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

FORM 10-Q

(Mark one)

☒ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2019

or

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from ______ to ______

Commission file number: **0-28104**

JAKKS Pacific, Inc.
(Exact Name of Registrant as Specified in Its Charter)

Delaware	**95-4527222**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
2951 28th Street	
Santa Monica, California	**90405**
(Address of Principal Executive Offices)	(Zip Code)

Registrant's Telephone Number, Including Area Code: **(424) 268-9444**

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 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, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "non-accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

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

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

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

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

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock $.001 Par Value	JAKK	The NASDAQ Global Select Market

The number of shares outstanding of the issuer's common stock is 32,524,913 as of August 9, 2019.

JAKKS PACIFIC, INC. AND SUBSIDIARIES
INDEX TO QUARTERLY REPORT ON FORM 10-Q
QUARTER ENDED JUNE 30, 2019
ITEMS IN FORM 10-Q

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 condensed consolidated 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,” “expect” or words of similar import, we are making forward-looking statements. We believe that the assumptions and expectations reflected in such forward-looking statements are reasonable and are 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.

PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

JAKKS PACIFIC, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except share amounts)

Assets	June 30, 2019	December 31, 2018
	(Unaudited)	
Current assets		
Cash and cash equivalents	$ 32,125	$ 53,282
Restricted cash	4,923	4,923
Accounts receivable, net of allowance for doubtful accounts of $1,613 and $2,149 at June 30, 2019 and December 31, 2018, respectively	85,119	122,278
Inventory	53,521	53,880
Prepaid expenses and other assets	28,523	15,780
Total current assets	204,211	250,143
Property and equipment		
Office furniture and equipment	11,876	11,999
Molds and tooling	108,250	108,315
Leasehold improvements	7,220	7,735
Total	127,346	128,049
Less accumulated depreciation and amortization	106,239	107,147
Property and equipment, net	21,107	20,902
Operating lease right-of-use assets	35,848	—
Intangible assets, net	14,931	17,312
Other long term assets	17,264	19,101
Goodwill	35,083	35,083
Trademarks	300	300
Total assets	$ 328,744	$ 342,841
Liabilities and Stockholders' Equity		
Current liabilities		
Accounts payable	$ 64,388	$ 57,574
Accrued expenses	33,628	29,914
Reserve for sales returns and allowances	24,498	29,403
Short term operating lease liabilities	9,182	—
Short term debt, net	1,892	27,211
Total current liabilities	133,588	144,102
Long term operating lease liabilities	29,829	—
Long term debt, net	160,656	139,792
Other liabilities	137	4,409
Income taxes payable	1,471	1,458
Deferred income taxes, net	1,431	1,431
Total liabilities	327,112	291,192
Stockholders' equity		
Preferred stock, $.001 par value; 5,000,000 shares authorized; nil outstanding	—	—
Common stock, $.001 par value; 100,000,000 shares authorized; 29,463,689 and 29,169,913 shares issued and outstanding at June 30, 2019 and December 31, 2018, respectively	30	30
Treasury stock, at cost; 3,112,840 shares	(24,000)	(24,000)
Additional paid-in capital	218,897	218,155
Accumulated deficit	(179,301)	(127,601)
Accumulated other comprehensive loss	(14,994)	(15,847)
Total JAKKS Pacific, Inc. stockholders' equity	632	50,737
Non-controlling interests	1,000	912
Total stockholders' equity	1,632	51,649
Total liabilities and stockholders' equity	$ 328,744	$ 342,841

See accompanying notes to condensed consolidated financial statements.

JAKKS PACIFIC, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS
(In thousands, except per share data)

	Three Months Ended June 30, (Unaudited)		Six Months Ended June 30, (Unaudited)	
	2019	**2018**	**2019**	**2018**
Net sales	$ 95,182	$ 105,781	$ 166,008	$ 198,785
Cost of sales	77,436	77,840	133,922	147,885
Gross profit	17,746	27,941	32,086	50,900
Selling, general and administrative expenses	33,870	39,748	69,136	98,365
Restructuring charge	22	—	270	—
Acquisition related and other	2,503	333	5,370	333
Loss from operations	(18,649)	(12,140)	(42,690)	(47,798)
Income from joint ventures	—	205	—	227
Other income (expense), net	(242)	31	(159)	81
Change in fair value of convertible senior notes	(106)	(2,410)	(2,529)	(3,431)
Interest income	20	14	47	28
Interest expense	(2,919)	(2,197)	(5,937)	(4,133)
Loss before provision for (benefit from) income taxes	(21,896)	(16,497)	(51,268)	(55,026)
Provision for (benefit from) income taxes	589	2,091	344	(245)
Net loss	(22,485)	(18,588)	(51,612)	(54,781)
Net income (loss) attributable to non-controlling interests	57	(29)	88	22
Net loss attributable to JAKKS Pacific, Inc.	$ (22,542)	$ (18,559)	$ (51,700)	$ (54,803)
Loss per share - basic and diluted	$ (0.96)	$ (0.80)	$ (2.19)	$ (2.37)
Shares used in loss per share - basic and diluted	23,600	23,106	23,578	23,103
Comprehensive loss	$ (22,935)	$ (19,978)	$ (50,759)	$ (55,121)
Comprehensive loss attributable to JAKKS Pacific, Inc.	$ (22,992)	$ (19,949)	$ (50,847)	$ (55,143)

See accompanying notes to condensed consolidated financial statements.

JAKKS PACIFIC, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(In thousands)

Three and Six Months Ended June 30, 2019

(Unaudited)

	Common Stock	Treasury Stock	Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	JAKKS Pacific, Inc. Stockholders' Equity	Non-Controlling Interests	Total Stockholders' Equity
Balance, December 31, 2018	$ 30	$ (24,000)	$ 218,155	$ (127,601)	$ (15,847)	$ 50,737	$ 912	$ 51,649
Stock-based compensation expense	—	—	618	—	—	618	—	618
Repurchase of common stock for employee tax withholding	—	—	(249)	—	—	(249)	—	(249)
Net income (loss)	—	—	—	(29,158)	—	(29,158)	31	(29,127)
Foreign currency translation adjustment	—	—	—	—	1,303	1,303	—	1,303
Balance, March 31, 2019	$ 30	$ (24,000)	$ 218,524	$ (156,759)	$ (14,544)	$ 23,251	$ 943	$ 24,194
Stock-based compensation expense	—	—	397	—	—	397	—	397
Repurchase of common stock for employee tax withholding	—	—	(24)	—	—	(24)	—	(24)
Net income (loss)	—	—	—	(22,542)	—	(22,542)	57	(22,485)
Foreign currency translation adjustment	—	—	—	—	(450)	(450)	—	(450)
Balance, June 30, 2019	$ 30	$ (24,000)	$ 218,897	$ (179,301)	$ (14,994)	$ 632	$ 1,000	$ 1,632

Three and Six Months Ended June 30, 2018

(Unaudited)

	Common Stock	Treasury Stock	Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	JAKKS Pacific, Inc. Stockholders' Equity	Non-Controlling Interests	Total Stockholders' Equity
Balance, December 31, 2017	$ 27	$ (24,000)	$ 215,809	$ (85,233)	$ (13,059)	$ 93,544	$ 969	$ 94,513
Restricted stock grants	3	—	—	—	—	3	—	3
Stock-based compensation expense	—	—	674	—	—	674	—	674
Repurchase of common stock for employee tax withholding	—	—	(85)	—	—	(85)	—	(85)
Net income (loss)	—	—	—	(36,244)	—	(36,244)	51	(36,193)
Foreign currency translation adjustment	—	—	—	—	1,050	1,050	—	1,050
Balance, March 31, 2018	$ 30	$ (24,000)	$ 216,398	$ (121,477)	$ (12,009)	$ 58,942	$ 1,020	$ 59,962
Stock-based compensation expense	—	—	313	—	—	313	—	313
Adjustment to additional paid in capital	—	—	(2)	—	—	(2)	—	(2)
Net loss	—	—	—	(18,559)	—	(18,559)	(29)	(18,588)
Foreign currency translation adjustment	—	—	—	—	(1,390)	(1,390)	—	(1,390)
Balance, June 30, 2018	$ 30	$ (24,000)	$ 216,709	$ (140,036)	$ (13,399)	$ 39,304	$ 991	$ 40,295

See accompanying notes to condensed consolidated financial statements.

