
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark one)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2001

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: 0-28104

JAKKS Pacific, Inc.
(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

95-4527222
(I.R.S. Employer
Identification No.)

22619 Pacific Coast Highway
Malibu, California
(Address of principal executive offices)

90265
(Zip Code)

Registrant's telephone number, including area code: (310) 456-7799

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

The number of shares outstanding of the issuer's common stock is 18,472,176 (as of November 13, 2001).

TABLE OF CONTENTS

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Condensed Consolidated Balance Sheets

Condensed Consolidated Statements of Operations

Condensed Consolidated Statements of Cash Flows

Notes to Condensed Consolidated Financial Statements (Unaudited)

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

PART II. OTHER INFORMATION

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

SIGNATURES

Exhibit 10.1

**JAKKS PACIFIC, INC. AND SUBSIDIARIES
INDEX TO QUARTERLY REPORT ON FORM 10-Q
QUARTER ENDED SEPTEMBER 30, 2001**

ITEMS IN FORM 10-Q

	<u>PAGE</u>
Facing page	
Part I	FINANCIAL INFORMATION
Item 1.	Financial Statements.
	Condensed consolidated balance sheets - December 31, 2000 and September 30, 2001 (unaudited)
	Condensed consolidated statements of operations for the three and nine months ended September 30, 2000 and 2001 (unaudited)
	Condensed consolidated statements of cash flows for the nine months ended September 30, 2000 and 2001 (unaudited)
	Notes to condensed consolidated financial statements (unaudited)
Item 2.	Management's Discussion and Analysis of Financial Condition and Results of Operations.
Item 3.	Quantitative and Qualitative Disclosures About Market Risk.
Part II	OTHER INFORMATION
Item 1.	Legal Proceedings.
Item 2.	Changes in Securities and Use of Proceeds.
Item 3.	Defaults Upon Senior Securities.
Item 4.	Submission of Matters to a Vote of Security Holders.
Item 5.	Other Information.
Item 6.	Exhibits and Reports on Form 8-K.
Signatures	

DISCLOSURE REGARDING FORWARD-LOOKING STATEMENTS

This report includes "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. For example, statements included in this report regarding our financial position, business strategy and other plans and objectives for future operations, and assumptions and predictions about future product demand, supply, manufacturing, costs, marketing and pricing factors are all forward-looking statements. When we use words like "intend," "anticipate," "believe," "estimate," "plan" or "expect," we are making forward-looking statements. We believe that the assumptions and expectations reflected in such forward-looking statements are reasonable, based on information available to us on the date hereof, but we cannot assure you that these assumptions and expectations will prove to have been correct or that we will take any action that we may presently be planning. We are not undertaking to publicly update or revise any forward-looking statement if we obtain new information or upon the occurrence of future events or otherwise.

JAKKS PACIFIC, INC. AND SUBSIDIARIES**Condensed Consolidated Balance Sheets**

	December 31, 2000	September 30, 2001
	(*)	(unaudited)
ASSETS		
Current assets		
Cash and cash equivalents	\$ 29,275,424	\$ 25,759,721
Marketable securities	13,617,912	47,224,713
Accounts receivable, net	47,053,699	84,178,944
Inventory, net	30,534,826	30,030,752
Advanced royalty payments	2,495,027	1,515,050
Prepaid expenses and other current assets	5,655,480	3,998,421
	<hr/>	<hr/>
Total current assets	128,632,368	192,707,601
	<hr/>	<hr/>
Office furniture and equipment	3,779,585	4,561,638
Molds and tooling	23,929,329	26,317,332
Leasehold improvements	1,927,805	1,970,213
	<hr/>	<hr/>
Total	29,636,719	32,849,183
Less accumulated depreciation and amortization	10,653,467	16,821,159
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Property and equipment, net	18,983,252	16,028,024
	<hr/>	<hr/>
Notes receivable-officers	2,450,000	2,224,000
Investment in joint venture	9,758,359	927,434
Goodwill, net	74,590,189	76,993,649
Trademarks, net	12,104,546	11,699,747
Intangibles and deposits, net	2,203,679	2,131,162
	<hr/>	<hr/>
Total assets	\$248,722,393	\$302,711,617
	<hr/>	<hr/>
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Accounts payable and accrued expenses	\$ 33,712,040	\$ 55,102,137
Income taxes payable	7,623,355	13,950,715
Current portion of long term debt	400,000	400,000
	<hr/>	<hr/>
Total current liabilities	41,735,395	69,452,852
	<hr/>	<hr/>
Long term debt, net of current portion	1,000,000	700,000
Deferred income taxes	1,456,817	756,817
	<hr/>	<hr/>
Total liabilities	44,192,212	70,909,669
	<hr/>	<hr/>
Stockholders' equity		
Common stock, \$.001 par value; 25,000,000 shares authorized; 19,485,582 and 19,830,540 shares issued, respectively	19,485	19,831
Additional paid-in capital	156,475,343	159,903,532
Treasury stock, at cost, 1,493,600 and 1,493,600 shares, respectively	(12,911,483)	(12,911,483)
Retained earnings	60,946,836	84,790,068
	<hr/>	<hr/>
Total stockholders' equity	204,530,181	231,801,948
	<hr/>	<hr/>
Total liabilities and stockholders' equity	\$248,722,393	\$302,711,617
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See accompanying notes to condensed consolidated financial statements.

(*) Derived from audited financial statements



JAKKS PACIFIC, INC. AND SUBSIDIARIES**Condensed Consolidated Statements of Operations
For the Three and Nine Months Ended September 30, 2000 and 2001 (Unaudited)**

	Three Months Ended September 30, Nine Months Ended September 30,			
	2000	2001	2000	2001
Net sales	\$ 91,838,086	\$ 92,767,943	\$193,197,882	\$222,871,202
Cost of sales	54,165,752	53,711,569	113,674,062	126,737,725
Gross profit	37,672,334	39,056,374	79,523,820	96,133,477
Selling, general and administrative expenses	26,470,917	24,155,145	57,602,848	63,936,204
Acquisition shut-down and other costs	—	338,766	1,072,375	1,488,786
Income from operations	11,201,417	14,562,463	20,848,597	30,708,487
Profit from joint venture	(1,382,539)	(86,475)	(8,167,676)	(967,230)
Other (income) expense, net	(91,670)	—	(91,670)	—
Interest, net	(939,073)	(600,685)	(3,099,361)	(1,532,127)
Income before provision for income taxes	13,614,699	15,249,623	32,207,304	33,207,844
Provision for income taxes	3,846,152	4,300,392	9,598,563	9,364,612
Net income	\$ 9,768,547	\$ 10,949,231	\$ 22,608,741	\$ 23,843,232
Earnings per share — basic	\$ 0.50	\$ 0.60	\$ 1.17	\$ 1.32
Earnings per share — diluted	\$ 0.48	\$ 0.56	\$ 1.11	\$ 1.24

See accompanying notes to condensed consolidated financial statements.

JAKKS PACIFIC, INC. AND SUBSIDIARIES**Condensed Consolidated Statements of Cash Flows
For the Nine Months Ended September 30, 2000 and 2001 (Unaudited)**

	Nine Months Ended September 30,	
	2000	2001
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$ 22,608,741	\$ 23,843,232
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	5,830,026	8,994,025
Earned compensation from stock option grants	—	1,475,707
Change in operating assets and liabilities		
Accounts receivable	(40,738,534)	(37,125,245)
Preferred return from joint venture	1,396,834	8,830,925
Inventory	(12,936,242)	504,074
Advanced royalty payments	(793,821)	979,977
Prepaid expenses and other current assets	(1,746,213)	1,657,059
Accounts payable and accrued expenses	19,367,170	21,390,097
Income taxes payable	4,632,781	6,327,360
Deferred income taxes	(543,451)	(700,000)
Marketable securities	32,329,655	(33,606,801)
Total adjustments	6,798,205	(21,272,822)
Net cash provided by operating activities	29,406,946	2,570,410
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of Property and equipment	(10,962,538)	(3,212,464)
Other assets	(35,693)	(252,477)
Notes receivable-officers	(2,606,706)	226,000
Cash paid in excess of fair value of business assets acquired (goodwill)	(24,327,997)	(4,500,000)
Net cash used by investing activities	(37,932,934)	(7,738,941)
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from stock options and warrants exercised	1,119,806	1,952,828
Repayment of long term debt	(13,681)	(300,000)
Repurchase of common shares	(3,324,007)	—
Acquired debt	1,500,000	—
Net cash (used) provided by financing activities	(717,882)	1,652,828
Net increase (decrease) in cash and cash equivalents	(9,243,870)	(3,515,703)
Cash and cash equivalents, beginning of period	57,546,406	29,275,424
Cash and cash equivalents, end of period	\$ 48,302,536	\$ 25,759,721
Supplemental disclosure of cash flow information:		
Cash paid during the period for:		
Income taxes	\$ 5,660,289	\$ 2,873,981
Interest	\$ 172,881	\$ 55,663

See accompanying notes to condensed consolidated financial statements.

