16, 2019. The Form S-3 allows 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

The following summarizes our principal future minimum commitments as of December 31, 2019 (in thousands):

	2020	2021	2022	2023	2024	Thereafter	Total
Long term debt and related interest ⁽¹⁾	\$ 26,825	\$ 34,532	\$ 34,683	\$ 37,565	\$ 132,849	\$ —	\$ 266,454
Operating leases	11,758	12,678	11,159	11,425	10,982	37,168	95,170
Liabilities under tax receivable agreement ⁽²⁾	4,262	3,762	3,525	3,592	3,665	47,010	65,816
Minimum royalty obligations ⁽³⁾	24,011	2,489	29	19	—	—	26,548
New Revolving Credit Facility ⁽⁴⁾	25,822	—	—	—	—	—	25,822
Total	\$ 92,678	\$ 53,461	\$ 49,396	\$ 52,601	\$ 147,496	\$ 84,178	\$ 479,810

- (1) We estimated interest payments through the maturity of our New Credit Facilities by applying the interest rate of 5.99% in effect as of December 31, 2019 under our New Term Loan Facility. See Note 10, Debt of the notes to our consolidated financial statements.
- (2) Represents amounts owed under our Tax Receivable Agreement. See Note 13, Liabilities under Tax Receivable Agreement for additional information.
- (3) Represents minimum guaranteed royalty payments under licensing arrangements.
- (4) Represents the amount owed as of December 31, 2019 under our New Revolving Credit Facility.

Off-Balance Sheet Arrangements

As of December 31, 2019, we did not have any off-balance sheet arrangements.

Recent Accounting Pronouncements

See discussion of recently adopted and recently issued accounting pronouncements in Note 2, Significant Accounting Policies of the notes to our consolidated financial statements.

Critical Accounting Policies and Estimates

Discussion and analysis of our financial condition and results of operations are based on our 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 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.

The JOBS Act permits us, as an "emerging growth company," to take advantage of an extended transition period to comply with new or revised accounting standards applicable to public companies. We have chosen to "opt out" of this provision and, as a result, we will adopt new or revised accounting standards upon or prior to required public company adoption dates. This decision to opt out of the extended transition period under the JOBS Act is irrevocable.

Revenue Recognition and Sales Allowance. Revenue from the sale of our products is recognized when control of the goods is transferred to the customer, which is upon shipment or upon receipt of finished goods by the customer, depending on the contract terms. The majority of revenue is recognized upon shipment of products to the customer.

We routinely enter into arrangements with our customers to provide sales incentives, support customer promotions, and provide allowances for returns and defective merchandise. These sales adjustments require management to make estimates. In making these estimates, management considers all available information including the overall business environment, historical trends and information from customers, such as agreed upon customer contract terms as well as historical experience from the customer. The estimated costs of these programs reduce gross sales in the period the related sale is recognized. We adjust our estimates at least quarterly or when facts and circumstances used in the estimate process change; historically adjustments to these estimates have not been material.

We have elected to account for shipping and handling activities that occur after control of the related good transfers as fulfillment activities instead of assessing such activities as performance obligations. Accordingly, shipping and handling activities that are performed by us, whether before or after a customer has obtained control of the products, are considered fulfillment costs to satisfy our performance obligation to transfer the products and are recorded as incurred within cost of goods sold.

We have made an accounting policy election to exclude from revenue all taxes assessed by a governmental authority that are both imposed on and concurrent with a specific revenue-producing transaction and collected by the Company from a customer (for example, sales, use, value added, and certain excise taxes).

Royalties. We enter into agreements for rights to licensed trademarks, copyrights and likenesses for use in our products. These licensing agreements require the payment of royalty fees to the licensor based on a percentage of revenue. Many licensing agreements also require minimum royalty commitments. When royalty fees are paid in advance, we record these payments as a prepaid asset, either current or long-term based on when we expect to realize revenues under the related licensing agreement. If we determine that it is probable that the expected revenue will not be realized, a reserve is recorded against the prepaid asset for the non-recoverable portion. As of December 31, 2019, we recorded a prepaid asset of \$13.0 million, net of a reserve of \$2.4 million. As of December 31, 2018, we recorded a prepaid asset of \$5.5 million, net of a reserve of \$5.5 million. As of December 31, 2017, we recorded a prepaid asset of \$6.4 million, net of a reserve of \$2.9 million.

We record a royalty liability as revenues are earned based on the terms of the licensing agreement. In situations where a minimum commitment is not expected to be met based on expected revenues, we will accrue up to the minimum amount when it is reasonably certain that revenues generated will not meet the minimum commitment. Royalty and license expense is recorded within cost of sales on the consolidated statements of operations. Royalty expenses for the years ended December 31, 2019, 2018 and 2017, were \$126.8 million, \$110.7 million and \$77.1 million, respectively.

Inventory. Inventory consists primarily of figures, plush and accessories and other finished goods, and is accounted for using the first-in, first-out, or FIFO, method. We maintain reserves for excess and obsolete inventories to reflect the inventory balance at the lower of cost or net realizable value. This valuation requires us to make judgments, based on currently available information, about the likely method of disposition, through sales to customers, or liquidation, and expected recoverable value of each disposition category. We estimate obsolescence based on assumptions regarding future demand.

Inventory costs include direct product costs and freight costs. As a result of the ACON Acquisition, the Underground Toys Acquisition and the Loungefly Acquisition, inventory was adjusted to fair value as of October 31, 2015, January 27, 2017 and June 28, 2017, respectively. See Note 3, Acquisitions of the notes to our consolidated financial statements.

In addition, during the year ended December 31, 2019, we recorded a one-time \$16.8 million charge related to the write-down of inventory as a result of the Company's decision to dispose of slower moving inventory to increase operational capacity. This charge is incremental to normal course reserves.

Goodwill and Intangible Assets. Goodwill represents the excess of the purchase price over the net amount of identifiable assets acquired and liabilities assumed in a business combination measured at fair value. We evaluate goodwill for impairment annually on October 1 of each year and upon the occurrence of triggering events or substantive changes in circumstances that could indicate a potential impairment by assessing qualitative factors or performing a quantitative analysis in determining whether it is more likely than not that the fair value of the net assets is below their carrying amounts.

Intangible assets acquired in a business combination are recognized separately from goodwill and are initially recognized at their fair value at the acquisition date. Intangible assets acquired include intellectual property (product design), customer relationships, and trade names. These are definite-lived assets and are amortized on a straight-line basis over their useful lives. Intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets might not be recoverable. Conditions that would necessitate an impairment assessment include a significant decline in the observable market value of an asset, a significant change in the extent or manner in which an asset is used, or any other significant adverse change that would indicate that the carrying amount of an asset or group of assets may not be recoverable.

Income Taxes. We apply the provisions of Accounting Standards Codification (“ASC”) Topic No. 740, “Income Taxes” (“ASC 740”). Under ASC 740, deferred tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. We record a valuation allowance against our deferred tax assets when it is more likely than not that all or a portion of a deferred tax asset will not be realized. In evaluating our ability to recover our deferred tax assets, we consider all available positive and negative evidence, including our operating results, ongoing tax planning and forecasts of future taxable income on a jurisdiction-by-jurisdiction basis. If we determine we will not be able to fully utilize all or part of these deferred tax assets, we would record a valuation allowance through earnings in the period the determination was made, which would have an adverse effect on our results of operations and earnings. In accordance with ASC 740, we recognize, in our consolidated financial statements, the impact of our tax positions that are more likely than not to be sustained upon examination based on the technical merits of the positions. We recognize interest and penalties for uncertain tax positions in selling, general and administrative expenses.

We are subject to U.S. federal, state and local income taxes with respect to our allocable share of any taxable income of FAH, LLC and are taxed at the prevailing corporate tax rates. FAH, LLC is treated as a partnership for U.S. federal income tax purposes and, as such, generally is not subject to any 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 any net taxable income of FAH, LLC. Pursuant to the Second Amended and Restated FAH, LLC Agreement, FAH, LLC will generally make pro rata tax distributions to holders of common units in an amount sufficient to fund all or part of their tax obligations with respect to the taxable income of FAH, LLC that is allocated to them.

In connection with the consummation of the IPO, we entered into the Tax Receivable Agreement with FAH, LLC and each of the Continuing Equity Owners. Pursuant to the Tax Receivable Agreement, we are 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 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 (“Tax Receivable Agreement Payments”). Amounts payable under the Tax Receivable Agreement are contingent upon, among other things, (i) generation of taxable income over the term of the Tax Receivable Agreement and (ii) changes in tax laws. If we do not generate sufficient taxable income in the aggregate over the term of the Tax Receivable Agreement to utilize the tax benefits, then we would not be required to make the related Tax Receivable Agreement Payments. Therefore, we only recognize a liability for Tax Receivable Agreement Payments if we determine that it is probable that we will generate sufficient future taxable income over the term of the Tax Receivable Agreement to utilize the related tax benefits. Estimating future taxable income is inherently uncertain and requires judgment. In projecting future taxable income, we consider our historical results and incorporate certain assumptions, including projected revenue growth, and operating margins, among others.

Upon redemption or exchange of common units in FAH, LLC, we record a liability relating to the obligation if we believe that it is probable that we would have sufficient future taxable income to utilize the related tax benefits. If we determine in the future that we will not be able to fully utilize all or part of the related tax benefits, we would derecognize any portion of the liability related to the benefits not expected to be utilized.

Additionally, we will estimate the amount of Tax Receivable Agreement Payments expected to be paid within the next 12 months and classify this amount as current on our consolidated balance sheets. This determination is based on our estimate of taxable income for the next fiscal year. To the extent our estimate differs from actual results, we may be required to reclassify portions of our liabilities under the Tax Receivable Agreement between current and non-current.

During years ended December 31, 2019 and 2018, the Company acquired an aggregate of 9.5 million and 1.4 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 our investment in FAH, LLC subject to the provisions of the Tax Receivable Agreement. As a result of these exchanges, during the years ended December 31, 2019 and 2018, the Company recognized an increase to its net deferred tax assets in the amount of \$48.1 million and \$7.0 million, respectively, and corresponding Tax Receivable Agreement liabilities of \$59.0 million and \$6.8 million, respectively, representing 85% of the tax benefits due to the Continuing Equity Owners. In addition, during the year ended December 31, 2019, the Company recognized \$0.2 million of expenses in other (income) expense, net on our consolidated statements of operations related to remeasurement adjustments of Tax Receivable Agreement liabilities.

During the year ended December 31, 2017, there were no redemptions or exchanges of common units in FAH, LLC under the Tax Receivable Agreement. As such, we did not record any liabilities relating to our obligations under the Tax Receivable Agreement for 2017.

Refer to Note 2, Significant Accounting Policies of the notes to our consolidated financial statements for a discussion of recent accounting pronouncements.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

We are exposed to market risk from changes in interest rates, foreign currency and inflation. All of these market risks arise in the normal course of business, as we do not engage in speculative trading activities. The following analysis provides quantitative information regarding these risks.

Interest Rate Risk. Our operating results are subject to risk from interest rate fluctuations on our New Credit Facilities, which carry variable interest rates. Interest rate risk is the exposure to loss resulting from changes in the level of interest rates and the spread between different interest rates. Our New Credit Facilities include the New Term Loan Facility and the New Revolving Credit Facility with advances tied to a borrowing base and which bear interest at a variable rate. Because our New Credit Facilities bear interest at variable rates, we are exposed to market risks relating to changes in interest rates. Interest rate risk is highly sensitive due to many factors, including U.S. monetary and tax policies, U.S. and international economic factors and other factors beyond our control. As of December 31, 2019, we had \$242.3 million of variable rate debt outstanding under our New Credit Facilities, consisting of \$216.5 million outstanding under the New Term Loan Facility (net of unamortized discount of \$3.8 million) and \$25.8 million in outstanding variable rate borrowings under our New Revolving Credit Facility. Based upon a sensitivity analysis of our debt levels on December 31, 2019, an increase or decrease of 1% in the effective interest rate would cause an increase or decrease in interest expense of approximately \$2.2 million over the next 12 months. We do not use derivative financial instruments for speculative or trading purposes, but this does not preclude our adoption of specific hedging strategies in the future.

Foreign Currency Risk. In January 2017, we acquired certain assets of Underground Toys Limited and now sell directly to certain of our customers in Europe, the Middle East and Africa through our subsidiary, Funko UK, Ltd. While currently our inventory purchases for Funko UK, Ltd. are in U.S. dollars, their product sales are primarily in British pounds and euros. Funko UK, Ltd. also incurs a portion of its operating expenses in British pounds. In addition, we have other international subsidiaries in the United Kingdom and Hong Kong that primarily incur operating expenses in local currency and use the local currency as each subsidiary's functional currency. Therefore, our results of operations and cash flows are subject to fluctuations due to changes in foreign currency exchange rates, principally the British pound and euro. However, we believe that the exposure to foreign currency fluctuation from product sales and operating expenses is not significant at this time. As we grow our operations, our exposure to foreign currency risk could become more significant. To date, we have not entered into any foreign currency exchange contracts and currently do not expect to enter into foreign currency exchange contracts for trading or speculative purposes.

Impact of Inflation. Our results of operations and financial condition are presented based on historical cost. While it is difficult to accurately measure the impact of inflation due to the imprecise nature of the estimates required, we believe the effects of inflation, if any, on our historical results of operations and financial condition have been immaterial. We cannot assure you, however, that our results of operations and financial condition will not be materially impacted by inflation in the future.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

FUNKO, INC. AND SUBSIDIARIES
CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2019, 2018 AND 2017

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and Board of Directors of
Funko, Inc.

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of Funko, Inc. and subsidiaries (the Company) as of December 31, 2019 and 2018, the related consolidated statements of operations, comprehensive income, stockholders' and members' equity and cash flows, for each of the three years in the period ended December 31, 2019, and the related notes (collectively referred to as the "consolidated financial statements"). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company at December 31, 2019 and 2018, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2019, in conformity with U.S. generally accepted accounting principles.

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits we are required to obtain an understanding of internal control over financial reporting but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion.

Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ Ernst & Young LLP

We have served as the Company's auditor since 2015.
Seattle, Washington
March 5, 2020

FUNKO, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS

	Year Ended December 31,		
	2019	2018	2017
	(In thousands, except per share data)		
Net sales	\$ 795,122	\$ 686,073	\$ 516,084
Cost of sales (exclusive of depreciation and amortization shown separately below)	512,580	430,746	317,267
Selling, general, and administrative expenses	193,803	155,321	120,944
Acquisition transaction costs	—	28	3,641
Depreciation and amortization	42,126	39,116	31,975
Total operating expenses	748,509	625,211	473,827
Income from operations	46,613	60,862	42,257
Interest expense, net	14,342	21,739	30,636
Loss on extinguishment of debt	—	4,547	5,103
Other expense (income), net	(25)	4,082	(734)
Income before income taxes	32,296	30,494	7,252
Income tax expense	4,476	5,432	1,266
Net income	27,820	25,062	5,986
Less: net income attributable to non-controlling interests	16,095	17,599	2,047
Net income attributable to Funko, Inc.	\$ 11,725	\$ 7,463	\$ 3,939
Earnings per share of Class A common stock ⁽¹⁾ :			
Basic	\$ 0.38	\$ 0.31	\$ 0.04
Diluted	\$ 0.36	\$ 0.29	\$ 0.04
Weighted average shares of Class A common stock outstanding ⁽¹⁾ :			
Basic	30,898	23,821	23,338
Diluted	32,926	25,560	50,635

(1) Basic and diluted earnings per Class A common stock is applicable only for the period after the Company's IPO. See Note 20, Earnings Per Share.