JAKKS PACIFIC, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	Six Months Ended June 30, (Unaudited)	
	2019	**2018**
Cash flows from operating activities		
Net loss	$ (51,612)	$ (54,781)
Adjustments to reconcile net loss to net cash used in operating activities:		
Provision for doubtful accounts	(248)	12,468
Depreciation and amortization	7,473	7,428
Write-off and amortization of debt issuance costs	803	556
Share-based compensation expense	1,015	987
Gain on disposal of property and equipment	(61)	(28)
Change in fair value of convertible senior notes	2,529	3,431
Changes in operating assets and liabilities:		
Accounts receivable	37,407	29,710
Inventory	359	(3,729)
Prepaid expenses and other assets	(12,079)	(19,840)
Accounts payable	6,785	18,497
Accrued expenses	3,714	(6,675)
Reserve for sales returns and allowances	(4,905)	3,713
Income taxes payable	13	(267)
Other liabilities	(58)	(190)
Total adjustments	42,747	46,061
Net cash used in operating activities	(8,865)	(8,720)
Cash flows from investing activities		
Purchases of property and equipment	(5,205)	(6,510)
Net cash used in investing activities	(5,205)	(6,510)
Cash flows from financing activities		
Repayment of credit facility borrowings	(7,500)	(5,000)
Deferred issuance costs	—	(1,447)
Proceeds from term loan facility	—	20,000
Repayment of term loan	(167)	—
Repurchase of common stock for employee tax withholding	(273)	(85)
Net cash (used in) provided by financing activities	(7,940)	13,468
Net decrease in cash, cash equivalents and restricted cash	(22,010)	(1,762)
Effect of foreign currency translation	853	(224)
Cash, cash equivalents and restricted cash, beginning of period	58,205	64,977
Cash, cash equivalents and restricted cash, end of period	$ 37,048	$ 62,991
Cash paid during the period for:		
Income taxes	$ 68	$ 712
Interest	$ 5,063	$ 3,592

As of June 30, 2019, there was $3.4 million of property and equipment included in accounts payable. As of June 30, 2018, there was $4.9 million of property and equipment included in accounts payable.

See Notes 1, 5, 6 and 9 for additional supplemental information to the condensed consolidated statements of cash flows.

See accompanying notes to condensed consolidated financial statements.

JAKKS PACIFIC, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
June 30, 2019

Note 1 — Basis of Presentation

The accompanying 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 Management’s Discussion and Analysis of Financial Condition and Results of Operations and the financial statements and the notes thereto included in the Company’s Annual Report on Form 10-K, which contains audited financial information for the three years in the period ended December 31, 2018.

The information provided in this report reflects all adjustments (consisting solely of normal recurring items) that are, in the opinion of management, necessary to present fairly the financial position and the results of operations for the periods presented. Interim results are not necessarily, especially given seasonality, indicative of results to be expected for a full year.

The condensed consolidated financial statements include the accounts of JAKKS Pacific, Inc. and its wholly-owned subsidiaries (collectively, “the Company”). The condensed consolidated financial statements also include the accounts of DreamPlay Toys, LLC, a joint venture with NantWorks LLC, JAKKS Meisheng Trading (Shanghai) Limited, a joint venture with Meisheng Cultural & Creative Corp., Ltd., and JAKKS Meisheng Animation (HK) Limited, a joint venture with Hong Kong Meisheng Cultural Company Limited.

Certain prior period amounts have been reclassified for consistency with the current period presentation.

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Updates ("ASU") 2014-09, “Revenue from Contracts with Customers (Topic 606),” which supersedes the revenue recognition requirements in ASC 605, (Topic 605), and most industry-specific guidance. Under the new model, recognition of revenue occurs when a customer obtains control of promised goods or services in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In addition, the new standard requires that reporting companies disclose the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. In August 2015, the FASB issued ASU 2015-14, “Revenue from Contracts with Customers – Deferral of the Effective Date,” which defers the effective date of ASU 2014-09 to annual reporting periods beginning after December 15, 2017, and interim periods therein. In 2016, the FASB issued ASU 2016-08, “Principal versus Agent Considerations (Reporting Revenue Gross versus Net),” ASU 2016-10, “Identifying Performance Obligations and Licensing,” and ASU 2016-12, “Revenue from Contracts with Customers - Narrow-Scope Improvements and Practical Expedients.” Entities have the choice to adopt these updates using either of the following transition methods: (i) a full retrospective approach reflecting the application of the standard in each prior reporting period with the option to elect certain practical expedients, or (ii) a modified retrospective approach with the cumulative effect of these standards recognized at the date of the adoption.

On January 1, 2018, the Company adopted the new accounting standard ASC 606, (Topic 606), Revenue from Contracts with Customers and all the related amendments (“new revenue standard”) using the modified retrospective method applied to those contracts which were not completed as of January 1, 2018. Results for reporting periods beginning after January 1, 2018 are presented under Topic 606, while prior period amounts are not adjusted and continue to be reported in accordance with the Company’s historic accounting under ASC 605, (Topic 605).

There is no impact to the Company’s condensed consolidated financial statements resulting from the adoption of Topic 606 as the timing and measurement of revenue remained consistent with Topic 605, although the Company’s approach to revenue recognition is now based on the transfer of control. Further, there is no difference in the amounts of the revenue and cost of sales reported in the Company’s condensed consolidated statements of operations and comprehensive loss for the three and six months ended June 30, 2019 and 2018 that were recognized pursuant to Topic 606 and those that would have been reported pursuant to Topic 605.

JAKKS PACIFIC, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
June 30, 2019

In January 2016, the FASB issued ASU 2016-01, “Financial Instruments - Overall: Recognition and Measurement of Financial Assets and Financial Liabilities," (“ASU 2016-01”). The new guidance is intended to improve the recognition and measurement of financial instruments. The ASU is effective for fiscal years and interim periods within those years beginning after December 15, 2017. The adoption of this standard did not have an impact on the Company’s condensed consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, “Leases.” ASU 2016-02 establishes a right-of-use (“ROU”) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the statement of operations. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted. A modified retrospective transition approach is required, applying the new standard to all leases existing at the date of initial application. An entity may choose to use either (1) its effective date or (2) the beginning of the earliest comparative period presented in the financial statements as its date of initial application. If an entity chooses the second option, the transition requirements for existing leases also apply to leases entered into between the date of initial application and the effective date. The entity must also recast its comparative period financial statements and provide the disclosures required by the new standard for the comparative periods. On January 1, 2019, the Company adopted the new standard and uses the effective date as its date of initial application. Consequently, financial information will not be updated and the disclosures required under the new standard will not be provided for dates and periods before January 1, 2019. The new standard provides a number of optional practical expedients in transition. The Company elected certain practical expedients, which permits the Company not to reassess under the new standard its prior conclusions about lease identification, lease classification and initial direct costs. The Company did not elect the use-of-hindsight or the practical expedient pertaining to land easements; the latter not being applicable to the Company.

On adoption, the Company recognized operating lease liabilities of approximately $40.8 million with corresponding ROU assets of $37.6 million based on the present value of the remaining minimum rental payments for existing operating leases. The Company also derecognized deferred rent liabilities of $4.3 million and prepaid rent of $1.1 million upon the recognition of lease liabilities and ROU assets.

In October 2016, the FASB issued ASU 2016-16, “Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other than Inventory.” The amendments in this ASU reduce the complexity in the accounting standards by allowing the recognition of current and deferred income taxes for an intra-entity asset transfer, other than inventory, when the transfer occurs. Historically, recognition of the income tax consequence was not recognized until the asset was sold to an outside party. This ASU is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017. The adoption of this standard did not have an impact on the Company’s condensed consolidated financial statements.

In May 2017, the FASB issued ASU 2017-09, “Compensation - Stock Compensation (Topic 718): Scope of Modification Accounting,” which clarifies when to account for a change to the terms or conditions of a share-based payment award as a modification. Under the new guidance, modification accounting is required only if the fair value, vesting conditions, or the classification of the award (as equity or liability) changes as a result of the change in terms or conditions. ASU 2017-09 is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The adoption of this standard did not have an impact on the Company’s condensed consolidated financial statements.