JAKKS PACIFIC, INC. AND SUBSIDIARIES
Notes to Condensed Consolidated Financial Statements (Unaudited)
September 30, 2001

Note 1 — Basis of presentation

The accompanying 2000 and 2001 unaudited interim condensed consolidated financial statements included herein have been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (the "SEC"). Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations. However, the Company believes that the disclosures are adequate to prevent the information presented from being misleading. These financial statements should be read in conjunction with the financial statements and the notes thereto included in the Company's Form 10-K/A, which contains financial information for the years ended December 31, 1998, 1999 and 2000.

The information provided in this report reflects all adjustments (consisting solely of normal recurring accruals) that are, in the opinion of management, necessary to present fairly the results of operations for this period. The results for this period are not necessarily indicative of the results to be expected for the full year.

Certain reclassifications have been made to the 2000 condensed consolidated financial statements to conform to the current year presentation.

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries.

Basic earnings per share has been computed using the weighted average number of common shares. Diluted earnings per share has been computed using the weighted average number of common shares and common share equivalents (which consist of warrants and options, to the extent they are dilutive).

Note 2 — Business Segments

JAKKS Pacific is a worldwide producer and marketer of children's toys and related products, principally engaged in the design, development, production and marketing of traditional toys, including boys action figures, vehicles and playsets, craft and activity products, compounds, girls toys, and infant and preschool toys.

In North America, which includes the United States and Canada, the North America Toy segment includes the design, development, production and marketing of children's toys and related products. The Company has other segments, which sell most of the Company's products to non-North America markets and collectible toys to the specialty market in the United States. These other segments do not meet the quantitative thresholds for reportable segments and have been combined for reporting purposes.

Segment performance is measured at the operating income level. All sales are made to external customers, and general corporate expenses have been attributed to the North America Toy segment, which is a dominant segment. Segment assets are comprised of accounts receivable and inventories, net of applicable reserves and allowances.

The accounting policies of the segments are the same as those described in Note 2 to the Company's consolidated financial statements for the fiscal year ended December 31, 2000.

Results for the three months and nine months are not necessarily representative of those that may be expected for the full year 2001 nor were those of the comparable 2000 periods representative of those actually experienced for the full year 2000. Similarly, such results are not necessarily those that would be achieved were each segment an unaffiliated business enterprise. Information by segment and a reconciliation to reported amounts for the three months and nine months ended September 30, 2000 and 2001 are as follows:

	THREE MONTHS ENDED SEPTEMBER 30,		NINE MONTHS ENDED SEPTEMBER 30,	
	2000	2001	2000	2001
NET SALES				
North America Toys	\$87,640,065	\$84,178,218	\$179,868,660	\$204,583,958
Other	4,198,021	8,589,725	13,329,222	18,287,244
	<u>\$91,838,086</u>	<u>\$92,767,943</u>	<u>\$193,197,882</u>	<u>\$222,871,202</u>
	THREE MONTHS ENDED SEPTEMBER 30,		NINE MONTHS ENDED SEPTEMBER 30,	
	2000	2001	2000	2001

OPERATING INCOME				
North America Toys	\$10,689,388	\$13,214,071	\$19,410,198	\$28,188,764
Other	512,029	1,348,392	1,438,399	2,519,723
	<u>\$11,201,417</u>	<u>\$14,562,463</u>	<u>\$20,848,597</u>	<u>\$30,708,487</u>

SEPTEMBER 30,

	<u>2000</u>	<u>2001</u>
ASSETS		
North America Toys	\$103,866,154	\$104,838,451
Other	7,697,033	9,371,245
	<u>\$111,563,187</u>	<u>\$114,209,696</u>

Note 3 — Inventories

Inventories, which include the ex-factory cost of goods and in-bound freight, are stated at the lower of cost (first-in, first-out) or market and consist of the following:

	<u>December 31, 2000</u>	<u>September 30, 2001</u>
Deposits and raw materials	\$ 3,676,011	\$ 3,879,926
Finished goods	26,858,815	26,150,826
	<u>\$30,534,826</u>	<u>\$30,030,752</u>

Note 4 — Earnings per share

The following table is a reconciliation of the weighted-average shares used in the computation of basic and diluted earnings per share for the periods presented:

	THREE MONTHS ENDED SEPTEMBER 30,					
	<u>2000</u>			<u>2001</u>		
	<u>INCOME</u>	<u>WEIGHTED AVERAGE SHARES</u>	<u>PER-SHARE</u>	<u>INCOME</u>	<u>WEIGHTED AVERAGE SHARES</u>	<u>PER-SHARE</u>
Earnings per share — basic						
Income available to common stockholders	\$9,768,547	19,389,112	\$0.50	\$10,949,231	18,272,932	\$ 0.60
Effect of dilutive securities						
Options and warrants	—	941,085		—	1,313,536	
Earnings per share — diluted						
Income available to common stockholders plus assumed exercises	<u>\$9,768,547</u>	<u>20,330,197</u>	<u>\$0.48</u>	<u>\$10,949,231</u>	<u>19,586,468</u>	<u>\$ 0.56</u>
	NINE MONTHS ENDED SEPTEMBER 30,					
	<u>2000</u>			<u>2001</u>		
	<u>INCOME</u>	<u>WEIGHTED AVERAGE SHARES</u>	<u>PER-SHARE</u>	<u>INCOME</u>	<u>WEIGHTED AVERAGE SHARES</u>	<u>PER-SHARE</u>
Earnings per share — basic						
Income available to common stockholders	\$22,608,741	19,352,851	\$1.17	\$23,843,232	18,110,329	\$ 1.32
Effect of dilutive securities						

Options and warrants	—	1,008,160		—	1,175,586	
Earnings per share — diluted						
Income available to common stockholders plus assumed exercises	\$22,608,741	20,361,011	\$1.11	\$23,843,232	19,285,915	\$ 1.24

JAKKS PACIFIC, INC. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued) September 30, 2001

Note 5 — Common stock and preferred stock

The Company has 26,000,000 authorized shares of stock consisting of 25,000,000 shares of \$.001 par value common stock and 1,000,000 shares of \$.001 par value preferred stock.

During 2000, the Company purchased 1,493,600 shares of its common stock for a total of \$12,911,483 pursuant to a buy-back program approved by the Board of Directors.

Note 6 — Acquisitions

In October 1999, the Company acquired all of the stock of Flying Colors Toys, Inc. ("Flying Colors") for approximately \$52.9 million. Consideration paid at closing was in cash. Contingent consideration includes an earn-out in an amount of up to \$4.5 million in each of the three 12-month periods following the closing, if gross profits of Flying Colors branded products achieve certain prescribed levels in each such period. The maximum of \$4.5 million for each of the earn-out periods ended September 30, 2000 and 2001 was earned. The paid earn-outs have been recorded as goodwill and is being amortized over the remaining life of the related goodwill, except that \$464,938 of the 2000 earn-out was deemed to be compensation and was expensed in 2000. Flying Colors designs, produces and markets activity kits, compounds and lunch boxes.

In July 2000, the Company acquired all of the outstanding capital stock of Pentech International Inc. ("Pentech") for an aggregate purchase price of approximately \$20.6 million, which was paid in cash on the closing of the transaction. In addition, the Company paid on the closing \$10.0 million to pay down certain indebtedness of Pentech and assumed liabilities of approximately \$26.7 million. Pentech designs, produces and markets writing instruments and craft products.

Note 7 — Notes Receivable From Officers

As of September 30, 2001, there were two notes receivable from officers totaling \$1,974,000 issued at interest rates of 6.5% each, with interest payable on each April 28 and October 28 of each year, and principal payable at maturity on April 28, 2003. Additionally, there is a third note receivable from an officer for \$250,000 issued at an interest rate of 7.0%, with interest and principal payable at maturity on May 12, 2002.

Note 8 — Litigation

In March 2001, Rose Art Industries, Inc. and Licensing International, Ltd. commenced an action against the Company in the United States District Court for the District of New Jersey in which they allege the Company's willful infringement of a patent owned by Licensing International and licensed to Rose Art through the Company's production and sale of Zyrofoam modeling compound. The plaintiffs seek injunctive relief, monetary damages in an unspecified amount, together with interest thereon, and reasonable attorneys' fees. The Company believes that their claims are without merit and intends vigorously to defend against their action. At this early state in these proceedings, the Company is unable to predict the likely outcome of the action or its impact on its business, financial condition or results of operations. The Company is a party to, and certain property is the subject of, various pending claims and legal proceedings that routinely arise in the ordinary course of business, but the Company does not believe that any of these claims or proceedings will have a material effect on its business, financial condition or results of operations.