See accompanying notes to consolidated financial statements.

FUNKO, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Year Ended December 31,		
	2019	2018	2017
	(In thousands)		
Net income	\$ 27,820	\$ 25,062	\$ 5,986
Other comprehensive income:			
Foreign currency translation (loss) gain, net of tax effect of \$(282), \$51 and \$— for the years ended December 31, 2019, 2018 and 2017, respectively	1,458	(2,020)	802
Comprehensive income	29,278	23,042	6,788
Less: Comprehensive income attributable to non-controlling interests	16,595	16,552	1,031
Comprehensive income attributable to Funko, Inc.	<u>\$ 12,683</u>	<u>\$ 6,490</u>	<u>\$ 5,757</u>

See accompanying notes to consolidated financial statements.

FUNKO, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

	December 31,	
	2019	2018
	(In thousands)	
Assets		
Current assets:		
Cash and cash equivalents	\$ 25,229	\$ 13,486
Accounts receivable, net	151,564	148,627
Inventory	62,124	86,622
Prepaid expenses and other current assets	20,280	11,904
Total current assets	<u>259,197</u>	<u>260,639</u>
Property and equipment, net	65,712	44,296
Operating lease right-of-use assets	62,901	—
Goodwill	124,835	116,078
Intangible assets, net	221,492	233,645
Deferred tax asset	57,547	7,407
Other assets	4,783	4,275
Total assets	<u>\$ 796,467</u>	<u>\$ 666,340</u>
Liabilities and Stockholders' Equity		
Current liabilities:		
Line of credit	\$ 25,822	\$ 20,000
Current portion long-term debt, net of unamortized discount	13,685	10,593
Current portion of operating lease liabilities	11,314	—
Accounts payable	42,531	36,130
Income taxes payable	637	4,492
Accrued royalties	34,625	39,020
Accrued expenses and other current liabilities	28,955	33,015
Total current liabilities	<u>157,569</u>	<u>143,250</u>
Long-term debt, net of unamortized discount	202,816	216,704
Operating lease liabilities, net of current portion	61,622	—
Deferred tax liability	341	5
Liabilities under tax receivable agreement, net of current portion	61,554	6,504
Deferred rent and other long-term liabilities	7,421	6,623
Commitments and contingencies		
Stockholders' equity:		
Class A common stock, par value \$0.0001 per share, 200,000 shares authorized; 34,918 shares and 24,960 shares issued and outstanding as of December 31, 2019 and 2018, respectively	3	2
Class B common stock, par value \$0.0001 per share, 50,000 shares authorized; 14,515 shares and 23,584 shares issued and outstanding as of December 31, 2019 and 2018, respectively	1	2
Additional paid-in-capital	204,174	146,154
Accumulated other comprehensive income	791	(167)
Retained earnings	20,442	8,717
Total stockholders' equity attributable to Funko, Inc.	<u>225,411</u>	<u>154,708</u>
Non-controlling interests	79,733	138,546
Total stockholders' equity	<u>305,144</u>	<u>293,254</u>
Total liabilities and stockholders' equity	<u>\$ 796,467</u>	<u>\$ 666,340</u>

See accompanying notes to consolidated financial statements.

FUNKO, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' AND MEMBERS' EQUITY
(In thousands)

	Member Units		Recourse Loans To Management	Other Comprehensive Income	Members' Earnings (Deficit)	Class A Common Stock		Class B Common Stock		Additional Paid-In Capital	Other Comprehensive Income	Retained Earnings	Non-Controlling Interests	Total
	Units	Amounts				Shares	Amount	Shares	Amount					
January 1, 2017	243	\$ 277,401	\$ (773)	\$ —	\$ (59,251)	—	\$ —	—	\$ —	\$ —	\$ —	\$ —	\$ —	\$ 217,377
Equity issued in connection with acquisition prior to Transactions	2	5,313	—	—	—	—	—	—	—	—	—	—	—	5,313
Warrants issued in connection with long-term debt prior to Transactions	—	—	—	—	5,726	—	—	—	—	—	—	—	—	5,726
Equity-based compensation prior to Transactions	—	4,571	159	—	—	—	—	—	—	—	—	—	—	4,730
Net income prior to Transactions	—	—	—	—	2,684	—	—	—	—	—	—	—	—	2,684
Cumulative translation adjustment prior to Transactions	—	—	—	1,184	—	—	—	—	—	—	—	—	—	1,184
Distribution to members prior to Transactions	—	—	—	—	(72,965)	—	—	—	—	—	—	—	—	(72,965)
Contributions from members prior to Transactions	5	5,000	—	—	—	—	—	—	—	—	—	—	—	5,000
Recourse loans to management prior to Transactions	—	—	188	—	—	—	—	—	—	—	—	—	—	188
Effect of Transactions	(250)	(292,285)	426	(1,184)	123,806	12,921	1	—	—	168,052	572	—	612	—
Sale of Class A common stock in initial public offering, net	—	—	—	—	—	10,417	1	—	—	108,919	—	—	—	108,920
Issuance of Class B common stock	—	—	—	—	—	—	—	24,976	2	—	—	—	—	2
Net deferred tax adjustments resulting from the Transactions	—	—	—	—	—	—	—	—	—	(1,241)	—	—	—	(1,241)
Unrecognized tax benefits resulting from the Transactions	—	—	—	—	—	—	—	—	—	(254)	—	—	—	(254)
Non-controlling interests related to purchase of common units from FAH, LLC	—	—	—	—	—	—	—	—	—	(147,254)	—	—	147,254	—
Equity-based compensation subsequent to Transactions	—	—	—	—	—	—	—	—	—	844	—	—	—	844
Cumulative translation adjustment	—	—	—	—	—	—	—	—	—	—	234	—	249	483
Net income subsequent to the Transactions	—	—	—	—	—	—	—	—	—	—	—	1,254	2,047	3,301
Period ended December 31, 2017	—	\$ —	\$ —	\$ —	\$ —	23,338	\$ 2	24,976	\$ 2	\$ 129,066	\$ 806	\$ 1,254	\$ 150,162	\$ 281,292
Distribution to continuing equity owners	—	—	—	—	—	—	—	—	—	—	—	—	(20,441)	(20,441)
Equity-based compensation	—	—	—	—	—	—	—	—	—	9,140	—	—	—	9,140
Shares issued for equity-based compensation awards	—	—	—	—	—	175	—	—	—	28	—	—	—	28
Cumulative translation adjustment, net of tax	—	—	—	—	—	—	—	—	—	—	(973)	—	(1,047)	(2,020)
Establishment of liabilities under tax receivable agreement and related changes to deferred tax assets	—	—	—	—	—	—	—	—	—	193	—	—	—	193
Redemption of common units of FAH, LLC	—	—	—	—	—	1,447	—	(1,392)	—	7,727	—	—	(7,727)	—
Net income	—	—	—	—	—	—	—	—	—	—	—	7,463	17,599	25,062
Period ended December 31, 2018	—	\$ —	\$ —	\$ —	\$ —	24,960	\$ 2	23,584	\$ 2	\$ 146,154	\$ (167)	\$ 8,717	\$ 138,546	\$ 293,254
Distribution to continuing equity owners	—	—	—	—	—	—	—	—	—	—	—	—	(23,924)	(23,924)
Equity-based compensation	—	—	—	—	—	—	—	—	—	13,044	—	—	—	13,044
Shares issued for equity-based compensation awards	—	—	—	—	—	359	—	—	—	2,218	—	—	—	2,218
Shares issued for purchase consideration	—	—	—	—	—	127	—	—	—	2,221	—	—	—	2,221
Cumulative translation adjustment, net of tax	—	—	—	—	—	—	—	—	—	—	958	—	500	1,458
Establishment of liabilities under tax receivable agreement and related changes to deferred tax assets	—	—	—	—	—	—	—	—	—	(10,947)	—	—	—	(10,947)
Redemption of common units of FAH, LLC	—	—	—	—	—	9,472	1	(9,069)	(1)	51,484	—	—	(51,484)	—
Net income	—	—	—	—	—	—	—	—	—	—	—	11,725	16,095	27,820
Period ended December 31, 2019	—	\$ —	\$ —	\$ —	\$ —	34,918	\$ 3	14,515	\$ 1	\$ 204,174	\$ 791	\$ 20,442	\$ 79,733	\$ 305,144

See accompanying notes to consolidated financial statements.

FUNKO, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended December 31,		
	2019	2018	2017
(In thousands)			
Operating Activities			
Net income	\$ 27,820	\$ 25,062	\$ 5,986
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation, amortization and other	44,518	39,116	31,975
Equity-based compensation	13,044	9,140	5,574
Accretion of discount on long-term debt	952	1,414	3,887
Amortization of debt issuance costs	258	709	534
Loss on debt extinguishment	—	4,547	5,103
Deferred tax benefit	(2,293)	(964)	(718)
Other	635	4,288	30
Changes in operating assets and liabilities:			
Accounts receivable, net	(3,969)	(36,139)	(28,473)
Inventory	25,372	(8,886)	(17,206)
Prepaid expenses and other assets	(5,824)	8,736	(9,737)
Accounts payable	4,629	(16,375)	18,998
Income taxes payable	(3,618)	2,177	2,268
Accrued royalties	(4,403)	13,495	2,650
Accrued expenses and other liabilities	(6,356)	3,671	2,966
Net cash provided by operating activities	<u>90,765</u>	<u>49,991</u>	<u>23,837</u>
Investing Activities			
Purchase of property and equipment	(42,264)	(26,866)	(33,562)
Acquisitions, net of cash	(6,369)	(635)	(31,653)
Net cash used in investing activities	<u>(48,633)</u>	<u>(27,501)</u>	<u>(65,215)</u>
Financing Activities			
Borrowings on line of credit	42,083	316,390	153,383
Payments on line of credit	(36,383)	(307,191)	(149,311)
Debt issuance costs	(411)	—	—
Proceeds from long-term debt, net	—	230,011	66,336
Payment of long-term debt	(11,750)	(231,338)	(59,000)
Payment of subordinated debt, net	—	—	(20,000)
Proceeds from subordinated debt, net	—	—	20,000
Contingent consideration	—	(2,500)	(17,958)
Contributions from members	—	—	5,000
Proceeds from initial public offering, net of underwriters discount and commissions	—	—	117,337
Proceeds from issuance of Class B common stock	—	—	2
Distributions to continuing equity owners	(23,923)	(20,441)	(72,777)
Payments under tax receivable agreement	(173)	—	—
Proceeds from exercise of equity-based options	2,217	23	—
Net cash provided by (used in) financing activities	<u>(28,340)</u>	<u>(15,046)</u>	<u>43,012</u>
Effect of exchange rates on cash and cash equivalents	(2,049)	(1,686)	(67)
Net increase in cash and cash equivalents	11,743	5,758	1,567
Cash and cash equivalents at beginning of period	13,486	7,728	6,161
Cash and cash equivalents at end of period	<u>\$ 25,229</u>	<u>\$ 13,486</u>	<u>\$ 7,728</u>
Supplemental Cash Flow Information			
Cash paid for interest	\$ 12,313	\$ 19,403	\$ 25,360
Income tax payments	14,125	2,311	—
Accrual for purchases of property and equipment	5,362	1,137	1,607
Establishment of liabilities under tax receivable agreement	59,045	6,771	—
Issuance of equity instruments for acquisitions	2,221	—	5,313
Issuance of warrants for Class A units in connection with long-term debt	—	—	5,061
Issuance of warrants for common units in connection with long-term debt	—	—	665
Reimbursement of management recourse loans	—	—	773
Tenant allowance	3,201	168	—

See accompanying notes to consolidated financial statements.

FUNKO, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation and Description of Business

The 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 (the “IPO”), 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 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”).

As the Transactions, discussed further in Note 18, Stockholders’ Equity, are considered transactions between entities under common control, the financial statements reflect the combined entities for all periods presented.

2. Significant Accounting Policies

Certain of the significant accounting policies are discussed within the note to which they specifically relate.

Use of Estimates

The preparation of the Company’s 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.

Cash Equivalents

Cash equivalents include amounts due from third-party financial institutions for credit and debit card transactions. These receivables typically settle in less than 5 days and were \$0.2 million and \$0.1 million for December 31, 2019 and 2018, respectively.

Concentrations of Business and Credit Risk

The Company grants credit to its customers on an unsecured basis. As of December 31, 2019 and 2018, the balance of accounts receivable consisted of 8% and 10%, respectively, of amounts owed from the largest customer for the given period. The collection of these receivables has been within the terms of the associated customer agreement.

For the years ended December 31, 2019, 2018 and 2017 there was no individual customer that generated net sales over 10%.

For the year ended December 31, 2019, 13%, 11%, and 11% of sales were related to the Company's three largest license agreements with no other license agreements accounting for more than 10% of sales. For the year ended December 31, 2018, there were three license agreements that accounted for more than 10% of sales. For the year ended December 31, 2017, there were no license agreements that accounted for more than 10% of sales.

The Company maintains its cash within bank deposit accounts at high quality, accredited financial institutions. These amounts at times may exceed federally insured limits. The Company has not experienced any credit losses in such accounts and does not believe it is exposed to significant credit risk on cash.

Inventory

Inventory consists primarily of figures, plush, apparel, homewares, accessories, games and other finished goods, and is accounted for using the first-in, first-out ("FIFO") method. The Company maintains reserves for excess and obsolete inventories to reflect the inventory balance at the lower of cost or net realizable value. This valuation requires us to make judgments, based on currently available information, about the likely method of disposition, such as through sales to customers, or liquidation, and expected recoverable value of each disposition category. The Company estimates obsolescence based on assumptions regarding future demand. Inventory costs include direct product costs and freight costs.

During the year ended December 31, 2019, we recorded a \$16.8 million charge related to the write-down of inventory as a result of the Company's decision to dispose of slower moving inventory to increase operational capacity. This charge is incremental to normal course reserves.

Property and Equipment

Property and equipment is stated at historical cost, net of accumulated depreciation, and, if applicable, impairment charges. Depreciation of property and equipment is recorded using the straight-line method over the shorter of the estimated useful life of the asset or the lease term. The estimated useful lives of our property and equipment are generally as follows:

Asset	Lives (in years)
Tooling and molds	2
Furniture, fixtures, and warehouse equipment	2 to 7
Computer equipment, software and other	3 to 5
Leasehold improvements	Lesser of useful life or term of lease

Revenue Recognition and Sales Allowance

Revenue from the sale of Company products is recognized when control of the goods is transferred to the customer, which is upon shipment or upon receipt of finished goods by the customer, depending on the contract terms.