In January 2018, the FASB issued ASU 2018-02, “Income Statement - Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income,” which gives entities the option to reclassify to retained earnings the tax effects resulting from the U.S. Tax Cuts and Jobs Act ("the Act") related to items in Accumulated Other Comprehensive Income (“AOCI”) that the FASB refers to as having been stranded in AOCI. The new guidance may be applied retrospectively to each period in which the effect of the Act is recognized in the period of adoption. The Company could adopt this guidance for fiscal years beginning after December 15, 2018 and interim periods within those fiscal years. Early adoption is permitted for periods for which financial statements have not yet been issued or made available for issuance, including the period the Act was enacted. The guidance, when adopted, will require new disclosures regarding a company’s accounting policy for releasing the tax effects in AOCI and permit the company the option to reclassify to retained earnings the tax effects resulting from the Act that are stranded in AOCI. The Company adopted this guidance on January 1, 2019 and the impact was not material.

JAKKS PACIFIC, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
June 30, 2019

In March 2018, the FASB issued ASU 2018-03, “Technical Corrections and Improvements to Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities,” which made targeted improvements to address certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. The ASU is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years beginning after June 15, 2018. The adoption of this standard did not have an impact on the Company’s condensed consolidated financial statements.

In June 2018, the FASB issued ASU 2018-07, “Improvements to Nonemployee Share-Based Payment Accounting,” which supersedes most of the prior accounting guidance on nonemployee share-based payments, and instead aligns it with existing guidance on employee share-based payments in Topic 718. The new standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years, and early adoption is permitted. The adoption of this standard did not have an impact on the Company’s condensed consolidated financial statements.

In August 2018, the FASB issued ASU 2018-13, “Disclosure Framework - Changes to the Disclosure Requirements for Fair Value Measurement,” which improves the effectiveness of the disclosures required under ASC 820 and modifies the disclosure requirements on fair value measurements, including the consideration of costs and benefits. The new standard is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years, and early adoption is permitted. The Company is currently evaluating the impact of the pending adoption of this new standard on its condensed consolidated financial statements.

In October 2018, the FASB issued ASU 2018-17, "Consolidation: Targeted Improvements to Related Party Guidance for Variable Interest Entities," which improves the accounting for variable interest entities by considering indirect interests held through related parties under common control for determining whether fees paid to decision makers and service providers are variable interests. This new standard is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. The amendments are required to be applied retrospectively with a cumulative-effect adjustment to retained earnings at the beginning of the earliest period presented. Early adoption is permitted. The Company is currently evaluating the impact of the pending adoption of this new standard on its condensed consolidated financial statements.

Note 2 — Business Segments, Geographic Data, and Sales by Major Customers

The Company is a worldwide producer and marketer of children’s toys and other consumer products, principally engaged in the design, development, production, marketing and distribution of its diverse portfolio of products. The Company has aligned its operating segments into three reporting segments that reflect the management and operation of the business. The Company’s segments are (i) U.S. and Canada, (ii) International, and (iii) Halloween.

The U.S. and Canada segment includes action figures, vehicles, play sets, plush products, dolls, electronic products, construction toys, infant and pre-school toys, role play and everyday costume play, foot to floor ride-on vehicles, wagons, novelty toys, seasonal and outdoor products, kids’ indoor and outdoor furniture, and related products.

Within the International segment, the Company markets and sells its toy products in markets outside of the U.S. and Canada, primarily in the European, Asia Pacific, and Latin American regions.

Within the Halloween segment, the Company markets and sells Halloween costumes and accessories and everyday costume play products, primarily in the U.S. and Canada.

Segment performance is measured at the operating income (loss) level. All sales are made to external customers and general corporate expenses have been attributed to the various segments based upon relative sales volumes. Segment assets are primarily comprised of accounts receivable and inventories, net of applicable reserves and allowances, goodwill and other assets. Certain assets which are not tracked by operating segment and/or that benefit multiple operating segments have been allocated on the same basis.

Results are not necessarily those which would be achieved if each segment was an unaffiliated business enterprise. Information by segment and a reconciliation to reported amounts for the three and six months ended June 30, 2019 and 2018 and as of June 30, 2019 and December 31, 2018 are as follows (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
Net Sales				
U.S. and Canada	$ 48,502	$ 59,381	$ 105,935	$ 129,916
International	10,293	22,044	20,046	39,343
Halloween	36,387	24,356	40,027	29,526
	$ 95,182	$ 105,781	$ 166,008	$ 198,785

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
Loss from Operations				
U.S. and Canada	$ (10,910)	$ (6,423)	$ (26,364)	$ (29,402)
International	(2,694)	(2,744)	(7,117)	(9,683)
Halloween	(5,045)	(2,973)	(9,209)	(8,713)
	$ (18,649)	$ (12,140)	$ (42,690)	$ (47,798)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
Depreciation and Amortization Expense				
U.S. and Canada	$ 2,625	$ 2,886	$ 5,312	$ 5,302
International	566	993	1,016	1,574
Halloween	1,048	453	1,145	552
	$ 4,239	$ 4,332	$ 7,473	$ 7,428

	June 30, 2019	December 31, 2018
Assets		
U.S. and Canada	$ 200,748	$ 223,877
International	82,876	108,669
Halloween	45,120	10,295
	$ 328,744	$ 342,841

The following tables present information about the Company by geographic area as of June 30, 2019 and December 31, 2018 and for the three and six months ended June 30, 2019 and 2018 (in thousands):

	June 30, 2019	December 31, 2018
Long-lived Assets		
China	$ 16,758	$ 15,825
United States	4,121	4,920
Hong Kong	228	157
	$ 21,107	$ 20,902

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
Net Sales by Customer Area				
United States	$ 82,409	$ 79,673	$ 139,967	$ 151,046
Europe	6,546	15,307	13,737	23,936
Canada	2,182	3,811	4,742	7,572
Hong Kong	937	300	1,192	527
Other	3,108	6,690	6,370	15,704
	$ 95,182	$ 105,781	$ 166,008	$ 198,785

Major Customers

Net sales to major customers for the three and six months ended June 30, 2019 and 2018 were as follows (in thousands, except for percentages):

	Three Months Ended June 30,				Six Months Ended June 30,			
	2019		2018		2019		2018	
	Amount	Percentage of Net Sales	Amount	Percentage of Net Sales	Amount	Percentage of Net Sales	Amount	Percentage of Net Sales
Wal-Mart	$ 29,709	31.2%	$ 18,454	17.4%	$ 51,818	31.2%	$ 43,211	21.7%
Target	14,016	14.7	21,532	20.4	26,195	15.8	36,844	18.5
	$ 43,725	45.9%	$ 39,986	37.8%	$ 78,013	47.0%	$ 80,055	40.2%

No other customer accounted for more than 10% of the Company's total net sales.

As of June 30, 2019 and December 31, 2018, the Company’s three largest customers accounted for approximately 68.1% and 61.4%, respectively, of the Company’s gross accounts receivable. The concentration of the Company’s business with a relatively small number of customers may expose the Company to material adverse effects if one or more of its large customers were to experience financial difficulty. The Company performs ongoing credit evaluations of its top customers and maintains an allowance for potential credit losses. For the six months ended June 30, 2018, the Company recorded bad debt expense of $12.5 million primarily due to the bankruptcy and liquidation of Toys “R” Us.

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Note 3 — Inventory

Inventory, which includes the ex-factory cost of goods, in-bound freight, duty and capitalized warehouse costs, is valued at the lower of cost (first-in, first-out) or net realizable value, net of inventory obsolescence reserve, and consists of the following (in thousands):

	June 30, 2019	December 31, 2018
Raw materials	$ 288	$ 311
Finished goods	53,233	53,569
	$ 53,521	$ 53,880

Note 4 — Revenue Recognition and Reserve for Sales Returns and Allowances

The Company's contracts with customers only include one performance obligation (i.e., sale of the Company's products). Revenue is recognized in the gross amount at a point in time when delivery is completed and control of the promised goods is transferred to the customers. Revenue is measured as the amount of consideration the Company expects to be entitled to in exchange for those goods. The Company's contracts do not involve financing elements as payment terms with customers are less than one year. Further, because revenue is recognized at the point in time goods are sold to customers, there are no contract assets or contract liability balances.

The Company disaggregates its revenues from contracts with customers by reporting segment: U.S. and Canada, International, and Halloween. The Company further disaggregates revenues by major geographic region. See Note 2, Business Segments, Geographic Data, and Sales by Major Customers, for further information.