Note 9 — Recent Accounting Pronouncements

In July 2001, the FASB issued Statement of Financial Accounting Standards No. 141, "Business Combinations" (SFAS 141) and Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" (SFAS 142). SFAS 141 is effective for business combinations initiated after June 30, 2001. SFAS 141 requires that all business combinations completed after its adoption be accounted for under the purchase method of accounting and establishes specific criteria for the recognition of intangible assets separately from goodwill. SFAS 142 will be effective for the Company on January 1, 2002 and primarily addresses the accounting for goodwill and intangible assets subsequent to their acquisition. Upon adoption of SFAS 142, goodwill and other intangible assets will no longer be amortized and will be tested for impairment at least annually at the reporting unit level.

Based on current levels of amortization expense, the Company estimates that the elimination of amortization expense will positively impact net income by approximately \$2.1 million, or approximately \$0.11 per common share (diluted), on an annual basis.



JAKKS PACIFIC, INC. AND SUBSIDIARIES

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis of financial condition and results of operations should be read together with the Company's Condensed Consolidated Financial Statements and Notes thereto which appear elsewhere herein.

OVERVIEW

JAKKS was founded to design, develop, produce and market children's toys and related products. We commenced business operations in 1995 when we assumed operating control over the toy business of Justin Products, which consisted primarily of fashion dolls and accessories and electronic products for children.

One of our key strategies has been to grow through the acquisition or licensing of product lines, concepts and characters. In 1996, we expanded our product lines to include products based on licensed characters and properties, such as World Wrestling Federation action figures and accessories.

We acquired Road Champs in February 1997, and have included the results of operations of Road Champs from February 1, 1997, the effective date of the acquisition. We acquired the Child Guidance and Remco trademarks in October 1997, both of which contributed to operations nominally in 1997, but contributed more significantly to operations commencing in 1998. In June 1999, we acquired Berk with its lines of educational toy foam puzzle mats and activity sets. Berk began to contribute modestly beginning in the third quarter of 1999. In October 1999, we acquired Flying Colors, whose product lines include licensed activity kits, compound playsets and lunch boxes as well as other related products. Flying Colors product lines contributed to operations beginning in the fourth quarter of 1999. In July 2000, we acquired Pentech whose product lines include writing instruments and craft products. Pentech product lines contributed to operations beginning in August 2000.

Our products currently include (1) action figures and accessories featuring licensed characters, principally from the World Wrestling Federation license, (2) Flying Colors molded plastic activity sets, clay compound playsets and lunch boxes, (3) Wheels division products, including Road Champs die-cast collectible and toy vehicles and Remco toy vehicles and role-play toys and accessories, (4) Child Guidance infant and pre-school electronic toys, educational toy foam puzzle mats and blocks and activity sets, (5) Pentech writing instruments and craft products, and (6) fashion dolls and related accessories.

In general, we acquire products or product concepts from others or we engage unaffiliated third parties to develop our own products, thus minimizing operating costs. Royalties payable to our developers generally range from 1% to 6% of the wholesale price for each unit of a product sold by us. We expect that outside inventors will continue to be a source of new products in the future. We also generate internally new product concepts, for which we pay no royalties.

[Table of Contents](#)

In June 1998, we formed a joint venture with THQ, a developer, publisher and distributor of interactive entertainment software, and the joint venture licensed the rights from World Wrestling Federation Entertainment to publish World Wrestling Federation electronic video game software on all platforms. The first games produced under this license were released in November 1999. We are entitled to receive a guaranteed preferred return based on the sales of the video games, and THQ is entitled to receive the balance of the profits generated by the joint venture. The minimum preferred return to be distributed to us by the joint venture during the remaining term of the license agreement ending December 31, 2009 is \$2.6 million per year. We expect our aggregate return over this period to be significantly in excess of this amount, although we cannot predict with certainty that expected levels of return will be achieved and, in any case, we anticipate substantial fluctuations in the amount of the preferred return distributed to us from year to year.

We contract the manufacture of most of our products to unaffiliated manufacturers located in China. We sell a substantial portion of the finished products on a letter of credit basis or on open account to our customers, who take title to the goods in Hong Kong. These methods allow us to reduce certain operating costs and working capital requirements. A portion of our sales, primarily sales of our Road Champs, Flying Colors and Pentech products, originate in the United States, so we hold certain inventory in our warehouse and fulfillment facility. In addition, we hold inventory of other products from time to time in support of promotions or other domestic programs with retailers. Prior to 2001, our inventory was maintained in warehouses owned and operated by unaffiliated third-parties that also oversaw the shipment of products to our customers. To date, substantially all of our sales have been to domestic customers, although we have made efforts to expand distribution of our products into foreign territories, including (1) engaging representatives to oversee sales in certain territories, (2) engaging distributors in certain territories, and (3) establishing direct relationships with retailers in certain territories.

We establish reserves for sales allowances, including promotional allowances and allowances for anticipated defective product returns at the time of shipment. The reserves are determined as a percentage of net sales based upon either historical experience or on estimates or programs agreed upon by our customers.

Our cost of sales consists primarily of the cost of goods produced for us by unaffiliated third-party manufacturers, royalties earned by licensors on the sale of these goods and amortization of the tools, dies and molds owned by us that are used in the manufacturing process. Other costs include inbound freight and provisions for obsolescence. Significant factors affecting our cost of sales as a percentage of net sales include (1) the proportion of net sales generated by various products with disparate gross margins, (2) the proportion of net sales made domestically, which typically carry lower gross margins than sales made in Hong Kong, and (3) the effect of amortizing the fixed cost components of cost of sales, primarily amortization of tools, dies and molds, over varying levels of net sales.

Selling, general and administrative expenses include costs directly associated with the selling process, such as sales commissions, advertising and travel expenses, as well as general corporate expenses, goodwill and trademark amortization and product development. We have recorded goodwill of approximately \$82.7 million and trademarks of approximately \$13.9 million in connection with acquisitions made to date. Goodwill is being amortized over a 30-year period, while trademark acquisition costs are being amortized over periods ranging from 5 to 30 years.

RESULTS OF OPERATIONS

The following unaudited table sets forth, for the periods indicated, certain statement of operations data as a percentage of net sales.

	THREE MONTHS ENDED SEPTEMBER 30,		NINE MONTHS ENDED SEPTEMBER 30,	
	2000	2001	2000	2001
Net sales	100.0%	100.0%	100.0%	100.0%
Cost of sales	59.0	57.9	58.8	56.9
Gross profit	41.0	42.1	41.2	43.1
Selling, general and administrative expenses	28.8	26.0	29.9	28.6
Acquisition shut-down costs	—	0.4	0.5	0.7
Income from operations	12.2	15.7	10.8	13.8
Profit from joint venture	(1.5)	(0.1)	(4.2)	(0.4)
Other (income) expense	(0.1)	—	—	—
Interest, net	(1.0)	(0.6)	(1.6)	(0.7)
Income before provision for income taxes	14.8	16.4	16.6	14.9
Provision for income taxes	4.2	4.6	5.0	4.2
Net income	10.6%	11.8%	11.6%	10.7%

THREE MONTHS ENDED SEPTEMBER 30, 2001 AND 2000

Net Sales. Net sales increased \$1.0 million to \$92.8 million in 2001 from \$91.8 million in 2000. The growth in net sales was due primarily to the continuing growth in sales of our Flying Colors products and an increase in sales of our World Wrestling Federation wrestling products, as well as the addition of Pentech products, which began contributing to operations in August 2000, and the introduction of our products based on the Battlebots television show offset by a decrease in sales of our Wheels products, consisting primarily of our Road Champs die-cast toy and collectible vehicles including BXS die-cast bicycles, MXS die-cast motorcycles and other extreme sports products.

Gross Profit. Gross profit increased \$1.4 million to \$39.1 million, or 42.1% of net sales, in 2001 from \$37.7 million, or 41.0% of net sales, in 2000. The overall increase in gross profit was attributable to the increase in net sales and the increase in the gross profit margin. The increase in gross profit margin of 1.1% of net sales is primarily attributable to the decrease in royalty expense as a percentage of net sales due to changes in the product mix and lower product costs, which was partially offset by an increase in amortization expense relating to molds and tools used in the manufacture of our products.