The Company routinely enters into arrangements with its customers to provide sales incentives, support customer promotions, and provide allowances for returns and defective merchandise. These sales adjustments require management to make estimates. In making these estimates, management considers all available information including the overall business environment, historical trends and information from customers, such as agreed upon

customer contract terms as well as historical experience from the customer. The costs of these programs reduce gross sales in the period the related sale is recognized. The Company adjusts its estimates at least quarterly or when facts and circumstances used in the estimate process change; historically these adjustments have not been material.

We have made an accounting policy election to exclude from revenue all taxes assessed by a governmental authority that are both imposed on and concurrent with a specific revenue-producing transaction and collected by the Company from a customer (for example, sales, use, value-added, and certain excise taxes).

We have elected to account for shipping and handling activities that occur after control of the related good transfers as fulfillment activities instead of assessing such activities as performance obligations. Accordingly, shipping and handling activities that are performed by the Company, whether before or after a customer has obtained control of the products, are considered fulfillment costs to satisfy our performance obligation to transfer the products, and are recorded as incurred within cost of sales.

We have elected the practical expedient to not recognize a significant financing component for contracts that include payments terms of one year or less. We have also elected the practical expedient permitting expensing of costs to obtain a contract when the expected amortization period is one year or less.

Shipping Revenue and Costs

Shipping and handling costs include inbound freight costs and the cost to ship product to the customer and are included in cost of sales. Shipping fees billed to customers are included in net sales.

Royalties

We enter into agreements for rights to licensed trademarks, copyrights and likenesses for use in our products. These licensing agreements require the payment of royalty fees to the licensor based on a percentage of revenue. Many licensing agreements also require minimum royalty commitments. When royalty fees are paid in advance, we record these payments as a prepaid asset, either current or long-term based on when we expect to realize revenues under the related licensing agreement. If we determine that it is probable that the expected revenue will not be realized, a reserve is recorded against the prepaid asset for the non-recoverable portion. As of December 31, 2019, we recorded a prepaid asset of \$13.0 million, net of a reserve of \$2.4 million. As of December 31, 2018, we recorded a prepaid asset of \$5.5 million, net of a reserve of \$5.5 million.

We record a royalty liability as revenues are earned based on the terms of the licensing agreement. In situations where a minimum commitment is not expected to be met based on expected revenues, we will accrue up to the minimum amount when it is reasonably certain that revenues generated will not meet the minimum commitment. Royalty and license expense is recorded within cost of sales on the consolidated statements of operations. Royalty expenses for the years ended December 31, 2019, 2018 and 2017, were \$126.8 million, \$110.7 million and \$77.1 million, respectively.

Advertising and Marketing Costs

Advertising and marketing costs are expensed when the advertising or marketing event takes place. These costs include the fees to participate in trade shows and Comic-Cons, as well as costs to develop promotional video and other online content created for advertising purposes. These costs are included in selling, general and administrative expenses and for the years ended December 31, 2019, 2018 and 2017 were \$11.3 million, \$10.1 million, and \$9.1 million, respectively.

The Company enters into cooperative advertising arrangements with customers. The fees related to these arrangements are recorded as a reduction of net sales in the accompanying consolidated statements of operations because the Company has determined it does not receive an identifiable benefit and cannot reasonably estimate the fair value of these arrangements.

Product Design and Development Costs

Product design and development costs are recognized in selling, general and administrative expenses in the consolidated statements of operations as incurred. Product design and development costs for the years ended December 31, 2019, 2018 and 2017, were \$5.2 million, \$4.7 million, and \$4.7 million, respectively.

Foreign currency

We have international sales and operating expenses that are denominated in local functional currencies. The functional currency of our international subsidiaries is the same as the local currency. Assets and liabilities of these subsidiaries are translated into U.S. dollars at period-end foreign exchange rates, and revenues and expenses are translated at average rates prevailing throughout the period. Translation adjustments are included in other comprehensive income on the consolidated statements of comprehensive income. Transaction gains and losses including intercompany transactions denominated in a currency other than the functional currency of Funko, Inc. are included in other expense (income), net on our consolidated statements of operations. In connection with the settlement and remeasurement of intercompany balances, we recorded gains of \$0.7 million, \$0.1 million and a nominal amount for the years ended December 31, 2019, 2018 and 2017, respectively.

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 short-term leases.

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

3. Acquisitions

Acquisitions completed during the year ended December 31, 2019

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 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 has finalized its analysis of the opening balance sheet balances and assumptions over the fair value of assets and liabilities acquired and purchase consideration transferred.

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 consolidated statements of operations from the acquisition date to December 31, 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	

Acquisitions completed during the year ended December 31, 2017

In 2017, the Company completed three acquisitions that were accounted for as business combinations 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.

A Large Evil Corporation Limited. On November 28, 2017, the Company acquired all of the outstanding equity of A Large Evil Corporation Limited (“A Large Evil Corporation Acquisition”), an animation studio based in the United Kingdom. The preliminary purchase consideration included \$3.9 million paid in cash and additional \$1.0 million due to the sellers based on certain working capital adjustments and other conditions as per the agreement. The purchase price allocation was finalized during the third quarter of 2018 and the estimated fair value of the assets acquired and liabilities assumed has been finalized. The finalization of the purchase price allocation resulted in no change from the preliminary estimate. Costs, such as advisory, legal and accounting fees the Company incurred related to A Large Evil Corporation Acquisition were \$0.1 million for the year ended December 31, 2017 and are recorded within acquisition transaction costs in the consolidated statements of operations.

The activity of A Large Evil Corporation included in the Company’s consolidated statements of operations from the acquisition date to December 31, 2017 was not material.

Loungefly. On June 28, 2017, the Company acquired all of the outstanding equity interests of Loungefly, LLC (“Loungefly”), a designer of licensed pop culture fashion handbags, small leather goods and accessories (the “Loungefly Acquisition”). The purchase consideration included \$17.9 million paid in cash, which included \$1.8 million in transaction fees paid on behalf of the seller, and the issuance of \$2.1 million of FAH, LLC’s Class A units. The Company recorded certain fair value adjustments to Loungefly’s assets and liabilities as of the acquisition date, including a \$1.4 million increase to inventory. The purchase price allocation was finalized during the first quarter of 2018 and the estimated fair value of the assets acquired and liabilities assumed has been finalized. The finalization of purchase price allocation resulted primarily in a reduction of \$1.7 million to intangible assets and an increase in goodwill of \$1.8 million. Costs, such as advisory, legal, accounting fees and change of control fees, the Company incurred related to the Loungefly Acquisition were \$1.1 million for the year ended December 31, 2017, and are recorded within acquisition transaction costs in the consolidated statements of operations.

The activity of Loungefly included in the Company’s consolidated statements of operations from the acquisition date to December 31, 2017 was net sales of \$17.0 million and net income of \$1.9 million.

Underground Toys Limited. On January 27, 2017, the Company acquired certain assets of Underground Toys Limited, a manufacturer and distributor of licensed products based in the United Kingdom (the “Underground Toys Acquisition”). The acquired assets primarily consisted of inventory and identifiable intangible assets, which are now used by the Company’s newly formed subsidiary Funko UK, Ltd. The purchase consideration included \$12.6 million in cash, the issuance of \$3.2 million of FAH, LLC’s Class A units, an additional payment in cash of up to \$2.5 million contingent upon the assignment of certain license agreements and certain working capital adjustments of \$1.8 million. The Company has recorded certain adjustments to the working capital assumed, including a \$1.3 million decrease to inventory. The purchase price allocation has been finalized. Costs, such as advisory, legal, accounting fees and change of control fees incurred by the Company related to the acquisition of certain assets of Underground

Toys Limited were \$1.8 million for the year ended December 31, 2017, and are recorded within acquisition transaction costs in the consolidated statements of operations.

Foreign currency transaction gains and losses are included in other income, net on the consolidated statements of operations. Foreign currency transaction gain, net for the year ended December 31, 2017 was \$0.7 million.

The activity of Funko UK, Ltd. included in the Company's consolidated statements of operations from the acquisition date to December 31, 2017 was net sales of \$93.4 million and a net income of \$2.3 million for the year ended December 31, 2017. The Company's U.K. operations are subject to U.K. income taxes, which were \$0.5 million for the period from the acquisition date to December 31, 2017 and are included within income tax expense on the consolidated statements of operations.

For the acquisitions described above, the Company recorded goodwill amounting to \$15.4 million in the aggregate, which relates to a number of factors, including the future earnings and cash flow potential of the businesses, the multiple to earnings, cash flow and other factors at which similar businesses have been purchased by other acquirers, the competitive nature of the processes by which the Company acquired the businesses, the avoidance of the time and costs which would be required (and the associated risks that would be encountered) to enhance its existing offerings to key target markets and develop new and profitable businesses, and the complimentary strategic fit and resulting expected synergies to be achieved. Goodwill is not deductible for tax purposes.

The purchase consideration for the acquisitions was as follows:

	Purchase Consideration		
	Loungefly	Underground Toys Limited	A Large Evil Corporation Limited
	(in thousands)		
Cash paid	\$ 16,113	\$ 12,554	\$ 3,862
Transaction fees paid (incurred) on behalf of seller	1,777	—	—
Working capital adjustment to be paid in cash	635	1,784	1,003
Fair value of Class A Units issued	2,131	3,182	—
Fair value of contingent consideration	—	2,470	—
Purchase consideration	<u>\$ 20,656</u>	<u>\$ 19,990</u>	<u>\$ 4,865</u>

The purchase price allocations for the acquisitions were as follows:

	Assets (Liabilities) Acquired (Assumed) at Fair Value		
	Loungefly	Underground Toys Limited	A Large Evil Corporation Limited
	(in thousands)		
Cash	\$ 1,501	\$ —	\$ 645
Accounts receivable	3,315	—	30
Inventory	2,351	15,263	—
Other current assets	132	1,122	321
Property and equipment	214	289	76
Intangible assets	12,605	6,500	—
Goodwill	11,249	3,438	4,000
Current liabilities	(10,711)	(6,622)	(207)
Consideration transferred	<u>\$ 20,656</u>	<u>\$ 19,990</u>	<u>\$ 4,865</u>

The following table summarizes the estimated identifiable intangible assets acquired in connection with the transactions described above and their estimated useful lives:

Intangible asset type:	Estimated Fair Value of Assets Acquired		Estimated Useful Life (Years)
	Loungefly	Underground Toys Limited	
	(in thousands)		
Customer relationships	\$ 2,015	\$ 3,700	10
Licensor relationships	8,590	2,500	10
Trade name	2,000	—	10
Supplier relationships	—	300	2
Intangible assets	<u>\$ 12,605</u>	<u>\$ 6,500</u>	

4. Goodwill and Intangible Assets

Goodwill represents the excess of the purchase price over the net amount of identifiable assets acquired and liabilities assumed in a business combination measured at fair value. The Company evaluates goodwill for impairment annually on October 1 of each year and upon the occurrence of triggering events or substantive changes in circumstances that could indicate a potential impairment by assessing qualitative factors or performing a quantitative analysis in determining whether it is more likely than not that the fair value of the net assets is below their carrying amounts.

No impairment charges relating to goodwill were recorded in the years ended December 31, 2019, 2018 and 2017.

The following table presents the balances of goodwill as of 2019 and 2018 (in thousands).

	Goodwill
Balance as of January 1, 2018	\$ 114,162
Measurement period adjustment	1,773
Foreign currency remeasurement	143
Balance as of December 31, 2018	\$ 116,078
Acquisitions	8,465
Foreign currency remeasurement	292
Balance as of December 31, 2019	<u>\$ 124,835</u>

Intangible assets acquired in a business combination are recognized separately from goodwill and are initially recognized at their fair value at the acquisition date. Intangible assets acquired include intellectual property (product design), customer relationships, and trade names. These are definite-lived assets and are amortized on a straight-line basis over their useful lives. Intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets might not be recoverable. Conditions that would necessitate an impairment assessment include a significant decline in the observable market value of an asset, a significant change in the extent or manner in which an asset is used, or any other significant adverse change that would indicate that the carrying amount of an asset or group of assets may not be recoverable. No impairment charges relating to intangible assets were recorded in the years ended December 31, 2019, 2018 and 2017.

The following table provides the details of identified intangible assets, by major class, for the periods indicated (in thousands):

	Estimated Useful Life (Years)	December 31, 2019			December 31, 2018		
		Gross Carrying Amount	Accumulated Amortization	Intangible Assets, Net	Gross Carrying Amount	Accumulated Amortization	Intangible Assets, Net
Intangible assets subject to amortization:							
Intellectual property	3 - 20	\$ 115,131	\$ (24,047)	\$ 91,084	\$ 114,411	\$ (18,115)	\$ 96,296
Trade names	10 - 20	83,359	(17,450)	65,909	83,358	(13,182)	70,176
Customer relationships	3 - 20	71,620	(15,633)	55,987	68,891	(11,053)	57,838
Licensor relationships	10 - 20	11,222	(2,915)	8,307	11,122	(1,790)	9,332
Supplier relationships	2	316	(316)	—	304	(301)	3
Noncompetition agreements	3	290	(85)	205	—	—	—
Total		<u>\$ 281,938</u>	<u>\$ (60,446)</u>	<u>\$ 221,492</u>	<u>\$ 278,086</u>	<u>\$ (44,441)</u>	<u>\$ 233,645</u>

Amortization expense for the years ended December 31, 2019, 2018 and 2017 was \$15.9 million, \$15.0 million, and \$14.4 million, respectively. The future five-year amortization of intangibles subject to amortization at December 31, 2019 was as follows (in thousands):

	Amortization
2020	\$ 16,057
2021	16,057
2022	15,004
2023	14,860
2024	14,860
Thereafter	144,654
Total	<u>\$ 221,492</u>

5. Accounts Receivable, Net

Accounts receivable, net, primarily represent customer receivables, recorded at invoiced amount, net of a sales allowance and an allowance for doubtful accounts. An allowance for doubtful accounts is determined based on various factors, including specific identification of balances at risk for not being collected, historical experience and existing economic conditions. Receivables are written-off when all reasonable collection efforts have been exhausted and it is probable the balance will not be collected.

Accounts receivable, net consisted of the following (in thousands):

	December 31,	
	2019	2018
Accounts receivable	\$ 153,918	\$ 151,676
Less: Allowance for doubtful accounts	(2,354)	(3,049)
Accounts receivable, net	\$ 151,564	\$ 148,627

Accounts receivable includes a \$3.4 million and \$0.2 million tenant improvement receivable from a lessor as of December 31, 2019 and 2018, respectively. In addition, accounts receivable as of December 31, 2019 includes an income tax receivable of \$3.8 million. The remaining balance is customer receivables. Bad debt expense was \$1.1 million, \$1.9 million and \$5.5 million for the years ended December 31, 2019, 2018 and 2017, respectively.