The Company offers various discounts, pricing concessions, and other allowances to customers, all of which are considered in determining the transaction price. Certain discounts and allowances are fixed and determinable at the time of sale and are recorded at the time of sale as a reduction to revenue. Other discounts and allowances can vary and are determined at management's discretion (variable consideration). Specifically, the Company occasionally grants discretionary credits to facilitate markdowns and sales of slow moving merchandise, and consequently accrues an allowance based on historic credits and management estimates. Further, while the Company generally does not allow product returns, the Company does make occasional exceptions to this policy, and consequently records a sales return allowance based upon historic return amounts and management estimates. These allowances (variable consideration) are estimated using the expected value method and are recorded at the time of sale as a reduction to revenue. The Company adjusts its estimate of variable consideration at least quarterly or when facts and circumstances used in the estimation process may change. The variable consideration is not constrained as the Company has sufficient history on the related estimates and does not believe there is a risk of significant revenue reversal.

The Company also participates in cooperative advertising arrangements with some customers, whereby it allows a discount from invoiced product amounts in exchange for customer purchased advertising that features the Company's products. Generally, these allowances range from 1% to 20% of gross sales, and are generally based upon product purchases or specific advertising campaigns. Such allowances are accrued when the related revenue is recognized. These cooperative advertising arrangements provide a distinct benefit at fair value, and are accounted for as direct selling expenses.

Sales commissions are expensed when incurred as the related revenue is recognized at a point in time and therefore the amortization period is less than one year. As a result these costs are recorded as direct selling expenses, as incurred.

Shipping and handling activities are considered part of the Company's obligation to transfer the products and therefore are recorded as direct selling expenses, as incurred.

The Company's reserve for sales returns and allowances amounted to $24.5 million as of June 30, 2019, compared to $29.4 million as of December 31, 2018.

Note 5 — Credit Facilities

Wells Fargo

In March 2014, the Company and its domestic subsidiaries entered into a secured credit facility with General Electric Capital Corporation ("GECC"). The credit facility, as amended and subsequently assigned to Wells Fargo Bank, N.A. ("Wells Fargo") pursuant to its acquisition of GECC, provides for a $75.0 million revolving credit facility subject to availability based on prescribed advance rates on certain domestic accounts receivable and inventory amounts used to compute the borrowing base (the "Credit Facility"). The Credit Facility includes a sub-limit of up to $35.0 million for the issuance of letters of credit. The amounts outstanding under the Credit Facility, as amended, were payable in full upon maturity of the facility on September 27, 2019, except that the Credit Facility would mature on June 15, 2018 if the Company did not refinance or extend the maturity of the convertible senior notes that mature in 2018, provided that any such refinancing or extension shall have a maturity date that is no sooner than six months after the stated maturity of the Credit Facility (i.e., on or about September 27, 2019). On June 14, 2018, the Company entered into a Term Loan Agreement with Great American Capital Partners to provide the necessary capital to refinance the 2018 convertible senior notes (see additional details regarding the Term Loan Agreement below). In addition, on June 14, 2018, the Company revised certain of the Credit Facility documents (and entered into new ones) so that certain of its Hong Kong based subsidiaries became additional parties to the Credit Facility. As a result, the receivables of these subsidiaries can now be included in the borrowing base computation, subject to certain limitations, thereby effectively increasing the amount of funds the Company can borrow under the Credit Facility. Any additional borrowings under the Credit Facility will be used for general working capital purposes.

The Credit Facility is secured by a security interest in favor of Wells Fargo covering a substantial amount of the consolidated assets and a pledge of the majority of the capital stock of various of the Company's subsidiaries. As of June 30, 2019, there were no outstanding borrowings and the amount of outstanding stand-by letters of credit totaled $9.5 million; the total excess borrowing capacity was $19.3 million. As of December 31, 2018, the amount of outstanding borrowings was $7.5 million and outstanding stand-by letters of credit totaled $12.8 million; the total excess borrowing capacity was $40.7 million. In July 2019, the Company borrowed $5.0 million under the Credit Facility.

The Company's ability to borrow under the Credit Facility is also subject to its ongoing compliance with certain financial covenants, including the maintenance by the Company of a fixed charge coverage ratio of at least 1.25:1.0 based on the trailing four fiscal quarters in the event minimum excess availability of $10.0 million under the Credit Facility is not maintained. As of June 30, 2019 and December 31, 2018, the Company was in compliance with the financial covenants under the Credit Facility.

The Company may borrow funds at LIBOR or at a Base Rate, plus applicable margins of 225 basis point spread over LIBOR and 125 basis point spread on Base Rate loans. The Base Rate is the highest of (i) the Federal Funds Rate plus a margin of 0.50%, (ii) the rate last quoted by The Wall Street Journal as the "Prime Rate," or (iii) the sum of a LIBOR rate plus 1.00%. In addition to standard fees, the Credit Facility has an unused credit line fee, which ranges from 25 to 50 basis points. As of June 30, 2019 and December 31 2018, the weighted average interest rate on the Credit Facility was approximately 4.77% and 5.53%, respectively.

The Credit Facility also contains customary events of default, including a cross default provision and a change of control provision. In the event of a default, all of the obligations of the Company and its subsidiaries under the Credit Facility may be declared immediately due and payable. For certain events of default relating to insolvency and receivership, all outstanding obligations become due and payable.

In August 2019, in connection with the Recapitalization transaction (See Note 19 - Subsequent Event), the Company entered into an amended and extended revolving credit facility with Wells Fargo, which includes, among other changes, a revised revolving credit facility limit of $60.0 million and an extended maturity date to August 2022.

Great American Capital Partners

On June 14, 2018, the Company entered into a Term Loan Agreement, Term Note, Guaranty and Security Agreement and other ancillary documents and agreements (the “Term Loan”) with Great American Capital Partners Finance Co., LLC (“GACP”), for itself as a Lender (as defined below) and as the Agent (in such capacity, “Agent”) for the Lenders from time to time party to the Term Loan (collectively, “Lenders”) and the other “Secured Parties” under and as defined therein, with respect to the issuance to the Company by Lenders of a $20.0 million term loan. To secure the Company’s obligations under the Term Loan, the Company granted to Agent, for the benefit of the Secured Parties, a security interest in a substantial amount of the Company’s consolidated assets and a pledge of the majority of the capital stock of various of its subsidiaries. The Term Loan is a secured obligation, second only to the Credit Facility with Wells Fargo, except with respect to certain of the Company’s inventory in which GACP has a priority secured position. The Company may use the funds from the Term Loan to repurchase or retire its outstanding convertible senior notes due August 2018, for working capital, capital expenditures and other general corporate purposes, subject to certain negative covenants set forth in the Term Loan.

The Term Loan requires the repayment of principal in the amount of 10% of the outstanding Term Loan per year (payable monthly) beginning after the first anniversary. All then-outstanding borrowings under the Term Loan are due, and the Term Loan terminates, no later than June 14, 2021, unless sooner terminated in accordance with its terms, which includes the date of termination of the Wells Fargo Credit Facility and the date that is 91 days prior to the maturity of the Company’s various convertible senior notes due in 2020 (see Note 6). The Company is permitted, and may be required under certain circumstances as set forth in the Term Loan documents, to prepay the Term Loan, which would require a prepayment fee (i) in year one of up to any unearned and unpaid interest that would have become due and payable in year one had the prepayment not occurred plus 2% of the initial amount of the Term Loan (i.e., $20.0 million), (ii) in year two of 2% of the initial amount of the Term Loan and (iii) in year three of 1% of the initial amount of the Term Loan.

The Company’s ability to continue to borrow the initial Term Loan amount of $20.0 million is based on certain accounts receivable and inventory amounts used to compute the borrowing base. In the event the Term Loan balance exceeds the borrowing base computation, the shortfall would be (i) applied to any excess availability under the Wells Fargo Credit Facility or (ii) prepaid. Similar to the Wells Fargo Credit Facility, the Company is subject to ongoing compliance with certain financial covenants, including the maintenance by the Company of a fixed charge coverage ratio of at least 1.25:1.0 based on the trailing four fiscal quarters in the event minimum excess availability of $10.0 million under the Wells Fargo Credit Facility is not maintained. The Company must also maintain a minimum amount of liquidity, as defined in the Term Loan, of $10.0 million. As of June 30, 2019 and December 31, 2018, the Company was in compliance with the financial covenants under the Term Loan.

