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

FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2021
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	35-2593276
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
2802 Wetmore Avenue	
Everett, Washington	**98201**
(Address of principal executive offices)	(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	Trading Symbol(s)	Name of exchange on which registered
Class A Common Stock, $0.0001 Par value	**FNKO**	**The Nasdaq Stock Market LLC**

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

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

Indicate by check mark whether the registrant has filed a report on and attestation to its management's assessment of the effectiveness of its internal control over financial reporting under Section 404(b) of the Sarbanes-Oxley Act (15 U.S.C. 7262(b)) by the registered public accounting firm that prepared or issued its audit report ☐

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

As of June 30, 2021, 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 $588.7 million.

As of March 1, 2022, the registrant had 40,197,814 shares of Class A common stock outstanding and 10,589,729 shares of Class B common stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive Proxy Statement relating to its 2022 Annual Meeting of Stockholders to be filed with the SEC within 120 days after the end of the fiscal year ended December 31, 2021 are incorporated herein by reference in Part III of this Annual Report on Form 10-K.

INDEX

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, certain former warrant holders and certain current and former executive officers, employees and directors and each of their permitted transferees that own common units in FAH, LLC after the Transactions and who may redeem at each of their options (subject in certain circumstances to time-based vesting requirements) their common units for, at our election, cash or newly-issued shares of Funko, Inc.’s Class A common stock.
- *“FAH, LLC”* refers to Funko Acquisition Holdings, L.L.C.
- *“FAH LLC Agreement”* refers to FAH, LLC’s second amended and restated limited liability company agreement, as amended from time to time.
- *“Former Equity Owners”* refers to those Original Equity Owners affiliated with ACON who transferred their indirect ownership interests in common units of FAH, LLC for shares of Funko, Inc.’s Class A common stock (to be held by them either directly or indirectly) in connection with the consummation of the Transactions.
- *“Former Profits Interests Holders”* refers collectively to certain of our directors and certain current executive officers and employees, in each case, who, prior to the consummation of the Transactions, held existing vested and unvested profits interests in FAH, LLC pursuant to FAH, LLC’s prior equity incentive plan and received common units of FAH, LLC in exchange for their profits interests (subject to any common units received in exchange for unvested profits interests remaining subject to their existing time-based vesting requirements) in connection with the Transactions.
- “*Fundamental*” refers collectively to Fundamental Capital, LLC and Funko International, LLC.
- *“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 initial public offering ("IPO") in November 2017.

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, the expected impact of the COVID-19 pandemic on our business, results of operations and financial condition, our business strategy and plans, potential acquisitions, market growth and trends, demand for our products, 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.

Summary of Risk Factors

Our business is subject to numerous risks and uncertainties, including those described in Part II, Item 1A. "Risk Factors" in this Annual Report on Form 10-K. Some of the factors that could materially and adversely affect our business, financial condition, results of operations or prospects include, but are not limited to, the following:

- We are subject to risks related to the retail industry including, but not limited to, the impacts of the COVID-19 pandemic, potential negative impacts of global and regional economic downturns, changes in retail practices, and our ability to maintain and further develop relationships with our retail customers and distributors.
- As a purveyor of licensed pop culture consumer products, we are largely dependent on content development and creation by third parties, and are subject to a number of related risks including, but not limited to, the market appeal of the properties we license and the products we create.
- We are subject to risks related to the operation of our business, including, but not limited to, our ability to execute our business strategy, manage our growth and our inventories, and attract and retain qualified personnel.
- We are subject to risks related to intellectual property, including our ability to obtain, protect and enforce our intellectual property rights and our ability to operate our business without violating the intellectual property rights of other parties.
- Our success is dependent on our ability to manage fluctuations in our business, including fluctuations in gross margin, seasonal impacts and fluctuations due to the timing and popularity of new product releases.
- Our substantial sales and manufacturing operations outside the United States subject us to risks associated with international operations, including, but not limited to, changes in the global trade markets, as well as fluctuations in foreign currency or tax rates.
- Our business depends in large part on our third-party vendors, manufacturers 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 are subject to potential legal risks including, but not limited to, ongoing securities class action litigation, future product liability suits or product recalls, or risks associated with failure to comply to the various laws and regulations to which we are subject, any of which could have a significant adverse effect on our financial condition and results of operations.
- We are subject to risks related to information technology including, but not limited to, risks related to the operation of our e-commerce business, our ability to operate our information systems and our compliance with laws related to privacy and the protection of data.
- Our indebtedness could adversely affect our financial health and competitive position, and we may not be able to secure additional financing on favorable terms, or at all, to meet our future capital needs.
- ACON has significant influence over us, and its interests may conflict with the interests of our other stockholders.
- There are risks related to our organizational structure, including the Tax Receivable Agreement, which 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.
- There are risks associated with the ownership of our Class A common stock including, but not limited to, potential dilution by future issuances and volatility in the price of our Class A common stock.

PART I

ITEM 1. BUSINESS

Overview

Funko is a leading pop culture lifestyle brand. Our business is built on the belief that everyone is a fan of something, and Funko aims to have something for every fan. 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 our extensive portfolio of licensed content over a wide variety of product categories, including figures, bags, wallets, apparel, accessories, board games, plush, homewares and digital non-fungible tokens ("NFTs"), which we make available at highly accessible price points. We believe we sit at the nexus of pop culture—content providers value us for our ability to connect fans to their properties with our creative products and broad distribution; retailers value us for our broad portfolio of licensed pop culture products that we can curate to resonate with their consumers; 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.

The Pop Culture Industry

Pop culture encompasses virtually everything that someone can be a fan of—movies, TV shows, anime, video games, music, sports, books and more. Pop culture fandom has evolved from niche communities around specific properties to having a broad presence in modern life. Today, there is more quality content than ever before and technology innovation has made that content accessible anytime, anywhere. 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.

The Forces at Work in The Pop Culture Industry

Technology Innovation

The proliferation of mobile technology, and the emergence of new content distribution services, such as Amazon Prime, AppleTV+, Disney+, HBO Max, Hulu, Netflix, Peacock and more have enabled fans to connect and engage with content anywhere, at any time, in larger “binge” quantities. An increasing array of content and greater accessibility have led to more fans spending more time per day consuming content. In addition, fans can 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. Additionally, there has been an increase in high-quality scripted television series as content providers vie for binge worthy shows to attract consumers. For example, in 2021 there were 559 original scripted series in the U.S., a 13% increase over 2020, according to FX networks research. We expect content providers such as Amazon, Apple, Disney, Warner Bros., Hulu, Netflix and NBCUniversal to continue to invest in new high-quality original content. The proliferation and globalization across content types has fostered fan loyalty and stimulated licensed product purchases.

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. Furthermore, as it becomes increasingly easy to access a large quantity of quality content, fans seek more ways to expand and express connections 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

As pop culture engagement has increased, we believe fandom has become a pastime, and fans are more openly passionate about all forms of pop culture. Social media is driving the importance of pop culture as fans increasingly want to engage with the content across their social communities to show affinity for their favorite content. Three of the top U.S. pop culture-related conventions, including New York Comic Con, Comic Con International: San Diego and Anime Expo 2019, drew close to half a million attendees in 2019, representing a sharp increase of over 80% from 2010. This represents a cultural shift supporting the acceptability of fan affinity for pop culture content across all demographic categories of fans. In 2020 and 2021, due to COVID-19 impacts on in-person events, many pop-culture conventions such as Comic Con International: San Diego, New York Comic Con and others were cancelled or pivoted to virtual events, which continued to attract and engage fans in the new virtual format.

Our Strategic Differentiation

Deep and Extensive Licensing Partnerships

We have strong licensing relationships with many established content providers, such as Disney, Warner Bros., Marvel, LucasFilm, NBCUniversal, Netflix, Epic Games, Blizzard Entertainment, the National Football League, the National Basketball Association and many more. We strive to partner with content providers across multiple genres, including movies, television, video games, anime, sports, and music. In 2021, we had license agreements with over 250 content providers covering over 1,000 licensed properties. We believe our numerous licensing relationships have allowed us to build one of the largest portfolios of licensed property 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. We believe we have benefited from 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. 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.

Diverse Range of Properties

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 licenses covering hundreds of properties that we believe is one of the industry’s largest. Our licensed property portfolio encompasses a diverse range of genres to ensure our products have broad consumer appeal. Many of our licensed properties are "evergreen" in nature—properties that are not tied to a current or new content release, such as Mickey Mouse, Harry Potter or classic Batman. 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 evergreen properties and new releases, depending on the media release cycle. As a result, we can manage our business to capitalize on pop culture trends, which has allowed us to lessen our dependence on individual content releases. This allows our business to be diversified across properties, as well as evergreen and current content.

For the years ended December 31, 2021, 2020 and 2019, no single property accounted for more than 7% of our sales, and the portion of our sales for the years ended December 31, 2021, 2020 and 2019 attributable to our top five properties was 20%, 22% and 23%, respectively. Additionally, the portion of our sales related to evergreen properties for the years ended December 31, 2021, 2020 and 2019 was approximately 67%, 66% and 51%, respectively.

Broad Portfolio of Products and Brands

We create products to attract a broad array of fans across consumer demographic groups. We believe our broad appeal comes from our large selection of licenses and properties that we apply across a variety of product categories and brands. We do not limit ourselves by targeting discrete demographics such as only collectors or children seeking the latest (and often short-lived) toy craze. We strive to have something for everyone by offering figures and other product categories including bags, wallets, apparel, board games, plush, accessories, homewares and more. We expect to continue to look for ways to diversify our product offerings to reach an even broader group of consumers.

In addition to offering multiple properties and product categories, we create and sell a variety of unique brands that have their own look and feel. Our brand portfolio includes Pop! and Loungefly as well as others such as Funko, Mystery Mini, Paka Paka, Vinyl Gold and Popsies. Pop! is our largest and most recognized brand that encompasses multiple product categories, including figures, accessories, apparel, games, bags and more. The portion of sales attributed to Pop! branded products in the years ended December 31, 2021, 2020 and 2019 was 74%, 76% and 79%, respectively. Loungefly branded products include stylized fashion accessories such as bags, wallets and backpacks as well as apparel. The portion of sales attributed to Loungefly branded products in the years ended December 31, 2021, 2020 and 2019 was 14%, 13% and 9%, respectively. Additionally, from time-to-time our in-house creative team creates new brands and products based on Funko’s own intellectual property and non-licensed board games.

Broad Consumer Appeal and Engagement

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 consumers. We create products to appeal to a broad array of fans across consumer demographic groups. We strive to keep our products at an accessible price point, generally under $12 for our figure category, which allows our fans to express their fandom frequently and impulsively. We continue to introduce innovative products designed to facilitate fan engagement across different price points and categories. 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. Additionally, we seek to drive direct engagement with our fans through in person experiences at our flagship retail stores and fan events, as well as digitally through our websites, mobile application and various social media platforms. In 2020, given the impact of COVID-19 on in-person events, we began conducting virtual events including multiple Funko Virtual Con events, to continue to drive engagement with fans. We continued this throughout 2021 with a few hybrid events (both in person and virtual) where we could safely do so. 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.

Diversified Global Distribution Network

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, as well as directly to consumers primarily through our owned websites and two flagship retail stores. We can provide our retail customers a customized product mix designed to appeal to their consumer bases. Our key retail partners in the United States include Amazon, GameStop, Hot Topic, Target and Walmart. Internationally, we sell our products directly to similar retailers, primarily in Europe, through our subsidiary Funko UK, Ltd. Our key international retail customers include Amazon, GameStop, Fnac and Tesco. 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.

Additionally, we are continuing to invest in our direct-to-consumer channel to expand our reach and further strengthen our relationship with our fan base. Our direct-to-consumer channel includes our own e-commerce websites in the U.S. and Europe as well as our two flagship retail stores located in the U.S.

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. We have developed a nimble and low fixed-cost production model built on the strength of our in-house creative team as well as our relationships with content providers, retailers and third-party manufacturers. Our production model enables us to go from product design of a figure to the store shelf within 110 to 200 days and we can typically 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. During 2021, we saw, and in 2022, we continue to see some delays with the global capacity constraints and the availability of shipping containers, but we have employed mitigation strategies to get product in the hands of our customer base as soon as feasible. 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. 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.

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. We believe content providers trust us with their properties, and consumers passionately engage with our products and brands because of our creativity. In addition, our creativity and designs allow us to reinvigorate classic evergreen content by infusing a fresh, unique aesthetic into characters that enjoy enduring passion and nostalgia from fans. With the help of our in-house creative team, we have also begun to develop our own proprietary intellectual property as well as various non-licensed board games. As a result of our creative capabilities and broad portfolio of licenses, we create a substantial number of new products each year.

Growth Strategies

Grow our Core Pop Culture Business

We intend to grow our core business by utilizing our strength in building fun, creative and nostalgic programs at retail through: (1) leveraging an increasing array of content, categories and distribution; (2) creating programs that utilize evergreen content with a focus on targeting underpenetrated content genres to expand our addressable market; and (3) continued product innovation to bring new designs and products to market.

We also intend to continue licensing content that will allow us to capitalize on the popularity of current releases across movies, TV shows, video games, and other content types, and to leverage those licenses across a broader array of products and expanded distribution to reach new consumers.

We have the ability to leverage evergreen or back catalog content by creating fun, whimsical and nostalgic programs to be sold at retail that resonate with fans. Our evergreen programs include new versions of well-known characters such as our Marvel Venomized line or, products built around nostalgic content or places such as Disney theme parks.

Additionally, we intend to strategically focus on growing within genres that we believe we have underpenetrated, such as anime, sports and music. We expect to do this by expanding our license portfolio, creating new products or designs that resonate with fans and strategically expanding our distribution of these products. Within anime, we continue to add new license relationships with multiple new properties. For example, in 2018 we recorded approximately $29.4 million in sales over 32 properties and in 2021 we recorded approximately $81.4 million in sales over 48 properties. In the sports category, we are continuing to leverage our broad range of sports licenses, which includes the NFL, NBA, NHL, WWE, English Premier League, MLB and more. In 2021, we launched Funko Gold, which is initially focused on sports and music figures in a head-to-toe stylized look. Additionally, within the music category, we are expanding our license base to include more artists for Pop! Albums, a product line introduced in 2020 under the Pop! brand that seeks to appeal to music fans by recreating iconic covers of music albums.

We expect to continue to utilize our in-house creative team to create new designs, products and brands that resonate with our core consumers. For example, in 2019 we launched Funko Vinyl Soda, a stylized collectible vinyl figure to that comes with the opportunity to be surprised by a rare chase piece.

Diversify our Revenue Streams through Product Innovation

We are leveraging Funko’s pop culture platform to diversify our revenue streams across product categories, channels and geographies. In addition to designing products to address both new and evergreen content, we have introduced new toy lines, board games and softlines to leverage our existing retail partnerships and open up potential new channels of distribution. In 2020, we added new non-licensed toy lines such as Snapsies and launched dozens of new offerings under our Funko Games brand, including Funkoverse branded games, and many other licensed games and non-licensed games. We also continually evaluate product innovations and potential acquisition targets to complement our existing product categories, lines and brands. For example, in 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 2019, we acquired Forrest-Pruzan Creative LLC, a leading board game development studio, to help us expand our product offerings into the board game category and to develop the Funko Games brand. In 2021, we launched, through our acquisition of the majority interest in TokenWave, LLC, the Company's first NFTs. These exclusive digital card packs are currently sold on the WAX blockchain platform and have often sold out in a matter of minutes, with residual buyers still waiting in the queue.

Extend Funko’s International Reach

We believe the rise of pop culture and deep fan loyalty are global. We believe our sales are currently underpenetrated internationally as we generate the majority of our net sales in the United States. Sales generated from customers outside of the United States accounted for approximately 28%, 25% and 34% of our sales for the years ended December 31, 2021, 2020 and 2019, respectively. We are continuing to invest in the growth of our international business, primarily in Europe, both directly and through third party distributors. In 2020, we launched our own e-commerce website in Europe, www.funkoeurope.com, which initially served the U.K., Ireland, Spain, Germany, France and Italy, and has since expanded into six additional countries throughout Europe. We believe there are opportunities to further grow our sales in other regions, such as Latin America, Canada, Oceania and APAC, by expanding our direct sales to retailers or through distributor relationships.

Increase our Direct-to-Consumer Business

We view our direct-to-consumer business, which includes our e-commerce websites, www.funko.com, www.funkoeurope.com and www.loungefly.com, and two flagship retail stores, as a significant growth opportunity and an important vehicle for expanding our reach and broadening our relationship with our fans. We plan to build a robust online platform and to enhance our digital capabilities to provide the infrastructure to scale this business over the long-term. In 2020, we relaunched www.funko.com with an expanded product offering, and enhanced features and functionality to serve our customers in the U.S., and also launched www.funkoeurope.com to serve our customers in the UK and several countries in Europe. Our direct-to-consumer strategy also provides us with an opportunity to utilize data and trend analysis to inform our overall business strategy. We believe our direct-to-consumer business will help us strengthen our connection with our fans, deepen consumer engagement to drive customer lifetime value, build brand awareness with new audience segments, and 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 or new release, and which are less subject to pop culture trends. Additionally, by utilizing our in-house creative team we have the ability to develop our own content and intellectual property as well as various board game offerings.