Activity in our allowance for doubtful accounts was as follows:

	December 31,	
	2019	2018
Allowance for doubtful accounts - beginning	\$ 3,049	\$ 3,855
Charged to costs and other	1,094	1,908
Write offs	(1,789)	(2,714)
Allowance for doubtful accounts - ending	<u>\$ 2,354</u>	<u>\$ 3,049</u>

6. Prepaid Expenses and Other Current Assets

Prepaid expenses and other current assets consisted of the following (in thousands):

	December 31,	
	2019	2018
Prepaid deposits for inventory and molds	\$ 835	\$ 2,138
Prepaid royalties, net	13,016	5,465
Other prepaid expenses and current assets	6,429	4,301
Prepaid expenses and other current assets	<u>\$ 20,280</u>	<u>\$ 11,904</u>

7. Property and Equipment, Net

Property and equipment, net consisted of the following (in thousands):

	December 31,	
	2019	2018
Tooling and molds	\$ 88,070	\$ 70,368
Leasehold improvements	33,942	18,366
Computer equipment, software and other	10,186	8,401
Furniture, fixtures and warehouse equipment	11,231	8,868
Construction in progress	9,434	97
	<u>\$ 152,863</u>	<u>\$ 106,100</u>
Less: Accumulated depreciation	(87,151)	(61,804)
Property and equipment, net	<u>\$ 65,712</u>	<u>\$ 44,296</u>

Depreciation expense for the years ended December 31, 2019, 2018 and 2017 was \$26.2 million, \$24.1 million, and \$17.6 million, respectively.

8. Accrued Expenses and Other Current Liabilities

Accrued expenses and other current liabilities consisted of the following (in thousands):

	December 31,	
	2019	2018
Accrued payroll and compensation	\$ 13,141	\$ 11,138
Accrued shipping & freight costs	1,732	3,628
Accrued sales taxes	687	673
Deferred rent	—	429
Current liabilities under tax receivable agreement	4,262	266
Other current liabilities	9,133	16,881
Accrued liabilities and other current liabilities	<u>\$ 28,955</u>	<u>\$ 33,015</u>

9. 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. These tiers include Level 1, defined as observable inputs such as quoted prices in active markets; Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and Level 3, defined as unobservable inputs that reflect the Company's own assumptions about the assumptions market participants would use in pricing the asset or liability.

Contingent Consideration. The Company measures contingent consideration obligations at the acquisition date of a business combination, and at each balance sheet date, at fair value, with changes in fair value recognized in its consolidated statements of operations. Fair value is measured using the discounted cash flow method and based on assumptions the Company believes would be made by a market participant. Significant market inputs used to determine fair value included probabilities of the likelihood of assignment of license agreements and successful achievement of the EBITDA threshold that would trigger contingent purchase consideration, the timing of when the payments will be made, and the discount rate. Significant changes to these assumptions would result in a significantly lower or higher fair value measurement. The valuation represents a Level 3 measurement within the fair value hierarchy.

The Company recorded an estimated \$2.5 million in contingent consideration at the time the Company acquired Underground Toys Limited, which was paid out in 2018.

The following table sets forth the fair value and a summary of changes to the fair value of these Level 3 financial liabilities (in thousands):

	Contingent Consideration
Balance at December 31, 2017	\$ 2,500
Payments	(2,500)
Balance at December 31, 2018	<u>\$ —</u>

Changes in fair value reflect changes to the Company's assumptions regarding probabilities of the likelihood of assignment of license agreements and successful achievement of the earnings-based metrics, the timing of when the payment will be made, and the discount rate used to estimate the fair value of the obligation, and are recorded within selling, general and administrative expense in the consolidated statements of operations.

Debt. The estimated fair values of the Company's debt instruments, which are classified as Level 3 financial instruments, at December 31, 2019 and 2018, was approximately \$246.1 million and \$252.1 million, respectively. The carrying values of the Company's debt instruments at December 31, 2019 and 2018, were \$242.3 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 our standalone credit risk.

10. Debt

Debt consists of the following (in thousands):

	December 31,	
	2019	2018
New Revolving Credit Facility	<u>\$ 25,822</u>	<u>\$ 20,000</u>
New Term Loan Facility	220,313	232,063
Debt issuance costs	(3,812)	(4,766)
Total term debt	<u>216,501</u>	<u>227,297</u>
Less: current portion	13,685	10,593
Long-term debt, net	<u>\$ 202,816</u>	<u>\$ 216,704</u>

Maturities of long-term debt for each of the next five years and thereafter are as follows (in thousands):

	New Term Loan Facility
2020	\$ 14,688
2021	23,500
2022	24,969
2023	29,375
2024	127,781
Total	<u>\$ 220,313</u>

Former Senior Secured Credit Facilities

In October 2015, the Company entered into a credit agreement which provided for the \$175.0 million Term Loan A Facility and the Revolving Credit Facility, including a \$3.0 million subfacility for the issuance of letters of credit. On September 8, 2016, the Company entered into an amendment to the credit agreement which, among other things, increased borrowings under the Term Loan A Facility by \$50.0 million and changed the interest rate applicable to the Revolving Credit Facility. On January 17, 2017, the Company entered into an amendment to its credit agreement which provided for, among other things, an additional \$50.0 million Term Loan B Facility, providing for interest rate options that can be chosen by the Company and an increase in commitments under the Revolving Credit Facility to \$80.0 million.

In June 2017, the Company entered into additional amendments to its credit agreement to, among other things, (1) permit the Company to enter into certain subordinated loan documents, and (2) increase borrowings under the Term Loan A Facility by \$20.0 million, increase commitments under the Revolving Credit Facility to \$100.0 million and make certain changes to certain covenants and definitions. Proceeds from the additional Term Loan A Facility borrowings were used to fund a portion of the purchase price for the Loungefly Acquisition and to pay related fees and expenses.

In November 2017, all of the outstanding aggregate principal balance and accrued interest of \$46.1 million on the Company's Term Loan B Facility was repaid in connection with the IPO, and the Company recorded a \$5.1 million loss on debt extinguishment as a result of the write-off of unamortized discount.

On March 7, 2018, the Company entered into an amendment to its credit agreement which provides 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 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.

The Former Senior Secured Credit Facilities were collateralized by substantially all of the assets of, and the equity interests held by, the borrowers and any subsidiary guarantor that may become party to the credit agreement in the future, subject to certain exceptions. The Former Senior Secured Credit Facilities also contained certain financial and restrictive covenants. As of December 31, 2017 the Company was in compliance with all covenants under the Former Senior Secured Credit Facilities.

In November 2017, all of the then outstanding aggregate principal balance and accrued interest of \$55.6 million was repaid on the Revolving Credit Facility in connection with the IPO. The Company had \$10.8 million of borrowings outstanding under the Revolving Credit Facility as of December 31, 2017.

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, reflecting the incremental capacity of \$25.0 million contemplated under the New Credit Facilities prior to such amendment. On September 23, 2019, the Company entered into a second amendment to the New Credit Facilities (the "Amendment") The Amendment extends the maturity date of the term loans and revolving credit facility under the credit agreement to September 23, 2024, reduces the interest margin applicable to all loans under the credit agreement by 0.75% and reduces certain fees incurred under the credit agreement. The Amendment also allows the Company to request that the New Term Loan Facility be increased by an additional \$25.0 million.

As amended, the New Term Loan Facility matures on September 23, 2024 (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 and sixth 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.

As amended, loans under the New Credit Facilities bear interest, at the Company's option, at either the Euro-Rate (as defined in the Credit Agreement), or in the case of swing loans, the Swing Rate (as defined in the Credit Agreement), plus 2.50% or the Base Rate (as defined in the Credit Agreement) plus 1.50%, 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 assets of the Company and any of its existing or future material domestic subsidiaries, subject to customary exceptions. As of December 31, 2019, we were in compliance with all of the covenants in our New Credit Facilities.

The Borrowers may request that the New Credit Facilities be increased by an additional \$25.0 million. At December 31, 2019, the Company had \$220.3 million and \$25.8 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 December 31, 2019 and 2018.

Subordinated Promissory Notes

On June 26, 2017, FAH, LLC issued promissory notes payable to certain of its members, including several members of management and its majority owner, in the aggregate principal amount of \$20.0 million (the "Subordinated Promissory Notes"). Borrowings under the Subordinated Promissory Notes accrued interest at a rate equal to 11.0% per year for the first 90 days after their effective date, increasing to 13.0% per year 91 days after such effective date and 15.0% per year 181 days after such effective date. Proceeds from the Subordinated Promissory Notes were used to finance a portion of the contingent consideration related to the ACON Acquisition that was paid out during the year ended December 31, 2018.

In November 2017, all of the outstanding aggregate principal balance and accrued interest on the Subordinated Promissory Notes of \$20.9 million was repaid in connection with Funko, Inc.'s IPO.

11. Leases

The Company has entered into non-cancellable operating leases for office, warehouse, and distribution facilities, with original lease periods expiring through 2032. 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. For the year ended December 31, 2019, differences between rent expense and rent paid are recognized as adjustments to operating lease right-of-use assets on the audited 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 audited consolidated balance sheets and amortize the lease incentives on a straight-line basis over the lease term as an adjustment to rent expense. For the years ended December 31, 2018 and 2017, differences between rent expense and rent paid was recorded as deferred rent on the consolidated balance sheets. In addition, for the years ended December 31, 2018 and 2017, tenant improvement allowances were recorded as deferred rent on the consolidated balance sheets and amortized

on a straight-line basis over the lease term as a reduction of rent expense. Rent expense was \$14.9 million, \$11.7 million and \$6.1 million for the years ended December 31, 2019, 2018 and 2017, respectively.

As of December 31, 2019, the Company had recorded operating lease liabilities of \$72.9 million and operating lease right-of-use assets of \$62.9 million. During the year ended December 31, 2019, operating cash outflows relating to operating lease liabilities was \$8.3 million and operating lease right-of-use assets obtained in exchange for new operating lease obligations was \$33.3 million, net of lease incentives obtained of \$3.2 million. As of December 31, 2019, the Company's operating leases had a weighted-average remaining term of 7.9 years and weighted-average discount rate of 6.55%. 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 December 31, 2019 were as follows (in thousands):

2020	\$	11,758
2021		12,678
2022		11,159
2023		11,425
2024		10,982
Thereafter		37,168
Total lease payments		95,170
Less: imputed interest		(22,234)
Total	\$	72,936

12. Income Taxes

Income before income taxes consisted of (in thousands):

	Year Ended December 31,		
	2019	2018	2017
Domestic	\$ 21,414	\$ 22,157	\$ 4,583
Foreign	10,882	8,337	2,669
Income before income taxes	\$ 32,296	\$ 30,494	\$ 7,252

Income Tax Expense

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 results for the year ended December 31, 2017 reflect the U.K. Corporation Tax attributable to Funko UK, Ltd., but do not reflect the U.S. tax expense of FAH, LLC prior to the IPO, which as a pass-through entity, was not subject to U.S. income tax.

The components of the Company's income tax expense consisted of the following (in thousands):

	Year Ended December 31,		
	2019	2018	2017
Current income taxes:			
Federal	\$ 4,216	\$ 4,075	\$ 1,178
State and local	601	486	365
Foreign	1,952	1,758	952
Current income taxes	\$ 6,769	\$ 6,319	\$ 2,495
Deferred income taxes:			
Federal	\$ (2,333)	\$ (803)	\$ (727)
State and local	(185)	(70)	(16)
Foreign	225	(14)	(486)
Deferred income taxes	(2,293)	(887)	(1,229)
Income tax expense	\$ 4,476	\$ 5,432	\$ 1,266

A reconciliation of income tax expense from operations computed at the U.S. federal statutory income tax rate to the Company's effective income tax rate is as follows:

	Year Ended December 31,		
	2019	2018	2017
Expected U.S. federal income taxes at statutory rate	21.0 %	21.0 %	34.0 %
State and local income taxes, net of federal benefit	1.0	1.1	4.5
Foreign taxes	5.9	5.1	6.4
Non-deductible expenses	(0.8)	4.3	0.1
Enactment of the Tax Cuts and Jobs Act	—	—	64.7
Change in valuation allowance	4.9	—	(69.2)
Non-controlling interest	(10.8)	(13.7)	(9.5)
Share-based Compensation	(2.6)	—	0.0
LLC flow-through structure	—	—	(16.9)
Return to Provision	(3.0)	(1.7)	—
Other, net	(1.7)	1.7	3.4
Income tax expense	13.9 %	17.8 %	17.5 %

Our effective income tax rate for 2019 and 2018 was 13.9% and 17.8%, respectively. The Company's annual effective tax rate in 2019 and 2018 was 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. In addition, the 2017 effective tax rate was impacted by the Tax Act and LLC flow through structure. The Tax Act reduces the U.S. federal corporate tax rate to 21%, which negatively impacted our effective tax rate by reducing our deferred tax assets. The non-controlling interest benefited our effective tax rate by reducing our allocable share of taxable income subject to U.S. federal, state and local income taxes. In 2017, the LLC flow-through structure benefited our effective tax rate as prior to the IPO we were subject to certain LLC entity-level taxes and foreign taxes but generally not subject to entity-level U.S. federal income taxes.

Deferred Income Taxes

The significant items comprising deferred tax assets and liabilities is as follows (in thousands):

	December 31,	
	2019	2018
Deferred tax assets:		
Investment in partnership	\$ 53,464	\$ 18,290
Tax Receivable Agreement liability	14,929	1,544
Stock-based compensation	2,666	456
Foreign Tax Credit	208	—
Property and equipment	—	10
Other	—	51
Gross deferred tax assets	71,267	20,351
Valuation allowance	(11,242)	(8,803)
Deferred tax assets, net of valuation allowance	60,025	11,548
Deferred tax liabilities:		
Investment in partnership	(2,246)	(4,146)
Property and equipment	(341)	—
Other	(232)	—
Gross deferred tax liabilities	(2,819)	(4,146)
Net deferred tax liabilities	\$ 57,206	\$ 7,402

As of December 31, 2019 and 2018, the Company did not have any federal or state net operating loss carryforwards for income tax purposes.

The Company evaluates its ability to realize deferred tax assets on a quarterly basis and establishes a valuation allowance when it is more likely than not that all or a portion of a deferred tax asset may not be realized. As of December 31, 2019 and 2018, the Company recognized a deferred tax asset of \$53.5 million and \$18.3 million, respectively, associated with the basis difference in its investment in FAH, LLC upon acquiring these LLC interests. However, a portion of the total basis difference will only reverse upon the eventual sale of its interest in FAH, LLC, which we expect would result in a capital loss. As of December 31, 2019 and 2018, the Company established a valuation allowance in the amount of \$11.2 million and \$8.8 million, respectively, against the deferred tax asset.

Accounting for the Tax Cuts and Jobs Act

In December 2017, the Tax Act was passed. The Tax Act changed existing U.S. tax law, including U.S. corporate tax rates, business-related exclusions, and deductions and credits. The accounting for the income tax effects of the Tax Act has been completed. The significant impacts from the Tax Act are primarily due to the lower U.S. federal corporate tax rate of 21%. The impact to the consolidated statement of operations was an additional \$4.7 million of income tax expense recorded for the year ended December 31, 2017. This expense reflects the revaluation of our net deferred tax assets based on a U.S. federal corporate tax rate of 21%.