The Term Loan is accelerated and becomes immediately due and payable (and the Term Loan terminates) in the event of a default under the Term Loan which includes, among other things, breach of certain covenants or representations contained in the Term Loan documents, defaults under other loans or obligations, involvement in bankruptcy proceedings or an occurrence of a change of control (as such terms are defined in the Term Loan). The Term Loan Documents also contain negative covenants which, during the life of the Term Loan, prohibit and/or limit the Company from, among other things, incurring certain types of other debt, acquiring other companies, making certain expenditures or investments and changing the character of its business.

As of June 30, 2019 and December 31, 2018, the amount outstanding under the Term Loan was $19.8 million and $20.0 million, respectively. Borrowings under the Term Loan accrue interest at LIBOR plus 9.00% per annum. As of June 30, 2019 and December 31, 2018, the weighted average interest rate on the Term Loan was approximately 11.5% and 11.1%, respectively.

Amortization expense classified as interest expense related to the $1.3 million debt issuance costs associated with the transactions that closed on June 14, 2018 (i.e., the amendment of the Wells Fargo Credit Facility and the GACP Term Loan) was nil and $0.4 million for the three and six months ended June 30, 2019 and $0.1 million for the three and six months ended June 30, 2018.

In August 2019, in connection with the Recapitalization transaction (See Note 19 - Subsequent Event), the Term Loan with a principal amount outstanding as of June 30, 2019 of $19.8 million has been paid in full and refinanced with new secured term debt with a face amount of approximately $30.0 million that matures in February 2023. As a result, the Term Loan is reflected as a long term liability on the accompanying condensed consolidated balance sheet at June 30, 2019.

Note 6 — Convertible Senior Notes

Convertible senior notes consist of the following (in thousands):

	June 30, 2019			December 31, 2018		
	Principal/ Fair Value Amount	Debt Issuance Costs	Net Amount	Principal/ Fair Value Amount	Debt Issuance Costs	Net Amount
4.875% convertible senior notes (due 2020)	$ 113,000	$ 788	$ 112,212	$ 113,000	$ 1,182	$ 111,818
3.25% convertible senior notes (due 2020) *	30,503	—	30,503	27,974	—	27,974
Total convertible senior notes, net of debt issuance costs	$ 143,503	$ 788	$ 142,715	$ 140,974	$ 1,182	$ 139,792

* The amount presented for the 3.25% 2020 convertible senior notes within the table represents the fair value as of June 30, 2019 and December 31, 2018 (see Note 16). The principal amount of these notes totals $29.5 million as of June 30, 2019 and December 31, 2018.

Amortization expense classified as interest expense related to debt issuance costs was $0.2 million and $0.2 million for the three months ended June 30, 2019 and 2018, respectively, and $0.4 million and $0.5 million for the six months ended June 30, 2019 and 2018.

In July 2013, the Company sold an aggregate of $100.0 million principal amount of 4.25% convertible senior notes due 2018 (the “2018 Notes”). The 2018 Notes, which were senior unsecured obligations of the Company, paid interest semi-annually in arrears on August 1 and February 1 of each year at a rate of 4.25% per annum and matured on August 1, 2018. The initial conversion rate for the 2018 Notes was 114.3674 shares of the Company’s common stock per $1,000 principal amount of notes, equivalent to an initial conversion price of approximately $8.74 per share of common stock, subject to adjustment in certain events. In 2016, the Company repurchased and retired an aggregate of approximately $6.1 million principal amount of the 2018 Notes. In addition, approximately $0.1 million of the unamortized debt issuance costs were written off and a nominal gain was recognized in conjunction with the retirement of the 2018 Notes. During the first quarter of 2017, the Company exchanged and retired $39.1 million principal amount of the 2018 Notes at par for $24.1 million in cash and approximately 2.9 million shares of its common stock. During the second quarter of 2017, the Company exchanged and retired $12.0 million principal amount of the 2018 Notes at par for $11.6 million in cash and 112,400 shares of its common stock, and approximately $0.1 million of the unamortized debt issuance costs were written off and a $0.1 million gain was recognized in conjunction with the exchange and retirement of the 2018 Notes.

In August 2017, the Company agreed with Oasis Management and Oasis Investments II Master Fund Ltd., (collectively, “Oasis”) the holder of approximately $21.5 million face amount of its 4.25% convertible senior notes due in 2018, to extend the maturity date of these notes to November 1, 2020. In addition, the interest rate was reduced to 3.25% per annum and the conversion rate was increased to 328.0302 shares of the Company’s common stock per $1,000 principal amount of notes, among other things. After execution of a definitive agreement for the modification and final approval by the other members of the Company’s Board of Directors and Oasis’ Investment Committee the transaction closed on November 7, 2017. In connection with this transaction, the Company recognized a loss on extinguishment of the debt of approximately $0.6 million. On July 26, 2018, the Company closed a transaction with Oasis to exchange $8.0 million face amount of the 4.25% convertible senior notes due in August 2018 with convertible senior notes similar to those issued to Oasis in November 2017. The new notes mature on November 1, 2020, accrue interest at an annual rate of 3.25% and are convertible into shares of the Company’s common stock at an initial rate of 322.2688 shares per $1,000 principal amount of the new notes. In connection with this transaction, the Company recognized a loss on extinguishment of the debt of approximately $0.5 million. The conversion price for the 3.25% convertible senior notes was reset on November 1, 2018 and will be reset on November 1, 2019 (each, a “reset date”) to a price equal to 105% above the 5-day Volume Weighted Average Price ("VWAP") preceding the reset date; provided, however, among other reset restrictions, that if the conversion price resulting from such reset is lower than 90 percent of the average VWAP during the 90 calendar days preceding the reset date, then the reset price shall be the 30-day VWAP preceding the reset date. The conversion price of the 3.25% 2020 Notes reset on November 1, 2018 to $2.54 per share and the conversion rate was increased to 393.7008 shares of the Company's common stock per $1,000 principal amount of notes.

The remaining $13.2 million of 2018 Notes were redeemed at par at maturity on August 1, 2018.

The Company has elected to measure and present the debt held by Oasis at fair value using Level 3 inputs and as a result, recognized a loss of $0.1 million and $2.4 million for the three months ended June 30, 2019 and 2018, respectively, related to changes in the fair value of the 3.25% 2020 Notes. At June 30, 2019 and December 31, 2018, the 3.25% 2020 Notes had a fair value of approximately $30.5 million and $28.0 million, respectively. The Company evaluated its credit risk as of June 30, 2019, and determined that there was no change from December 31, 2018.

In June 2014, the Company sold an aggregate of $115.0 million principal amount of 4.875% convertible senior notes due 2020 (the “2020 Notes”). The 2020 Notes are senior unsecured obligations of the Company paying interest semi-annually in arrears on June 1 and December 1 of each year at a rate of 4.875% per annum and will mature on June 1, 2020. The initial and still current conversion rate for the 2020 Notes is 103.7613 shares of the Company’s common stock per $1,000 principal amount of notes, equivalent to an initial conversion price of approximately $9.64 per share of common stock, subject to adjustment in certain events. Upon conversion, the 2020 Notes will be settled in shares of the Company’s common stock. Holders of the 2020 Notes may require that the Company repurchase for cash all or some of their notes upon the occurrence of a fundamental change (as defined in the 2020 Notes). In January 2016, the Company repurchased and retired an aggregate of $2.0 million principal amount of the 2020 Notes. In addition, approximately $0.1 million of the unamortized debt issuance costs were written off and a $0.1 million gain was recognized in conjunction with the retirement of the 2020 Notes.

The fair value of the 4.875% convertible senior notes payable due 2020 as of June 30, 2019 and December 31, 2018 was $102.5 million and $93.2 million, respectively, based upon the most recent quoted market prices. The fair values of the convertible senior notes are considered to be Level 3 measurements on the fair value hierarchy.

In August 2019, in connection with the Recapitalization transaction (See Note 19 - Subsequent Event), 2020 Notes outstanding with a face amount of $111.1 million of the total $113.0 million outstanding at June 30, 2019 were refinanced to extend the maturity date. Of the refinanced amount, $103.8 million were refinanced with the issuance of new secured term debt that matures in February 2023. The remaining refinanced amount of $7.3 million was exchanged into similar convertible senior notes previously issued to Oasis with a total face amount of $29.5 million with an original maturity of November 2020. The convertible senior notes issued to Oasis were amended to, among other things, extend the maturity date to the earlier of (i) 91 days after the repayment in full of the newly issued secured term debt that matures in February 2023 or (ii) July 2023. As a result, the refinanced portion of $111.1 million is reflected as a long term liability on the accompanying condensed consolidated balance sheet at June 30, 2019.