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, and Funko Soda. Additionally, from time to time we will create figures that are not licensed such as our Paka Paka brand.

Other. Our other category is comprised of stylized fashion accessories (including bags, backpacks and wallets); apparel; board games; plush products; accessories (including keychains, pens and pins); apparel (including t-shirts and hats); homewares (including drinkware and other home accessories); NFTs and other.

Our Brands and Designs

Under the Funko brand, we have multiple proprietary brands under which most of our products are marketed. 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. Our standard Pop! Vinyl figure stands about four inches tall. The Pop! brand has also been applied across many of our other product categories, including games, plush, accessories, apparel and homewares. Pop! branded products represented 74%, 76% and 79% of our sales in 2021, 2020, and 2019, respectively.

Our Loungefly branded products are generally fashion accessories including stylized handbags, backpacks, wallets, clothing, and other accessories. Loungefly branded products represented 14%, 13% and 9% in 2021, 2020 and 2019, respectively.

Other brands we market under include Mystery Minis, Paka Paka, and Popsies. In addition, we also develop product lines that we market under the broader Funko brand, such as Funko Games, Funko action figures, Funko Soda, Funko Plush, and Funko Gold product lines. We expect to continue to 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, Netflix, Pokémon, the National Football League, NBCUniversal, Epic Games, Blizzard Entertainment and Warner Bros. We seek to establish new licensing relationships with content providers in order to capitalize on new and emerging trends in pop culture. We believe we also 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, 2021, 2020 and 2019, the average royalty rate was 15.7%, 16.1% and 15.9%, respectively. Our royalty expense for any given year will vary depending on the mix of products and properties sold during that year. For the years ended December 31, 2021, 2020 and 2019, we incurred royalty expenses of $162.0 million, $105.0 million and $126.8, 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, 2021, 2020 and 2019, we recorded reserves of $0.7 million, $1.0 million and $2.4 million, respectively, related to prepaid royalties we estimated would not be recovered through sales.

For the year ended December 31, 2021, 26% of sales were related to the Company's two largest license agreements (13% each) with no other license agreements accounting for more than 10% of sales. For the year ended December 31, 2020, 12% and 11% of sales were related to the Company's two largest license agreements with no other license agreements accounting for more than 10% of 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.

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 primarily divide our licensed properties between classic evergreen and current or new releases. We also license certain properties that fall outside of these 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 Classic, Harry Potter, DC Comics, Marvel Comics, Pokémon and WWE.

- *Current Releases.* Properties in the current release category typically are tied to new movie releases, current television series or new video game titles. These properties are intended to capitalize on the excitement of fans surrounding the launch of new content. Products that we design and sell based on new movie releases are expected to have a limited duration of market demand, depending on the popularity of the title. Examples of new movie releases are Spider-Man: No Way Home, Avengers Endgame, Space Jam 2. Additionally, products that we design and sell based on current television series or new video game titles are expected to have a market demand depending on the popularity and longevity of the title, which is generally expected to be multiple years. Examples of our current TV and video game properties include The Mandalorian, Dragon Ball Z, Naruto, My Hero Academia, Avatar: The Last Airbender. Examples of our current video game properties are Fortnite, Overwatch and Five Nights at Freddy's.

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. The percent of our sales attributable to classic evergreen and current releases 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. Additionally, from time to time our creative team will develop new styles and products based on our own intellectual property. Our creative team is passionate about pop culture, and we believe 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 (both physical and digital) to maximize the value of their properties.

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 manufacturers. 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 to the store shelf 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. During 2021 we saw, and in 2022, we have seen some delays with the global capacity constraints and the availability of shipping containers, but employed mitigation strategies to get product in the hands of our customer base as soon as feasible. 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. We believe that 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, Mexico and Cambodia. 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 typically based on the strength and popularity 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, timing and/or availability 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 or delays in shipping to the factories as a result of global capacity constraints. 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 as well as directly to our consumers primarily through our own websites and two flagship retail stores. 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. Internationally, we sell our products directly to similar retailers, primarily in Europe, through our subsidiary Funko UK, Ltd. Our key international retail customers include Amazon, GameStop, Fnac and Tesco. 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 our products directly to consumers through our e-commerce business, two flagship retail stores 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 11%, 8% and 4% of our sales for 2021, 2020 and 2019, respectively. 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. In 2020, we relaunched www.funko.com with an expanded product offering, and enhanced features and functionality, to serve our customers in the U.S., and we also launched www.funkoeurope.com to serve customers in the UK and several countries in Europe.

We believe we have a diverse customer base, with our top ten customers representing approximately 45%, 48% and 44%, of our 2021, 2020, and 2019 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. 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 several 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. 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 or third-party logistics facilities in the United States, the United Kingdom and the Netherlands. While most of our sales originate in the United States and the United Kingdom from inventory we hold in our warehouses and third-party logistics locations, 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, 2021 and 2020, we had reserves for sales allowances of $40.6 million and $28.0 million, respectively.

Marketing

We believe Funko's trendsetting and nostalgia-based product assortment is a unique voice in the pop culture marketplace, and 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 high profile social media sites such as Facebook, Twitter, Instagram and YouTube. As of December 31, 2021, Funko's Twitter handle, @OriginalFunko, had over one million followers. We continue to expand our reach globally through our compelling content, events and personal engagement with our fan base. For example, in 2019 we opened a 40,000-square foot retail-tainment experience on Hollywood Boulevard in Los Angeles, California to further increase our brand presence and create additional opportunities to engage with our fan base. We also plan to develop and implement new marketing programs aimed at driving traffic to our websites and new customer acquisition targeted to specific products and properties.

Competition

We are a worldwide leader in the design, manufacture and marketing of licensed pop culture and other products, in a highly competitive industry. We compete with toy, board game and fashion accessory companies across 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 and board game companies for shelf space at leading mass market and other retailers. We also compete with numerous smaller domestic and foreign collectible toy, board game and fashion accessory designers and manufacturers across our product categories. Our competitive advantage is based primarily on the creativity and quality of the design of our products, our price points, our broad consumer appeal, 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, 2021, we owned approximately 101 registered U.S. trademarks, 247 registered international trademarks, 29 pending U.S. trademark applications and 16 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.”

In relation to our sales and marketing activities, we are subject to various consumer protection rules and regulations promulgated and/or enforced by various federal and state regulators such as the U.S. Federal Trade Commission, and state attorneys general as well as non-U.S. regulatory authorities that relate to advertising, product delivery and other consumer-facing practices. In addition, our online products and services, including our e-commerce and digital communications activities, are or may be subject to U.S. and non-U.S. data privacy and cybersecurity laws, such as the U.S. Children’s Online Privacy Protection Act, the California Consumer Privacy Protection Act (“CCPA”), and the EU/UK General Data Protection Regulation (“GDPR”).

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.

Human Capital

Our workforce is critical to our success. We seek out employees who are passionate about pop culture, our products and our business, and who can help us build strong relationships with our partners, customers, fans and local communities. Pop culture changes constantly, and we look to build teams that are nimble and can execute in our fast-paced environment. We strive to foster a sense of community with our employees and make the workplace fun despite the demands of our rapidly changing business. We believe our passion for pop culture of all forms is reflected in our fans around the world. We believe that fully serving those fans requires a diverse and inclusive workforce. We have implemented programs to advance these principles and embrace the opportunity to work with people of diverse backgrounds and perspectives.

In addition to offering market competitive salaries and wages, we offer comprehensive health and 401(k) benefits to eligible employees. Our core benefits packages are supplemented with specific programs centered around voluntary benefits, paid time away from work and employee physical and mental well-being. In response to the COVID-19 pandemic, we have implemented significant changes that we determined were in the best interest of our employees, as well as the communities in which we operate, and which comply with government regulations. This includes adopting remote work policies for our corporate employees as appropriate, while also implementing significant safety measures designed to protect the health of all those working at or entering our distribution centers, retail outlets and other facilities that have remained open during the pandemic.

As of December 31, 2021, we employed 1,089 full-time employees. We employed 902 people in North America, 172 people in Europe and 15 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, 2021, 2020 and 2019 approximately 59%, 64% and 55%, 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. The revenue distribution for the year ended December 31, 2020 was in part due to the COVID-19 pandemic, rather than typical seasonality, as we experienced weakened demand for our products in the first half of the year ended December 31, 2020, which had a negative impact on our net sales for the same period.

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 3, 2022):

Name	Age	Position(s)
Andrew Perlmutter	44	Chief Executive Officer, Director
Brian Mariotti	54	Chief Creative Officer, Director
Jennifer Fall Jung	51	Chief Financial Officer
Tracy Daw	56	Chief Legal Officer and Secretary
Charles Denson	65	Chairman of the Board of Directors
Ken Brotman	56	Director
Diane Irvine	63	Director
Adam Kriger	55	Director
Sarah Kirshbaum Levy	51	Director
Michael Lunsford	54	Director

Executive Officers

Andrew Perlmutter has served as Funko, Inc.'s Chief Executive Officer and as a member of the Funko, Inc. board of directors since January 2022. Previously, Mr. Perlmutter served as the President of Funko, Inc. and FAH, LLC from October 2017 to January 2022. 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. We believe Mr. Perlmutter's knowledge of the pop culture industry and many years of experience as our President make him well-qualified to serve as a member of our board of directors.

Brian Mariotti has served as Funko, Inc.'s Chief Creative Officer since January 2022, prior to which Mr. Mariotti served as Funko, Inc.'s Chief Executive Officer since April 2017. Mr. Mariotti has been a member of Funko, Inc.'s board of directors since its formation in April 2017. Prior to the formation of Funko, Inc., Mr. Mariotti served as the Chief Executive Officer of FAH, LLC and as a member of FAH, LLC's board of directors from October 2015 to April 2017, and as Chief Executive Officer of Funko Holdings LLC ("FHL") and as a member of FHL's board of directors since May 2013. Mr. Mariotti 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.

Tracy Daw has served as Funko, Inc.'s Chief Legal Officer and Secretary since March 2022 and as the Senior Vice President and General Counsel of FAH, LLC since July 2016. Previously, Mr. Daw served as Senior Vice President, General Counsel and Secretary from its formation in April 2017 to March 2022. 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

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 as the Chairman of our board of 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 of 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 Farfetch Limited (on whose board she has served since August 2020), Yelp Inc. (on whose board she has served since November 2011), and D.A. Davidson Companies (on whose board she has served since January 2018). She previously served on the boards of directors of Casper Sleep Inc. from August 2019 to January 2022, 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. Mr. Kriger also served as Chief Executive Officer and a director of ACON S2 Acquisition Corp., a public special purpose acquisition company, from July 2020 to October 2021. 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 has served as the Chief Executive Officer and a director of Betterment, LLC, a financial advisory company, since December 2020. Ms. Levy previously served as the Chief Operating Officer of Viacom Media Networks, a division of the entertainment and media company, ViacomCBS, from 2016 through January 2020, 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 sits on the board of Lucius Littauer Foundation, which makes grants in the areas of education, social welfare, health care, and Jewish studies. She also sat on the board of ACON S2 Acquisition Corp., a public special purpose acquisition company, from September 2020 through October 2021, where she served on the Audit and Compensation Committees. 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 served as an Advisor and Vice President of McClatchy, Inc. from 2017 to September 2020. 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. From 2014 to 2018, Mr. Lunsford 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 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 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, www.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.

BUSINESS, ECONOMIC, MARKET AND OPERATING RISKS

The COVID-19 pandemic adversely impacted our business in 2020. Ongoing impacts of the COVID-19 pandemic or its variants could materially adversely impact our business, financial condition and results of operations going forward.

In 2020, the COVID-19 outbreak was declared a pandemic and spread throughout the world. COVID-19 and new variants of the virus have caused and continue to cause significant loss of life and disruption to the global economy. Although by the end of December 31, 2021 our business, financial condition and operations did not experience a material effect from COVID-19, any renewed surge that leads to the curtailment of activities by businesses and consumers in much of the world, including as a result of restrictions imposed by governments and others to limit the spread of the disease and its variants such as through business and transportation shutdowns and restrictions on people's movement and congregation, would adversely affect our business going forward.

In addition, during 2020 and through 2021, certain of our suppliers and the manufacturers of certain of our products have been adversely impacted by COVID-19. As a result, we faced and continue to face delays and difficulty sourcing products, and significant increases in shipping costs, which have negatively affected our business and financial results. If such supplier and manufacturer challenges continue or recur, the impact on our supply chain and manufacturing could negatively affect our financial results for future reporting periods. 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.

Additionally, concerns over the economic impact of the COVID-19 pandemic have previously caused extreme volatility in financial and capital markets and may continue to do so in the future, which may materially adversely impact our stock price and our ability to access capital markets.

The COVID-19 pandemic continues to rapidly evolve. The extent to which the pandemic impacts our business, liquidity, results of operations and financial condition will depend on future developments, which are highly uncertain and cannot be predicted with confidence, such as the transmission rate of the disease, new variants or mutations in the disease, the duration and extent of the pandemic, the effectiveness, timing and distribution of vaccines and treatments, travel restrictions and social distancing in the United States, the United Kingdom and other countries in Europe, the duration and extent of business closures and business disruptions and the effectiveness of actions taken to contain, treat and prevent the disease. If we or our retail customers continue to experience prolonged shutdowns or other business disruptions, our ability to conduct our business and, in turn, our liquidity, results of operations and financial condition, are likely to be materially and adversely affected.

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

Our net sales and profitability have generally grown rapidly in the last several years; 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, particularly in light of the ongoing nature of the COVID-19 pandemic and its continuing impact on the global economy and consumer demand. 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 and chief creative 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 74%, 74% and 73% of our sales for the years ended December 31, 2021, 2020 and 2019, 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 43%, 41% and 38% of our sales for the years ended December 31, 2021, 2020 and 2019, respectively. The termination or failure to renew 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. 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, 2021, we had a reserve of $12.6 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, among other things, obligations to:

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

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

Our success is also partially dependent on the reputation of our licensors and the goodwill associated with their intellectual property, and 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.”

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, such as the recent downturn caused by the COVID-19 pandemic, 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. In addition, our business is subject to significant pressure on costs and pricing caused by constrained sourcing capacity and related inflationary pressure, the availability of qualified labor and related wage inflation, and associated changes in consumer demand. 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 pandemics, 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 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. During periods of increased inflation or supply constraints, like we are currently facing, we have increased prices of certain products, and may in the future need to increase our prices further in order to cover increased costs of goods sold, which may reduce demand for our products and may not fully offset our increased costs.

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, in 2020 and 2021, the retail industry has experienced dramatic reductions in sales due to the store closures related to the COVID-19 pandemic and weakened consumer demand, which has adversely impacted our net sales.

Prior to the onset of the COVID-19 pandemic, due to the challenging environment for traditional “brick-and-mortar” retail locations caused by declining in-store traffic, many retailers were closing physical stores, and some traditional retailers were engaging in significant reorganizations, filing for bankruptcy and going out of business. 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, as a result of the COVID-19 pandemic or otherwise, 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, a majority of 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 45%, 48% and 44% of our sales for the years ended December 31, 2021, 2020 and 2019, 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. As a result of the COVID-19 pandemic, we have had certain of our retail customers reduce and, in some instances, cancel purchase orders as a result of store closures or a shift of purchasing to focus only on essential consumer products.

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 generally 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 1,089 as of December 31, 2021. We also have multiple distribution centers in the U.S. and the United Kingdom. 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 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 have invested in the development of a new enterprise resource planning system, additional platforms to support our direct-to-consumer experience, and capital build out of new leased warehouse and office spaces. We will need to continue to improve our product development, supply chain, financial and management controls and our reporting processes and procedures to support our infrastructure and new business initiatives. 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, 2021, 2020 and 2019, our gross margins (exclusive of depreciation and amortization) were 37.0%, 38.2% and 35.5%, 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. For example, in 2020 there was a lack of new content releases due to the impact of COVID-19 on new content production and the movie theater industry. Due to this impact, the percent of our sales attributable to classic evergreen properties was higher compared to historical trends.

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 74%, 76% and 79% of our sales for the years ended December 31, 2021, 2020 and 2019, 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.

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, 2021, 2020 and 2019, we recorded reserves of $0.7 million, $1.0 million and $2.4 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. For example, inventories at the end of the fourth quarter 2021 increased 178% over the prior year period, primarily from longer transit times due to the COVID-19 pandemic’s impact on the global supply chain, resulting in a significant amount of inventory being “in transit” as of December 31, 2021. If, as a result of longer transit times, consumer preferences have shifted by the time we receive inventory, demand for our products and our results of operations could be adversely affected. If we are not successful in managing our inventory, our business, financial condition and results of operations could be adversely affected.

We may also be negatively affected by changes in retailers’ inventory policies and practices. As a result of the desire of retailers to more closely manage inventory levels, there is a growing trend to make purchases on a “just-in-time” basis. This requires us to more closely anticipate demand and could require us to carry additional inventory. Policies and practices of individual retailers may adversely affect us as well, including those relating to access to and time on shelf space, price demands, payment terms and favoring the products of our competitors. Our retail customers make no binding long-term commitments to us regarding purchase volumes and make all purchases by delivering purchase orders. Any retailer can therefore freely reduce its overall purchase of our products, including the number and variety of our products that it carries, and reduce the shelf space allotted for our products. If demand or future sales do not reach forecasted levels, we could have excess inventory that we may need to hold for a long period of time, write down, sell at prices lower than expected or discard. 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. 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, 2021, we owned approximately 101 registered U.S. trademarks, 247 registered international trademarks, 29 pending U.S. trademark applications and 16 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, Andrew Perlmutter, and our former Chief Executive Officer and current Chief Creative Officer since January 3, 2022, Brian Mariotti. We are dependent on their talents and continuing employment, and believe they are integral to our relationships with our licensors, certain of our key retail customers and to our overall selling and creative design processes. 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. In 2021, we also faced and we continue to face higher than normal recruitment and personnel costs in efforts to seek and retain qualified personnel.