Uncertain Tax Positions

The Company regularly evaluates the likelihood of realizing the benefit from income tax positions that we have taken in various federal, state and foreign filings by considering all relevant facts, circumstances and information available. If the Company determines it is more likely than not that the position will be sustained, a benefit will be recognized at the largest amount that we believe is cumulatively greater than 50% likely to be realized.

The following table summarizes changes in the amount of the Company's unrecognized tax benefits for uncertain tax positions for the three years ended December 31, 2019, 2018 and 2017 (in thousands):

	Year Ended December 31,		
	2019	2018	2017
Unrecognized tax benefits at January 1	\$ 490	\$ 490	\$ —
Increases for positions taken in current year	—	—	490
Unrecognized tax benefits at December 31	\$ 490	\$ 490	\$ 490

Of the \$0.5 million of unrecognized tax benefits as of December 31, 2019, 2018 and 2017, \$0.2 million would impact the effective tax rate if recognized.

Interest and penalties related to income tax matters are classified as a component of income tax expense. As of December 31, 2019, and 2018, we have not recorded any interest or penalties as the amounts were not material. Unrecognized tax benefits are recorded in other long-term liabilities on the consolidated balance sheets.

Other Matters

The Company files income tax returns in the U.S. federal jurisdiction and various state and foreign jurisdictions. The Company is subject to U.S. federal, state, and local income tax examinations by tax authorities for years after 2016 and subject to examination for all foreign income tax returns for fiscal 2018 and 2019. There were no open tax examinations at December 31, 2019 and 2018.

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 13, Liabilities under Tax Receivable Agreement.

13. Liabilities under Tax Receivable Agreement

On November 1, 2017, the Company entered into 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 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. FAH, LLC intends to have in effect an election under Section 754 of the Internal Revenue Code effective for each taxable year in which a redemption or exchange (including deemed exchange) of common units for cash or stock occurs. These tax benefit payments are not conditioned upon one or more of the Continuing Equity Owners maintaining a continued ownership interest in FAH, LLC. In general, the Continuing Equity Owners' rights under the Tax Receivable Agreement are assignable, including to transferees of common units in FAH, LLC (other than the Company as transferee pursuant to a redemption or exchange of common units in FAH, LLC). The Company expects to benefit from the remaining 15% of the tax benefits, if any, that the Company may realize.

The Company is not obligated to make any payments under the Tax Receivable Agreement until the tax benefits associated with the transaction that gave rise to the payment are realized. Amounts payable under the Tax Receivable Agreement are contingent upon, among other things, (i) the generation of future taxable income over the term of the Tax Receivable Agreement and (ii) future changes in tax laws. If the Company does not generate sufficient taxable income in the aggregate over the term of the Tax Receivable Agreement to utilize the tax benefits, then it would not be required to make the related Tax Receivable Agreement payments. During years ended December 31, 2019 and 2018, the Company acquired an aggregate of 9.5 million and 1.4 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 our investment in FAH, LLC subject to the provisions of the Tax Receivable Agreement. As a result of these exchanges, during the years ended December 31, 2019 and 2018, the Company recognized an increase to its net deferred tax assets in the amount of \$48.1 million and \$7.0 million, respectively, and corresponding Tax Receivable Agreement liabilities of \$59.0 million and \$6.8 million, respectively, representing 85% of the aggregate tax benefits

we expect 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 our estimate of future taxable income. The Company did not record any liabilities for the Tax Receivable Agreement during the year ended December 31, 2017.

In addition, during the year ended December 31, 2019 the Company recognized \$0.2 million of expenses in other (income) expense, net on our consolidated statements of operations related to remeasurement adjustments of Tax Receivable Agreement liabilities. There were no remeasurement adjustments made to Tax Receivable Agreement liabilities during the years ended December 31, 2018 and 2017.

There were \$0.2 million payments made pursuant to the Tax Receivable Agreement during the year ended December 31, 2019. There were no payments made during the years ended December 31, 2018 and 2017.

As of December 31, 2019 and 2018, the Company's total obligation under the Tax Receivable Agreement was \$65.8 million and \$6.8 million, respectively, of which \$4.3 million and \$0.3 million, respectively, was included in Accrued expenses and other current liabilities consolidated balance sheets. There were no transactions subject to the Tax Receivable Agreement for which the Company did not recognize the related liability, as we concluded that it was probable that the Company would have sufficient future taxable income to utilize all of the related tax benefits. The Company did not have any obligations under the Tax Receivable Agreement as of December 31, 2017.

14. Commitments and Contingencies

The following table summarizes the Company's future minimum commitments as of December 31, 2019 (in thousands):

	2020	2021	2022	2023	2024	Thereafter	Total
Long term debt and related interest ⁽¹⁾	\$ 26,825	\$ 34,532	\$ 34,683	\$ 37,565	\$ 132,849	\$ —	\$ 266,454
Operating leases	11,758	12,678	11,159	11,425	10,982	37,168	95,170
Liabilities under tax receivable agreement ⁽²⁾	4,262	3,762	3,525	3,592	3,665	47,010	65,816
Minimum royalty obligations ⁽³⁾	24,011	2,489	29	19	—	—	26,548
New Revolving Credit Facility ⁽⁴⁾	25,822	—	—	—	—	—	25,822
Total	\$ 92,678	\$ 53,461	\$ 49,396	\$ 52,601	\$ 147,496	\$ 84,178	\$ 479,810

(1) We estimated interest payments through the maturity of our New Credit Facilities by applying the effective interest rate of 5.99% in effect as of December 31, 2019 under our Term Loan A Facility. See Note 10, Debt.

(2) See Note 13, Liabilities under Tax Receivable Agreement.

(3) Represents minimum guaranteed royalty payments under licensing arrangements.

(4) Represents the amount owed as of December 31, 2019 under our New Revolving Credit Facility.

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, we renewed our licensing agreements with Disney and its controlled affiliates, LucasFilm and Marvel. As of December 31, 2018, we recorded a \$2.0 million consent fee under our existing licensing agreements with Disney, which we subsequently paid.

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 10, Debt.

Leases

The Company has entered into non-cancellable operating leases for office, warehouse, and distribution facilities, with original lease periods expiring through 2032. 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. See Note 11, Leases.

Liabilities under 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 13, 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 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 entitled 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 argument on the motion to dismiss was 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." On October 3, 2019, plaintiffs filed a first amended consolidated complaint. The Company moved to dismiss that complaint on December 5, 2019. The Company anticipates that the motion will be fully briefed by March 11, 2020, and that oral argument on the motion will take place March 27, 2020.

Additionally, on June 4, 2018, a putative class action lawsuit entitled Kanugonda 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 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 parties to the federal action, now captioned Berkelhammer v. Funko, Inc. et al. have agreed to a stay of that action pending developments in the state case. The complaints in both state and federal court allege 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 lawsuits seek, among other things, compensatory statutory damages and rescissory damages in account of the consideration paid for our Class A common stock by 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.

15. 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 for which is regularly reviewed by its Chief Operating Decision Maker ("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 product categories as a percent of sales:

	Year ended December 31,		
	2019	2018	2017
Figures	80.8 %	81.6 %	81.8 %
Other	19.2 %	18.4 %	18.2 %

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

	Year ended December 31,		
	2019	2018	2017
Net sales:			
United States	\$ 523,897	\$ 466,044	\$ 376,087
International	271,225	220,029	139,997
Total net sales	<u>\$ 795,122</u>	<u>\$ 686,073</u>	<u>\$ 516,084</u>

	December 31,	
	2019	2018
Long-lived assets:		
United States	\$ 78,394	\$ 23,781
Vietnam and China	19,606	20,662
United Kingdom	35,396	4,128
Total long-lived assets	<u>\$ 133,396</u>	<u>\$ 48,571</u>

16. Related Party Transactions

Members' Equity Contribution

On June 26, 2017, the Company issued 5,000 Class A units in exchange for a contribution of \$5.0 million from several members of management and ACON. As a result of this issuance, the Company recorded equity-based compensation expense in the consolidated statements of operations of \$2.2 million.

ACON Equity Management Agreement

On October 31, 2015, the Company entered into a management services agreement with ACON Equity Management, L.L.C. (“ACON Equity Management”), which requires payment of a monitoring fee equal to the greater of (1) \$500,000 and (2) 2% prior year Adjusted EBITDA, up to a maximum fee of \$2.0 million. Pursuant to the management services agreement, Funko, LLC also agreed to pay ACON Equity Management a one-time advisory fee of \$2.0 million, and agreed to reimburse ACON Equity Management for certain costs and expenses in connection with ACON Equity Management’s performance under the agreement. In connection with the IPO, on November 6, 2017, the management fee agreement terminated. ACON Equity Management waived the \$5.8 million termination fee.

The Company had no management fees for the year ended December 31, 2019 and 2018, respectively. The Company recognized \$1.7 million in management fees for the years ended December 31, 2017. These fees are recorded within selling, general and administrative expenses. As of December 31, 2019 and 2018, there were no amounts due to ACON Equity Management.

Promissory and Subordinated Promissory Notes

In October 2015, the Company entered into subscription agreements with several members of management (the “Purchasers”) to purchase FAH, LLC Class A units having an aggregate purchase price of \$0.9 million. Funko, LLC entered into a secured promissory note with each Purchaser in an amount equal to the purchase price of the Class A units purchased by such individual. Amounts outstanding under the promissory notes were collateralized by all direct or indirect ownership interests of the Purchasers in FAH, LLC. The promissory notes had an 8% interest rate compounded on an annual basis, and were recorded as a non-cash transaction within members’ equity. The Company recognized interest on a cash basis when principal payments were made, and recorded a nominal amount of interest income for the year ended December 31, 2017. On October 5, 2017, outstanding aggregate principal and accrued interest of \$0.2 million was forgiven for certain of FAH, LLC’s officers and executives. The remaining promissory notes were repaid as part of the reorganization Transactions, as defined below in “Reorganization Transactions.”

See discussion of the Subordinated Promissory Notes in Note 10, Debt. The Subordinated Promissory Notes were repaid in November 2017, with proceeds from the IPO.

Other Agreements

In June 2017, in connection with the Loungefly Acquisition, 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 of the Company’s employees, who were the former owners of Loungefly. For the period from January 1, 2018 through July 12, 2018 and for the year ended December 31, 2017, the Company recorded \$0.2 million and \$0.2 million in rental expense related to the lease, which was recorded in selling, general and administrative expenses in the Company’s 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, Ltd. For the years ended December 31, 2019 and 2018, the Company recorded approximately \$2.3 million and \$5.1 million, respectively, in net sales from business with Forbidden Planet. At December 31, 2019 and 2018, accounts receivable from Forbidden Planet were \$0.2 million and \$0.8 million on the consolidated balance sheet, respectively.

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 year ended December 31, 2019, the Company obtained operating lease right-of-use assets in exchange for new operating lease obligations of \$1.0 million and recorded \$0.2 million of rental expense related to the leases, which was recorded in selling, general and administrative expenses in the Company’s audited consolidated statements of operations. On October 12, 2019, one of the leases was modified, which had the effect of reducing the carrying value of the lease liability and associated right-of-use asset by \$0.4 million. At December 31, 2019, the Company had recorded operating lease right-of-use assets and operating lease liabilities of \$0.6 million related to the leases.

17. Employee Benefit Plans

We currently maintain the Funko 401(k) Plan, a defined contribution retirement and savings plan, for the benefit of our employees, including our named executive officers, who satisfy certain eligibility requirements. Our named executive officers are eligible to participate in the 401(k) Plan on the same terms as other full-time employees. The Code allows eligible employees to defer a portion of their compensation, within prescribed limits, on a pre-tax basis through contributions to the 401(k) Plan. Currently, we match contributions made by participants in the 401(k) Plan up to 4% of the employee earnings, and these matching contributions are fully vested as of the date on which the contribution is made. We believe that providing a vehicle for tax-deferred retirement savings through our 401(k) Plan, and making fully vested matching contributions, adds to the overall desirability of our compensation package and further incentivizes our employees, including our named executive officers, in accordance with our compensation policies. The Company's employer matching contributions were \$1.6 million, \$1.1 million and \$0.7 million for the years ended December 31, 2019, 2018 and 2017, respectively.

18. Stockholders' Equity

In connection with the Company's IPO, the Company's board of directors approved an amended and restated certificate of incorporation (the "Amended and Restated Certificate of Incorporation"), which became effective on November 1, 2017. The Amended and Restated Certificate of Incorporation authorizes the issuance of up to 200,000,000 shares of Class A common stock, up to 50,000,000 shares of Class B common stock and 20,000,000 shares of preferred stock, each having a par value of \$0.0001 per share. Shares of Class A common stock have both economic and voting rights. Shares of Class B common stock have no economic rights, but do have voting rights. Holders of shares of Class A common stock and Class B common stock are entitled to one vote per share on all matters presented to stockholders. The Company's board of directors has the discretion to determine the rights, preferences, privileges, restrictions and liquidation preferences of any series of preferred stock.

Reorganization Transactions

On November 1, 2017, in connection with the completion of the IPO, the Company completed a series of reorganization Transactions. The Transactions included the following:

- The amendment and restatement of the existing FAH, LLC limited liability company agreement (the "FAH LLC Agreement") to, among other things, (i) convert all existing ownership interests (including vested profits interests and all unvested profits interests and existing warrants to purchase ownership interests in FAH, LLC) into common units of FAH, LLC (subject to common units received in exchange for unvested profits interests remaining subject to time-based vesting requirements), and (ii) appoint the Company as FAH, LLC's sole managing member upon its acquisition of common units in connection with the IPO;
- The amendment and restatement of the Company's certificate of incorporation to, among other things, provide (i) for Class A common stock, with each share of Class A common stock entitling its holders to one vote per share on all matters presented to stockholders generally and (ii) for Class B common stock, with each share of Class B common stock entitling its holders to one vote per share on all matters presented to stockholders generally and that shares of Class B common stock may only be held by the Continuing Equity Owners and their permitted transferees;
- Certain funds affiliated with ACON Funko Investors (the "Former Equity Owners") exchanged their indirect ownership interests in common units of FAH, LLC for 12,921,039 shares of Class A common stock on a one-for-one basis; and
- The Company entered into (i) a stockholders' agreement with ACON Funko Investors and the Former Equity Owners, Fundamental Capital, LLC and Funko International, LLC (collectively, "Fundamental") and Brian Mariotti, the Company's Chief Executive Officer, (ii) a registration rights agreement with certain of the Original Equity Owners (including each of the Company's executive officers), and (iii) a tax receivable agreement (the "Tax Receivable Agreement") with FAH, LLC and each of the Continuing Equity Owners.

The Transactions were effected on November 1, 2017, prior to the time the Company's Class A common stock was registered under the Exchange Act, and prior to the completion of the IPO.