Selling, General and Administrative Expenses. Selling, general and administrative expenses were \$24.2 million in 2001 and \$26.5 million in 2000, constituting 26.0% and 28.8% of net sales, respectively. The overall decrease of \$2.3 million in such costs was due to cost efficiencies and reduction of fixed operating expenses following the integration of Pentech's operations into our own operations as well as lower advertising rates. We produced and aired television commercials in support of several of our products, including World Wrestling Federation action figures, Road Champs extreme sports products and Flying Colors products in 2000 and 2001. From time to time, we may increase our advertising efforts, if we deem it appropriate for particular products.

Acquisition Shut-down and Other Costs. Acquisition shut-down and other costs in 2001 relate to shut-down costs, including lease termination, relocation expenses, and consulting fees and expenses of certain operations of Pentech, acquired in 2000. Total costs for 2001 is comprised of \$0.2 million relating to lease terminations and abandonments and \$0.1 million relating to relocation expenses and consulting fees and expenses incurred to facilitate the integration. There were no such costs in 2000. The integration of Pentech was substantially completed in the second quarter of 2001 and related costs are expected to be nominal in future quarters.

[Table of Contents](#)

Profit from Joint Venture. Beginning in the fourth quarter of 1999, we began to earn our preferred return on the sale of World Wrestling Federation video games by our joint venture with THQ. In 2001, the joint venture had sales of only one new GameBoy Color title with lower unit sales and sales price than the other gaming platforms and older carryover titles that generate lower unit sales than more recent carryover titles. However, in 2000, the joint venture had one new Sega Dreamcast title, with higher unit sales and higher sales price than the GameBoy Color title, and more recent carryover titles.

Interest, Net. Interest income decreased in 2001 due to lower average cash balances during 2001 than in 2000 as a result of significant disbursements made in the third and fourth quarters of 2000 related to the acquisition of Pentech and the repurchase by the Company of its common stock as well as lower interest rates in 2001. Interest expense was nominal in 2000 and 2001.

Provision for Income Taxes. Provision for income taxes included Federal, state and foreign income taxes in 2000 and 2001, at effective tax rates of 28.3% in 2000 and 28.2% in 2001, benefiting from a flat 16.5% Hong Kong Corporation Tax on our income arising in, or derived from, Hong Kong.

NINE MONTHS ENDED SEPTEMBER 30, 2001 AND 2000

Net Sales. Net sales increased \$29.7 million, or 15.4%, to \$222.9 million in 2001 from \$193.2 million in 2000. The growth in net sales was due primarily to the continuing growth in sales of our Flying Colors products and an increase in sales of our World Wrestling Federation wrestling products, as well as the addition of Pentech products, which began contributing to operations in August 2000, and the introduction of our products based on the Battlebots television show offset by a decrease in sales of our Doll products and our Wheels products, consisting primarily of our Road Champs die-cast toy and collectible vehicles including BXS die-cast bicycles, MXS die-cast motorcycles and other extreme sports products.

Gross Profit. Gross profit increased \$16.6 million, or 20.9%, to \$96.1 million, or 43.1% of net sales, in 2001 from \$79.5 million, or 41.2% of net sales, in 2000. The overall increase in gross profit was attributable to the increase in net sales and the increase in the gross profit margin. The increase in gross profit margin of 1.9% of net sales is primarily attributable to the decrease in royalty expense as a percentage of net sales due to changes in the product mix and lower product costs, though partially offset by an increase in amortization expense relating to molds and tools used in the manufacture of our products.

Selling, General and Administrative Expenses. Selling, general and administrative expenses were \$63.9 million in 2001 and \$57.6 million in 2000, constituting 28.6% and 29.9% of net sales, respectively. The overall increase of \$6.3 million in such costs was due to costs incurred in support of the Company's development, marketing and distribution of products under its recently acquired Pentech brand and the increase in net sales with its proportionate impact on variable selling costs such as freight and shipping related expenses, sales commissions, cooperative advertising and travel expenses, among others. The decrease as a percentage of net sales is primarily attributable to the fixed nature of certain of these expenses with a concurrent increase in net sales. We produced and aired television commercials in support of several of our products, including World Wrestling Federation action figures, Road Champs extreme sports products and Flying Colors products in 2000 and 2001. From time to time, we may increase our advertising efforts, if we deem it appropriate for particular products.

Acquisition Shut-down and Other Costs. Acquisition shut-down and other costs in 2001 relate to shut-down costs, including lease termination, relocation and consulting fees and expenses, of certain operations of Pentech, acquired in 2000, and such costs in 2000 relate to shut-down costs, including lease termination, relocation, and consulting fees and expenses of certain operations of Flying Colors, acquired in 1999. Operations impacted by both shut-downs were sales, design, distribution, and administration. Total Pentech costs is comprised of \$0.3 million relating to lease terminations and abandonments, \$0.2 million in consulting fees and expenses incurred to facilitate the integration, \$0.4 million relating to relocation expense, and \$0.1 million relating to the abandonments of other assets. Twenty-one Pentech employees received severance totaling \$0.4 million, that was accrued in the fourth quarter of 2000 and was fully paid out by June 30, 2001. The integration of Pentech was substantially completed in the second quarter of 2001 and related costs are expected to be nominal in future quarters. In 2000, total Flying Colors costs is comprised of \$0.2 million relating to lease terminations and abandonments and \$0.3 million relating to relocation expense. The integration of Flying Colors was completed in 2000. Additionally, 2000 includes \$0.6 million relating to the recall of one of our products.

Profit from Joint Venture. The joint venture had sales of only one new GameBoy Color title with lower unit sales and sales price than the other gaming platforms and carryover titles in 2001 compared to releasing new Sony Play Station and Sega Dreamcast titles, which had higher unit sales and sales price than GameBoy Color, in addition to having sales of carryover titles in 2000. The minimum annual preferred return guarantee of \$2.6 million is expected to be earned in 2001.

Interest, Net. Interest income decreased in 2001 due to lower average cash balances during 2001 than in 2000 as a result of significant disbursements made in the third and fourth quarters of 2000 related to the acquisition of Pentech and the repurchase by the Company of its common stock. Interest expense was nominal in 2000 and 2001.

Provision for Income Taxes. Provision for income taxes included Federal, state and foreign income taxes in 2000 and 2001, at effective tax rates of 29.8% in 2000 and 28.2% in 2001, benefiting from a flat 16.5% Hong Kong Corporation Tax on our income arising in, or derived from, Hong Kong. As of September 30, 2001, we had deferred tax assets of approximately \$0.4 million for which no allowance has been provided since, in the opinion of management, realization of the future benefit is probable. In making

this determination, management considered all available evidence, both positive and negative, as well as the weight and importance given to such evidence.

SEASONALITY

The retail toy industry is inherently seasonal. Generally, in the past, the Company's sales have been highest during the third and fourth quarters, and collections for those sales have been highest during the succeeding fourth and first fiscal quarters. The writing instrument industry is likewise seasonal with sales highest during the back to school season which occurs in the second and third quarters. The Company's working capital needs have been highest during the third and fourth quarters.

LIQUIDITY AND CAPITAL RESOURCES

As of September 30, 2001, we had working capital of \$123.3 million, as compared to \$86.9 million as of December 31, 2000. This increase was primarily attributable to our operating results and the receipt of the preferred return from our joint venture with THQ.

Operating activities provided net cash of \$2.6 million, including \$33.6 million used for the purchase of marketable securities in 2001, as compared to \$29.4 million in 2000, including \$32.3 million provided from the sale of marketable securities. Net cash was provided primarily by net income, non-cash charges, such as depreciation and amortization and earned compensation from stock option grants, as well as a decrease in preferred return from the joint venture with THQ, inventory, advanced royalty payments, prepaid expenses and other current operating assets, and an increase in accounts payable and accrued expenses, income taxes payable, which were offset by an increase in accounts receivable, a decrease in deferred income taxes, as well as the purchase of marketable securities. As of September 30, 2001, we had cash and cash equivalents of \$25.8 million and marketable securities of \$47.2 million.

Our investing activities used net cash of \$7.7 million in 2001, as compared to \$37.9 million in 2000, consisting primarily of the purchase of molds and tooling used in the manufacture of our products and office furniture and equipment, plus \$24.3 million in goodwill relating to the acquisition of Pentech, the 2000 earn-out for Flying Colors and the notes receivable from officers of \$2.6 million in 2000 and \$4.5 million in goodwill relating to the 2001 earn-out for Flying Colors in 2001. As part of our strategy to develop and market new products, we have entered into various character and product licenses with royalties ranging from 1% to 12% payable on net sales of such products. As of September 30, 2001, these agreements required future aggregate minimum guarantees of \$12.3 million, exclusive of \$1.5 million in advances already paid.