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. Conversely, when we are forced to furlough or lay off employees, as we did during the year ended December 31, 2020, there have been and may in the future be adverse consequences for our corporate culture and employee morale. 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 59.0%, 64.0% and 55.0%, of our net sales for the years ended December 31, 2021, 2020 and 2019, respectively, were made in the third and fourth quarters, as our customers build up their inventories in anticipation of the holiday season. This seasonal pattern requires significant use of working capital, mainly to manufacture inventory during the portion of the year prior to the holiday season and requires accurate forecasting of demand for products during the holiday season in order to avoid losing potential sales of highly popular products or producing excess inventory of less popular products. In addition, as a result of the seasonal nature of our business, we would be significantly and adversely affected, in a manner disproportionate to the impact on a company with sales spread more evenly throughout the year, by unforeseen events such as a terrorist attack or economic shock that harm the retail environment or consumer buying patterns during our key selling season, or by events such as strikes or port delays that interfere with the shipment of goods during the critical months leading up to the holiday shopping season.

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 risk that one or more of our third-party manufacturers will not comply with our requirements, and that we will not promptly discover such non-compliance. For example, the Consumer Product Safety Improvement Act of 2008 (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."

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 currently located in Everett, Washington. We also have additional warehouse facilities and/or offices located in Coventry, England; London, England; Burbank, California; Puyallup, Washington, and Eindhoven, Netherlands, and we also recently announced our intention to consolidate our distribution facilities in the U.S. into a new facility in Buckeye, Arizona. 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 currently 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 or Arizona 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 2020 and through 2021, certain of our suppliers and the manufacturers of certain of our products have been adversely impacted by COVID-19. As a result, we faced delays or difficulty sourcing products, which negatively affected our business and financial results. In response, we shifted a greater amount of our production from China to Vietnam. 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 28%, 25% and 34% of our sales for the years ended December 31, 2021, 2020 and 2019, respectively. We expect sales to our international customers to account for an increasing portion of our sales in future fiscal years. 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, war and economic instability, such as the current situation with Ukraine and Russia;
- 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 COVID-19 pandemic, 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. 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. More recently, the U.S. government enacted the Uyghur Forced Labor Prevention Act, which bars the importation into the United States of products made from forced labor in the Xinjiang region of China. The Xinjiang region of China is the source of a large portion of the world's cotton supply and this import ban may impact prices and the availability of cotton for our clothing products.

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.

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 United Kingdom's 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 ratified an agreement on the future trading relationship between the parties (the "UK-EU Trade and Cooperation Agreement" or "TCA"). The agreement, which entered into force May 1, 2021, addresses trade, economic arrangements, law enforcement, judicial cooperation and a governance framework including procedures for dispute resolution, among other things. Because the agreement merely sets forth a framework in many respects and will require complex additional bilateral negotiations between the United Kingdom and the European Union as both parties continue to work on the rules for implementation, significant political and economic uncertainty remains about how the precise terms of the relationship between the parties will differ from the terms before withdrawal.

These developments, or the perception that any of them could occur, have had and may continue to have a material adverse effect on global economic conditions and the stability of global financial markets, and may significantly reduce global market liquidity and restrict the ability of key market participants to operate in certain financial markets.

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.

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. We use third party logistics companies to process and fulfill customer orders in Europe and the U.S. Any shortcoming of one of our vendors or outsourcers, including our third party logistics providers, 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. This includes potential shipping delays as a result of container availability or other global capacity constraints. 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, 2021. 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 had 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 March 10, 2020, a purported stockholder of the Company filed a putative class action lawsuit in the United States District Court for the Central District of California against us and certain of our officers, entitled *Ferreira v. Funko, Inc. et al.* The original complaint alleged that we violated Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, as amended (the "Exchange Act") as well as Rule 10b-5 promulgated thereunder, by making allegedly materially misleading statements in our earnings announcement and Quarterly Report on Form 10-Q for the quarter ended September 30, 2019, as well as by omitting material facts necessary to make the statements made therein not misleading. The lawsuit sought, among other things, compensatory damages and attorneys' fees and costs. Two additional complaints making substantially similar allegations were filed April 3, 2020 in the United States District Court for the Central District of California and April 9, 2020 in the United States District Court for the Western District of Washington, respectively. On June 11, 2020, the Central District of California actions were consolidated for all purposes into one action under the *Ferreira* caption, and lead plaintiffs and lead counsel were appointed pursuant to the Private Securities Litigation Reform Act; shortly thereafter, the Western District of Washington action was voluntarily dismissed. Lead plaintiffs filed the consolidated complaint on July 31, 2020, against us and certain of our officers and directors, as well as entities affiliated with ACON. The consolidated complaint added Section 10(b) and 20(a) claims based on our earnings announcement and Quarterly Report on Form 10-Q for the quarter ended June 30, 2019, as well as claims under Section 20A of the Exchange Act. All defendants moved to dismiss the consolidated action on October 2, 2020, and on February 25, 2021, the Court granted all defendants' motions to dismiss the *Ferreira* action, allowing the lead plaintiffs leave to amend the complaint. Lead plaintiffs filed their amended complaint on March 29, 2021, and all defendants moved to dismiss. On October 25, 2021, the Court issued an order granting defendants' motion in part and denying the motion in part. Specifically, the court dismissed with prejudice all claims related to statements regarding Funko's projected net sales and the claims based on inventory risk warnings in our Quarterly Report on Form 10-Q for the quarter ended June 30, 2019, but denied the motion to dismiss as to claims based on inventory risk warnings in our Quarterly Report on Form 10-Q for the quarter ended September 30, 2019.

Several shareholder derivative actions based on the earnings announcement and Quarterly Report on Form 10-Q for the quarter ended September 30, 2019 have been brought on behalf of the Company against certain of our directors and officers. Specifically, on April 23, June 5, and June 10, 2020, the actions captioned *Cassella v. Mariotti et al.*, *Evans v. Mariotti et al.*, and *Igelido v. Mariotti et al.*, respectively, were filed in the United States District Court for the Central District of California. On July 6, 2020, these three actions were consolidated for all purposes into one action under the title *In re Funko, Inc. Derivative Litigation*, and on August 13, 2020, the consolidated action was stayed pending final resolution of the motion to dismiss in the *Ferreira* action. Additionally, on July 14 and July 31, 2020, the actions captioned *Rubin v. Mariotti et al*. and *Fletcher v. Mariotti et al.*, respectively, were filed in the United States District Court for the District of Delaware. These two actions were consolidated for all purposes into one action under the title *In re Funko, Inc. Stockholder Derivative Litigation* on September 8, 2020 and were subsequently transferred to the United States District Court for the Central District of California. On April 23, 2021, both cases pending under the "Stockholder Derivative Litigation" caption were voluntarily dismissed, without prejudice.

On June 11, 2021, one of those purported stockholders filed an additional derivative action, captioned *Silverberg v. Mariotti, et al.*, was filed in the Court of Chancery of the State of Delaware. In response, on July 8, 2021, the Company moved to stay and dismiss the action. On December 1, 2021, Silverberg stipulated to a stay of the action pending resolution of *Ferreira v. Funko, Inc., et al.*, Case No. 2:20-cv-02319.

Additionally, between November 16, 2017 and June 12, 2018, seven purported stockholders of the Company filed putative class action lawsuits in the Superior Court of Washington in and for King County against us, certain of our officers and directors, ACON, Fundamental, the underwriters of our IPO, and certain other defendants.

On July 2, 2018, the suits were ordered consolidated for all purposes into one action under the title *In re Funko, Inc. Securities Litigation*. 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 the action. The motion was fully briefed as of November 30, 2018, and oral argument on the motion was held on May 3, 2019. On August 2, 2019, the Court granted our motion to dismiss the action, allowing plaintiffs leave to amend the complaint. On October 3, 2019, plaintiffs filed a first amended consolidated complaint. We moved to dismiss that complaint on December 5, 2019 and on August 5, 2020, the Superior Court of Washington in and for King County dismissed the consolidated action with prejudice. Plaintiffs appealed and on November 1, 2021, the Court of Appeals reversed the trial court's dismissal decision in most respects, and remanded the case to the trial court for further proceedings. On January 13, 2022, we filed a petition seeking review of the Washington State Court of Appeals' reversal by the Washington Supreme Court. That petition is pending, and accordingly the case has not yet been remanded to the trial court.

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 cases in Washington state court and *Berkelhammer v. Funko, Inc. et al.* allege that we violated Sections 11, 12, and 15 of the Securities Act of 1933, as amended, by making allegedly materially misleading statements in documents filed with the U.S. Securities and Exchange Commission in connection with our IPO 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.

On January 18, 2022, a stockholder filed a putative class action lawsuit in the Court of Chancery of the State of Delaware relating to our corporate "Up-C" structure and bringing direct claims for breach of fiduciary duties against certain current and former officers and directors. On February 14, 2022, we moved to dismiss the complaint. A briefing schedule on the motion to dismiss has not yet been set.

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.

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. 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 grow our business. For example, in the first quarter of 2021, we acquired a majority interest in TokenWave LLC, the developer of a mobile application for tracking and displaying non-fungible tokens, or NFTs, to accelerate our entry into the digital collectible space. We launched our first Digital Pop! NFT collection in the third quarter of 2021 and we currently plan to conduct future NFT “drops” on a regular cadence. The market and consumer demand for NFT and digital collectible products is new, rapidly developing and highly uncertain. No assurance can be given that our investment in TokenWave LLC, or our development or future launch of NFT or digital collectible products, will be successful. We may have increased financial and reputational risks if there is a security or system failure or if there is a failure to launch one or more products. In addition, NFT products have new and different risks than our other consumer products, including potential consumer litigation or regulatory challenge, which could harm our financial results.

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, usage errors by our employees, software bugs or misconfigurations, cybersecurity attacks, computer viruses, malware and other security breaches, as well as catastrophic events such as hurricanes, fires, floods, earthquakes, tornadoes, acts of war or terrorism, and global pandemics. 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. We are also in process of upgrading our enterprise resource planning software globally, beginning 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.

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

On September 17, 2021, we entered into a new credit agreement (the "New Credit Agreement"), providing for a term loan facility in the amount of $180.0 million (the "New Term Loan Facility") and a revolving credit facility of $100.0 million (the "New Revolving Credit Facility" and together with the New Term Loan Facility, the " New Credit Facilities"). Proceeds from the New Term Loan Facility were primarily used to repay the Company’s former term loan facility. As of December 31, 2021, we had $173.2 million of indebtedness outstanding under our New Credit Facilities, consisting of $173.2 million outstanding under our New Term Loan Facility (net of unamortized discount of $2.3 million) and no outstanding borrowings 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;
- 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 sale and leaseback transactions in respect to real property;
- enter into swap agreements;
- 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 New 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 New 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, including due to market volatility and uncertainty resulting from the COVID-19 pandemic. As discussed above, the New 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.

ORGANIZATIONAL STRUCTURE RISKS

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. Based on a Form 4, filed on February 18, 2022, ACON holds approximately 34.2% of the combined voting power of our common stock through its ownership of 9,604,766 shares of our Class A common stock and 7,789,936 shares of our Class B common stock, as of March 1, 2022. 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 1, 2022, collectively hold approximately 40.5% 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 creative 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 two ACON Directors for as 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 creative 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. 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; and (3) the individuals designated in accordance with the terms of the Stockholders Agreement to fill the applicable vacancies on the board of directors.

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.

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 40,088,451 common units of FAH, LLC as of December 31, 2021, representing approximately 77.3% 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 "Ownership of Our Class A Common Stock Risks."

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. Our board of directors will determine the appropriate uses for any excess cash so accumulated, which may include, among other uses, the payment of a cash dividend on our Class A common stock, the payment of obligations under the Tax Receivable Agreement, the declaration of a stock dividend on our Class A common stock, along with the purchase of a corresponding number of common units in FAH, LLC, or the purchase of additional common units in FAH, LLC, along with a recapitalization of all of the outstanding common units in FAH, LLC. To the extent we do not take such actions 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.

OWNERSHIP OF OUR CLASS A COMMON STOCK RISKS

The Continuing Equity Owners own common units in FAH, LLC, and the Continuing Equity Owners 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 1, 2022, we had an aggregate of 159,802,186 shares of Class A common stock authorized but unissued, as well as approximately 11,752,329 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, 2021, 2,680,487 shares of Class A common stock underlying stock options we granted to certain of our directors, executive officers and other employees and 2,101,114 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) 3,000,0000 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. As of December 31, 2021, we had granted 1,002,556 shares of Class A common stock underlying stock options and 919,980 shares of Class A common stock underlying restricted stock units under the 2019 Plan to certain of our executive officers and other employees. 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.

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 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;
- 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 not be taken by written consent in lieu of a meeting;
- 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 “Organizational Structure Risks—ACON has significant influence over us, including over decisions that require the approval of stockholders, and its interests, along with the interests of our other Continuing Equity Owners, in our business may conflict with the interests of our other stockholders.”

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

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

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

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

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

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

- be exempt from the provisions of Section 404(b) of the Sarbanes-Oxley Act of 2002, as amended, or the Sarbanes-Oxley Act, requiring that its independent registered public accounting firm provide an attestation report on the effectiveness of its internal control over financial reporting;
- be exempt from the "say on pay" and "say on golden parachute" advisory vote requirements of the Dodd-Frank Wall Street Reform and Customer Protection Act, or the Dodd-Frank Act;
- be exempt from certain disclosure requirements of the Dodd-Frank Act relating to compensation of its executive officers and be permitted to omit the detailed compensation discussion and analysis from the proxy statements and reports it files under the 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 will 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.

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.

We have in the past identified material weaknesses in our internal control over financial reporting. As a result of any other material weakness that may be identified in the future, our senior management 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 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 identify, 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.

GENERAL RISKS

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 2022 and beyond may have a significant negative impact on our sales and earnings as they are reported in U.S. dollars.

If our or our third-party providers' electronic data is compromised our business could be significantly harmed.

We rely extensively on various information technology systems and software applications (collectively “IT Systems”) for internal and external operations and while we operate certain of these IT Systems, we also rely on third-party providers for a host of technologies, products and services. In addition, in the ordinary course of business, both we and our third-party providers collect, process and maintain significant amounts of data electronically, including proprietary and confidential business information as well as personal information. This data relates to all aspects of our business, including but not limited to 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.

We and many third parties have experienced and expect to continue to experience cyberattacks and other security incidents. Threat actors are becoming more sophisticated and increasingly using techniques designed to circumvent security controls, to evade detection and to obfuscate or remove forensic evidence, which means we may be unable to timely or effectively detect, identify, contain, or remediate future attacks or incidents. Such attacks may involve internal or external actors, and may result from the exploitation of bugs, misconfigurations or vulnerabilities in our IT Systems, human error, social engineering, supply chain attacks, or malware deployment (for example, ransomware), and may disrupt our operations and/or compromise 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 litigation or regulatory actions, to additional costs for remediation and compliance, as well to liabilities and loss of business that could be material. Global consumer protection, data privacy and cybersecurity legal requirements, such as under the GDPR and CCPA, are evolving rapidly and increasingly exposing companies to significant fines and penalties for violations. While we carry insurance, our policies may not cover, or may not fully cover or reimburse us for, any or all costs and losses associated with cybersecurity related events.

Uncertainty relating to the LIBOR calculation process and potential phasing out of LIBOR after 2021, or in certain cases, 2023, 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, discontinued certain tenors of LIBOR in 2021, and the remaining tenors are expected to be discontinued by 2023. The Secured Overnight Financing Rate ("SOFR"), which is a new index calculated by short-term repurchase agreements and is backed by U.S. Treasury securities, has been proposed as an alternative to LIBOR. The market transition away from LIBOR towards SOFR is expected to be complicated, and there is no guarantee that SOFR will become a widely accepted benchmark in place of LIBOR. There remains uncertainty regarding the future utilization of LIBOR and the nature of any replacement rate, and we are uncertain what impact the transition away from LIBOR may have on our business, financial results, and operations.

Any impairment in the value of our goodwill or other assets could 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.

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 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;
- short sales of our stock or trading phenomena such as "short squeezes";
- 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, pandemics such as COVID-19, 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.

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

We are 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.

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.

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.

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: providing detailed disclosures about how personal data is collected and processed; demonstrating an appropriate legal basis; granted new rights for data subjects in regard to their personal data; and imposing limitations on retention of personal data; and maintaining a record of data processing. Each of the GDPR and the UK data protection regime can result in fines up to the greater of EUR 20 million or £17 million, as applicable, or 4% of total global annual turnover. We are also subject to European Union rules with respect to cross-border transfers of personal data out of the EEA and the United Kingdom. Recent legal developments in Europe have created complexity and uncertainty regarding transfers of personal information from the EEA and the United Kingdom to the United States. These recent developments may require us to review and amend the legal mechanisms by which we make and/or receive personal data transfers to/in the U.S. 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. Additionally, a new law, the California Privacy Rights Act (the “CPRA”), will impose additional data protection obligations on companies doing business in California, including additional consumer rights processes, limitations on data uses, new audit requirements for higher risk data, and opt outs for certain uses of sensitive data. It will also create a new California data protection agency authorized to issue substantive regulations and could result in increased privacy and information security enforcement. The majority of the provisions will go into effect on January 1, 2023, and additional compliance investment and potential business process changes may be required.