FAH, LLC Recapitalization

As noted above, the FAH LLC Agreement, among other things, appointed the Company as FAH, LLC's sole managing member and reclassified all outstanding membership interests in FAH, LLC as non-voting common units. As the sole managing member of FAH, LLC, the Company controls the management of FAH, LLC. As a result, the Company consolidates FAH, LLC's financial results and reports a non-controlling interest related to the economic interest of FAH, LLC held by the Continuing Equity Owners.

The Amended and Restated Certificate of Incorporation and the FAH LLC Agreement discussed above requires FAH, LLC and the Company to, at all times, maintain (i) a one-to-one ratio between the number of shares of Class A common stock issued by the Company and the number of common units owned by the Company and (ii) a one-to-one ratio between the number of shares of Class B common stock owned by the Continuing Equity Owners and the number of common units owned by the Continuing Equity Owners (other than common units issuable upon the exercise of options and common units that are subject to time-based vesting requirements (the "Excluded Common Units")). The Company may issue shares of Class B common stock only to the extent necessary to maintain the one-to-one ratio between the number of common units of FAH, LLC held by the Continuing Equity Owners (other than the Excluded Common Units) and the number of shares of Class B common stock issued to the Continuing Equity Owners. Shares of Class B common stock are transferable only together with an equal number of common units of FAH, LLC. Only permitted transferees of common units held by the Continuing Equity Owners will be permitted transferees of Class B common stock.

The Continuing Equity Owners may from time to time at each of their options (subject, in certain circumstances, to time-based vesting requirements) require FAH, LLC to redeem all or a portion of their common units in exchange for, at the Company's 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 the Company's election, the Company may effect a direct exchange 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. Simultaneously with the payment of cash or shares of Class A common stock, as applicable, in connection with a redemption or exchange of common units pursuant to the terms of the FAH LLC Agreement, a number of shares of our Class B common stock registered in the name of the redeeming or exchanging Continuing Equity Owner will be cancelled for no consideration on a one-for-one basis with the number of common units so redeemed or exchanged.

Initial Public Offering

As noted above, on November 6, 2017, the Company completed its IPO of 10,416,666 shares of Class A common stock at a public offering price of \$12.00 per share and received approximately \$117.3 million in net proceeds, after deducting underwriting discounts and commissions. The Company 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 initial public offering price per share of Class A common stock sold in the IPO less underwriting discounts and commissions. Immediately following the completion of the IPO, there were 24,975,932 shares of Class B common stock outstanding and 23,337,705 shares of Class A common stock outstanding, comprised of 10,416,666 shares issued in connection with the IPO and 12,921,039 shares issued in connection with the Transactions described above.

Equity-Based Compensation

Funko, Inc. 2017 Incentive Award Plan. On October 23, 2017, the Company adopted the Funko, Inc. 2017 Incentive Award Plan (the "2017 Plan"), which became effective on November 1, 2017, upon the effectiveness of the registration statement on Form S-1 (File No. 333-220856), as amended, filed with the SEC in connection with the IPO. The Company reserved a total of 5,518,518 shares of Class A common stock for issuance pursuant to the 2017 Plan. In connection with the IPO, the Company granted 1,028,500 options to purchase shares of Class A common stock to certain of its directors, executive officers and employees. Subsequent to the IPO, the Company has granted options to purchase shares of Class A common stock and restricted stock units on Class A common stock to certain of its directors, executive officers and employees under the 2017 Plan.

Funko, Inc. 2019 Incentive Award Plan. Effective April 18, 2019, the Company adopted the Funko, Inc. 2019 Incentive Award Plan (the "2019 Plan"). We have also reserved for issuance an aggregate number of shares under the 2019 Plan equal to the sum of (i) 3,000,000 shares of our Class A common stock and (ii) an annual increase on the first day of each calendar year beginning on January 1, 2020 and ending on and including January 1, 2029,

equal to the lesser of (A) 2% of the shares of Class A Common Stock outstanding as of the last day of the immediately preceding fiscal year on a fully-diluted basis and (B) such lesser number of shares of Class A common stock as determined by our board of directors.

A summary of 2017 Plan stock option activity for the year ended December 31, 2019 is as follows:

	Funko, Inc. Stock Options	Weighted Average Exercise Price	Aggregate Intrinsic Value	Remaining Contractual Life
	(in thousands)		(in thousands)	(years)
Outstanding at December 31, 2018	1,853	\$ 12.79	\$ 1,950	8.84
Granted	1,073	20.23	—	
Exercised	(115)	13.52	996	
Forfeited	(128)	16.48	609	
Outstanding at December 31, 2019	<u>2,683</u>	15.55	7,524	8.60
Options exercisable at December 31, 2019	839	\$ 12.62	\$ 3,875	8.16

A summary of 2017 Plan restricted stock unit activity for the year ended December 31, 2019 is as follows:

	Funko, Inc. Restricted Stock Units	Weighted Average Grant Date Fair Value	Aggregate Intrinsic Value	Remaining Contractual Life
	(in thousands)		(in thousands)	(years)
Unvested at December 31, 2018	1,674	\$ 14.81	\$ 22,023	4.06
Granted	123	20.45	2,515	
Vested	(203)	11.88	4,116	
Forfeited	(46)	12.09	986	
Unvested at December 31, 2019	<u>1,548</u>	\$ 15.72	\$ 26,564	3.14

As of December 31, 2019, the Company had not issued any awards under the 2019 Plan.

Options to purchase common units in FAH, LLC. In connection with the IPO, existing options to purchase Class A units in FAH, LLC were converted into 555,867 options to purchase common units in FAH, LLC.

A summary of FAH, LLC stock option activity for the year ended December 31, 2019 is as follows:

	FAH, LLC Stock Options	Weighted Average Exercise Price	Aggregate Intrinsic Value	Remaining Contractual Life
	(in thousands)		(in thousands)	(years)
Outstanding at December 31, 2018	552	0.41	7,038	4.91
Exercised	(116)	0.31	2,408	
Forfeited	—			
Cancelled	—			
Outstanding at December 31, 2019	<u>436</u>	\$ 0.43	\$ 7,299	3.87
Options exercisable at December 31, 2019	436	\$ 0.43	\$ 7,299	3.87

Unvested common units in FAH, LLC. In connection with the IPO, unvested common units to purchase profit interests in FAH, LLC were converted into 1,901,327 unvested common units of FAH, LLC.

A summary of unvested common unit activity for the year ended December 31, 2019 is as follows:

	Common Units	Weighted Average Grant Date Fair Value
	(in thousands)	
Unvested at December 31, 2018	625	\$ 2,360
Granted	—	—
Vested	(562)	2,204
Forfeited	(21)	46
Unvested at December 31, 2019	42	\$ 110

Equity-based compensation expense. The Company measures and recognizes expense for its equity-based compensation granted to employees and directors based on the fair value of the awards on the grant date. The fair value of restricted stock units is based on the market price of Class A common stock on the date of grant. The fair value of option awards is estimated at the grant date using the Black-Scholes option pricing model that requires management to apply judgment and make estimates, including:

- *Volatility*—this is estimated based primarily on historical volatilities of a representative group of publicly traded consumer product companies with similar characteristics
- *Risk-free interest rate*—this is the U.S. Treasury rate as of the grant date having a term equal to the expected term of the award
- *Expected term*—represents the estimated period of time until an award is exercised and was calculated based on the simplified method
- *Dividend yield*—the Company does not plan to pay dividends in the foreseeable future

For each of the options granted under the 2017 Plan, the following were the weighted-average of the option pricing model inputs:

	Year ended December 31,		
	2019	2018	2017
Expected term (years)	6.07	6.25	6.25
Expected volatility	38.7 %	34.4 %	29.5 %
Risk-free interest rate	2.4 %	2.8 %	2.1 %
Dividend yield	— %	— %	— %

Equity-based compensation expense is recognized on a straight-line basis over the vesting period of the award. The Company records equity-based compensation to selling, general and administrative expense on the consolidated statement of operations. Equity-based compensation for the years ended December 31, 2019, 2018 and 2017 were \$13.0 million, \$9.1 million and \$5.4 million, respectively.

As of December 31, 2019, there was \$29.0 million of total unrecognized equity-based compensation expense that the Company expected to recognize over a remaining weighted-average period of 3.0 years. Of this, \$10.7 million is related to options to purchase Class A common stock in Funko, Inc., \$18.2 million related to unvested restricted stock units in Class A common stock of Funko, Inc. and \$0.1 million is related to unvested common units in FAH, LLC. As of December 31, 2019, the Company expected to recognize these costs over a remaining weighted average period of 2.9 years for options to purchase Class A units in Funko, Inc., and 3.1 years for unvested restricted stock units in Class A common stock of Funko, Inc. and 0.7 years for unvested common units in FAH, LLC.

19. Non-controlling Interests

In connection with the Transactions described in Note 18, Stockholders' Equity, the Company became the sole managing member of FAH, LLC and as a result consolidates the financial results of FAH, LLC. The Company 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.

The Company used the net proceeds from its IPO to purchase 10,416,666 newly-issued common units of FAH, LLC. Additionally, in connection with the Transactions, certain funds affiliated with the Former Equity Owners exchanged their indirect ownership interests in common units of FAH, LLC for 12,921,039 shares of Class A common stock on a one-for-one basis.

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 December 31, 2019, 2018 and 2017, Funko, Inc. owned 34.9 million, 25.0 million and 23.3 million of FAH, LLC common units, respectively, representing a 68.7%, 50.2% and 48.3% economic ownership interest in FAH, LLC, respectively.

Net income and comprehensive income of FAH, LLC excludes certain activity attributable to Funko, Inc., including \$10.8 million, \$6.4 million and \$0.4 million of equity-based compensation expense for share-based compensation awards issued by Funko, Inc. for the years ended December 31, 2019, 2018 and 2017, respectively, and \$2.2 million, \$3.6 million and \$0.5 million of income tax expense for corporate, federal, state and local taxes attributable to Funko, Inc. for the years ended December 31, 2019, 2018 and 2017, respectively.

20. Earnings per Share

Basic and Diluted 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.

As described in Note 18, Stockholders' Equity, on November 1, 2017, the LLC Agreement was amended and restated to, among other things, (i) provide for a new single class of common membership interests, the common units of FAH, LLC, and (ii) exchange all of the then-existing membership interests of the Original Equity Owners for common units of FAH, LLC. This Recapitalization changed the relative membership rights of the Original Equity Owners such that retroactive application of the Recapitalization to periods prior to the IPO for the purposes of calculating earnings per share would not be appropriate.

Prior to the IPO, the FAH, LLC membership structure included Class A Units, Profits Units and HR Units. The Company analyzed the calculation of earnings per unit for periods prior to the IPO using the two-class method and determined that it resulted in values that would not be meaningful to the users of these consolidated financial statements. Therefore, earnings per share information has not been presented for periods prior to the IPO on November 6, 2017. The basic and diluted earnings per share period for the year ended December 31, 2017 represents only the period of November 6, 2017 to December 31, 2017.

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:

	Year Ended December 31, 2019	Year Ended December 31, 2018	Period from November 6, 2017 through December 31, 2017
Numerator:			
Net income	\$ 27,820	\$ 25,062	\$ 3,085
<i>Less:</i> net income attributable to non-controlling interests	16,095	17,599	2,047
Net income attributable to Funko, Inc. — basic	\$ 11,725	\$ 7,463	\$ 1,038
<i>Add:</i> Reallocation of net income attributable to non- controlling interests from the assumed exchange of common units of FAH, LLC for Class A common stock	—	—	1,219
Net income attributable to Funko, Inc. — diluted	\$ 11,725	\$ 7,463	\$ 2,257
Denominator:			
Weighted-average shares of Class A common stock outstanding — basic	30,897,569	23,821,025	23,337,705
<i>Add:</i> Dilutive common units of FAH, LLC that are convertible into Class A common stock	2,028,204	1,739,033	27,297,348
Weighted-average shares of Class A common stock outstanding — diluted	32,925,773	25,560,058	50,635,053
Earnings per share of Class A common stock — basic	\$ 0.38	\$ 0.31	\$ 0.04
Earnings per share of Class A common stock — diluted	\$ 0.36	\$ 0.29	\$ 0.04

For the years ended December 31, 2019 and 2018 and the period of November 6, 2017 to December 31, 2017 an aggregate of 20.1 million, 25.7 million and 1.8 million of potentially dilutive securities, respectively, 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 years ended December 31, 2019 and 2018, anti-dilutive securities included 19.1 million and 25.1 million 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.

21. Quarterly Financial Information (Unaudited)

	Three Months Ended							
	Dec. 31, 2019	Sept. 31, 2019	June 30, 2019	March 31, 2019	Dec. 31, 2018	Sept. 31, 2018	June 30, 2018	March 31, 2018
	(In thousands)							
Net sales	\$ 213,551	\$ 223,307	\$ 191,199	\$ 167,065	\$ 233,224	\$ 176,915	\$ 138,723	\$ 137,211
Cost of sales (exclusive of depreciation and amortization)	151,125	137,801	119,998	103,656	149,172	109,046	85,884	86,644
Selling, general and administrative expenses	57,264	52,424	43,647	40,468	45,015	41,267	34,537	34,502
Net (loss) income	(6,288)	15,548	11,415	7,145	15,519	7,551	274	1,719
Net (loss) income attributable to non-controlling interests	(2,047)	6,909	6,283	4,950	10,292	5,981	204	1,122
Net (loss) income attributable to Funko, Inc.	(4,241)	8,639	5,132	2,195	5,227	1,570	70	597
Earnings (loss) per share of Class A common stock — basic	\$ (0.12)	\$ 0.27	\$ 0.17	\$ 0.08	\$ 0.21	\$ 0.07	\$ —	\$ 0.03
Earnings (loss) per share of Class A common stock — diluted	\$ (0.12)	\$ 0.25	\$ 0.16	\$ 0.08	\$ 0.20	\$ 0.06	\$ —	\$ 0.02

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

Not Applicable.

ITEM 9A. CONTROLS AND PROCEDURES

Limitations on Effectiveness of 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 December 31, 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.

Management's Report on Internal Control over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rule 13a-15(f) under the Securities Exchange Act of 1934, as amended.

Our management, under the supervision and with the participation of our chief executive officer and our chief financial officer, conducted an assessment of the effectiveness of our internal control over financial reporting based on the criteria set forth in "Internal Control—Integrated Framework (2013)" issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this assessment, management concluded that, as of December 31, 2019, our internal control over financial reporting was not effective as a result of a material weakness in our internal control over financial reporting 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.

This annual report does not include an attestation report of our independent registered public accounting firm on internal control over financial reporting due to an exemption established by the JOBS Act for "emerging growth companies".

Remediation Plan

We are implementing a plan to remediate the material weakness, which includes identifying key stakeholders across the relevant departments, providing training and education from outside experts, formalizing a customs policy and procedures manual which includes, 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

Except for the remediation measures described above, there were no changes in our internal control over financial reporting during the quarter ended December 31, 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

Item 9B. OTHER INFORMATION

Not applicable.