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Note 7 — Income Taxes

The Company’s income tax expense of $0.6 million for the three months ended June 30, 2019 reflects an effective tax rate of (2.7)%. The Company’s income tax expense of $2.1 million for the three months ended June 30, 2018 reflects an effective tax rate of (12.7)%. The majority of the tax expense for the three months ended June 30, 2019 relates to foreign income taxes and discrete items. The majority of the tax expense for the three months ended June 30, 2018 relates to foreign income taxes partially offset by discrete items.

The Company’s income tax expense of $0.3 million for the six months ended June 30, 2019 reflects an effective tax rate of (0.7)%. The Company’s income tax benefit of $0.2 million for the six months ended June 30, 2018 reflects an effective tax rate of 0.4%. The majority of the tax expense for the six months ended June 30, 2019 relates to foreign income taxes and discrete items. The majority of the tax benefit for the six months ended June 30, 2018 relates to favorable discrete items and foreign income tax benefit.

Note 8 — Loss Per Share

The following table is a reconciliation of the weighted average shares used in the computation of loss per share for the periods presented (in thousands, except per share data):

	Three Months Ended June 30,					
	2019			2018		
	Loss	Weighted Average Shares	Per-Share	Loss	Weighted Average Shares	Per-Share
Loss per share - basic and diluted						
Net loss available to common stockholders	$ (22,542)	23,600	$ (0.96)	$ (18,559)	23,106	$ (0.80)

	Six Months Ended June 30,					
	2019			2018		
	Loss	Weighted Average Shares	Per-Share	Loss	Weighted Average Shares	Per-Share
Loss per share - basic and diluted						
Net loss available to common stockholders	$ (51,700)	23,578	$ (2.19)	$ (54,803)	23,103	$ (2.37)

Basic loss per share is calculated using the weighted average number of common shares outstanding during the period. Diluted earnings per share is calculated using the weighted average number of common shares and common share equivalents outstanding during the period (which consist of warrants, options, restricted stock awards, restricted stock units and convertible debt to the extent they are dilutive). The weighted average number of common shares outstanding excludes 3,112,840 shares repurchased pursuant to a prepaid forward share repurchase agreement associated with the issuance of the convertible senior notes due 2020. Common share equivalents that could potentially dilute basic earnings per share in the future, which were excluded from the computation of diluted earnings per share due to being anti-dilutive, totaled 27,675,542 for the three and six months ended June 30, 2019. Common share equivalents that could potentially dilute basic earnings per share in the future, which were excluded from the computation of diluted earnings per share due to being anti-dilutive, totaled 25,268,205 for the three and six months ended June 30, 2018.

Note 9 — Common Stock and Preferred Stock

In January 2018, the Company issued an aggregate of 1,914,894 shares of restricted stock at a value of approximately $4.5 million to two executive officers, which vest, subject to certain company financial performance criteria and market conditions, over a 3 years period. In addition, an aggregate of 249,480 shares of restricted stock at an aggregate value of approximately $0.6 million were issued to its six non-employee directors, which vested in January 2019.

During 2018, an executive officer surrendered an aggregate of 42,346 shares of restricted stock for $98,000 to cover income taxes due on the vesting of restricted shares.

In January 2019, the Company was obligated to issue an aggregate of 3,061,224 shares of restricted stock at a value of approximately $4.5 million to two executive officers pursuant to the applicable employment contracts. The shares were not issued at that time due to insufficient shares available in the 2002 Stock Award and Incentive Plan. Such shares were subsequently approved by the Company's shareholders and issued in July 2019. In addition, an aggregate of 328,230 shares of restricted stock at an aggregate value of approximately $0.5 million were issued to its six non-employee directors, which will vest in January 2020.

During the first quarter of 2019, two executive officers surrendered an aggregate of 143,913 shares of restricted stock for approximately $215,000 to cover income taxes due on the vesting of restricted shares.

During the second quarter of 2019, an executive officer surrendered an aggregate of 24,281 shares of restricted stock for approximately $25,000 to cover income taxes due on the vesting of restricted stock units.

All issuances of common stock, including those issued pursuant to stock option and warrant exercises, restricted stock grants and acquisitions, are issued from the Company’s authorized but not issued and outstanding shares.

No dividend was declared or paid in the three and six months ended June 30, 2019 or 2018.

Note 10 — Joint Ventures

The Company owns a fifty percent interest in a joint venture (“Pacific Animation Partners”) with the U.S. entertainment subsidiary of a leading Japanese advertising and animation production company. The joint venture was created to develop and produce a boys’ animated television show, which it licensed worldwide for television broadcast as well as consumer products. The Company produced toys based upon the television program under a license from the joint venture which also licensed certain other merchandising rights to third parties. The joint venture completed and delivered 65 episodes of the show, which began airing in February 2012, and has since ceased production of the television show. For the three and six months ended June 30, 2019, the Company recognized income from the joint venture of nil. For the three and six months ended June 30, 2018, the Company recognized income from the joint venture of nil and $22,000, respectively.

As of June 30, 2019 and December 31, 2018, the balance of the investment in the Pacific Animation Partners joint venture is nil.

In September 2012, the Company entered into a joint venture (“DreamPlay Toys”) with NantWorks LLC (“NantWorks”) in which it owns a fifty percent interest. Pursuant to the operating agreement of DreamPlay Toys, the Company paid to NantWorks cash in the amount of $8.0 million and issued NantWorks a warrant to purchase 1.5 million shares of the Company’s common stock at a value of $7.0 million in exchange for the exclusive right to arrange for the provision of the NantWorks recognition technology platform for toy products. The Company had classified these rights as an intangible asset, which was being amortized over the anticipated revenue stream from the exploitation of these rights. However, the Company has abandoned the use of the technology in connection with its toy products and no future sales are anticipated, and the Company recorded an impairment charge to income of $2.9 million to write off the remaining unamortized technology rights during the third quarter of 2017. The Company retains the financial risk of the joint venture and is responsible for the day-to-day operations, which are expected to be nominal in future periods. The results of operations of the joint venture are consolidated with the Company’s results.

In addition, in 2012, the Company invested $7.0 million in cash in exchange for a five percent economic interest in a related entity, DreamPlay, LLC, that was expected to monetize the exploitation of the recognition technologies in non-toy consumer product categories. Adoption of the technology has been inadequate to establish a commercially viable market for the technology. NantWorks has the right to repurchase the Company’s interest for $7.0 million, but the Company does not anticipate that NantWorks will do so. As of September 30, 2017, the Company determined the value of this investment will not be realized and that full impairment of the value had occurred. Accordingly, the Company recorded an impairment charge of $7.0 million during the quarter ended September 30, 2017.

In November 2014, the Company entered into a joint venture with Meisheng Culture & Creative Corp., for the purpose of providing certain JAKKS licensed and non-licensed toys and consumer products to agreed-upon territories of the People’s Republic of China. The joint venture includes a subsidiary in the Shanghai Free Trade Zone that sells, distributes and markets these products, which include dolls, plush, role play products, action figures, costumes, seasonal items, technology and app-enhanced toys, based on entertainment licenses and JAKKS’ own proprietary brands. The Company owns fifty-one percent of the joint venture and consolidates the joint venture since control rests with the Company. The non-controlling interest’s share of the income (loss) was $57,000 and ($29,000) for the three months ended June 30, 2019 and 2018, respectively, and $88,000 and $22,000 for the six months ended June 30, 2019 and 2018, respectively.

In October 2016, the Company entered into a joint venture with Hong Kong Meisheng Cultural Company Limited ("Meisheng"), a Hong Kong-based subsidiary of Meisheng Culture & Creative Corp., for the purpose of creating and developing original, multiplatform content for children including new short-form series and original shows. JAKKS and Meisheng each own fifty percent of the joint venture and will jointly own the content. JAKKS will retain merchandising rights for kids’ consumer products in all markets except China, which Meisheng Culture & Creative Corp. will oversee through the Company’s existing distribution joint venture. The results of operations of the joint venture are consolidated with the Company's results. The non-controlling interest’s share of the income from the joint venture for the three and six months ended June 30, 2019 and 2018 was nil. As of June 30, 2019, Meisheng beneficially owns more than 10% of the Company’s outstanding common stock.