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.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

As of December 31, 2021, 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
Offices, Main Warehouse and Distribution Facility	Everett, Washington	201,000	January 31, 2026
Warehouse and Distribution Facility	Everett, Washington	119,000	January 31, 2023
Corporate Headquarters and Retail Store	Everett, Washington	99,000	January 31, 2027
Warehouse and Distribution Facility	Everett, Washington	83,000	January 31, 2023
Administrative Offices	Everett, Washington	52,000	January 31, 2032
Office and Warehouse Facility	Everett, Washington	21,000	January 31, 2025
Warehouse and Distribution Facility	Puyallup, Washington	142,000	July 31, 2022
Administrative Offices, Licensing and Apparel Sales	Burbank, California	15,000	December 31, 2024
Retail Store	Hollywood, California	40,000	March 31, 2030
Warehouse and Distribution Facility	Buckeye, Arizona	862,000	October 31, 2032
Warehouse and Administrative Offices	Coventry, England	349,000	July 7, 2029
Sales and Administrative Offices	London, United Kingdom	11,000	June 27, 2027

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. In September 2021, we entered into a lease agreement for a Warehouse and Distribution Facility in Buckeye, Arizona. We expect to begin utilization of that facility in the second quarter of 2022. 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

See Note 14 "Commitments and Contingencies - Legal Contingencies" in the Notes to Consolidated Financial Statements included in this Form 10-K for a discussion of material legal proceedings.

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 1, 2022, there were 11 stockholders of record of our Class A common stock. As of March 1, 2022, there were 14 stockholders of record of our Class B common stock.

Issuer Purchases of Equity Securities

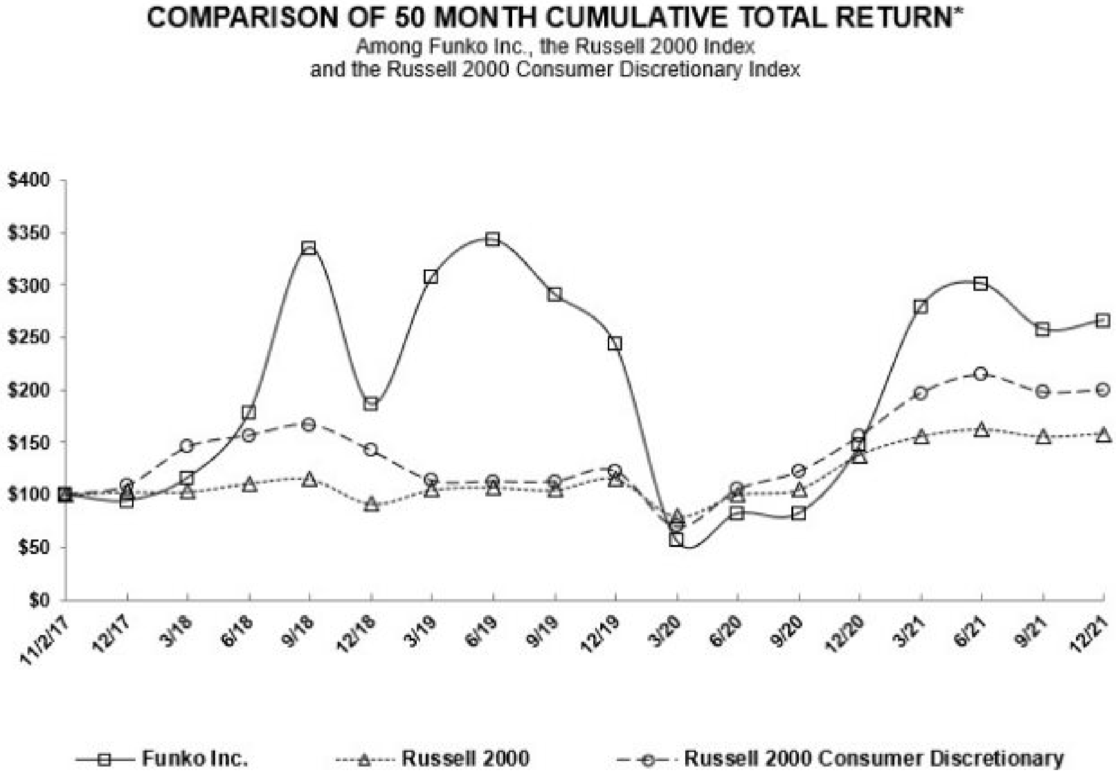
There were no share repurchases during the fourth quarter of the fiscal year ended December 31, 2021.

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. 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.

Stock Performance Graph

The following graph and table illustrate the total return from November 2, 2017 through December 31, 2021, 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.



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

	11/2/2017	12/29/2017	12/31/2018	12/31/2019	12/31/2020	12/31/2021
Funko, Inc.	100.00	94.06	186.00	242.72	146.82	265.91
Russell 2000	100.00	102.89	91.56	114.93	137.87	158.30
Russell 2000 Consumer Discretionary	100.00	108.40	141.97	122.60	155.65	199.87

ITEM 6. [RESERVED.]

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. Our results of operations for the year ended December 31, 2019, including a discussion of the year ended December 31, 2020 compared to the year ended December 31, 2019, have been reported previously under "Management's Discussion and Analysis of Financial Condition and Results of Operations" in our Annual Report on Form 10-K for the year ended December 31, 2020.

Overview

Funko is a leading pop culture lifestyle brand. 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.

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,	
	2021	2020
	(in thousands)	
Net sales	$ 1,029,293	$ 652,537
Net income	$ 67,854	$ 9,763
EBITDA (1)	$ 133,277	$ 66,868
Adjusted EBITDA (1)	$ 149,931	$ 80,216

(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 benefited 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 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 74% and 76% of our sales for the years ended December 31, 2021 and 2020, respectively, and which is sold across multiple product categories.

Relationships with Content Providers

We generate a majority 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 45% and 48% of our sales for the years ended December 31, 2021 and 2020, respectively. During the years ended December 31, 2021 and 2020, we saw shifts in our client mix as a direct result of the COVID-19 pandemic and the related retail shutdowns and limited store occupancy upon reopening.

We depend on retailers to provide adequate and attractive space for our products and point of purchase displays in their stores. We continue to have dedicated shelf space for our products in a variety of aisles in mass-market retailer and specialty stores, with our growing diversified product offerings. In recent years, traditional retailers have been affected by a shift in consumer preferences towards other channels, particularly e-commerce.

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 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. For example, in 2020 there was a lack of new content releases due to the impact of COVID-19 on new content production and the movie theater industry. Due to this impact, the percent of our sales attributable to classic evergreen properties was higher compared to historical trends. 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, 2021 and 2020, we had sales of our products across 955 and 854 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. 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 fail to meet expectations or are delayed in their release, our operating results could be adversely affected.

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 incur expenses related to our operations, as well as payments under the Tax Receivable Agreement. We have caused and intend to continue 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.

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, games homewares and NFTs, primarily to retail customers and distributors. We also sell our products directly to consumers through our e-commerce operations, our retail stores 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. We evaluate the need for price increases along with other incentive arrangements and cost of product to help manage gross margins. In 2021, we instituted price increases for certain of our products and we expect to see the impact of those increases in 2022 and beyond. 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 Loungefly branded products tend to have a higher product cost and higher duties as a percentage of sales and therefore lower gross margins than our Pop! branded products.

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. In 2021, we experienced significant increases in shipping rates dues to the global capacity constraints and the availability of shipping containers.

We anticipate inflationary pressures throughout our supply chain in future periods, specific to shipping and, to a lesser extent, product costs.

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 anticipate inflationary pressures paired with the competition for talent to increase wages, commissions and benefits expense in future periods. 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.

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 2017 acquisition of Underground Toys, the 2017 acquisition of Loungefly and the 2019 acquisition of Forrest-Pruzan.

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, 2021 Compared to Year Ended December 31, 2020

The following table sets forth information comparing the components of net income for the years ended December 31, 2021 and 2020:

	Year Ended December 31,		Period over Period Change	
	2021	2020	Dollar	Percentage
	(in thousands, except percentages)			
Net sales	$ 1,029,293	$ 652,537	$ 376,756	57.7 %
Cost of sales (exclusive of depreciation and amortization shown separately below)	648,302	403,392	244,910	60.7 %
Selling, general, and administrative expenses	244,331	181,234	63,097	34.8 %
Depreciation and amortization	41,195	44,368	(3,173)	(7.2) %
Total operating expenses	933,828	628,994	304,834	48.5 %
Income from operations	95,465	23,543	71,922	nm
Interest expense, net	7,167	10,712	(3,545)	(33.1) %
Loss on extinguishment of debt	675	—	675	nm
Other expense, net	2,708	1,043	1,665	nm
Income before income taxes	84,915	11,788	73,127	nm
Income tax expense	17,061	2,025	15,036	nm
Net income	67,854	9,763	58,091	nm
Less: net income attributable to non-controlling interests	23,954	5,802	18,152	nm
Net income attributable to Funko, Inc.	$ 43,900	$ 3,961	$ 39,939	nm

Net Sales

Net sales were $1.0 billion for the year ended December 31, 2021, an increase of 57.7% compared to $652.5 million for the year ended December 31, 2020. In addition to the impacts of the COVID-19 pandemic for the year ended December 31, 2020, the increase in net sales was also due increased sales to our specialty retailers, commerce sites, direct-to-consumer and distributor customers.

In the year ended December 31, 2021, the number of active properties increased 12.0% to 955 from 854 in the year ended December 31, 2020, and average net sales per active property increased 41.0% to $1.1 million for the year ended December 31, 2021 from $0.8 million for the year ended December 31, 2020. 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 52.2% to $743.8 million in the year ended December 31, 2021 as compared to $488.8 million in the year ended December 31, 2020, net sales in Europe increased 91.7% to $214.7 million in the year ended December 31, 2021 from $112.0 million in the year ended December 31, 2020 and net sales in other international locations increased 36.7% to $70.7 million in the year ended December 31, 2021 from $51.7 million in the year ended December 31, 2020. On a product category basis, net sales of Pop! branded products increased 54.3% to $767.6 million in the year ended December 31, 2021 as compared to $497.3 million in the year ended December 31, 2020. Net sales of Loungefly branded products increased 65.7% to $140.6 million in the year ended December 31, 2021 as compared to $84.8 million in the year ended December 31, 2020. Net sales of other products increased 72.1% to $121.2 million in the year ended December 31, 2021 as compared to $70.4 million the year ended December 31, 2020.

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

Cost of sales (exclusive of depreciation and amortization) was $648.3 million for the year ended December 31, 2021, an increase of 60.7%, compared to $403.4 million for the year ended December 31, 2020. Cost of sales (exclusive of depreciation and amortization) increased primarily as a result of the increase in net sales, which drove a $113.6 million increase in product costs, a $75.6 million increase in shipping and freight costs and a $56.6 million increase in royalty expenses.

Gross margin (exclusive of depreciation and amortization), calculated as net sales less cost of sales as a percentage of sales, was 37.0% for the year ended December 31, 2021, compared to 38.2% for the year ended December 31, 2020. Gross margin (exclusive of depreciation and amortization) decreased 120 basis points for the year ended December 31, 2021 compared to the year ended December 31, 2020, due primarily to global supply chain capacity constraints driving increased freight costs, partially offset by improved global product margins. We expect the increased freight costs to continue at least through early 2022.

Selling, General, and Administrative Expenses

Selling, general, and administrative expenses were $244.3 million for the year ended December 31, 2021, an increase of 34.8%, compared to $181.2 million for the year ended December 31, 2020. The increase was driven primarily by a $38.8 million increase in personnel expenses and commissions, a $9.4 million increase in advertising and marketing, a $4.2 million increase in professional fees, a $3.3 million increase in facilities and rent, and a $2.9 million increase in equity-based compensation. In 2020, selling, general, and administrative expenses decreased in response to the COVID-19 pandemic and efforts to reduce costs and preserve liquidity. For the year ended December 31, 2021, such restrictions were lifted to support current year and future net sales growth opportunities.

Selling, general, and administrative expenses were 23.7% of sales for the year ended December 31, 2021, compared to 27.8% of sales for the year ended December 31, 2020, primarily due to the increase in net sales outpacing selling, general and administrative expenses.

Depreciation and Amortization

Depreciation and amortization expense was $41.2 million for the year ended December 31, 2021, compared to $44.4 million for the year ended December 31, 2020, primarily driven by the type and timing of assets placed into service.

Interest Expense, Net

Interest expense, net was $7.2 million for the year ended December 31, 2021, a decrease of 33.1%, compared to $10.7 million for the year ended December 31, 2020. 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, 2021.

Loss on debt extinguishment

As a result of the debt refinancing in September 2021, $0.7 million loss on debt extinguishment was recorded for the year ended December 31, 2021 as unamortized debt financing fees were written-off.

Income Tax Expense

Income tax expense was $17.1 million for the year ended December 31, 2021, compared to $2.0 million for the year ended December 31, 2020. The increase was primarily due to an increase in income before income taxes of $73.1 million for the year ended December 31, 2021 as compared to the year ended December 31, 2020.

Net Income

Net income was $67.9 million for the year ended December 31, 2021, compared to $9.8 million for the year ended December 31, 2020. The increase in net income was primarily the result of the increase in net sales and decreases in interest expense, net, offset by increases in cost of goods sold, selling, general and administrative for the year ended December 31, 2021 as compared to the year ended December 31, 2020, 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, earnings per share or any other performance measure derived in accordance with U.S. GAAP. We define EBITDA as net income before interest expense, net, income tax expense, depreciation and amortization. We define Adjusted EBITDA as EBITDA further adjusted for non-cash charges related to equity-based compensation programs, loss of extinguishment of debt, certain severance, relocation and related 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 for newly issued-shares of Class A common stock of Funko, Inc. and further adjusted for the impact of certain non-cash charges and other items that we do not consider in our evaluation of ongoing operating performance. These items include, among other things, reallocation of net income attributable to non-controlling interests, non-cash charges related to equity-based compensation programs, loss on extinguishment of debt, certain severance, relocation and related costs, foreign currency transaction gains and losses, Tax Receivable Agreement liability adjustments, and the income tax expense effect of these adjustments. We define Adjusted Earnings per Diluted Share as Adjusted Net Income divided by the weighted-average shares of Class A common stock outstanding, assuming (1) the full exchange of all outstanding common units and options in FAH, LLC for newly issued-shares of Class A common stock of Funko, Inc. and (2) the dilutive effect of stock options and unvested common units, if any. We caution investors that amounts presented in accordance with our definitions of the Non-GAAP Financial Measures may not be comparable to similar measures disclosed by our competitors, because not all companies and analysts calculate the Non-GAAP Financial Measures in the same manner. We present the Non-GAAP Financial Measures because we consider them to be important supplemental measures of our performance and believe they are frequently used by securities analysts, investors, and other interested parties in the evaluation of companies in our industry. Management believes that investors’ understanding of our performance is enhanced by including these Non-GAAP Financial Measures as a reasonable basis for comparing our ongoing results of operations.

Management uses the Non-GAAP Financial Measures:

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

By providing these Non-GAAP Financial Measures, together with reconciliations, we believe we are enhancing investors' understanding of our business and our results of operations, as well as assisting investors in evaluating how well we are executing our strategic initiatives. 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 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, loss on extinguishment of debt, 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. Each of the normal recurring adjustments and other adjustments described herein and in the reconciliation table below help management with a measure of our core operating performance over time by removing items that are not related to day-to-day operations.

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

	Year Ended December 31, 2021	Year Ended December 31, 2020
	(in thousands, except per share data)	
Net income attributable to Funko, Inc.	$ 43,900	$ 3,961
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)	23,954	5,802
Equity-based compensation (2)	12,994	10,116
Loss on extinguishment of debt (3)	675	—
Certain severance, relocation and related costs (4)	277	2,190
Foreign currency transaction loss (5)	1,118	955
Tax receivable agreement liability adjustments (6)	1,590	87
Income tax expense (7)	(8,331)	(4,259)
Adjusted net income	$ 76,177	$ 18,852
Weighted-average shares of Class A common stock outstanding-basic	38,392	35,271
Equity-based compensation awards and common units of FAH, LLC that are convertible into Class A common stock	15,437	16,227
Adjusted weighted-average shares of Class A stock outstanding-diluted	53,829	51,498
Adjusted earnings per diluted share	$ 1.42	$ 0.37

	Year Ended December 31, 2021	Year Ended December 31, 2020
	(in thousands)	
Net income	$ 67,854	$ 9,763
Interest expense, net	7,167	10,712
Income tax expense	17,061	2,025
Depreciation and amortization	41,195	44,368
EBITDA	$ 133,277	$ 66,868
Adjustments:		
Equity-based compensation (2)	12,994	10,116
Loss on extinguishment of debt (3)	675	—
Certain severance, relocation and related costs (4)	277	2,190
Foreign currency transaction loss (5)	1,118	955
Tax receivable agreement liability adjustments (6)	1,590	87
Adjusted EBITDA	$ 149,931	$ 80,216

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

(3) Represents write-off of unamortized debt financing fees for the year ended December 31, 2021.