PART III**ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE**

Pursuant to General Instruction G(3) to Form 10-K and Instruction 3 to Item 401(b) of Regulation S-K, information regarding our executive officers is provided in Item 1 of this Annual Report on Form 10-K under the caption “Executive Officers of the Registrant,” and will also appear in our definitive proxy statement for our 2020 Annual Meeting of Stockholders. The remaining information required by Items 401, 405, 406 and 407(c)(3), (d)(4) and (d)(5) of Regulation S-K will be included under the headings “Election of Directors,” “Corporate Governance,” and “Delinquent Section 16(a) Reports” in our definitive proxy statement for our 2020 Annual Meeting of Stockholders, and such required information is incorporated herein by reference.

ITEM 11. EXECUTIVE COMPENSATION

The information required by Items 402, 407(e)(4), and (e)(5) of Regulation S-K will be included under the headings “Executive Compensation” and “Compensation Committee Interlocks and Insider Participation” in our definitive proxy statement for our 2020 Annual Meeting of Stockholders, and such information is incorporated herein by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**Securities Authorized for Issuance Under Equity Compensation Plans (as of December 31, 2019)**

Plan category:	Number of Securities to be Issued Upon Exercise of Outstanding Options, Warrants, and Rights	Weighted-Average Exercise Price of Outstanding Options, Warrants, and Rights	Number of Securities Available for Future Issuance Under Equity Compensation Plans (Excludes Securities Reflected in First Column)
Equity compensation plans approved by security holders			4,287,465 ⁽¹⁾
Stock Options	2,683,024	\$ 15.55	—
Restricted Stock Units	1,548,029	—	—
Equity compensation plans not approved by security holders	—	—	—
Total	4,231,053	\$ 15.55	4,287,465

- (1) Includes 1,287,465 shares of Class A common stock available for issuance under our 2017 Incentive Award Plan and 3,000,000 shares of Class A common stock available for issuance under our 2019 Incentive Award Plan. The number of shares authorized under our 2019 Incentive Award Plan will increase on the first day of each calendar year beginning on January 1, 2020 and ending on and including January 1, 2029, equal to the lesser of (A) 2% of the shares of Class A Common Stock outstanding as of the last day of the immediately preceding fiscal year on a fully-diluted basis and (B) such lesser number of shares of Class A common stock as determined by our Board of Directors.

Other

The remaining information required by Item 403 of Regulation S-K will be included under the heading “Security Ownership of Certain Beneficial Owners and Management” in our definitive proxy statement for our 2020 Annual Meeting of Stockholders, and such required information is incorporated herein by reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

The information required by Items 404 and 407(a) of Regulation S-K will be included under the headings “Certain Relationships and Related Person Transactions,” “Corporate Governance” and “Director Independence” in our definitive proxy statement for our 2020 Annual Meeting of Stockholders, and such information is incorporated herein by reference.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The information required by Item 9(e) of Schedule 14A of the Exchange Act will be included under the heading “Independent Registered Public Accounting Firm Fees and Other Matters” in our definitive proxy statement for our 2020 Annual Meeting of Stockholders, and such information is incorporated herein by reference.

PART IV

ITEM 15. EXHIBITS

(a) Documents filed as part of this report:

1. Financial Statements

The consolidated financial statements of the Company are listed in the index under Part II, Item 8, of this Annual Report on Form 10-K.

2. Financial Statement Schedules

All schedules are omitted because they are not applicable, not required or the required information is shown in the consolidated financial statements or notes thereto.

3. List of 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	11/7/2017	
3.2	Amended and Restated Bylaws of Funko, Inc.	S-8	333-221390	4.2	11/7/2017	
4.1	Specimen Stock Certificate evidencing the shares of Class A common stock	S-1	333-220856	4.1	10/23/2017	
4.2	Description of Securities					*
10.1 †	Funko Acquisition Holdings, L.L.C. 2015 Option Plan, Amended and Restated as of November 1, 2017.015 Option Plan, Amended and Restated as of November 1, 2017.	10-K	001-38274	10.1	3/19/2018	
10.2 †	Form of Option Agreement Form of Option Agreement under Funko Acquisition Holdings, L.L.C. 2015 Option Plan. Funko Acquisition Holdings, L.L.C. 2015 Option Plan.	S-1	333-220856	10.15	10/6/2017	
10.3 †	2017 Incentive Award Plan, dated October 23, 2017.	10-K	001-38274	10.3	3/19/2018	
10.4 †	Form of Stock Option Agreement under 2017 Incentive Award Plan.	S-1/A	333-220856	10.19	10/23/2017	
10.5 †	2017 Executive Annual Incentive Plan, dated October 23, 2017.	10-K	001-38274	10.5	3/19/2018	
10.6 †	Employment Agreement, dated October 30, 2015, by and between Funko, LLC and Brian Mariotti.	S-1	333-220856	10.18	10/6/2017	
10.7 †	Offer letter, dated September 29, 2013, by and between Funko, LLC and Russell Nickel.	S-1	333-220856	10.19	10/6/2017	
10.8 †	Employment Agreement, dated October 20, 2017, by and between Funko, Inc. and Russell Nickel.	10-K	001-38274	10.8	3/19/2018	
10.9 †	Offer letter, dated June 15, 2016, by and between Funko, LLC and Tracy Daw.	S-1	333-220856	10.21	10/6/2017	
10.10 †	Employment Agreement, dated October 20, 2017, by and between Funko, Inc. and Tracy Daw.	10-K	001-38274	10.10	3/19/2018	
10.11 †	Employment Agreement, dated October 20, 2017, by and between Funko, Inc. and Andrew Perlmutter.	10-K	001-38274	10.13	3/19/2018	

Exhibit Number	Exhibit Description	Incorporated by Reference				Filed/ Furnished Herewith
		Form	File No.	Exhibit	Filing Date	
10.12 †	Form of Indemnification Agreement for Directors and Officers.	S-1/A	333-220856	10.27	10/12/2017	
10.13 †	Form of Restricted Stock Unit Award Agreement under 2017 Incentive Award Plan	10-Q	001-38274	10.1	8/10/2018	
10.14 †	Funko, Inc. Non-Employee Director Compensation Policy.	10-K	001-38274	10.16	3/6/2019	
10.15	Pledge and Security Agreement, dated as of October 30, 2015, by Funko Acquisition Holdings, L.L.C., Funko Holdings LLC and Funko, LLC, in favor of Cerberus Business Finance, LLC, as Collateral Agent.	S-1	333-220856	10.11	10/6/2017	
10.16	Security Agreement Supplement, dated as of June 28, 2017, by Loungefly, LLC, in favor of Cerberus Business Finance, LLC, as Collateral Agent.	S-1	333-220856	10.12	10/6/2017	
10.17	Tax Receivable Agreement, dated as of November 1, 2017, between Funko, Inc., Funko Acquisition Holdings, L.L.C., the Members of the LLC, and Tax Receivable Agreement, dated as of November 1, 2017, between Funko, Inc., Funko Acquisition Holdings, L.L.C., the Members of the LLC, and the Management Representative. Management Representative.	10-K	001-38274	10.25	3/19/2018	
10.18	Stockholders Agreement, dated as of November 1, 2017, between Funko, Inc., ACON Funko Investors, L.L.C. and related entities, Fundamental Capital, LLC, Funko International, LLC, and Brian Mariotti.	10-K	001-38274	10.26	3/19/2018	
10.19	Second Amended and Restated LLC Agreement of Funko Acquisition Holdings, L.L.C., dated as of November 1, 2017.	10-K	001-38274	10.27	3/19/2018	
10.20	Amendment No. 1 to Second Amended and Restated Limited Liability Company Agreement of Funko Acquisition Holdings L.L.C., dated as of May 10, 2018.	10-Q	001-38274	10.2	5/11/2018	
10.21	Registration Rights Agreement, dated as of November 1, 2017, between Funko, Inc., ACON Funko Investors, L.L.C. and related entities, Fundamental Capital, LLC, Funko International, LLC, Brian Mariotti, Tracy Daw, The Jon P. and Trishawn P. Kipp Children's Trust uad 5/31/14, Russell Nickel, and Andrew Perlmutter.	10-K	001-38724	10.28	3/19/2018	
10.22	Credit Agreement dated October 22, 2018, among Funko Acquisition Holdings, L.L.C., Funko Holdings LLC, Funko, LLC and Loungefly, LLC, PNC Bank, National Association, as Administrative Agent and Collateral Agent, and each other financial institution from time to time party thereto	8-K	001-38274	10.1	10/25/2018	
10.23	First Amendment to Credit Agreement, dated February 11, 2019, among Funko Acquisition Holdings, L.L.C., Funko Holdings LLC, Funko, LLC and Loungefly, LLC, PNC Bank, National Association, as Administrative Agent, Collateral Agent and L/C Issuer.	10-K	001-38274	10.33	3/6/2019	

Exhibit Number	Exhibit Description	Incorporated by Reference				Filed/ Furnished Herewith
		Form	File No.	Exhibit	Filing Date	
10.24	Amendment No. 2, dated as of September 23, 2019, among Funko Acquisition Holdings, L.L.C., Funko Holdings LLC, Funko, LLC, Loungefly, LLC, Funko Games, LLC, PNC Bank, National Association, as administrative agent and collateral agent, and each other financial institution from time to time party thereto.	8-K	001-38274	10.1	9/24/2019	
10.25 †	Transition and Release of Claims Agreement, dated April 15, 2019, between Funko, Inc. and Russell Nickel.	8-K	001-38274	10.1	4/18/2019	
10.26 †	Amendment to Employment Agreement, dated April 24, 2019, by and between Funko, Inc. and Andrew Perlmutter.	10-Q	001-38274	10.2	5/3/2019	
10.27 †	Employment Agreement, dated July 22, 2019, between Funko, Inc. and Jennifer Fall Jung.	8-K	001-38274	10.1	7/23/2019	
10.28 †	Funko, Inc. 2019 Incentive Award Plan.	8-K	001-38274	10.1	6/27/2019	
21.1	List of Subsidiaries					*
23.1	Consent of Independent Registered Public Accounting Firm					*
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

† Management contract or compensation plan or arrangement

ITEM 16. FORM 10-K SUMMARY

None.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Date: March 5, 2020

FUNKO, INC.(Registrant)

By: /s/ Jennifer Fall Jung

Jennifer Fall Jung

Chief Financial Officer (Principal Financial Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of Registrant and in the capacities and on the dates indicated.

Signature	Title	Date
<u>/s/ Brian Mariotti</u> Brian Mariotti	Chief Executive Officer and Director (Principal Executive Officer)	March 5, 2020
<u>/s/ Jennifer Fall Jung</u> Jennifer Fall Jung	Chief Financial Officer (Principal Financial and Accounting Officer)	March 5, 2020
<u>/s/ Ken Brotman</u> Ken Brotman	Chairman of the Board and Director	March 5, 2020
<u>/s/ Gino Dellomo</u> Gino Dellomo	Director	March 5, 2020
<u>/s/ Charles Denson</u> Charles Denson	Director	March 5, 2020
<u>/s/ Diane Irvine</u> Diane Irvine	Director	March 5, 2020
<u>/s/ Adam Kriger</u> Adam Kriger	Director	March 5, 2020
<u>/s/ Sarah Kirshbaum Levy</u> Sarah Kirshbaum Levy	Director	March 5, 2020
<u>/s/ Michael Lunsford</u> Michael Lunsford	Director	March 5, 2020

DESCRIPTION OF CAPITAL STOCK

The following description of the capital stock of Funko, Inc. (the “Company,” “we,” “us,” and “our”) and certain provisions of our amended and restated certificate of incorporation (our “certificate”) and amended and restated bylaws (our “bylaws”) are summaries and are qualified in their entirety by reference to the full text of our certificate and bylaws and applicable provisions of the General Corporation Law of the State of Delaware (the “DGCL”).

Our certificate authorizes capital stock consisting of:

- 200,000,000 shares of Class A common stock, par value \$0.0001 per share;
- 50,000,000 shares of Class B common stock, par value \$0.0001 per share; and
- 20,000,000 shares of preferred stock, par value \$0.0001 per share.

Common Stock

Class A Common Stock

Holders of shares of our Class A common stock are entitled to one vote for each share held of record on all matters submitted to a vote of the holders of Class A common stock, whether voting separately as a class or otherwise. The holders of our Class A common stock do not have cumulative voting rights in the election of directors.

Holders of shares of our Class A common stock are entitled to receive dividends when and if declared by our board of directors out of funds legally available therefor, subject to any statutory or contractual restrictions on the payment of dividends and to any restrictions on the payment of dividends imposed by the terms of any outstanding preferred stock.

Upon our dissolution or liquidation, after payment in full of all amounts required to be paid to creditors and to the holders of preferred stock having liquidation preferences, if any, the holders of shares of our Class A common stock and Class B common stock will be entitled to receive pro rata our remaining assets available for distribution; provided, that the holders of shares of Class B common stock shall be entitled to receive \$0.0001 per share, and upon receiving such amount, the holders of shares of Class B common stock, as such, shall not be entitled to receive any other assets or funds of the Company.

Holders of shares of our Class A common stock do not have preemptive, subscription, redemption or conversion rights. There are no redemption or sinking fund provisions applicable to the Class A common stock.

Class B Common Stock

Each share of our Class B common stock entitles its holders to one vote per share on all matters submitted to a vote of the holders of Class B common stock, whether voting separately as a class or otherwise. The holders of shares of our Class B common stock do not have cumulative voting rights in the election of directors.

Additional shares of Class B common stock may be issued only to the extent necessary to maintain a one-to-one ratio between the number of common units of Funko Acquisition Holdings, L.L.C., a Delaware limited liability company ("FAH, LLC") held by the Permitted Class B Owners (as defined below) and the number of shares of Class B common stock issued to the Permitted Class B Owners.

Shares of Class B common stock are transferable only together with an equal number of common units of FAH, LLC. Only permitted transferees of common units held by the Permitted Class B Owners will be permitted transferees of Class B common stock. "Permitted Class B Owners" means collectively, the holders of common units of FAH, LLC, or any successor entities thereto, as set forth on Schedule A of our certificate, their respective successors and assigns as well as their respective transferees.

Holders of shares of our Class B common stock vote together with holders of our Class A common stock as a single class (or, if any holders of shares of Preferred Stock are entitled to vote together with the holders of Common Stock, as a single class with such holders of Preferred Stock) on all matters presented to our stockholders for their vote or approval, except for certain amendments to our certificate described below or as otherwise required by applicable law or the certificate.

Holders of our Class B common stock do not have any right to receive dividends or to receive a distribution upon dissolution or liquidation. Additionally, holders of shares of our Class B common stock do not have preemptive, subscription, redemption or conversion rights. There are no redemption or sinking fund provisions applicable to the Class B common stock. Any amendment of our certificate of incorporation that gives holders of our Class B common stock (1) any rights to receive dividends or any other kind of distribution, (2) any right to convert into or be exchanged for Class A common stock or (3) any other economic rights will require, in addition to stockholder approval, the affirmative vote of holders of our Class A common stock voting separately as a class.