Our financing activities provided net cash of \$1.7 million in 2001, consisting primarily of proceeds from the exercise of options and warrants partially offset by the repayment of long term debt. In 2000, financing activities used net cash of \$0.7 million, consisting primarily of the repurchase of common shares totaling \$3.3 million, which was offset by the assumption of \$1.5 million of debt in conjunction with the acquisition of Pentech and \$1.1 million of proceeds from the exercise of options and warrants.

In October 1999, we acquired Flying Colors Toys. We paid approximately \$34.7 million for the stock and paid off approximately \$17.6 million of indebtedness. We also agreed to pay an earn-out of up to \$4.5 million in each of the three 12-month periods following the closing if gross profit of Flying Colors products achieves certain targeted levels during each such period. The maximum of \$4.5 million was earned in each of the earn-out periods ended September 30, 2000 and 2001. Flying Colors' principal products include molded plastic activity kits, compounds and lunch boxes featuring licensed characters, including Rugrats, Blue's Clues and Looney Tunes characters. The kits cover a broad range of products and activities, such as make and paint your own characters, jewelry making, art studios, posters, puzzles and other projects.

In July 2000, the Company acquired all of the outstanding capital stock of Pentech for an aggregate purchase price of approximately \$20.6 million, which was paid in cash on the closing of the transaction. In addition, the Company paid on the closing \$10.0 million to pay down certain indebtedness of Pentech and assumed liabilities of approximately \$26.7 million. In December 1999, Pentech renewed a three-year \$25,000,000 Revolving Credit Agreement with Bank America Business Credit, Inc. now known as Bank of America, N.A. (the "Credit Agreement"). Borrowings under the Credit Agreement are subject to limitations based upon eligible inventory and accounts receivable as defined in the Credit Agreement. Amounts borrowed under the Credit Agreement accrue interest, at Pentech's option, at either prime plus 0.5% or LIBOR plus 2.5%. As we have reallocated Pentech's assets in the course of integrating its operations into our own, we depleted the borrowing base which would support borrowings under the Credit Agreement and, accordingly, we do not expect to be able to draw down any funds under the Credit Agreement. As of September 30, 2001, we do not have any outstanding balances on this facility. Pentech designs, produces and markets writing instruments and craft products.

We believe that our cash flow from operations, cash and cash equivalents on hand and marketable securities will be sufficient to meet our working capital and capital expenditure requirements and provide us with adequate liquidity to meet our anticipated operating needs for at least the next 12 months. Although operating activities are expected to provide cash, to the extent we grow significantly in the future, our operating and investing activities may use cash and, consequently, this growth may require us to obtain additional sources of financing. There can be no assurance that any necessary additional financing will be available to us on commercially reasonable terms, if at all.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk represents the risk of loss that may impact our financial position, results of operations or cash flows due to adverse changes in financial and commodity market prices and rates. We are exposed to market risk in the areas of changes in United States and international borrowing rates and changes in foreign currency exchange rates. In addition, we are exposed to market risk in certain geographic areas that have experienced or remain vulnerable to an economic downturn, such as China. We purchase substantially all of our inventory from companies in China, and, therefore, we are subject to the risk that such suppliers will be unable to provide inventory at competitive prices. While we believe that, if such an event were to occur we would be able to find alternative sources of inventory at competitive prices, we cannot assure you that we would be able to do so. These exposures are directly related to our normal operating and funding activities. Historically and as of September 30, 2001, we have not used derivative instruments or engaged in hedging activities to minimize our market risk.

INTEREST RATE RISK

As of September 30, 2001, we do not have any outstanding balances on our credit facility, nor will we be able to draw on the facility prior to its termination or expiration, and we have only nominal interest-bearing obligations. Accordingly, we are not generally subject to any direct risk of loss arising from changes in interest rates.

FOREIGN CURRENCY RISK

We have wholly-owned subsidiaries in Hong Kong. Sales from these operations are denominated in U.S. dollars. However, purchases of inventory and operating expenses are typically denominated in Hong Kong dollars, thereby creating exposure to changes in exchange rates. Changes in the Hong Kong dollar/U.S. dollar exchange rate may positively or negatively affect our gross margins, operating income and retained earnings. The exchange rate of the Hong Kong dollar to the U.S. dollar has been fixed by the Hong Kong government since 1983 at HK\$7.80 to US\$1.00 and, accordingly, has not represented a currency exchange risk to the U.S. dollar. We do not believe that near-term changes in exchange rates, if any, will result in a material effect on our future earnings, fair values or cash flows, and therefore, we have chosen not to enter into foreign currency hedging transactions. We cannot assure you that this approach will be successful, especially in the event of a significant and sudden change in the value of the Hong Kong dollar.

PART II. OTHER INFORMATION**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

We held our most recent Annual Meeting of Stockholders on July 12, 2001. At the meeting, our stockholders considered and voted on several matters, as follows:

1. All six of our incumbent directors were nominated by management for reelection to the Board. Our stockholders voted in connection with the election of directors as follows:

Nominee	For	Against	Withheld
Jack Friedman	13,879,563	0	1,984,304
Stephen G. Berman	14,003,313	0	1,860,554
David C. Blatte	15,655,847	0	208,020
Robert E. Glick	15,654,824	0	209,043
Michael G. Miller	15,655,651	0	208,216
Murray L. Skala	15,351,488	0	512,379

A plurality of the shares represented at the meeting having been voted for each of these nominees, each of them was elected as a director.

2. Our stockholders ratified the appointment of Pannell Kerr Forster, Certified Public Accountants, A Professional Corporation, as our independent auditors for our current fiscal year by a majority vote as follows:

For	Against	Abstain	Broker Non-Votes
15,635,253	186,682	41,932	0

3. Our stockholders ratified and approved the 2001 Amendment to our Third Amended and Restated 1995 Stock Option Plan by a majority vote as follows:

For	Against	Abstain	Broker Non-Votes
12,961,488	2,838,648	63,731	0

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K*(a) Exhibits*

NUMBER	DESCRIPTION
3.1	Restated Certificate of Incorporation of the Company(1)
3.1.1	Certificate of Designation and Preferences of Series A Cumulative Convertible Preferred Stock of the Company(2)
3.1.2	Certificate of Elimination of All Shares of 4% Redeemable Convertible Preferred Stock of the Company(2)
3.1.3	Certificate of Amendment of Restated Certificate of Incorporation of the Company(3)
3.2.1	By-Laws of the Company(1)
3.2.2	Amendment to By-Laws of the Company(4)
10.1	Amended and Restated Employment Agreement between the Company and Michael Bianco dated July 12, 2001(5)(*)

- (1) Filed previously as an exhibit to the Company's Registration Statement on Form SB-2 (Reg. No. 333-2048-LA), effective May 1, 1996, and incorporated herein by reference.
- (2) Filed previously as an exhibit to the Company's Current Report on Form 8-K, filed April 7, 1998, and incorporated herein by reference.
- (3) Filed previously as exhibit 4.1.2 of the Company's Registration Statement on Form S-3 (Reg. No. 333-74717), filed on March 9, 1999, and incorporated herein by reference.
- (4) Filed previously as an exhibit to the Company's Registration Statement on Form SB-2 (Reg. No. 333-22583), effective May 1, 1997, and incorporated herein by reference.
- (5) Filed herewith.
- (*) Management contract or compensatory plan, contract or arrangement.

(b) Reports on Form 8-K

We did not file a current report on Form 8-K in our fiscal quarter ended September 30, 2001.

SIGNATURES

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

Registrant:

JAKKS PACIFIC, INC.

Date: November 14, 2001

By: /s/ Joel M. Bennett

Executive Vice President and Chief Financial Officer
(Principal Financial Officer)

Exhibit Index

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AMENDED AND RESTATED EMPLOYMENT AGREEMENT

AMENDED AND RESTATED EMPLOYMENT AGREEMENT dated as of July 12, 2001 by and between JAKKS Pacific, Inc., a Delaware corporation (the "Company"), and Michael Bianco ("Executive")

W I T N E S S E T H :
- - - - -

WHEREAS, since October 1, 1999, Executive has served as Senior Vice President - Sales and Development of the Company's Flying Colors division pursuant to this Employment Agreement as hereinbefore in effect; and

WHEREAS, the Company and Executive desire to amend and restate this Employment Agreement to provide for Executive's continued employment by the Company on the terms and subject to the conditions hereinafter set forth;

NOW, THEREFORE, in consideration of the premises and the mutual covenants hereinafter set forth, the Company and Executive agree as follows:

1. Offices and Duties. The Company hereby employs Executive during the Term (as hereinafter defined) to serve as an Executive Vice President of the Company and, as such, to perform such executive and supervisory duties on behalf of the Company as the Company's Board of Directors, chief executive officer or chief operating officer may from time to time reasonably direct. The Company's Board of Directors may elect or designate Executive to serve in such other corporate offices of the Company or a subsidiary thereof as they may from time to time deem necessary, proper or advisable. Executive hereby accepts such employment and agrees that throughout the Term he shall faithfully, diligently and to the best of his ability, in furtherance of the business of the Company, perform the duties assigned to him or incidental to the offices assumed by him pursuant to this Section. Executive shall devote substantially all of

his business time and attention to the business and affairs of the Company, but Executive shall not be required to devote any minimum amount of time or report or perform his duties hereunder on a fixed or periodic basis, and, subject to Sections 9, 10 and 11, Executive may engage or participate in such other activities incidental to any other employment, occupation or business venture or enterprise as do not materially interfere with or compromise his ability to perform his duties hereunder. Executive shall at all times be subject to the direction and control of the Company's Board of Directors, chief executive officer and chief operating officer and observe and comply with such rules, regulations, policies and practices as they may from time to time establish.