(4) Represents certain severance, relocation and related costs. For the year ended December 31, 2021, includes charges related to one-time relocation costs for U.S. warehouse personnel in connection with the new opening of a warehouse and distribution facility in Buckeye, Arizona and residual severance payments related to the global workforce reduction implemented in response to the COVID-19 pandemic. For the year ended December 31, 2020, includes charges related to the global workforce reduction implemented in response to the COVID-19 pandemic and impairment related charges to the right-of-use leased and fixed assets related to Funko Animation Studios.

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

(6) Represents recognized adjustments to the tax receivable agreement liability.

(7) Represents the income tax expense effect of the above adjustments. This adjustment uses an effective tax rate of 25% for the years ended December 31, 2021 and 2020.

Liquidity and Financial Condition

Introduction

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

On September 17, 2021, the Company, entered into a new credit agreement (the “New Credit Agreement”) providing for a term loan facility in the amount of $180.0 million (the “New Term Loan Facility”) and a revolving credit facility of $100.0 million (the “New Revolving Credit Facility”) (together the “New Credit Facilities”). Proceeds from the New Credit Facilities were primarily used to repay the Company’s $235.0 million term loan facility (the "Former Term Loan Facility") and its $75.0 million revolving credit facility (the “Former Revolving Credit Facility” and together with the Former Term Loan Facility, the “Former Credit Facilities”). The New Credit Facilities are secured by substantially all assets of the Borrowers and any of their existing or future material domestic subsidiaries, subject to customary exceptions.

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

- 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 FAH 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 consecutive fiscal quarters as long as after giving pro forma effect to such distribution (i) no event of default then exists or would result therefrom and (ii) the Net Leverage Ratio (as defined in the New Credit Agreement) is not greater than a ratio that is 0.50:1.00 less than the Net Leverage Ratio set forth in the financial covenant for the applicable fiscal quarter.

We expect these limitations to continue in the future under the terms of our New Credit Agreement 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 April 19, 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 and will remain effective until through September 15, 2022. 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.

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, 2021 and 2020 (in thousands):

	Year Ended December 31,	
	2021	2020
Net cash provided by operating activities	$ 87,362	$ 108,739
Net cash used in investing activities	(27,381)	(18,482)
Net cash used in financing activities	(28,628)	(63,338)
Effect of exchange rates on cash and cash equivalents	(51)	107
Net increase in cash and cash equivalents	$ 31,302	$ 27,026

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, 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 $87.4 million for the year ended December 31, 2021, compared to $108.7 million for the year ended December 31, 2020. 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 decrease for the year ended December 31, 2021 compared to the year ended December 31, 2020 was primarily due to changes in working capital, which decreased net cash provided by operating activities by $71.9 million and were primarily due to increases in accounts receivable, net, inventory, and prepaid expenses and other assets of $76.7 million, $110.0 million and $8.6 million, respectively, and increases in accrued expenses and other liabilities, accounts payable, accrued royalties, and income taxes payable of $55.7 million, $40.2 million, $11.7 million and $15.8 million, respectively. The decrease in net cash provided by operating activities was also offset by an increase in net income, excluding non-cash adjustments of $50.5 million, driven primarily by an increase in net sales.

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, 2021, net cash used in investing activities was $27.4 million, which was used for the purchase of property and equipment, primarily related to tooling and molds used for the expansion of product lines.

For the year ended December 31, 2020, net cash used in investing activities was $18.5 million and which was used for the purchase of property and equipment, primarily related to tooling and molds used for the expansion of product lines.

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, distributions to members and the payment of contingent consideration.

For the year ended December 31, 2021, net cash used in financing activities was $28.6 million, primarily related to payments under the Tax Receivable Agreement of $1.7 million, distributions to the Continuing Equity Owners of $9.3 million, and net payments on the Term Loan Facility of $18.4 million, partially offset by $3.8 million proceeds from the exercise of equity-based options.

For the year ended December 31, 2020, net cash used in financing activities was $63.3 million, primarily related to payments under the Tax Receivable Agreement of $4.6 million, distributions to the Continuing Equity Owners of $3.6 million, net payments on the Term Loan Facility of $26.4 million, and net payments on the Revolving Credit Facility of $26.8 million, partially offset by $0.2 million proceeds from the exercise of equity-based options.

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 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 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 September 17, 2021, we entered into the New Credit Facilities which, as amended, are secured by substantially all assets of the Borrowers and any of their existing or future material domestic subsidiaries, subject to customary exceptions.

The New Term Loan Facility matures on September 17, 2026 (the “Maturity Date”) and amortizes in quarterly installments in aggregate amounts equal to 2.50% of the original principal amount of the New Term Loan Facility, with any outstanding balance due and payable on the Maturity Date. The first amortization payment commenced with the quarter ending on December 31, 2021. The New Revolving Credit Facility also 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 (i) LIBOR, EURIBOR, HIBOR, CDOR, Daily Simple SONIA and/or the Central Bank Rate, as applicable, plus 2.50% or (ii) ABR or the Canadian prime rate, as applicable, plus 1.50%, in each case of clauses (i) and (ii), subject to two 0.25% step-downs based on the achievement of certain leverage ratios following the Closing Date. Each of LIBOR, EURIBOR, HIBOR, CDOR and Daily Simple SONIA rates are subject to a 0.00% floor. For loans based on ABR, the Central Bank Rate or the Canadian prime rate, interest payments are due quarterly. For loans based on Daily Simple SONIA, interest payments are due monthly. For loans based on LIBOR, EURIBOR, HIBOR or CDOR, interest payments are due at the end of each applicable interest period.

The New Credit Agreement 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;
- 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 sale and leaseback transactions in respect to real property;
- enter into swap agreements;
- 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 New Credit Agreement requires FAH, LLC and its subsidiaries to comply on a quarterly basis with a maximum Net Leverage Ratio and a minimum fixed charge coverage ratio (in each case, measured on a trailing four-quarter basis). The maximum Net Leverage Ratio and the minimum fixed charge coverage ratio for the fiscal quarter ending December 31, 2021 are 2.50:1.00 and 1.25:1.00, respectively.

As of December 31, 2021 and December 31, 2020, we were in compliance with all covenants in our respective credit agreements in effect at such time. We expect to maintain compliance with our covenants for at least one year from the issuance of these financial statements based on our current expectations and forecasts. If economic conditions caused by the COVID-19 global pandemic worsen and negatively impact the Company's earnings and operating cash flows, this could impact our ability to maintain compliance with our amended financial covenants and require the Company to seek additional amendments to our New Credit Agreement.

The New 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 material monetary judgments and changes of control. The New 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, 2021, we had \$83.6 million of cash and cash equivalents and \$167.6 million of working capital, compared with \$52.3 million of cash and cash equivalents and \$120.7 million of working capital as of December 31, 2020. 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 Credit Facilities. We expect these sources of liquidity to continue to be our primary sources of liquidity.

Credit Facilities. On September 17, 2021, the Company entered into the New Credit Facilities. For a discussion of our Credit Facilities, 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 and will remain effective until through September 15, 2022. 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

As noted above, our primary requirements for liquidity and capital are working capital, inventory management, capital expenditures, debt service and general corporate needs. For a description of the Company's future maturities of debt, see Note 10, Debt, and for a description of the Company's operating lease agreements, see Note 11, Leases. See Note 13 "Liabilities under Tax Receivable Agreement" in the Notes to Consolidated Financial Statements included in this Form 10-K for a discussion of our obligations under the Tax Receivable Agreement. See Note 14 "Commitments and Contingencies" in the Notes to Consolidated Financial Statements included in this Form 10-K for a discussion of other material contractual obligations.

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 (including future enterprise resource planning (ERP) system, additional platforms to support our direct-to-consumer experience, and capital build out of new leased warehouse and office space). 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.

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 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 have adopted, or 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. 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, 2021, we recorded a prepaid asset of $4.7 million, net of a reserve of $0.7 million. As of December 31, 2020, we recorded a prepaid asset of $6.3 million, net of a reserve of $1.0 million.

We record a royalty liability as revenues are recognized 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 income. Royalty expenses for the years ended December 31, 2021 and 2020, were $162.0 million and $105.0 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. Inventory costs include direct product costs and freight costs. 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.

In addition, during the year ended December 31, 2019, we recognized 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, 2021 and 2020, the Company acquired an aggregate of 3.9 million and 0.5 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, 2021 and 2020, the Company recognized an increase to its net deferred tax assets in the amount of $17.2 million and $0.5 million, respectively, and corresponding Tax Receivable Agreement liabilities of $20.7 million and $1.0 million, respectively, representing 85% of the tax benefits due to the Continuing Equity Owners. In addition, during the year ended December 31, 2021 and 2020, the Company recognized $1.6 million and $0.1 million, respectively of expenses in other expense (income), net on our consolidated statements of income related to remeasurement adjustments of Tax Receivable Agreement liabilities.

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 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 Credit Facilities include the Term Loan Facility and the Revolving Credit Facility with advances tied to a borrowing base and which bear interest at a variable rate. Because our 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, 2021, we had $173.2 million of variable rate debt outstanding under our Credit Facilities, consisting of $173.2 million outstanding under the Term Loan Facility (net of unamortized discount of $2.3 million) in outstanding variable rate borrowings. We had no outstanding variable rate borrowings under our Revolving Credit Facility. Based upon a sensitivity analysis of our debt levels on December 31, 2021, an increase or decrease of 1% in the effective interest rate would cause an increase or decrease in interest expense of approximately $1.8 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 another international subsidiary in 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.

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 have experienced and anticipate experiencing inflationary pressures on the inbound shipping and product costs which we have partially mitigated through price increases of certain products. We also anticipate inflationary pressures paired with competition for talent to increase wages, commissions and benefits expense. 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, 2021, 2020 AND 2019

CONTENTS

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, 2021 and 2020, the related consolidated statements of income, comprehensive income, stockholders' equity and cash flows, for each of the three years in the period ended December 31, 2021, and the related notes, and the financial statement schedule listed in the index at Item 15(a) (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, 2021 and 2020, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2021, 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 3, 2022

FUNKO, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME

	Year Ended December 31,		
	2021	2020	2019
	(in thousands, except per share data)		
Net sales	$ 1,029,293	$ 652,537	$ 795,122
Cost of sales (exclusive of depreciation and amortization shown separately below)	648,302	403,392	512,580
Selling, general, and administrative expenses	244,331	181,234	193,803
Depreciation and amortization	41,195	44,368	42,126
Total operating expenses	933,828	628,994	748,509
Income from operations	95,465	23,543	46,613
Interest expense, net	7,167	10,712	14,342
Loss on extinguishment of debt	675	—	—
Other expense (income), net	2,708	1,043	(25)
Income before income taxes	84,915	11,788	32,296
Income tax expense	17,061	2,025	4,476
Net income	67,854	9,763	27,820
Less: net income attributable to non-controlling interests	23,954	5,802	16,095
Net income attributable to Funko, Inc.	$ 43,900	$ 3,961	$ 11,725
Earnings per share of Class A common stock:			
Basic	$ 1.14	$ 0.11	$ 0.38
Diluted	$ 1.08	$ 0.11	$ 0.36
Weighted average shares of Class A common stock outstanding:			
Basic	38,392	35,271	30,898
Diluted	40,611	35,770	32,926

See accompanying notes to consolidated financial statements.

FUNKO, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Year Ended December 31,		
	2021	2020	2019
	(in thousands)		
Net income	$ 67,854	$ 9,763	$ 27,820
Other comprehensive income:			
Foreign currency translation (loss) gain, net of tax effect of $163, $(274) and $(282) for the years ended December 31, 2021, 2020 and 2019, respectively	(683)	1,415	1,458
Reclassification of foreign currency translation gain into net income	(96)	—	—
Comprehensive income	67,075	11,178	29,278
Less: Comprehensive income attributable to non-controlling interests	23,815	6,290	16,595
Comprehensive income attributable to Funko, Inc.	$ 43,260	$ 4,888	$ 12,683

See accompanying notes to consolidated financial statements.

FUNKO, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

	December 31, 2021	December 31, 2020
	(in thousands, except per share data)	
Assets		
Current assets:		
Cash and cash equivalents	$ 83,557	$ 52,255
Accounts receivable, net	187,688	131,837
Inventory	166,428	59,773
Prepaid expenses and other current assets	14,925	15,486
Total current assets	452,598	259,351
Property and equipment, net	58,828	56,141
Operating lease right-of-use assets	53,466	58,079
Goodwill	126,651	125,061
Intangible assets, net	189,619	205,541
Deferred tax asset	74,412	54,682
Other assets	11,929	4,735
Total assets	$ 967,503	$ 763,590
Liabilities and Stockholders' Equity		
Current liabilities:		
Current portion long-term debt, net of unamortized discount	$ 17,395	$ 10,758
Current portion of operating lease liabilities	14,959	13,840
Accounts payable	57,238	29,199
Income taxes payable	15,994	425
Accrued royalties	58,158	40,525
Accrued expenses and other current liabilities	121,267	43,949
Total current liabilities	285,011	138,696
Long-term debt, net of unamortized discount	155,818	180,012
Operating lease liabilities, net of current portion	50,459	57,512
Deferred tax liability	648	780
Liabilities under tax receivable agreement, net of current portion	75,523	60,297
Other long-term liabilities	3,486	3,848
Commitments and contingencies (Note 14)		
Stockholders' equity:		
Class A common stock, par value $0.0001 per share, 200,000 shares authorized; 40,088 shares and 35,657 shares issued and outstanding as of December 31, 2021 and 2020, respectively	4	4
Class B common stock, par value $0.0001 per share, 50,000 shares authorized; 10,691 shares and 14,040 shares issued and outstanding as of December 31, 2021 and 2020, respectively	1	1
Additional paid-in-capital	252,505	216,141
Accumulated other comprehensive income	1,078	1,718
Retained earnings	68,050	24,403
Total stockholders' equity attributable to Funko, Inc.	321,638	242,267
Non-controlling interests	74,920	80,178
Total stockholders' equity	396,558	322,445
Total liabilities and stockholders' equity	$ 967,503	$ 763,590

See accompanying notes to consolidated financial statements.

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

	Class A Common Stock		Class B Common Stock						
	Shares	Amount	Shares	Amount	Additional Paid-In Capital	Other Comprehensive Income	Retained Earnings	Non-Controlling Interests	Total
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
Activity under equity-based compensation plans	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
Distribution to continuing equity owners	—	—	—	—	—	—	—	(3,576)	(3,576)
Equity-based compensation	—	—	—	—	10,116	—	—	—	10,116
Activity under equity-based compensation plans	226	—	—	—	118	—	—	—	118
Cumulative translation adjustment, net of tax	—	—	—	—	—	927	—	488	1,415
Establishment of liabilities under tax receivable agreement and related changes to deferred tax assets	—	—	—	—	(536)	—	—	—	(536)
Redemption of common units of FAH, LLC	513	1	(475)	—	2,269	—	—	(2,269)	1
Net income	—	—	—	—	—	—	3,961	5,802	9,763
Period ended December 31, 2020	35,657	$ 4	14,040	$ 1	$ 216,141	$ 1,718	$ 24,403	$ 80,178	$ 322,445
Distribution to continuing equity owners	—	—	—	—	—	—	—	(9,277)	(9,277)
Equity-based compensation	—	—		—	12,994	—	—	—	12,994
Activity under equity-based compensation plans	554	—		—	5,956	—	—	—	5,956
Cumulative translation adjustment, net of tax	—	—	—	—	—	(544)	—	(139)	(683)
Establishment of liabilities under tax receivable agreement and related changes to deferred tax assets	—	—	—	—	(3,532)	—	—	—	(3,532)
Redemption of common units of FAH, LLC	3,877	—	(3,349)	—	20,746	—	—	(20,746)	—
Other	—	—	—	—	200	(96)	(253)	950	801
Net income	—	—	—	—	—	—	43,900	23,954	67,854
Period ended December 31, 2021	40,088	$ 4	10,691	$ 1	$ 252,505	$ 1,078	$ 68,050	$ 74,920	$ 396,558

See accompanying notes to consolidated financial statements.