Meisheng also serves as a significant manufacturer of the Company. For the three and six months ended June 30, 2019, the Company made inventory-related payments to Meisheng of approximately $23.0 million and $25.2 million, respectively. For the three and six months ended June 30, 2018, the Company made inventory-related payments to Meisheng of approximately $12.1 million and $14.1 million, respectively. As of June 30, 2019 and 2018, amounts due Meisheng for inventory received by the Company, but not paid totaled $18.8 million and $13.0 million, respectively.

Note 11 — Goodwill

The Company applies a fair value-based impairment test to the carrying value of goodwill and indefinite-lived intangible assets on an annual basis and, on an interim basis, if certain events or circumstances indicate that an impairment loss may have been incurred. Goodwill impairment exists when the estimated fair value of goodwill is less than its carrying value. Based on the Company's April 1 annual assessment, it determined that the fair values of its reporting units were not less than the carrying amounts. No goodwill impairment was determined to have occurred for the six months ended June 30, 2019.

Note 12 — Intangible Assets Other Than Goodwill

Intangible assets other than goodwill consist primarily of licenses, product lines, customer relationships and trademarks. Amortized intangible assets are included in intangibles in the accompanying condensed consolidated balance sheets. Trademarks are disclosed separately in the accompanying condensed consolidated balance sheets. Intangible assets as of June 30, 2019 and December 31, 2018 include the following (in thousands, except for weighted useful lives):

		June 30, 2019			December 31, 2018		
	Weighted Useful Lives (Years)	Gross Carrying Amount	Accumulated Amortization	Net Amount	Gross Carrying Amount	Accumulated Amortization	Net Amount
Amortized Intangible Assets:							
Licenses	5.81	$ 20,130	$ (19,694)	$ 436	$ 20,130	$ (19,383)	$ 747
Product lines	10.36	33,858	(19,363)	14,495	33,858	(17,293)	16,565
Customer relationships	4.90	3,152	(3,152)	—	3,152	(3,152)	—
Trade names	5.00	3,000	(3,000)	—	3,000	(3,000)	—
Non-compete agreements	5.00	200	(200)	—	200	(200)	—
Total amortized intangible assets		$ 60,340	$ (45,409)	$ 14,931	$ 60,340	$ (43,028)	$ 17,312
Unamortized Intangible Assets:							
Trademarks		$ 300	$ —	$ 300	$ 300	$ —	$ 300

Note 13 — Comprehensive Loss

The table below presents the components of the Company's comprehensive loss for the three and six months ended June 30, 2019 and 2018 (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
Net Loss	$ (22,485)	$ (18,588)	$ (51,612)	$ (54,781)
Other comprehensive income (loss):				
Foreign currency translation adjustment	(450)	(1,390)	853	(340)
Comprehensive loss	(22,935)	(19,978)	(50,759)	(55,121)
Less: Comprehensive income (loss) attributable to non-controlling interests	57	(29)	88	22
Comprehensive loss attributable to JAKKS Pacific, Inc.	$ (22,992)	$ (19,949)	$ (50,847)	$ (55,143)

Note 14 — Litigation and Contingencies

The Company is a party to, and certain of its property is the subject of, various pending claims and legal proceedings that routinely arise in the ordinary course of its business. The Company accrues for losses when the loss is deemed probable and the liability can reasonably be estimated. Where a liability is probable and there is a range of estimated loss with no best estimate in the range, the Company records the minimum estimated liability related to the claim. As additional information becomes available, the Company assesses the potential liability related to its pending litigation and revises its estimates.

JAKKS PACIFIC, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
June 30, 2019

In the normal course of business, the Company may provide certain indemnifications and/or other commitments of varying scope to a) its licensors, customers and certain other parties, including against third party claims of intellectual property infringement, and b) its officers, directors and employees, including against third party claims regarding the periods in which they serve in such capacities with the Company. The duration and amount of such obligations is, in certain cases, indefinite. The Company's director's and officer's liability insurance policy may, however, enable it to recover a portion of any future payments related to its officer, director or employee indemnifications. For the past five years, costs related to director and officer indemnifications have not been significant. Other than certain liabilities recorded in the normal course of business related to royalty payments due the Company's licensors, no liabilities have been recorded for indemnifications and/or other commitments.

Note 15 — Share-Based Payments

The Company's *2002 Stock Award and Incentive Plan* (the "Plan"), as amended, provides for the awarding of stock options, restricted stock and restricted stock units to certain key employees, executive officers and non-employee directors. Current awards under the Plan include grants to directors, executive officers and certain key employees of restricted stock awards and units, with vesting contingent upon (a) the completion of specified service periods ranging from one to five years and/or (b) meeting certain financial performance and/or market-based metrics. Unlike the restricted stock awards, the shares for the restricted stock units are not issued until they vest. The Plan is more fully described in Notes 15 and 17 to the Consolidated Financial Statements in the Company's 2018 Annual Report on Form 10-K.

The following table summarizes the total share-based compensation expense recognized for the three and six months ended June 30, 2019 and 2018 (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
Share-based compensation expense	$ 397	$ 313	$ 1,015	$ 987

Restricted Stock Awards

Restricted stock award activity (including those with performance-based vesting criteria) for the six months ended June 30, 2019 is summarized as follows:

	Restricted Stock Awards	
	Number of Shares	Weighted Average Grant Date Fair Value
Outstanding, December 31, 2018	2,950,782	$ 2.41
Awarded	328,230	1.47
Released	(528,348)	2.81
Forfeited	—	—
Outstanding, June 30, 2019	2,750,664	2.22

As of June 30, 2019, there was $2.3 million of total unrecognized compensation cost related to non-vested restricted stock awards, which is expected to be recognized over a weighted-average period of 1.87 years.

JAKKS PACIFIC, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
June 30, 2019

Restricted Stock Units

Restricted stock unit activity (including those with performance-based vesting criteria) for the six months ended June 30, 2019 is summarized as follows:

	Restricted Stock Units	
	Number of Shares	**Weighted Average Grant Date Fair Value**
Outstanding, December 31, 2018	1,052,166	$ 3.72
Awarded	742,574	0.81
Released	(161,486)	3.80
Forfeited	(65,166)	4.51
Outstanding, June 30, 2019	1,568,088	2.30

As of June 30, 2019, there was $1.6 million of total unrecognized compensation cost related to non-vested restricted stock units, which is expected to be recognized over a weighted-average period of 1.78 years.

Note 16 — Fair Value Measurements

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In determining fair value, the Company uses various methods including market, income and cost approaches. Based upon these approaches, the Company often utilizes certain assumptions that market participants would use in pricing the asset or liability, including assumptions about risk and/or the risks inherent in the inputs to the valuation technique. These inputs can be readily observable, market-corroborated, or unobservable inputs. The Company utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. Based upon observable inputs used in the valuation techniques, the Company is required to provide information according to the fair value hierarchy. The fair value hierarchy ranks the quality and reliability of the information used to determine fair values into three broad levels as follows:

Level 1: Valuations for assets and liabilities traded in active markets from readily available pricing sources for market transactions involving identical assets or liabilities.

Level 2: Valuations for assets and liabilities traded in less active dealer or broker markets. Valuations are obtained from third-party pricing services for identical or similar assets or liabilities.

Level 3: Valuations incorporate certain assumptions and projections in determining the fair value assigned to such assets or liabilities.

In instances where the determination of the fair value measurement is based upon inputs from different levels of the fair value hierarchy, the level in the fair value hierarchy within which the entire fair value measurement falls is based upon the lowest level input that is significant to the fair value measurement in its entirety. The Company's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment, and considers factors specific to the asset or liability.