2. Term. The employment of Executive hereunder shall commence on the date hereof and continue for a term ending on December 31, 2007, subject to earlier termination upon the terms and conditions provided elsewhere herein (the "Term"). As used herein, "Termination Date" means the last day of the Term.

3. Compensation.

(a) As compensation for his services hereunder, the Company shall pay to Executive during the Term:

(i) a base salary in 2001 at the rate of \$550,000 per annum, and, in each subsequent year during the Term, at a rate to be determined by the Company's Board of Directors that is at least \$25,000 more than the rate in the immediately preceding year (the "Base Salary"), such Base Salary to be paid in substantially equal installments no less often than twice monthly;

(ii) a bonus for each year beginning in 2003, determined in accordance with Annex I (the "Bonus"); and

(iii) such additional incentive or bonus compensation as the Company's Board of Directors may from time to time determine.

(b) In addition to his Base Salary and other compensation provided herein, Executive shall be entitled to participate, to the extent he is eligible under the terms and conditions thereof, in any stock, stock option or other equity participation plan and any profit-sharing, pension, retirement, insurance, medical service or other employee benefit plan generally available to the executive officers of the Company, and to receive any other benefits or perquisites generally available to the executive officers of the Company pursuant to any employment policy or practice, which may be in effect from time to time during the Term. Except as otherwise expressly provided herein, the Company shall be under no obligation hereunder to institute or to continue any such employee benefit plan or employment policy or practice.

(c) During the Term, Executive shall not be entitled to additional compensation for serving as a director or corporate officer (other than Executive Vice President) of the Company (or any subsidiary thereof) to which he is elected or appointed. Throughout any period or periods during which he shall serve as a director of the Company (or such subsidiary), Executive shall be entitled to directors' fees in accordance with the policies and practices of the Company (or such subsidiary) then in effect.

4. Expense Allowance. The Company shall pay directly, or advance funds to Executive or reimburse Executive for, all expenses reasonably incurred by him in connection with the performance of his duties hereunder and the business of the Company, upon the submission to the Company of itemized expense reports, receipts or vouchers in accordance with its then customary policies and practices.

5. Location. Except for routine travel and temporary accommodation reasonably required to perform his services hereunder, Executive shall not be required to perform his

services hereunder at any location other than the Company's principal executive office, which office shall be located throughout the Term at its location on the date hereof, or, if relocated, at a location within a distance of 30 miles from its location on the date hereof, or at such other office or site to which Executive may, in his sole discretion, consent; nor shall he be required to relocate his principal residence to, or otherwise to reside at, any location specified by the Company.

6. Office. The Company shall provide Executive with suitable office space, furnishings and equipment, secretarial and clerical services and such other facilities and office support as are reasonably necessary for the performance of his services hereunder.

7. Vacation. Executive shall be entitled to four weeks paid vacation during each year of his employment hereunder, such vacation to be taken at such time or times as shall be agreed upon by Executive and the Company. Vacation time shall be cumulative from year to year, except that Executive shall not be entitled to take more than six weeks vacation during any consecutive 12-month period during the Term.

8. Key-Man Insurance. The Company shall have the right from time to time to purchase, increase, modify or terminate insurance policies on the life of Executive for the benefit of the Company in such amounts as the Company may determine in its sole discretion. In connection therewith, Executive shall, at such times and at such places as the Company may reasonably direct, submit himself to such physical examinations and execute and deliver such documents as the Company may deem necessary or appropriate.

9. Trade Secrets. Executive shall hold in a fiduciary capacity for the benefit of the Company all confidential or proprietary information relating to or concerned with its operations, business and affairs, and he shall not, at any time hereafter, use or disclose any such information to any Person other than the Company or its designees or except as may otherwise be required in connection with the business and affairs of the Company.

10. Intellectual Property. Subject to Sections 2870 and 2871 of the California Labor Code:

(a) Any invention, design, process, system, procedure, improvement, development or discovery conceived, developed, created or made by Executive, alone or with others, during the Term and applicable to the business of the Company, whether or not patentable or registrable, shall become the sole and exclusive property of the Company.

(b) Executive shall disclose the same promptly and completely to the Company and shall, during the Term or thereafter, (i) execute all documents requested by the Company for vesting in the Company the entire right, title and interest in and to the same, (ii) execute all documents requested by the Company for filing and procuring such applications for patents, trademarks, service marks or copyrights as the Company, in its sole discretion, may desire to prosecute, and (iii) give the Company all assistance it may reasonably require, including the giving of testimony in any Proceeding (as hereinafter defined), in order to obtain, maintain and protect the Company's right therein and thereto.

11. No Competition.

(a) During the Term, and unless his employment terminates pursuant to Section 14 or by action of the Company other than pursuant to Section 13, for a further period of one year thereafter, Executive shall not, directly or indirectly:

(i) own, control, manage, operate, participate or invest in, or otherwise be connected with, in any manner, any business activity, venture or enterprise which is engaged in any business in which the Company (or any subsidiary thereof) is engaged on the Termination Date; provided, however, that Executive may invest his funds in securities of an issuer engaged in such business if the securities of such issuer are listed for trading on a registered securities

exchange or actively traded in an over-the-counter market and Executive's holdings therein represent less than 1% of the total number of shares or principal amount of the securities of such issuer outstanding; or

(ii) for himself or on behalf of any other Person, employ or engage any Person who at the time shall have been within the preceding 12-month period an employee of the Company (or any subsidiary thereof) or contact any supplier, customer or employee of the Company (or such subsidiary) for the purpose of soliciting or diverting any supplier, customer or employee from the Company (or such subsidiary).

(b) Executive acknowledges that the provisions of this Section, and the period of time, geographic area and scope and type of restrictions on his activities set forth herein, are reasonable and necessary for the protection of the Company.

12. Termination Upon Death or Disability. Executive's employment hereunder shall terminate immediately upon his death. In the event that Executive is unable to perform his duties hereunder by reason of any disability or incapacity (due to any physical or mental injury, illness or defect) for an aggregate of 90 days in any consecutive 12-month period, the Company shall have the right to terminate Executive's employment hereunder within 60 days after the 90th day of his disability or incapacity by giving Executive notice to such effect at least 30 days prior to the date of termination set forth in such notice, and on such date such employment shall terminate.

13. Termination for Cause.

(a) In addition to any other rights or remedies provided by law or in this Agreement, the Company may terminate Executive's employment under this Agreement if:

(i) Executive is convicted of, or enters a plea of guilty or nolo contendere (which plea is not withdrawn prior to its approval by the court) to, a felony offense and either Executive fails to perfect an appeal of such conviction prior to the expiration of the maximum period of time within which, under applicable law or rules of court, such appeal may be perfected or, if Executive does perfect such an appeal, his conviction of a felony offense is sustained on appeal; or

(ii) the Company's Board of Directors determines, after due inquiry, that Executive has:

(A) committed fraud against, or embezzled or misappropriated funds or other assets of, the Company (or any subsidiary thereof);

(B) violated, or caused the Company (or any subsidiary thereof) or any officer, employee or other agent thereof, or any other Person to violate, any material law, regulation or ordinance, which violation has or would reasonably be expected to have a significant detrimental effect on the Company, or any material rule, regulation, policy or practice established by the Company's Board of Directors, chief executive officer or chief operating officer;

(C) willfully, or because of gross or persistent negligence, (A) failed properly to perform his duties hereunder or (B) acted in a manner detrimental to, or adverse to the interests of, the Company; or

(D) violated, or failed to perform or satisfy any material covenant, condition or obligation required to be performed or satisfied by Executive hereunder.