FUNKO, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended December 31,		
	2021	2020	2019
		(in thousands)	
Operating Activities			
Net income	$ 67,854	$ 9,763	$ 27,820
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation, amortization and other	40,056	46,742	44,518
Equity-based compensation	12,994	10,116	13,044
Amortization of debt issuance costs and debt discounts	1,118	1,352	1,210
Loss on debt extinguishment	675	—	—
Deferred tax expense (benefit)	(361)	3,323	(2,293)
Other	1,403	1,952	635
Changes in operating assets and liabilities:			
Accounts receivable, net	(56,648)	20,077	(3,969)
Inventory	(107,166)	2,845	25,372
Prepaid expenses and other assets	3,700	12,273	(5,824)
Accounts payable	26,933	(13,303)	4,629
Income taxes payable	15,585	(209)	(3,618)
Accrued royalties	17,633	5,906	(4,403)
Accrued expenses and other liabilities	63,586	7,902	(6,356)
Net cash provided by operating activities	87,362	108,739	90,765
Investing Activities			
Purchase of property and equipment	(27,759)	(18,482)	(42,264)
Acquisitions, net of cash	199	—	(6,369)
Other	179	—	—
Net cash used in investing activities	(27,381)	(18,482)	(48,633)
Financing Activities			
Borrowings on line of credit	—	28,267	42,083
Payments on line of credit	—	(55,103)	(36,383)
Debt issuance costs	(1,055)	(569)	(411)
Proceeds from long-term debt, net	180,000	—	—
Payment of long-term debt	(198,375)	(26,438)	(11,750)
Contingent consideration	(2,000)	(1,500)	—
Distributions to continuing equity owners	(9,277)	(3,575)	(23,923)
Payments under tax receivable agreement	(1,715)	(4,639)	(173)
Proceeds from exercise of equity-based options	3,794	219	2,217
Net cash used in financing activities	(28,628)	(63,338)	(28,340)
Effect of exchange rates on cash and cash equivalents	(51)	107	(2,049)
Net increase in cash and cash equivalents	31,302	27,026	11,743
Cash and cash equivalents at beginning of period	52,255	25,229	13,486
Cash and cash equivalents at end of period	$ 83,557	$ 52,255	$ 25,229
Supplemental Cash Flow Information			
Cash paid for interest	$ 5,679	$ 9,089	$ 12,313
Income tax payments	1,462	4,167	14,125
Accrual for purchases of property and equipment	—	—	5,362
Establishment of liabilities under tax receivable agreement	20,691	1,000	59,045
Issuance of equity instruments for acquisitions	—	—	2,221
Tenant allowance	—	269	3,201

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 owns 100% of Funko Holdings LLC ("FHL") and FHL owns 100% of Funko, LLC, a limited liability company formed in the state of Washington, which is its operating entity. The Company is headquartered in Everett, Washington and is a leading pop culture consumer products company. The Company designs, sources, and distributes licensed pop culture products.

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 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. Certain prior-year amounts have been reclassified to conform to the current year presentation.

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 transactions typically settle in less than 5 days and were $1.5 million and $0.9 million at December 31, 2021 and 2020, respectively.

Concentrations of Business and Credit Risk

The Company grants credit to its customers on an unsecured basis. The Company monitors the financial health of its customers and will take actions to mitigate a customer's credit risk if a negative financial forecast is expected. As of December 31, 2021 and 2020, the balance of accounts receivable consisted of 18% and 11%, 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, 2021, 2020 and 2019 there was no individual customer that generated net sales over 10%.

For the year ended December 31, 2021, 26% of sales were related to the Company's two largest license agreements (13% each) with no other license agreements accounting for more than 10% of sales. For the year ended December 31, 2020, 12% and 11% of sales were related to the Company's two largest license agreements with no other license agreements accounting for more than 10% of 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.

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. Inventory costs include direct product costs and freight costs. 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. Reserves for excess and obsolete inventories were $4.7 million and $8.6 million as of December 31, 2021 and 2020, respectively.

During the year ended December 31, 2019, the Company 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 was 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

The Company monitors our long-lived assets for impairment indicators on an ongoing basis in accordance with U.S. GAAP. If impairment indicators exist, the Company will perform the required impairment analysis by comparing the undiscounted cash flows expected to be generated from the long-lived assets to the related net book values. If the net book value exceeds the undiscounted cash flows, an impairment loss is measured and recognized. An impairment loss is measured as the difference between the net book value and the fair value of the long-lived assets. Fair value is estimated based upon a combination of market and cost approaches, as appropriate. Changes in economic or operating conditions impacting these estimates and assumptions could result in the impairment of the Company's long-lived assets.

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. 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, 2021, we recorded a prepaid asset of $4.7 million, net of a reserve of $0.7 million. As of December 31, 2020, we recorded a prepaid asset of $6.3 million, net of a reserve of $1.0 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 income. Royalty expenses for the years ended December 31, 2021, 2020 and 2019, were $162.0 million, $105.0 million and $126.8 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, 2021, 2020 and 2019 were $17.1 million, $7.7 million, and $11.3 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 income 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 income as incurred. Product design and development costs for the years ended December 31, 2021, 2020 and 2019, were $6.8 million, $5.1 million, and $5.2 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 income. In connection with the settlement and remeasurement of intercompany balances, we recorded a nominal loss, loss of $0.4 million and gain of $0.7 million for the years ended December 31, 2021, 2020 and 2019, respectively.

The income tax effects related to the unrealized foreign currency component of other comprehensive income are reclassified to earnings only when the net investment is sold, or when a liquidation of the respective net investment in the foreign entity is substantially completed.

Recently Adopted Accounting Standards

There were no recently adopted accounting standards during the year ended December 31, 2021 that had a material effect of the financial statements.

3. Acquisitions

On March 26, 2021, the Company acquired a majority of the membership interests of TokenWave LLC, the developer of TokenHead, a mobile app and website for showcasing and tracking Non-Fungible Token (“NFT”) holdings. This transaction represented an opportunity to expand the Company’s product offerings into digital NFTs. The Company accounted for the acquisition as a business combination. The purchase consideration, fair value of the assets acquired and liabilities assumed, and acquisition related transaction costs were not material. The activity of TokenWave LLC included in the Company’s consolidated statements of income from the acquisition date to December 31, 2021 was not material.

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. The total purchase consideration of $11.9 million was allocated on a 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 finalization of the purchase price allocation resulted in no change from the preliminary estimate. The activity of Funko Games, LLC included in the Company’s consolidated statements of income from the acquisition date to December 31, 2019 was not material.

The purchase consideration allocated to the Forrest-Pruzan 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

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. The Company has determined that it has one reporting unit for which discrete financial information is available and results are regularly reviewed by management.

The Company's long-lived asset groups, which includes intangible assets, property and equipment and operating lease right-of-use assets net of operating lease liabilities, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the asset group might not be recoverable. Conditions that would necessitate an impairment assessment include a significant decline in the observable market value of an asset (or asset group), a significant change in the extent or manner in which an asset (or asset group) 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 goodwill were recorded in the years ended December 31, 2021, 2020 and 2019.

The following table presents the balances of goodwill as of 2021 and 2020 (in thousands):

	Goodwill
Balance as of January 1, 2020	$ 124,835
Foreign currency remeasurement	226
Balance as of December 31, 2020	$ 125,061
Acquisition	1,662
Foreign currency remeasurement	(72)
Balance as of December 31, 2021	$ 126,651

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, licensor and supplier relationships, trade names, and noncompetition agreements. 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. As of December 31, 2021, there were also $0.1 million in indefinite-lived assets not subject to amortization but tested for impairment. No impairment charges relating to intangible assets were recorded in the years ended December 31, 2021, 2020 and 2019.

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

		December 31, 2021			December 31, 2020		
	Estimated Useful Life (Years)	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	$ 115,331	$ (36,060)	$ 79,271	$ 115,131	$ (30,008)	$ 85,123
Trade names	10 - 20	83,358	(25,985)	57,373	83,359	(21,717)	61,642
Customer relationships	3 - 20	71,699	(24,912)	46,787	71,736	(20,301)	51,435
Licensor relationships	10 - 20	11,276	(5,186)	6,090	11,301	(4,068)	7,233
Supplier relationships	2	322	(322)	—	325	(325)	—
Noncompetition agreements	3	290	(278)	12	290	(182)	108
Total		$ 282,276	$ (92,743)	$ 189,533	$ 282,142	$ (76,601)	$ 205,541

Amortization expense for the years ended December 31, 2021, 2020 and 2019 was $16.2 million, $16.0 million, and $15.9 million, respectively. The future five-year amortization of intangibles subject to amortization at December 31, 2021 was as follows (in thousands):

	Amortization
2022	$ 15,107
2023	14,893
2024	14,873
2025	14,873
2026	14,815
Thereafter	114,972
Total	$ 189,533

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, existing economic conditions and supportable forecasted changes.

The Company evaluates its general portion of the allowance for doubtful accounts based on historical loss information and applies reserve percentages based on aging schedule. Days past due is calculated from contractual due date of the trade receivable contract. The composition of the trade receivables is consistent with that used in developing the historical credit-loss percentages and evaluated to reflect current conditions and supportable forecasted changes. The trade receivables are generally due in 30 to 90 days.

In addition to the general portion of the allowance for doubtful accounts, certain doubtful accounts are evaluated for a specific reserve. These accounts generally include significantly past due or other factors known where a substantial portion or all of the balance is uncollectible. 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, 2021	December 31, 2020
Accounts receivable	$ 190,844	$ 135,417
Less: Allowance for doubtful accounts	(3,156)	(3,580)
Accounts receivable, net	$ 187,688	$ 131,837

Accounts receivable includes a $0.8 million tenant improvement receivable from a lessor as of both December 31, 2021 and 2020. In addition, accounts receivable as of December 31, 2021 includes an income tax receivable of $0.3 million. The remaining balance is customer receivables. Bad debt expense was $0.9 million, $2.4 million and $1.1 million for the years ended December 31, 2021, 2020 and 2019, respectively.

Activity in our allowance for doubtful accounts was as follows (in thousands):

	December 31, 2021	December 31, 2020
Allowance for doubtful accounts - beginning	$ 3,580	$ 2,354
Charged to costs	895	2,396
Write offs	(1,319)	(1,170)
Allowance for doubtful accounts - ending	$ 3,156	$ 3,580

6. Prepaid Expenses and Other Current Assets

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

	December 31, 2021	December 31, 2020
Prepaid deposits for inventory and molds	$ 1,111	$ 1,373
Prepaid royalties, net	4,746	6,260
Other prepaid expenses and current assets	9,068	7,853
Prepaid expenses and other current assets	$ 14,925	$ 15,486

7. Property and Equipment, Net

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

	December 31, 2021	December 31, 2020
Tooling and molds	$ 119,915	$ 102,865
Leasehold improvements	44,112	42,573
Computer equipment, software and other	13,007	11,310
Furniture, fixtures and warehouse equipment	12,177	11,762
Construction in progress	7,194	318
	$ 196,405	$ 168,828
Less: Accumulated depreciation	(137,577)	(112,687)
Property and equipment, net	$ 58,828	$ 56,141

Depreciation expense for the years ended December 31, 2021, 2020 and 2019 was $25.0 million, $28.3 million, and $26.2 million, respectively.

8. Accrued Expenses and Other Current Liabilities

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

	December 31, 2021	December 31, 2020
Accrued payroll and compensation	$ 23,439	$ 13,338
Accrued shipping & freight costs	42,649	4,733
Accrued sales taxes	1,978	757
Current liabilities under tax receivable agreement	7,362	2,020
Other current liabilities	45,839	23,101
Accrued liabilities and other current liabilities	$ 121,267	$ 43,949

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.

Cash equivalents. As of December 31, 2021 and 2020, cash equivalents included $56.9 million and $34.5 million, respectively, of highly liquid money market funds, which are classified as Level 1 within the fair value hierarchy.

Debt. The estimated fair values of the Company's debt instruments, which are classified as Level 3 financial instruments, at December 31, 2021 and 2020, was approximately $175.5 million and $193.9 million, respectively. The carrying values of the Company's debt instruments at December 31, 2021 and 2020, were $173.2 million and $190.8 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,	
	2021	2020
Term Loan Facility	175,500	193,875
Debt issuance costs	(2,287)	(3,105)
Total term debt	173,213	190,770
Less: current portion	17,395	10,758
Long-term debt, net	$ 155,818	$ 180,012

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

	Term Loan Facility
2022	$ 18,000
2023	18,000
2024	18,000
2025	18,000
2026	103,500
Total	$ 175,500

Former Credit Facilities

On October 22, 2018, the Company entered into a credit agreement (as amended, the "Former Credit Agreement") providing for a term loan facility in the amount of $235.0 million (the "Former Term Loan Facility") and a revolving credit facility of $50.0 million (the "Former Revolving Credit Facility") (together the "Former Credit Facilities"). On February 11, 2019, the Company amended the Former Credit Agreement to increase the Former Revolving Credit Facility to $75.0 million. On September 23, 2019, the Company entered into a second amendment to the Former Credit Agreement, which extended the maturity date of the Former Term Loan Facility and the Former Revolving Credit Facility under the Former Credit Facilities to September 23, 2024 (the "Former Facility Maturity Date"), reduced the interest margin applicable to all loans under the Former Credit Agreement by 0.75% and reduced certain fees incurred under the Former Credit Agreement. The second amendment also allowed the Company to request an additional $25.0 million increase to the Former Term Loan Facility.

On May 5, 2020 the Company entered into a third amendment to the Former Credit Agreement, which modified the financial covenants and adjusted the required leverage levels for the Leverage Ratio (as defined in the Former Credit Agreement) to provide the Company with additional flexibility.

The Former Term Loan Facility amortized in quarterly installments in aggregate amounts equal to 5.00% of the original principal amount of the Former Term Loan Facility in the first and second years of the Former Term Loan Facility, 10.00% of the original principal amount of the Former Term Loan Facility in the third and fourth years of the Former Term Loan Facility and 12.50% of the original principal amount of the Former Term Loan Facility in the fifth year of the Former Term Loan Facility, with any outstanding balance due and payable on the Maturity Date. The first amortization payment was on December 31, 2018. The Former Revolving Credit Facility would have terminated on the Former Facility Maturity Date and loans thereunder were eligible to be borrowed, repaid, and reborrowed up to such date.

As amended, loans under the Credit Facilities bore 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 3.00% or the Base Rate (as defined in the Credit Agreement) plus 2.00%, with 0.25% step-downs based on the achievement of certain leverage ratios. The Euro-Rate was subject to a 1.00% floor and for loans based on the Euro-Rate, interest payments were due at the end of each applicable interest period.

The Former Credit Facilities were secured by substantially all of the assets of the Company and its material domestic subsidiaries, subject to customary exceptions. As of December 31, 2020, the Company was in compliance with all of the covenants in its Former Credit Agreement.

In September 2021, all of the outstanding aggregate principal balance and accrued interest of $180.1 million on the Company's Former Term Loan Facility was repaid, and the Company recorded a $0.7 million loss on debt extinguishment as a result of the write-off of unamortized deferred financing fees.

New Credit Facilities

On September 17, 2021, the Company, entered into a new credit agreement (the "New Credit Agreement") providing for a term loan facility in the amount of $180.0 million (the "New Term Loan Facility") and a revolving credit facility of $100.0 million (the "New Revolving Credit Facility") (together the "New Credit Facilities"). Proceeds from the New Credit Facilities were primarily used to repay the Former Credit Facilities.

The New Term Loan Facility matures on September 17, 2026 (the "Maturity Date") and amortizes in quarterly installments in aggregate amounts equal to 2.50% of the original principal amount of the New Term Loan Facility, with any outstanding balance due and payable on the Maturity Date. The first amortization payment commences with the quarter ending on December 31, 2021. The New Revolving Credit Facility also 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 (i) LIBOR, EURIBOR, HIBOR, CDOR, Daily Simple SONIA and/or the Central Bank Rate, as applicable, plus 2.50% or (ii) ABR or the Canadian prime rate, as applicable, plus 1.50%, in each case of clauses (i) and (ii), subject to two 0.25% step-downs based on the achievement of certain leverage ratios following the Closing Date. Each of LIBOR, EURIBOR, HIBOR, CDOR and Daily Simple SONIA rates are subject to a 0% floor. For loans based on ABR, the Central Bank Rate or the Canadian prime rate, interest payments are due quarterly. For loans based on Daily Simple SONIA, interest payments are due monthly. For loans based on LIBOR, EURIBOR, HIBOR or CDOR, interest payments are due at the end of each applicable interest period.

The New Credit Facilities are secured by substantially all of the assets of the Company and any of its existing or future material domestic subsidiaries, subject to customary exceptions. As of December 31, 2021, the Company was in compliance with all of the covenants in its New Credit Agreement.

At December 31, 2021 and 2020, the Company had $175.5 million and $193.9 million of borrowings outstanding under the New Term Loan Facility and Former Term Loan Facility, respectively, and no outstanding borrowings under the New Revolving Credit Facility and Former Revolving Credit Facility, respectively. At December 31, 2021 and 2020, the Company had $100.0 million and $75.0 million available under the New Revolving Credit Facility and Former Revolving Credit Facility, respectively.

There were no outstanding letters of credit as of December 31, 2021 and 2020.

11. Leases

The Company has entered into non-cancellable operating leases for office, warehouse, and distribution facilities, with original lease periods expiring through 2032. Leases with an initial term of 12 months or less are not recorded on the consolidated balance sheets; the Company recognizes lease expense for these leases on a straight-line basis over the lease term. The Company combines lease and non-lease components for new and reassessed leases.

Some operating leases also contain the option to renew for five years 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 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 consolidated balance sheets and amortize the lease incentives on a straight-line basis over the lease term as an adjustment to rent expense. Rent expense, included in selling, general and administrative expenses on the consolidated statements of income, was $16.5 million, $15.3 million and $14.9 million for the years ended December 31, 2021, 2020 and 2019, respectively.