Preferred Stock

The total of our authorized shares of preferred stock is 20,000,000 shares. We have no shares of preferred stock outstanding.

Under the terms of our certificate, our board of directors is authorized to direct us to issue shares of preferred stock in one or more series without stockholder approval. Our board of directors has the discretion to determine the rights, preferences, privileges and restrictions, including voting rights, dividend rights, conversion rights, redemption privileges and liquidation preferences, of each series of preferred stock.

The purpose of authorizing our board of directors to issue preferred stock and determine its rights and preferences is to eliminate delays associated with a stockholder vote on specific issuances. The issuance of preferred stock, while providing flexibility in connection with possible acquisitions, future financings and other corporate purposes, could have the effect of making it more difficult for a third party to acquire, or could discourage a third party from seeking to acquire, a majority of our outstanding voting stock. Additionally, the issuance of preferred stock may adversely affect the holders of our Class A common stock by restricting dividends on the Class A common stock, diluting the voting power of the Class A common stock or subordinating the liquidation rights of the Class A common stock.

Registration Rights

In connection with our IPO in November 2017, we entered into a Registration Rights Agreement with certain of the Original Equity Owners (as defined below) (including each of our executive officers) granting such parties specified rights to require us to register all or a portion of their shares under the Securities Act of 1933, as amended (the "Securities Act"). "Original Equity Owners" means the owners of ownership interests in FAH, LLC prior to the IPO, which include ACON Funko Investors, L.L.C., a Delaware limited liability company, and certain funds affiliated with ACON Funko Investors, L.L.C.

(collectively, "ACON") and Fundamental Capital, LLC and Funko International, LLC (collectively, "Fundamental").

Forum Selection

Our certificate provides that unless we consent in writing to the selection of an alternative forum, the Court of Chancery of the State of Delaware will, to the fullest extent permitted by applicable 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 Delaware General Corporation Law of the State of Delaware (the "DGCL"), our certificate or our 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.

Dividends

Declaration and payment of any dividend will be subject to the discretion of our board of directors. The time and amount of dividends will be dependent upon our business prospects, results of operations, financial condition, cash requirements and availability, debt repayment obligations, capital expenditure needs, contractual restrictions, covenants in the agreements governing our current and future indebtedness, industry trends, the provisions of Delaware law affecting the payment of distributions to stockholders and any other factors our board of directors may consider relevant. 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, and therefore do not anticipate declaring or paying any cash dividends on our Class A common stock in the foreseeable future.

Anti-Takeover Provisions

Our certificate and bylaws contain provisions that may delay, defer or discourage another party from acquiring control of us. We expect that these provisions, which are summarized below, will discourage coercive takeover practices or inadequate takeover bids. These provisions are also designed to encourage persons seeking to acquire control of us to first negotiate with our board of directors, which we believe may result in an improvement of the terms of any such acquisition in favor of our stockholders. However, they also give our board of directors the power to discourage acquisitions that some stockholders may favor.

Authorized but Unissued Shares

The authorized but unissued shares of our common stock and our preferred stock are available for future issuance without stockholder approval, subject to any limitations imposed by the Nasdaq rules. These additional shares may be used for a variety of corporate finance transactions, acquisitions and employee benefit plans and funding of redemptions of common units. The existence of authorized but unissued and unreserved common stock and preferred stock could make more difficult or discourage an attempt to obtain control of us by means of a proxy contest, tender offer, merger or otherwise.

Classified Board of Directors

Our certificate provides that our board of directors is divided into three classes, with the classes as nearly equal in number as possible and each class serving three-year staggered terms. Pursuant to the terms of the Stockholders Agreement we entered into with ACON, Fundamental and Brian Mariotti, our chief executive officer, in connection with our IPO, each of ACON and Fundamental has the right to request that one or more of their respective designated directors tender their resignations from the board of directors, in each case, with or without cause at the request of the party entitled to designate such director. In all other cases and at any other time, directors may only be removed from our board of directors for cause by the affirmative vote of the holder of a majority of the voting power of all outstanding shares of stock of the Company which are present in person or by proxy and entitled to vote thereon. These provisions may have the effect of deferring, delaying or discouraging hostile takeovers, or changes in control of us or our management.

Stockholder Action by Written Consent

Our certificate provides that 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, subject to the rights of any series of Preferred Stock permitting the holders of such series of Preferred Stock to act by written consent and subject to the consent right of the Permitted Class B Holders provided for in Section 6.4 of our certificate, at such time as ACON, certain of its affiliates and their permitted transferees (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.

Special Meetings of Stockholders

Our bylaws provide that 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 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, a majority in voting power of the outstanding shares of our capital stock may also call special meetings of our stockholders.

Advance Notice Requirements for Stockholder Proposals and Director Nominations

In addition, our bylaws provide for an advance notice procedure for stockholder proposals to be brought before an annual meeting of stockholders, including proposed nominations of candidates for election to our board of directors. In order for any matter to be “properly brought” before a meeting, a stockholder will have to comply with advance notice and duration of ownership requirements and provide us with certain information. Stockholders at an annual meeting may only consider proposals or nominations specified in the notice of meeting or brought before the meeting by or at the direction of our

board of directors or by a qualified stockholder of record on the record date for the meeting, who is entitled to vote at the meeting and who has delivered timely written notice in proper form to our secretary of the stockholder's intention to bring such business before the meeting. These provisions could have the effect of delaying stockholder actions that are favored by the holders of a majority of our outstanding voting securities until the next stockholder meeting.

Amendment of Certificate of Incorporation or Bylaws

The DGCL provides generally that the affirmative vote of a majority of the shares entitled to vote on any matter is required to amend a corporation's certificate of incorporation or bylaws, unless a corporation's certificate of incorporation or bylaws, as the case may be, requires a greater percentage. Our bylaws may, subject to the Stockholders Agreement, 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. 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 bylaws may be amended or repealed by a majority vote of our board of directors or by the affirmative vote of the holders of at least 66^{2/3}% of the votes which all our stockholders would be entitled to cast in any annual election of directors. In addition, subject to the Stockholders Agreement, the affirmative vote of a majority of the votes which all our stockholders would be eligible to cast in an election of directors will be required to amend or repeal or to adopt any provisions inconsistent with any of the provisions of our certificate, and any amendment of our certificate that gives holders of our Class B common stock (1) any rights to receive dividends or any other kind of distribution, (2) any right to convert into or be exchanged for Class A common stock or (3) any other economic rights will require, in addition to stockholder approval, the affirmative vote of holders of our Class A common stock voting separately as a class. 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, the affirmative vote of the holders of at least 66^{2/3}% of the votes which all our stockholders would be entitled to cast in any election of directors will be required to amend or repeal or to adopt any provisions contained in our certificate of incorporation described above.

Section 203 of the DGCL

We have opted out of Section 203 of the DGCL. However, our certificate contains provisions that are similar to Section 203. Specifically, our certificate provides that, subject to certain exceptions, we will not be able to engage in a "business combination" with any "interested stockholder" for three years following the date that the person became an interested stockholder, unless the interested stockholder attained such status with the approval of our board of directors or unless the business combination is approved in a prescribed manner. A "business combination" includes, among other things, a merger or consolidation involving us and the "interested stockholder" and the sale of more than 10% of our assets. In general, an "interested stockholder" is any entity or person beneficially owning 15% or more of our outstanding voting stock and any entity or person affiliated with or controlling or controlled by such entity or person. However, in our case, ACON and Fundamental and any of their respective affiliates and any of their respective direct or indirect transferees receiving 15% or more of our outstanding voting stock will not be deemed to be interested stockholders regardless of the percentage of our outstanding voting stock owned by them, and accordingly will not be subject to such restrictions.

Washington Business Corporation Act

The laws of Washington, where our principal executive offices are located, impose restrictions on certain transactions between certain foreign corporations and significant stockholders. In particular, the Washington Business Corporation Act, or the WBCA, prohibits a “target corporation,” with certain exceptions, from engaging in certain “significant business transactions” with a person or group of persons which beneficially owns 10% or more of the voting power of the target corporation, an “acquiring person,” for a period of five years after such acquisition, unless the transaction or acquisition of shares is approved by a majority of the members of the target corporation’s board of directors prior to the time of acquisition. Such prohibited transactions may include, among other things, any merger or consolidation with, disposition of assets to, or issuance or redemption of stock to or from, the acquiring person; any termination of 5% or more of the employees of the target corporation as a result of the acquiring person’s acquisition of 10% or more of the shares; and allowing the acquiring person to receive any disproportionate benefit as a stockholder.

After the five-year period, a significant business transaction may take place as long as it complies with certain fair price provisions of the statute or is approved at an annual or special meeting of stockholders. We will be considered a “target corporation” so long as our shares are registered with the Securities and Exchange Commission, our principal executive office is located in Washington and (1) a majority of our employees are residents of the state of Washington or we employ more than one thousand residents of the state of Washington, (2) a majority of our tangible assets, measured by market value, are located in the state of Washington or we have more than \$50 million worth of tangible assets located in the state of Washington, and (3) any one of the following: (a) more than 10% of our stockholders of record are resident in the state of Washington; (b) more than 10% of our shares are owned of record by state residents; or (c) 1,000 or more of our stockholders of record are resident in the state. If we meet the definition of a target corporation, the WBCA may have the effect of delaying, deferring or preventing a change of control.

Limitations on Liability and Indemnification of Officers and Directors

Our certificate and bylaws provide indemnification for our directors and officers to the fullest extent permitted by the DGCL. We have entered into indemnification agreements with each of our directors and executive officers that may, in some cases, be broader than the specific indemnification provisions contained under Delaware law. In addition, as permitted by Delaware law, our certificate includes provisions that eliminate the personal liability of our directors for monetary damages resulting from breaches of certain fiduciary duties as a director. The effect of this provision is to restrict our rights and the rights of our stockholders in derivative suits to recover monetary damages against a director for breach of fiduciary duties as a director.

These provisions may be held not to be enforceable for violations of the federal securities laws of the United States.

Corporate Opportunity Doctrine

Delaware law permits corporations to adopt provisions renouncing any interest or expectancy in certain opportunities that are presented to the corporation or its officers, directors or stockholders. Our certificate, to the maximum extent permitted from time to time by Delaware law, renounces any interest or expectancy that we have in, or right to be offered an opportunity to participate in, specified business opportunities that are from time to time presented to certain of our officers, directors or stockholders or

their respective affiliates, other than those officers, directors, stockholders or affiliates acting in their capacity as our employee, or director. Our certificate provides that, to the fullest extent permitted by law, any director or stockholder who is not employed by us or our affiliates will not have any duty to refrain from (1) engaging in a corporate opportunity in the same or similar lines of business in which we or our affiliates now engage or propose to engage or (2) otherwise competing with us or our affiliates. In addition, to the fullest extent permitted by law, if any director or stockholder, other than a director or stockholder who is not employed by us or our affiliates acquires knowledge of a potential transaction or other business opportunity which may be a corporate opportunity for itself or himself or its or his affiliates or for us or our affiliates, such person will have no duty to communicate or offer such transaction or business opportunity to us or any of our affiliates and they may take any such opportunity for themselves or offer it to another person or entity, unless such opportunity was expressly offered to them solely in their capacity as a director, executive officer or employee of us or our affiliates. To the fullest extent permitted by Delaware law, no potential transaction or business opportunity may be deemed to be a corporate opportunity of the corporation or its subsidiaries unless (1) we or our subsidiaries would be permitted to undertake such transaction or opportunity in accordance with our certificate, (2) we or our subsidiaries, at such time have sufficient financial resources to undertake such transaction or opportunity, (3) we have an interest or expectancy in such transaction or opportunity and (4) such transaction or opportunity would be in the same or similar line of our or our subsidiaries' business in which we or our subsidiaries are engaged or a line of business that is reasonably related to, or a reasonable extension of, such line of business. Our certificate does not renounce our interest in any business opportunity that is expressly offered to an employee director or employee in his or her capacity as a director or employee of Funko, Inc. To the fullest extent permitted by law, no business opportunity will be deemed to be a potential corporate opportunity for us unless we would be permitted to undertake the opportunity under our certificate, we have sufficient financial resources to undertake the opportunity and the opportunity would be in line with our business.

Dissenters' Rights of Appraisal and Payment

Under the DGCL, with certain exceptions, our stockholders have appraisal rights in connection with a merger or consolidation of the Company. Pursuant to the DGCL, stockholders who properly request and perfect appraisal rights in connection with such merger or consolidation will have the right to receive payment of the fair value of their shares as determined by the Delaware Court of Chancery.

Stockholders' Derivative Actions

Under the DGCL, any of our stockholders may bring an action in our name to procure a judgment in our favor, also known as a derivative action, provided that the stockholder bringing the action is a holder of our shares at the time of the transaction to which the action relates or such stockholder's stock thereafter devolved by operation of law.

Transfer Agent and Registrar

The transfer agent and registrar for our Class A common stock is Computershare Trust Company, N.A.

Trading Symbol and Market

Our Class A common stock is listed on the Nasdaq Global Select Market under the symbol "FNKO."

LIST OF SUBSIDIARIES

Funko Acquisition Holdings, LLC

Funko Holdings, LLC

Funko, LLC

Loungefly, LLC

Funko UK, Ltd.

A Large Evil Corporation Ltd.

Funko Far East Limited

Funko Games, LLC

Exhibit 23.1

Consent of Independent Registered Public Accounting Firm

We consent to the incorporation by reference in the following Registration Statements:

- (a) Registration Statement (Form S-8 No. 333-221390) pertaining to the Funko, Inc. 2017 Incentive Award Plan,
- (b) Registration Statement (Form S-8 No. 333-234456) pertaining to the Funko, Inc. 2019 Incentive Award Plan, and
- (c) Registration Statement (Form S-3/A No. 333-230694) of Funko, Inc.;

of our report dated March 5, 2020, with respect to the consolidated financial statements of Funko, Inc. included in this Annual Report (Form 10-K) for the year ended December 31, 2019.

/s/ Ernst & Young LLP

Seattle, Washington

March 5, 2020

CERTIFICATION

I, Brian Mariotti, certify that:

1. I have reviewed this Annual Report on Form 10-K 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: March 5, 2020

/s/ Brian Mariotti

Brian Mariotti

Chief Executive Officer

CERTIFICATION

I, Jennifer Fall Jung, certify that:

1. I have reviewed this Annual Report on Form 10-K 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: March 5, 2020

/s/ Jennifer Fall Jung

Jennifer Fall Jung

Chief Financial Officer

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

In connection with this Annual Report on Form 10-K of Funko, Inc. (the "Company") for the year ended December 31, 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: March 5, 2020

/s/ Brian Mariotti

Brian Mariotti

Chief Executive Officer

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

In connection with this Annual Report on Form 10-K of Funko, Inc. (the "Company") for the year ended December 31, 2019 (the "Report"), I, Jennifer Fall Jung, 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: March 5, 2020

/s/ Jennifer Fall Jung

Jennifer Fall Jung

Chief Financial Officer