(b) The Company may effect such termination for cause by giving Executive notice to such effect, setting forth in reasonable detail the factual basis for such termination, at least 20 days prior to the date of termination set forth therein; provided however that Executive may avoid such termination if Executive, prior to the date of termination set forth in such notice, cures or explains to the reasonable satisfaction of the Company's Board of Directors the factual basis for termination set forth therein.

(c) In making any determination pursuant to Section 13(a) as to the occurrence of any act or event described in clauses (A) to (D) of paragraph (ii) thereof (each, a "For Cause Event"), each of the following shall constitute convincing evidence of such occurrence:

(i) if Executive is made a party to, or target of, any Proceeding arising under or relating to any For Cause Event, Executive's failure to defend against such Proceeding or to answer any complaint filed against him therein, or to deny any claim, charge, averment or allegation thereof asserting or based upon the occurrence of a For Cause Event;

(ii) any judgment, award, order, decree or other adjudication or ruling in any such Proceeding finding or based upon the occurrence of a For Cause Event (that is not reversed or vacated on appeal); or

(iii) any settlement or compromise of, or consent decree issued in, any such Proceeding in which Executive expressly admits the occurrence of a For Cause Event;

provided that none of the foregoing shall be dispositive or create an irrebuttable presumption of the occurrence of such For Cause Event; and provided further that the Company's Board of Directors may rely on any other factor or event as convincing evidence of the occurrence of a For Cause Event.

14. Termination by Executive for Good Reason or Upon a Change of Control. In addition to any other rights or remedies provided by law or in this Agreement, Executive may terminate his employment hereunder if:

(a) (i) the Company violates, or fails to perform or satisfy any material covenant, condition or obligation required to be performed or satisfied by it hereunder or (ii) as a result of any action or failure to act by the Company, there is a material adverse change in the nature or scope of the duties, obligations, rights or powers of Executive's employment, by giving the Company notice to such effect, setting forth in reasonable detail the factual basis for such termination, at least 20 days prior to the date of termination set forth therein; provided however that the Company may avoid such termination if it, prior to the date of termination set forth in such notice, cures or explains to the reasonable satisfaction of Executive the factual basis for termination set forth therein; or

(b) a Change of Control (as hereinafter defined) occurs during the Term, at any time within the two-year period thereafter, by giving the Company notice to such effect, setting forth the event or circumstance constituting such Change of Control, such termination to be effective upon the date of termination, not more than 30 days after the date of such notice, set forth therein or, if no such date is set forth therein, immediately upon delivery of such notice to the Company.

The termination by Executive of his employment pursuant to this Section 14 shall not constitute or be deemed to constitute for any purpose a "voluntary resignation" of his employment.

15. Compensation upon Termination.

(a) Upon termination of Executive's employment hereunder, he shall be entitled to receive, in any case, any compensation or other amount due to him pursuant to Section 3 or 4 in respect of his employment prior to the Termination Date.

(b) If Executive's employment hereunder terminates upon his death, disability or incapacity pursuant to Section 12 or he is discharged "for cause" pursuant to Section 13, except for the payment of any amount required to be made by Section 15(a), from and after the Termination Date, the Company shall have no further obligation to Executive hereunder.

(c) If Executive terminates his employment hereunder for Good Reason pursuant to Section 14(a) or if the Company terminates his employment hereunder other than upon his death, disability or incapacity pursuant to Section 12 and other than for cause pursuant to Section 13, he shall be entitled to receive an amount equal to the product of (i) the sum of (A) his Base Salary in effect on the Termination Date and (B) his Bonus for the last Bonus Period ending before the Termination Date (annualized if such Bonus Period is other than a 12-month fiscal year of the Company), and (ii) a fraction, the numerator of which is the number of full months remaining in the balance of the Term after the Termination Date and the denominator of which is 77.

(d) If his employment terminates pursuant to Section 14(b) and, if at the time Executive gives the Company the notice of termination referred to therein, the Company has not given to Executive a notice of termination upon his disability or incapacity pursuant to Section 12 or "for cause" pursuant to Section 13, he shall be entitled to receive, upon the terms and subject to the conditions set forth in Section 16, the Parachute Amount (as hereinafter defined).

(e) Any amount payable to Executive upon termination of his employment hereunder shall be paid promptly, and in any event within 30 days, after the Termination Date.

(f) Executive shall have no obligation hereunder to seek or to accept any other employment after the Termination Date or otherwise to mitigate the payments required to be made by this Section. No compensation or other amount received or receivable by Executive on

account of any employment or engagement after the Termination Date shall be offset against or deducted from any payment required to be made by this Section.

16. Change of Control.

(a) For the purposes of this Section 16:

(i) The "Act" is the Securities Exchange Act of 1934, as amended.

(ii) A "person" includes a "group" within the meaning of Section 13(d)(3) of the Act.

(iii) "Control" is used herein as defined in Rule 12b-2 under the Act.

(iv) "Beneficially owns" and "acquisition" are used herein as defined in Rules 13d-3 and 13d-5, respectively, under the Act.

(v) "Non-Affiliated Person" means any person, other than Executive, an employee stock ownership trust of the Company (or any trustee thereof for the benefit of such trust), or any person controlled by Executive, the Company or such a trust.

(vi) "Voting Securities" includes Common Stock and any other securities of the Company that ordinarily entitle the holders thereof to vote, together with the holders of Common Stock or as a separate class, with respect to matters submitted to a vote of the holders of Common Stock, but securities of the Company as to which the consent of the holders thereof is required by applicable law or the terms of such securities only with respect to certain specified transactions or other matters, or the holders of which are entitled to vote only upon the occurrence of certain specified events (such as default in the payment of a mandatory

dividend on preferred stock or a scheduled installment of principal or interest of any debt security), shall not be Voting Securities.

(vii) "Right" means any option, warrant or other right to acquire any Voting Security (other than such a right of conversion or exchange included in a Voting Security).

(viii) The "Code" is the Internal Revenue Code of 1986, as amended.

(ix) "Base amount," "present value" and "parachute payment" are used herein as defined in Section 280G of the Code.

(b) A "Change of Control" occurs when:

(i) a Non-Affiliated Person acquires control of the Company;

(ii) upon an acquisition of Voting Securities or Rights by a Non-Affiliated Person or any change in the number or voting power of outstanding Voting Securities, such Non-Affiliated Person beneficially owns Voting Securities or Rights entitling such person to cast a number of votes (determined in accordance with Section 16(g)) equal to or greater than 25% of the sum of (A) the number of votes that may be cast by all other holders of outstanding Voting Securities and (B) the number of votes that may be cast by such Non-Affiliated Person (determined in accordance with Section 16(g)); or

(iii) upon any change in the membership of the Company's Board of Directors, a majority of the directors are persons who are not nominated or appointed by the Company's Board of Directors as constituted prior to such change.

(c) The "Parachute Amount" to which Executive shall be entitled pursuant to Section 15(d) shall equal 2.99 times Executive's base amount.

(d) It is intended that the present value of any payments or benefits to Executive, whether hereunder or otherwise, that are includable in the computation of parachute payments shall not exceed 2.99 times the base amount. Accordingly, if Executive receives any payment or benefit from the Company prior to payment of the Parachute Amount which, when added to the Parachute Amount, would subject any of the payments or benefits to Executive to the excise tax imposed by Section 4999 of the Code, the Parachute Amount shall be reduced by the least amount necessary to avoid such tax. The Company shall have no obligation hereunder to make any payment or provide any benefit to Executive after the payment of the Parachute Amount which would subject any of such payments or benefits to the excise tax imposed by Section 4999 of the Code.

(e) Any other provision hereof notwithstanding, Executive may, prior to his receipt of the Parachute Amount pursuant to Section 15(d), waive the payment thereof, or, after his receipt of the Parachute Amount thereunder, treat some or all of such amount as a loan from the Company which Executive shall repay to the Company within 180 days after the receipt thereof, together with interest thereon at the rate provided in Section 7872 of the Code, in either case, by giving the Company notice to such effect.

(f) Any determination of the base amount, the Parachute Amount, any liability for excise tax under Section 4999 of the Code or other matter required to be made pursuant to this Section 16, shall be made by the Company's regularly-engaged independent certified public accountants, whose determination shall be conclusive and binding upon the Company and Executive; provided that such accountants shall give to Executive, on or before the date on which payment of the Parachute Amount or any later payment or benefit would be made, a notice setting forth in reasonable detail such determination and the basis therefor, and stating expressly that Executive is entitled to rely thereon.

(g) The number of votes that may be cast by holders of Voting Securities or Rights upon the issuance or grant thereof shall be deemed to be the largest number of votes that may be cast by the holders of such securities or the holders of any other Voting Securities into which such Voting Securities or Rights are convertible or for which they are exchangeable or exercisable, determined as though such Voting Securities or Rights were immediately convertible, exchangeable or exercisable and without regard to any anti-dilution or other adjustments provided for therein.