During the years ended December 31, 2021 and 2020, operating cash outflows relating to operating lease liabilities was $14.4 million and $11.6 million, respectively and operating lease right-of-use assets obtained in exchange for new operating lease obligations was $4.0 million, with no lease incentives obtained and $5.8 million, net of lease incentives obtained of $0.3 million, respectively. As of December 31, 2021 and 2020, the Company's operating leases had a weighted-average remaining term of 7.0 years and 7.3 years, respectively and weighted-average discount rate of 6.22% and 6.28%, respectively. 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.

During the year ended December 31, 2020, the Company recognized an impairment loss of $1.4 million related to the right of use lease asset in Bath, England. The related lease liability was remeasured and reduced by $0.9 million. The lease agreement was terminated in December 2021.

In January 2020, the Company has also entered into a non-cancellable operating sub-lease for office space expiring in 2024. Rental income recognized for the years ended December 31, 2021 and 2020 was $0.3 million and $0.3 million, respectively, included as a reduction of selling, general and administrative expenses on the consolidated statements of income.

The future payments on the Company's operating lease liabilities as of December 31, 2021 were as follows (in thousands):

2022	$	15,445
2023		12,582
2024		12,013
2025		10,504
2026		9,303
Thereafter		20,489
Total lease payments		80,336
Less: imputed interest		(14,918)
Total	$	65,418

Not included in the lease payments table above are future payments related to Warehouse and Distribution lease in Buckeye, Arizona. The Company expects lease commencement to occur in mid-2022 and extend through October 2032. The 862,000 square foot building is expected to add approximately $1.5 million, $4.6 million, $4.7 million, $4.8 million, $4.9 million and $31.2 million in minimum rental expense for 2022, 2023, 2024, 2025, 2026 and thereafter, respectively.

12. Income Taxes

Income before income taxes consisted of (in thousands):

	Year Ended December 31,					
	2021		2020		2019	
Domestic	$	72,758	$	4,149	$	21,414
Foreign		12,157		7,639		10,882
Income before income taxes	$	84,915	$	11,788	$	32,296

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

	Year Ended December 31,		
	2021	2020	2019
Current income taxes:			
Federal	$ 12,894	$ (3,030)	$ 4,216
State and local	1,825	59	601
Foreign	2,703	1,673	1,952
Current income taxes	$ 17,422	$ (1,298)	$ 6,769
Deferred income taxes:			
Federal	$ (185)	$ 2,585	$ (2,333)
State and local	(18)	206	(185)
Foreign	(158)	532	225
Deferred income taxes	(361)	3,323	(2,293)
Income tax expense	$ 17,061	$ 2,025	$ 4,476

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,		
	2021	2020	2019
Expected U.S. federal income taxes at statutory rate	21.0 %	21.0 %	21.0 %
State and local income taxes, net of federal benefit	1.7	2.5	1.0
Foreign taxes	2.5	18.7	5.9
Foreign tax credit	—	(9.3)	—
Non-deductible expenses	(1.1)	1.6	(0.8)
Change in valuation allowance	2.3	5.4	4.9
Non-controlling interest	(6.0)	(12.7)	(10.8)
Share-based Compensation	0.1	5.1	(2.6)
Return to Provision	1.5	(15.1)	(3.0)
Other, net	(1.9)	—	(1.7)
Income tax expense	20.1 %	17.2 %	13.9 %

The Company's annual effective tax rate in 2021, 2020 and 2019 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.

Deferred Income Taxes

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

	December 31,	
	2021	2020
Deferred tax assets:		
Investment in partnership	$ 64,335	$ 46,582
Tax Receivable Agreement liability	19,105	14,087
Stock-based compensation	6,197	4,195
Foreign Tax Credit	—	1,090
Other carryforwards	—	898
Net operating loss carryforward	—	756
Gross deferred tax assets	89,637	67,608
Valuation allowance	(14,829)	(12,367)
Deferred tax assets, net of valuation allowance	74,808	55,241
Deferred tax liabilities:		
Property and equipment	(701)	(833)
Other	(343)	(506)
Gross deferred tax liabilities	(1,044)	(1,339)
Net deferred tax assets	$ 73,764	$ 53,902

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, 2021 and 2020, the Company recognized a deferred tax asset of $64.3 million and $46.6 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, 2021 and 2020, the Company has a valuation allowance in the amount of $14.8 million and $12.4 million, respectively, against the deferred tax asset.

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, 2021, 2020 and 2019 (in thousands):

	Year Ended December 31,		
	2021	2020	2019
Unrecognized tax benefits at January 1	$ 490	$ 490	$ 490
Decreases for positions taken in current year	(490)	—	—
Unrecognized tax benefits at December 31	$ —	$ 490	$ 490

Of the $0.5 million of unrecognized tax benefits as of December 31, 2020 and 2019, $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, 2021, and 2020, 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 2018 and subject to examination for all foreign income tax returns for fiscal 2021 and 2020. There were no open tax examinations at December 31, 2021 and 2020.

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, 2021 and 2020, the Company acquired an aggregate of 3.9 million and 0.5 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, 2021 and 2020, the Company recognized an increase to its net deferred tax assets in the amount of $17.2 million and $0.5 million, respectively, and corresponding Tax Receivable Agreement liabilities, 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. There were no transactions subject to the Tax Receivable Agreement for which the Company did not recognize the related liability during the years ended December 31, 2021, 2020 and 2019, 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 following table summarizes changes in the amount of the Company’s Tax Receivable Agreement liability for the three years ended December 31, 2021, 2020 and 2019 (in thousands):

	Year Ended December 31,		
	2021	2020	2019
Beginning Balance	$ 62,318	$ 65,816	$ 6,771
Additional liabilities for exchanges	20,691	1,000	59,045
Adjustment to remeasurement of liabilities	1,590	87	152
Payments under tax receivable agreement	(1,715)	(4,585)	(152)
Ending balance	$ 82,884	$ 62,318	$ 65,816

The future payments on the Company’s tax receivable agreement liabilities as of December 31, 2021 are expected to be (in thousands):

2022	$ 7,362
2023	4,835
2024	4,902
2025	5,003
2026	5,119
Thereafter	55,663
Total	$ 82,884

14. Commitments and Contingencies

License Agreements

The Company enters into license agreements with various licensors of copyrighted and trademarked characters and design in connection with the products that it sells. The agreements generally require royalty payments based on product sales and in some cases may require minimum royalty and other related commitments. The Company is expected to incur $11.2 million in minimum guaranteed royalty payments under licensing arrangements, including, $5.3 million in 2022, $4.3 million in 2023 and $1.7 million in 2024.

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 March 10, 2020, a purported stockholder of the Company filed a putative class action lawsuit in the United States District Court for the Central District of California against the Company and certain of its officers, entitled *Ferreira v. Funko, Inc. et al.* The original complaint alleged that the Company violated Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, as amended (the "Exchange Act") as well as Rule 10b-5 promulgated thereunder, by making allegedly materially misleading statements in its earnings announcement and Quarterly Report on Form 10-Q for the quarter ended September 30, 2019, as well as by omitting material facts necessary to make the statements made therein not misleading. The lawsuit sought, among other things, compensatory damages and attorneys' fees and costs. Two additional complaints making substantially similar allegations were filed April 3, 2020 in the United States District Court for the Central District of California and April 9, 2020 in the United States District Court for the Western District of Washington, respectively. On June 11, 2020, the Central District of California actions were consolidated for all purposes into one action under the *Ferreira* caption, and lead plaintiffs and lead counsel were appointed pursuant to the Private Securities Litigation Reform Act; shortly thereafter, the Western District of Washington action was voluntarily dismissed. Lead plaintiffs filed the consolidated complaint on July 31, 2020, against the Company and certain of its officers and directors, as well as entities affiliated with ACON Funko Investors, L.L.C. ("ACON"). The consolidated complaint added Section 10(b) and 20(a) claims based on the Company's earnings announcement and Quarterly Report on Form 10-Q for the quarter ended June 30, 2019, as well as claims under Section 20A of the Exchange Act. All defendants moved to dismiss the consolidated action on October 2, 2020. On February 25, 2021, the Court granted all defendants' motions to dismiss the *Ferreira* action, allowing the lead plaintiffs leave to amend the complaint. Lead plaintiffs filed their amended complaint on March 29, 2021, and all defendants moved to dismiss. On October 25, 2021, the Court issued an order granting defendants' motion in part and denying the motion in part. Specifically, the court dismissed with prejudice all claims related to statements regarding Funko's projected net sales and the claims based on inventory risk warnings in our Quarterly Report on Form 10-Q for the quarter ended June 30, 2019, but denied the motion to dismiss as to claims based on inventory risk warnings in our Quarterly Report on Form 10-Q for the quarter ended September 30, 2019.

Several shareholder derivative actions based on the earnings announcement and Quarterly Report on Form 10-Q for the quarter ended September 30, 2019 have been brought on behalf of the Company against certain of its directors and officers. Specifically, on April 23, June 5, and June 10, 2020, the actions captioned *Cassella v. Mariotti et al.*, *Evans v. Mariotti et al.*, and *Igelido v. Mariotti et al.*, respectively, were filed in the United States District Court for the Central District of California. On July 6, 2020, these three actions were consolidated for all purposes into one action under the title *In re Funko, Inc. Derivative Litigation*, and on August 13, 2020, the consolidated action was stayed pending final resolution of the motion to dismiss in the *Ferreira* action. Additionally, on July 14 and July 31, 2020, the actions captioned *Rubin v. Mariotti et al.* and *Fletcher v. Mariotti et al.*, respectively, were filed in the United States District Court for the District of Delaware. These two actions were consolidated for all purposes into one action under the title *In re Funko, Inc. Stockholder Derivative Litigation* on September 8, 2020 and were subsequently transferred to the United States District Court for the Central District of California. On April 23, 2021, both cases pending under the "Stockholder Derivative Litigation" caption were voluntarily dismissed, without prejudice.

Additionally, between November 16, 2017 and June 12, 2018, seven purported stockholders of the Company filed putative class action lawsuits in the Superior Court of Washington in and for King County against the Company, certain of its officers and directors, ACON, Fundamental Capital, LLC and Funko International, LLC (collectively, "Fundamental"), the underwriters of its IPO, and certain other defendants.

On July 2, 2018, the suits were ordered consolidated for all purposes into one action under the title *In re Funko, Inc. Securities Litigation*. 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 the action. The motion was fully briefed as of November 30, 2018, and oral argument on the motion was held on May 3, 2019. On August 2, 2019, the Court granted the Company's motion to dismiss the action, allowing plaintiffs leave to amend the complaint. On October 3, 2019, plaintiffs filed a first amended consolidated complaint. The Company moved to dismiss that complaint on December 5, 2019 and on August 5, 2020, the Superior Court of Washington in and for King County dismissed the consolidated action with prejudice. Plaintiffs appealed, and on November 1, 2021, the Court of Appeals reversed the trial court's dismissal decision in most respects, and remanded the case to the trial court for further proceedings. On January 13, 2022, the Company filed a petition seeking review of the Washington State Court of Appeals' reversal by the Washington Supreme Court. That petition is pending, and accordingly the case has not yet been remanded to the trial court.

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 cases in Washington state court and *Berkelhammer v. Funko, Inc. et al.* allege that the Company violated Sections 11, 12, and 15 of the Securities Act of 1933, as amended, by making allegedly materially misleading statements in documents filed with the U.S. Securities and Exchange Commission in connection with the Company's IPO 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 the Company's Class A common stock by the plaintiffs and members of the putative class, as well as attorneys' fees and costs.

On June 11, 2021, one of those purported stockholders filed a related derivative action, captioned *Silverberg v. Mariotti, et al.*, was filed in the Court of Chancery of the State of Delaware. In response, on July 8, 2021, the Company moved to stay and dismiss the action. On December 1, 2021, Silverberg stipulated to a stay of the action pending resolution of *Ferreira v. Funko, Inc., et al.*, Case No. 2:20-cv-02319.

On January 18, 2022, a stockholder filed a putative class action lawsuit in the Court of Chancery of the State of Delaware relating to the Company's corporate "Up-C" structure and bringing direct claims for breach of fiduciary against certain current and former officers and directors. On February 14, 2022, the Company moved to dismiss the complaint. A briefing schedule on the motion to dismiss has not yet been set.

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

15. Segments

The Company identifies its 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, the Company has one segment.

The following tables present summarized product information as a percent of sales:

	Year ended December 31,		
	2021	2020	2019
Figures	77.6 %	77.2 %	80.8 %
Other	22.4 %	22.8 %	19.2 %

	Year ended December 31,		
	2021	2020	2019
Pop! Branded Products	74.5 %	76.2 %	78.6 %
Loungefly Branded Products	13.7 %	13.0 %	9.1 %
Other	11.8 %	10.8 %	12.3 %

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

	Year ended December 31,		
	2021	2020	2019
Net sales:			
United States	$ 743,846	$ 488,823	$ 523,897
Europe	214,732	111,997	198,203
Other International	70,715	51,717	73,022
Total net sales	$ 1,029,293	$ 652,537	$ 795,122

	December 31,	
	2021	2020
Long-lived assets:		
United States	$ 81,022	$ 72,813
Vietnam and China	16,701	16,144
United Kingdom	26,500	29,998
Total long-lived assets	$ 124,223	$ 118,955

16. Related Party Transactions

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, 2021, 2020 and 2019, the Company recorded approximately $0.8 million, $2.0 million and $2.3 million, respectively, in net sales from business with Forbidden Planet. At December 31, 2021 and 2020, accounts receivable from Forbidden Planet were $0.4 million and $0.5 million on the consolidated balance sheets, 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 years ended December 31, 2021 and 2020, the Company recorded $0.3 million and $0.2 million, of rental expense related to the leases, which was recorded in selling, general and administrative expenses in the Company's consolidated statements of Income.

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 though 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 $1.8 million, $1.5 million and $1.6 million for the years ended December 31, 2021, 2020 and 2019, respectively.

18. Stockholders' Equity

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 Creative 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

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.

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"). 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.

The number of unissued common shares reserved for future grants under the 2017 Plan and 2019 Plan was 736,917 and 1,077,464, respectively as of December 31, 2021.

A summary of stock option activity for the year ended December 31, 2021 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, 2020	2,905	$	13.05	$	4,069	8.05
Granted	821		19.82		—	
Exercised	(268)		14.12		2,543	
Forfeited	(216)		15.20		812	
Outstanding at December 31, 2021	3,242		14.54		15,973	7.61
Options exercisable at December 31, 2021	1,760	$	13.48	$	10,152	6.81

Stock options awarded to employees under the 2017 Plan and 2019 Plan are generally granted with an exercise price equal to the closing market price of the Company's common stock at the date of grant, vest over four years, and have ten years contractual terms.

A summary of restricted stock unit activity for the year ended December 31, 2021 is as follows:

	Funko, Inc. Restricted Stock Units		Weighted Average Grant Date Fair Value	Remaining Contractual Life
	(in thousands)			(years)
Unvested at December 31, 2020	1,868	$	12.58	2.37
Granted	638		16.41	
Vested	(284)		9.43	
Forfeited	(81)		11.29	
Unvested at December 31, 2021	2,141	$	14.18	2.22

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, 2021 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, 2020	228		0.05		2,437	2.41
Outstanding at December 31, 2021	228	$	0.05	$	4,278	1.41
Options exercisable at December 31, 2021	228	$	0.05	$	4,278	1.41

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. There were no unvested common units of FAH, LLC as of December 31, 2020.

The following table presents information on stock option exercises (in thousands):

	Year ended December 31,		
	2021	2020	2019
Cash received for exercise price	$ 3,794	$ 219	$ 2,217
Intrinsic value	2,543	957	3,404

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 and 2019 Plan, the following were the weighted-average of the option pricing model inputs:

	Year ended December 31,		
	2021	2020	2019
Expected term (years)	6.06	6.05	6.07
Expected volatility	48.6 %	45.6 %	38.7 %
Risk-free interest rate	1.0 %	0.5 %	2.4 %
Dividend yield	— %	— %	— %

The weighted-average fair value of stock options granted for the years ended December 31, 2021, 2020 and 2019 was $9.26, $1.90 and $8.35 per share, respectively.

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 statements of income. Equity-based compensation for the years ended December 31, 2021, 2020 and 2019 was $13.0 million, $10.1 million and $13.0 million, respectively.

As of December 31, 2021, there was $24.0 million of total unrecognized equity-based compensation expense that the Company expected to recognize over a remaining weighted-average period of 2.4 years. Of this, $9.1 million is related to options to purchase Class A common stock in Funko, Inc. and $15.0 million is related to unvested restricted stock units in Class A common stock of Funko, Inc. As of December 31, 2021, the Company expected to recognize these costs over a remaining weighted average period of 2.6 years for options to purchase Class A shares in Funko, Inc., and 2.2 years for unvested restricted stock units in Class A common stock of Funko, Inc.

19. Non-controlling Interests

The Company is 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.

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, 2021, 2020 and 2019, Funko, Inc. owned 40.1 million, 35.7 million and 34.9 million of FAH, LLC common units, respectively, representing a 77.3%, 69.5% and 68.7% economic ownership interest in FAH, LLC, respectively.

Net income and comprehensive income of FAH, LLC excludes certain activity attributable to Funko, Inc., including $13.0 million, $10.0 million and $10.8 million of equity-based compensation expense for share-based compensation awards issued by Funko, Inc. for the years ended December 31, 2021, 2020 and 2019, respectively, and $14.3 million of income tax expense, $0.4 million income tax benefit and $2.2 million of income tax expense for corporate, federal, state and local taxes attributable to Funko, Inc. for the years ended December 31, 2021, 2020 and 2019, 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.