17. Limitation of Authority. Except as expressly provided herein, no provision hereof shall be deemed to authorize or empower either party hereto to act on behalf of, obligate or bind the other party hereto.

18. Notices. Any notice or demand required or permitted to be given or made hereunder to or upon either party hereto shall be deemed to have been duly given or made for all purposes if (a) in writing and sent by (i) messenger or an overnight courier service against receipt, or (ii) certified or registered mail, postage paid, return receipt requested, or (b) sent by telegram, telecopy, telex or similar electronic means, provided that a written copy thereof is sent on the same day by postage-paid first-class mail, to such party at the following address:

to the Company at: 22619 Pacific Coast Highway
Malibu, California 90265
Attn: President
Fax: (310) 457-7099

with a copy to: Feder, Kaszovitz, Isaacson, Weber, Skala,
Bass & Rhine LLP
750 Lexington Avenue
New York, New York 10022
Attn: Murray L. Skala, Esq.
Fax: (212) 888-7776

to Executive at: 1625 Crown Ridge Court
Westlake Village, California 91362

or such other address as either party hereto may at any time, or from time to time, direct by notice given to the other party in accordance with this Section. The date of giving or making of any such notice or demand shall be, in the case of clause (a) (i), the date of the receipt; in the case of clause (a) (ii), five business days after such notice or demand is sent; and, in the case of clause (b), the business day next following the date such notice or demand is sent.

19. Amendment. No amendment of this Agreement shall be valid or effective, unless in writing and signed by or on behalf of the parties hereto.

20. Waiver. No course of dealing or omission or delay on the part of either party hereto in asserting or exercising any right hereunder shall constitute or operate as a waiver of any such right. No waiver of any provision hereof shall be effective, unless in writing and signed by or on behalf of the party to be charged therewith. No waiver shall be deemed a continuing waiver or waiver in respect of any other or subsequent breach or default, unless expressly so stated in writing.

21. Governing Law. This Agreement shall be governed by, and interpreted and enforced in accordance with, the laws of the State of New York without regard to principles of choice of law or conflict of laws.

22. Jurisdiction. Each of the parties hereto hereby irrevocably consents and submits to the jurisdiction of the courts of the State of New York and the United States District Court for the Southern District of New York in connection with any suit, action or proceeding arising out of or relating to this Agreement or the transactions contemplated hereby, waives any objection to venue in the County of New York, State of New York, or such District, and agrees that service of any summons, complaint, notice or other process relating to such proceeding may be effected in the manner provided by clause (a) (ii) of Section 18.

23. Remedies. In the event of any actual or prospective breach or default under this Agreement by either party hereto, the other party shall be entitled to equitable relief, including remedies in the nature of rescission, injunction and specific performance. All remedies hereunder are cumulative and not exclusive, and nothing herein shall be deemed to prohibit or limit either party from pursuing any other remedy or relief available at law or in equity for such actual or prospective breach or default, including the recovery of damages; provided that, except as otherwise provided in Section 15 and except with respect to a breach by Executive of his obligations pursuant to Sections 9, 10 and 11, no party hereto shall be liable under this Agreement for lost profits or consequential damages.

24. Severability. The provisions hereof are severable and in the event that any provision of this Agreement shall be determined to be invalid or unenforceable in any respect by a court of competent jurisdiction, the remaining provisions hereof shall not be affected, but shall, subject to the discretion of such court, remain in full force and effect, and any invalid or unenforceable provision shall be deemed, without further action on the part of the parties hereto, amended and limited to the extent necessary to render the same valid and enforceable.

25. Counterparts. This Agreement may be executed in counterparts, each of which shall be deemed an original and which together shall constitute one and the same agreement.

26. Assignment. This Agreement, and each right, interest and obligation hereunder, may not be assigned by either party hereto without the prior written consent of the other party hereto, and any purported assignment without such consent shall be void and without effect, except that this Agreement shall be assigned to, and assumed by, any Person with or into which the Company merges or consolidates, or which acquires all or substantially all of its assets, or which otherwise succeeds to and continues the Company's business substantially as an entirety. Except as otherwise expressly provided herein or required by law, Executive shall not have any power of anticipation, assignment or alienation of any payments required to be made to him

hereunder, and no other Person may acquire any right or interest in any thereof by reason of any purported sale, assignment or other disposition thereof, whether voluntary or involuntary, any claim in a bankruptcy or other insolvency Proceeding against Executive, or any other ruling, judgment, order, writ or decree.

27. Binding Effect. This Agreement shall be binding upon and inure to the benefit of the parties hereto and their respective successors and permitted assigns. This Agreement is not intended, and shall not be deemed, to create or confer any right or interest for the benefit of any Person not a party hereto.

28. Titles and Captions. The titles and captions of the Sections of this Agreement are for convenience of reference only and do not in any way define or interpret the intent of the parties or modify or otherwise affect any of the provisions hereof.

29. Grammatical Conventions. Whenever the context so requires, each pronoun or verb used herein shall be construed in the singular or the plural sense and each capitalized term defined herein and each pronoun used herein shall be construed in the masculine, feminine or neuter sense.

30. References. The terms "herein," "hereto," "hereof," "hereby," and "hereunder," and other terms of similar import, refer to this Agreement as a whole, and not to any Section or other part hereof.

31. No Presumptions. Each party hereto acknowledges that it has had an opportunity to consult with counsel and has participated in the preparation of this Agreement. No party hereto is entitled to any presumption with respect to the interpretation of any provision hereof or the resolution of any alleged ambiguity herein based on any claim that the other party hereto drafted or controlled the drafting of this Agreement.

32. Certain Definitions. As used herein:

(a) "Person" includes without limitation a natural person, corporation, joint stock company, limited liability company, partnership, joint venture, association, trust, government or governmental authority, agency or instrumentality, or any group of the foregoing acting in concert.

(b) A "Proceeding " is any suit, action, arbitration, audit, investigation or other proceeding before or by any court, magistrate, arbitration panel or other tribunal, or any governmental agency, authority or instrumentality of competent jurisdiction.

33. Entire Agreement. This Agreement embodies the entire agreement of the parties hereto with respect to the subject matter hereof and supersedes any prior agreement, commitment or arrangement relating thereto.

IN WITNESS WHEREOF, the undersigned have duly executed this Agreement as of the day and year first above written.

THE COMPANY:

JAKKS PACIFIC, INC.

By: /s/ STEPHEN G. BERMAN

Name: Stephen G. Berman
Title: President

EXECUTIVE:

/s/ MICHAEL BIANCO

Michael Bianco

ANNEX I

The Bonus shall be paid for each year including 2003 and thereafter during the Term in respect of each Bonus Period (as hereinafter defined) in which Pre-Tax Income (as hereinafter defined) equals or exceeds the Bonus Target (as hereinafter defined) for such Bonus Period, payable within 90 days after the end of such Bonus Period, in an amount equal to the lesser of (A) 2% of such Pre-Tax Income and (B) \$2,000,000. For these purposes:

(a) A "Bonus Period" is either a fiscal year of the Company ending during the Term after January 1, 2003 or, if the Term ends on a day other than the last day of a fiscal year of the Company, the portion of such fiscal year ending on the last day of the last full month ending during the Term.

(b) The "Bonus Target" for any Bonus Period is (i) \$2 million, if such Bonus Period consists of 12 calendar months, or (ii) in any other case, the product of (A) \$5,479.45 and (B) the number of days included in such Bonus Period.

(c) The "Pre-Tax Income" in any Bonus Period is the Company's income before any deduction or reserve for income taxes and without adjustment for any extraordinary item.

The determination of the Bonus Target, Pre-Tax Income and the Bonus for any Bonus Period, including all estimates, allocations or prorations required to be made in connection therewith, shall be made by the Company's regularly-engaged independent certified public accounts in accordance with generally accepted accounting principles applied on a basis consistent with past periods, which determination, absent manifest error, shall be conclusive and binding upon the Company and Executive. If a Bonus Period ends prior to the end of a fiscal year of the Company, and any year-end adjustment is subsequently made that affects the determination of the Bonus for such Bonus Period, the Company shall promptly give written notice to Executive

of any change proposed to be made to such Bonus, setting forth in reasonable detail therein the amount of and basis for such change. If such change involves an increase to such Bonus, the Company shall pay such increase to Executive concurrently with the delivery of such notice; and if such change involves a decrease to such Bonus, Executive shall repay the amount of such decrease to the Company promptly, and in any event within 60 days, after receipt of such notice.