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, 2021	Year Ended December 31, 2020	Year Ended December 31, 2019
	(in thousands, except per share data)		
Numerator:			
Net income	$ 67,854	$ 9,763	$ 27,820
Less: net income attributable to non-controlling interests	23,954	5,802	16,095
Net income attributable to Funko, Inc. — basic	$ 43,900	$ 3,961	$ 11,725
Add: Reallocation of net income attributable to non- controlling interests from the assumed exchange of common units of FAH, LLC for Class A common stock	—	—	—
Net income attributable to Funko, Inc. — diluted	$ 43,900	$ 3,961	$ 11,725
Denominator:			
Weighted-average shares of Class A common stock outstanding — basic	38,392,390	35,270,795	30,897,569
Add: Dilutive common units of FAH, LLC that are convertible into Class A common stock	227,500	304,327	1,064,145
Add: Dilutive Funko, Inc. equity compensation awards	1,990,728	194,891	964,059
Weighted-average shares of Class A common stock outstanding — diluted	40,610,618	35,770,013	32,925,773
Earnings per share of Class A common stock — basic	$ 1.14	$ 0.11	$ 0.38
Earnings per share of Class A common stock — diluted	$ 1.08	$ 0.11	$ 0.36

For the years ended December 31, 2021, 2020 and December 31, 2019 an aggregate of 14.7 million, 19.7 million and 20.1 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, 2021, 2020 and 2019 anti-dilutive securities included 13.2 million, 15.8 million and 19.1 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.

Schedule I: Condensed Financial Information of Registrant

FUNKO, INC.
CONDENSED STATEMENTS OF INCOME
(PARENT COMPANY ONLY)

	Year Ended December 31,		
	2021	2020	2019
	(in thousands)		
Intercompany revenue	$ 82	$ 307	$ 739
Selling, general, and administrative expenses	13,163	10,269	11,211
Total operating expenses	13,163	10,269	11,211
Loss from operations	(13,081)	(9,962)	(10,472)
Interest (expense) income, net	3	(36)	—
Tax receivable agreement liability adjustment	(1,590)	(87)	(152)
Equity in net income of subsidiaries	72,916	13,674	24,525
Income before income taxes	58,248	3,589	13,901
Income tax expense (benefit)	14,348	(372)	2,176
Net income	$ 43,900	$ 3,961	$ 11,725

See accompanying notes to condensed financial information

Schedule I: Condensed Financial Information of Registrant (continued)

FUNKO, INC.
CONDENSED STATEMENTS OF COMPREHENSIVE INCOME
(PARENT COMPANY ONLY)

	Year Ended December 31,		
	2021	2020	2019
	(in thousands)		
Net income	$ 43,900	$ 3,961	$ 11,725
Other comprehensive income:			
Foreign currency translation (loss) gain, net of tax effect of $163, $(274) and $(282) for the years ended December 31, 2021, 2020 and 2019, respectively	(544)	927	958
Reclassification of foreign currency translation gain into net income	$ (96)	$ —	$ —
Comprehensive income attributable to Funko, Inc.	$ 43,260	$ 4,888	$ 12,683

See accompanying notes to condensed financial information

Schedule I: Condensed Financial Information of Registrant (continued)

FUNKO, INC.
CONDENSED BALANCE SHEETS
(PARENT COMPANY ONLY)

	December 31, 2021	December 31, 2020
	(in thousands, except per share data)	
Assets		
Current assets:		
Cash and cash equivalents	$ 61,943	$ 34,568
Income tax receivable	—	294
Total current assets	61,943	34,862
Intercompany receivable	116,746	117,995
Deferred tax asset	74,464	54,734
Investment in subsidiaries	166,054	97,523
Total assets	$ 419,207	$ 305,114
Liabilities and Stockholders' Equity		
Current liabilities:		
Tax payable	$ 14,684	$ —
Current portion of liabilities under tax receivable agreement	7,362	2,020
Accrued expenses and other current liabilities	—	40
Total current liabilities	22,046	2,060
Liabilities under tax receivable agreement, net of current portion	75,523	60,297
Other long-term liabilities	—	490
Commitments and contingencies		
Stockholders' equity:		
Class A common stock, par value $0.0001 per share, 200,000 shares authorized; 40,088 shares and 35,657 shares issued and outstanding as of December 31, 2021 and 2020, respectively	4	4
Class B common stock, par value $0.0001 per share, 50,000 shares authorized; 10,691 shares and 14,040 shares issued and outstanding as of December 31, 2021 and 2020, respectively	1	1
Additional paid-in-capital	252,505	216,141
Accumulated other comprehensive income	1,078	1,718
Retained earnings	68,050	24,403
Total stockholders' equity	321,638	242,267
Total liabilities and stockholders' equity	$ 419,207	$ 305,114

See accompanying notes to condensed financial information

Schedule I: Condensed Financial Information of Registrant (continued)

FUNKO, INC.
CONDENSED STATEMENTS OF CASH FLOWS
(PARENT COMPANY ONLY)

	Year Ended December 31,		
	2021	2020	2019
		(in thousands)	
Operating Activities			
Net income	$ 43,900	$ 3,961	$ 11,725
Adjustments to reconcile net income to net cash provided by operating activities:			
Equity in net income of subsidiaries	(72,916)	(13,674)	(24,525)
Equity-based compensation	12,994	10,007	10,827
Deferred tax expense (benefit)	(203)	2,792	(2,518)
Tax receivable liability adjustment	1,590	87	152
Changes in operating assets and liabilities:			
Income tax receivable	294	3,521	(3,816)
Due from related parties, net	1,351	26,007	(19,182)
Prepaid expenses and other assets	—	—	(2,336)
Income taxes payable	14,684	—	(3,497)
Accrued expenses and other liabilities	(571)	304	1,985
Net cash provided by (used in) operating activities	1,123	33,005	(31,185)
Financing Activities			
Tax distribution received from FAH, LLC	24,173	5,825	29,502
Tax receivable agreement payments	(1,715)	(4,639)	(173)
Proceeds from exercise of equity-based options	3,794	41	2,148
Net cash provided by financing activities	26,252	1,227	31,477
Net increase in cash and cash equivalents	27,375	34,232	292
Cash and cash equivalents at beginning of period	34,568	336	44
Cash and cash equivalents at end of period	$ 61,943	$ 34,568	$ 336
Supplemental Cash Flow Information			
Income tax payments	$ 23	$ 2,116	$ 11,969
Establishment of liabilities under tax receivable agreement	20,691	1,000	59,045
Issuance of equity instruments for acquisitions	—	—	2,221

See accompanying notes to condensed financial information

Schedule I: Condensed Financial Information of Registrant (continued)

FUNKO, INC.
NOTES TO CONDENSED FINANCIAL INFORMATION
(PARENT COMPANY ONLY)
December 31, 2021

1. Organization

Funko, Inc. (the “Parent Company”) was formed on April 21, 2017 as a Delaware corporation and is a holding company with no direct operations. The Parent Company's assets consist primarily of cash and cash equivalents, its equity interest in FAH, LLC, and certain deferred tax assets. The Parent Company also had three wholly owned subsidiaries with direct ownership interest in FAH, LLC until the subsidiaries were dissolved and liquidated on June 30, 2020.

The Parent Company's cash inflows are primarily from distributions and other transfers from FAH, LLC. The amounts available to the Parent Company to fulfill cash commitments are subject to certain restrictions in FAH, LLC’s Credit Facilities. See Note 10 to the Funko, Inc. consolidated financial statements, appearing elsewhere in this Form 10-K.

2. Basis of Presentation

These condensed Parent Company financial statements should be read in conjunction with the consolidated financial statements of Funko, Inc. and its subsidiaries and the accompanying notes thereto, included in this Form 10-K. For purposes of this condensed financial information, the Parent Company's interest in FAH, LLC is recorded based upon its proportionate share of FAH, LLC's net assets (similar to presenting them on the equity method).

The Parent Company is the sole managing member of FAH, LLC, and pursuant to the Amended and Restated LLC Agreement of FAH, LLC (the “LLC Agreement”), receives compensation in the form of reimbursements for all costs associated with being a public company. Intercompany revenue consists of these reimbursement payments and is recognized when the corresponding expense to which it relates is recognized.

Certain intercompany balances presented in these condensed Parent Company financial statements are eliminated in the consolidated financial statements. For the years ended December 31, 2021, 2020, and 2019, the full amounts of intercompany revenue and equity in net income of subsidiaries in the Parent Company Statements of Operations were eliminated in consolidation. An intercompany receivable was owed to the Parent Company by FAH, LLC of $116.7 million and $118.0 million as of December 31, 2021 and 2020, respectively. Related party amounts that were not eliminated in the consolidated financial statements include the Parent Company's liabilities under the tax receivable agreement, which totaled $82.9 million and $62.3 million as of December 31, 2021 and 2020, respectively.

3. Commitments and Contingencies

The Parent Company is party to a tax receivable agreement with certain holders of common units in FAH, LLC (the "Continuing Equity Owners") that provides for the payment by the Parent Company to the Continuing Equity Owners of 85% of the amount of any tax benefits that the Parent Company actually realizes, or in some cases is deemed to realize, as a result of certain transactions. See Note 13 to the Funko, Inc. consolidated financial statements, appearing elsewhere in this Form 10-K, for more information regarding the Parent Company's tax receivable agreement. As described in Note 13 to the Funko, Inc. consolidated financial statements, appearing elsewhere in the Form 10-K, amounts payable under the tax receivable agreement are contingent upon, among other things, (i) generation of future taxable income of Funko, Inc. over the term of the tax receivable agreement and (ii) future changes in tax laws. As of December 31, 2021 and 2020, liabilities under the tax receivable agreement totaled $82.9 million and $62.3 million, respectively.

See Note 14 to the Funko, Inc. consolidated financial statements, appearing elsewhere in this Form 10-K, for information regarding pending and threatened litigation. Pursuant to the LLC Agreement, the Parent Company receives reimbursements for all costs associated with being a public company, which includes costs of litigation.

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, 2021, 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 effective at the reasonable assurance level as of December 31, 2021.

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 Exchange Act.

Our management, under the supervision and with the participation of our chief executive officer and chief financial officer, conducted an assessment of the effectiveness of our internal control over financial reporting as of December 31, 2021 based on the framework and criteria established 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, 2021, our internal control over financial reporting was effective.

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".

Changes in Internal Control Over Financial Reporting

There have been no changes in the Company’s internal control over financial reporting that occurred during the three months ended December 31, 2021 that have materially affected, or are reasonably likely to materially affect, the Company’s internal control over financial reporting.

Item 9B. OTHER INFORMATION

Not applicable.

Item 9C. DISCLOSURE REGARDING FOREIGN JURISDICTION THAT PREVENT INSPECTIONS

Not applicable.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

Code of Ethics

Our Code of Business Conduct and Ethics (the "Code of Conduct") applies to all of our officers, directors and employees, including our principal executive officer, principal financial officer and principal accounting officer. The Code of Conduct is publicly available on our Internet website at www.funko.com. We intend to satisfy the disclosure required by law or Nasdaq Stock Market listing standards regarding any amendment to, or waiver from, a provision of the Code of Conduct by posting such information on our website at www.funko.com.

Executive Officers and Directors

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 "Information about our Executive Officers and Board of Directors," and will also appear in our definitive proxy statement for our 2021 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" (if applicable) in our definitive proxy statement for our 2022 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" (if applicable) in our definitive proxy statement for our 2022 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, 2021)

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			1,814,381 (1)
Stock Options	3,241,935	$ 14.54	—
Restricted Stock Units	2,141,001	—	—
Equity compensation plans not approved by security holders	—	—	—
Total	5,382,936	$ 14.54	1,814,381

(1) Includes 736,917 shares of Class A common stock available for issuance under our 2017 Incentive Award Plan and 1,077,464 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 2022 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 2022 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 2022 Annual Meeting of Stockholders, and such information is incorporated herein by reference.

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(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

Schedule I: Condensed Financial Information of Registrant

All other 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				
		Form	File No.	Exhibit	Filing Date	Filed/ Furnished Herewith
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/A	333-220856	4.1	10/23/2017	
4.2	Description of Securities	10-K	001-38274	4.2	3/5/2020	
10.1 †	Funko Acquisition Holdings, L.L.C. 2015 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 January 3, 2022, between the Company and Brian Mariotti.	8-K	001-38274	10.2	1/7/2022	
10.7 †	Employment Agreement, dated October 20, 2017, by and between Funko, Inc. and Tracy Daw.	10-K	001-38274	10.10	3/19/2018	
10.8 †	Amended and Restated Employment Agreement, dated January 3, 2022, between the Company and Andrew Perlmutter.	8-K	001-38274	10.1	1/7/2022	
10.9 †	Form of Indemnification Agreement for Directors and Officers.	S-1/A	333-220856	10.27	10/12/2017	

Exhibit Number	Exhibit Description	Incorporated by Reference				
		Form	File No.	Exhibit	Filing Date	Filed/ Furnished Herewith
10.10 †	Form of Restricted Stock Unit Award Agreement under 2017 Incentive Award Plan	10-Q	001-38274	10.1	8/10/2018	
10.11 †	Funko, Inc. Non-Employee Director Compensation Policy.	10-K	001-38274	10.16	3/6/2019	
10.12	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	
10.13	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	
10.14	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	
10.15	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	
10.16	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	
10.17	Credit Agreement dated September 17, 2021, among Funko Acquisition Holdings, L.L.C., Funko Holdings LLC, Funko, LLC, Loungefly, LLC and Funko Games, LLC, JPMorgan Chase Bank, N.A., as Administrative Agent, and each other financial institution from time to time party thereto.	8-K	001-38274	10.1	9/22/2021	
10.18†	Employment Agreement, dated July 22, 2019, between Funko, Inc. and Jennifer Fall Jung.	8-K	001-38274	10.1	7/23/2019	
10.19†	Funko, Inc. 2019 Incentive Award Plan.	8-K	001-38274	10.1	6/27/2019	
10.20†	Form of Option Award Agreement under the Funko, Inc. 2019 Incentive Award Plan.	10-Q	001-38274	10.1	8/5/2021	
10.21†	Form of Restricted Stock Unit Award Agreement under the Funko, Inc. 2019 Incentive Award Plan.	10-Q	001-38274	10.2	8/5/2021	
10.22†	Form of Director Option Award Agreement under the Funko, Inc. 2019 Incentive Award Plan.	10-Q	001-38274	10.3	8/5/2021	
10.23†	Form of Director Restricted Stock Unit Award Agreement under the Funko, Inc. 2019 Incentive Award Plan.	10-Q	001-38274	10.4	8/5/2021	
21.1	List of Subsidiaries					*

Exhibit Number	Exhibit Description	Incorporated by Reference				Filed/ Furnished Herewith
		Form	File No.	Exhibit	Filing Date	
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	Inline XBRL Instance Document - the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document.					***
101.SCH	Inline XBRL Taxonomy Extension Schema Document.					***
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase Document.					***
101.DEF	Inline XBRL Taxonomy Definition Linkbase Document.					***
101.LAB	Inline XBRL Taxonomy Label Linkbase Document.					***
101.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase Document.					***
104	Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101)					***

* 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) the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

FUNKO, INC.(Registrant)

Date: March 3, 2022 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
/s/ Andrew Perlmutter Andrew Perlmutter	Chief Executive Officer and Director (Principal Executive Officer)	March 3, 2022
/s/ Jennifer Fall Jung Jennifer Fall Jung	Chief Financial Officer (Principal Financial and Accounting Officer)	March 3, 2022
/s/ Brian Mariotti Brian Mariotti	Chief Creative Officer and Director	March 3, 2022
/s/ Charles Denson Charles Denson	Chairman of the Board	March 3, 2022
/s/ Ken Brotman Ken Brotman	Director	March 3, 2022
/s/ Diane Irvine Diane Irvine	Director	March 3, 2022
/s/ Adam Kriger Adam Kriger	Director	March 3, 2022
/s/ Sarah Kirshbaum Levy Sarah Kirshbaum Levy	Director	March 3, 2022
/s/ Michael Lunsford Michael Lunsford	Director	March 3, 2022

EXHIBIT 21.1

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

TokenWave LLC

Funko EU, B.V.

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 No. 333-230964) of Funko, Inc.;

of our report dated March 3, 2022, with respect to the consolidated financial statements and schedule of Funko, Inc. and subsidiaries included in this Annual Report (Form 10-K) of Funko, Inc. for the year ended December 31, 2021.

/s/ Ernst & Young LLP

Seattle, Washington
March 3, 2022

EXHIBIT 31.1

CERTIFICATION

I, Andrew Perlmutter, 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 3, 2022

/s/ Andrew Perlmutter
Andrew Perlmutter
Chief Executive Officer

EXHIBIT 31.2

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 3, 2022

/s/ Jennifer Fall Jung
Jennifer Fall Jung
Chief Financial Officer

EXHIBIT 32.1

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, 2021 (the "Report"), I, Andrew Perlmutter, 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 3, 2022

/s/ Andrew Perlmutter
Andrew Perlmutter
Chief Executive Officer

EXHIBIT 32.2

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, 2021 (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 3, 2022

/s/ Jennifer Fall Jung
Jennifer Fall Jung
Chief Financial Officer