The following tables summarize the Company's financial liabilities measured at fair value on a recurring basis as of June 30, 2019 and December 31, 2018 (in thousands):

	Carrying Amount as of June 30, 2019	**Fair Value Measurements As of June 30, 2019**		
		Level 1	**Level 2**	**Level 3**
3.25% convertible senior notes due in 2020	$ 30,503	$ —	$ —	$ 30,503

JAKKS PACIFIC, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
June 30, 2019

	Carrying Amount as of December 31, 2018	Fair Value Measurements As of December 31, 2018		
		Level 1	Level 2	Level 3
3.25% convertible senior notes due in 2020	$ 27,974	$ —	$ —	$ 27,974

The following table provides a reconciliation of the beginning and ending balances of liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3) (in thousands):

	2019
Balance at January 1, 2019	$ 27,974
Change in fair value	2,529
Balance at June 30, 2019	$ 30,503

Note 17 — Liquidity

As of June 30, 2019 and December 31, 2018, the Company held cash and cash equivalents, including restricted cash, of $37.0 million and $58.2 million, respectively. Cash, and cash equivalents, including restricted cash held outside of the United States in various foreign subsidiaries totaled $21.8 million and $33.9 million as of June 30, 2019 and December 31, 2018, respectively. The cash and cash equivalents, including restricted cash balances in the Company's foreign subsidiaries have either been fully taxed in the U.S. or tax has been accounted for in connection with the Tax Cuts and Jobs Act, or may be eligible for a full foreign dividends received deduction under such Act, and thus would not be subject to additional U.S. tax should such amounts be repatriated in the form of dividends or deemed distributions. Any such repatriation may result in foreign withholding taxes, which the Company expects would not be significant as of June 30, 2019.The Company’s primary sources of working capital are cash flows from operations and borrowings under its credit facility (see Note 5 - Credit Facilities in the accompanying notes to the condensed consolidated financial statements for additional information).Typically, cash flows from operations are impacted by the effect on sales of (1) the appeal of the Company’s products, (2) the success of its licensed brands, (3) the highly competitive conditions existing in the toy industry, (4) dependency on a limited set of large customers, and (5) general economic conditions. A downturn in any single factor or a combination of factors could have a material adverse impact upon the Company’s ability to generate sufficient cash flows to operate the business. In addition, the Company’s business and liquidity are dependent to a significant degree on its vendors and their financial health, as well as the ability to accurately forecast the demand for products. The loss of a key vendor, or material changes in support by them, or a significant variance in actual demand compared to the forecast, can have a material adverse impact on the Company’s cash flows and business. Given the conditions in the toy industry environment in general, vendors, including licensors, may seek further assurances or take actions to protect against non-payment of amounts due to them. Changes in this area could have a material adverse impact on the Company’s liquidity.

Cash and cash equivalents, including restricted cash, projected cash flow from operations, and borrowings under the Company’s credit facility, as well as taking into account the August 2019 Recapitalization transaction (See Note 19 - Subsequent Event for further information), should be sufficient to meet working capital and capital expenditure requirements for the next 12 months. The Company’s ability to fund operations and retire debt when due is dependent on a number of factors, some of which are beyond the Company's control and/or inherently difficult to estimate, including the Company's future operating performance and the factors mentioned above, among other risks and uncertainties. To the extent we are unable to fund our operations or retire debt when due, no assurances can be given that the Company will have the financial resources required to obtain, or that the conditions of the capital markets will support, any future debt or equity financings which could have a material adverse impact on the Company’s business, results of operations and financial condition.

As of June 30, 2019, off-balance sheet arrangements include letters of credit issued by Wells Fargo of $9.5 million.

Note 18 — Leases

The Company determines if an arrangement is a lease at inception. Operating leases are included in operating lease right-of-use (“ROU”) assets and operating lease liabilities in its condensed consolidated balance sheets. The Company does not have any finance leases.

ROU assets represent the Company's right to use an underlying asset for the lease term and lease liabilities represent its obligation to make lease payments arising from the lease. Operating lease ROU assets and liabilities are recognized at commencement date based on the present value of lease payments over the lease term. As most of the Company’s leases do not provide an implicit interest rate, the Company uses its incremental borrowing rate based on the information available at commencement date in determining the present value of lease payments. The operating lease ROU asset also includes any prepaid lease amounts and excludes lease incentives. The Company’s lease terms may include options to extend or terminate the lease when it is reasonably certain that it will exercise that option. Lease expense for lease payments is recognized on a straight-line basis over the lease term.

The Company has lease agreements with lease and non-lease components, which are generally accounted for separately.

The Company has operating leases for corporate offices, warehouses, and certain equipment. The Company’s leases have remaining lease terms of 1 to 8 years, some of which include options to extend the lease for up to 10 years, and some of which include options to terminate the lease within 1 year. As of June 30, 2019, the Company’s weighted average remaining lease term is approximately 4 years and the weighted average discount rate used to calculate the Company’s lease liability is approximately 5.31%. For the three and six months ended June 30, 2019, rent expense under the Company's leases was approximately $3.6 million and $7.0 million, respectively. For the three and six months ended June 30, 2018, rent expense under the Company's leases was approximately $3.3 million and $6.6 million, respectively.

The following table represents a reconciliation of the Company’s undiscounted future minimum lease payments under operating leases to the lease liability as of June 30, 2019 (in thousands):

Year ending December 31,		
2019 (excluding the 6 months ended June 30, 2019)	$	5,756
2020		10,905
2021		10,598
2022		9,966
2023		5,499
Thereafter		773
Total lease payments		43,497
Less imputed interest		(4,486)
Total	$	39,011

Note 19 — Subsequent Event

As discussed in the Current Report on Form 8-K dated August 9, 2019, the Company entered into and consummated multiple, binding definitive agreements (collectively, the "Recapitalization") among Wells Fargo Bank, National Association, Oasis Investments II Master Fund Ltd. and an ad hoc group of holders of the 4.875% convertible senior notes due 2020 to recapitalize the Company's balance sheet, including the extension to the Company of incremental liquidity and three-year extensions of substantially all of the Company's outstanding convertible debt obligations and revolving credit facility. The Company's term loan agreement entered into with Great American Capital Partners has been paid in full in connection with the Recapitalization transaction.

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 our Condensed Consolidated Financial Statements and Notes thereto, which appear elsewhere herein.

Critical Accounting Policies and Estimates

The accompanying condensed consolidated financial statements and supplementary information were prepared in accordance with accounting principles generally accepted in the United States of America. Significant accounting policies are discussed in Note 2 to the Consolidated Financial Statements set forth in our Annual Report on Form 10-K for the fiscal year ended December 31, 2018. Inherent in the application of many of these accounting policies is the need for management to make estimates and judgments in the determination of certain revenues, expenses, assets and liabilities. As such, materially different financial results can occur as circumstances change and additional information becomes known. The policies with the greatest potential effect on our results of operations and financial position include:

Allowance for Doubtful Accounts. Our allowance for doubtful accounts is based upon management's assessment of the business environment, customers' financial condition, historical collection experience, accounts receivable aging, customer disputes and the collectability of specific customer accounts. If there were a deterioration of a major customer's creditworthiness, or actual defaults were higher than our historical experience, our estimates of the recoverability of amounts due to us could be overstated, which could have an adverse impact on our operating results. Our allowance for doubtful accounts is also affected by the time at which uncollectible accounts receivable balances are actually written off.

Major customers' accounts are monitored on an ongoing basis; more in-depth reviews are performed based upon changes in a customer's financial condition and/or the level of credit being extended. When a significant event occurs, such as a bankruptcy filing by a specific customer, and on a quarterly basis, the allowance is reviewed for adequacy and the balance or accrual rate is adjusted to reflect current risk prospects.

Revenue Recognition. Our contracts with customers only include one performance obligation (i.e., sale of our products). Revenue is recognized in the gross amount at a point in time when delivery is completed and control of the promised goods is transferred to the customers. Revenue is measured as the amount of consideration we expect to be entitled to in exchange for those goods. Our contracts do not involve financing elements as payment terms with customers are less than one year. Further, because revenue is recognized at the point in time goods are sold to customers, there are no contract assets or contract liability balances.

We disaggregate our revenues from contracts with customers by reporting segment: U.S. and Canada, International, and Halloween. We further disaggregate revenues by major geographic region.

We offer various discounts, pricing concessions, and other allowances to customers, all of which are considered in determining the transaction price. Certain discounts and allowances are fixed and determinable at the time of sale and are recorded at the time of sale as a reduction to revenue. Other discounts and allowances can vary and are determined at management's discretion (variable consideration). Specifically, we occasionally grant discretionary credits to facilitate markdowns and sales of slow moving merchandise, and consequently accrue an allowance based on historic credits and management estimates. Further, while we generally do not allow product returns, we do make occasional exceptions to this policy, and consequently record a sales return allowance based upon historic return amounts and management estimates. These allowances (variable consideration) are estimated using the expected value method and are recorded at the time of sale as a reduction to revenue. We adjust our estimate of variable consideration at least quarterly or when facts and circumstances used in the estimation process may change. The variable consideration is not constrained as we have sufficient history on the related estimates and do not believe there is a risk of significant revenue reversal.

We also participate in cooperative advertising arrangements with some customers, whereby we allow a discount from invoiced product amounts in exchange for customer purchased advertising that features our products. Generally, these allowances range from 1% to 20% of gross sales, and are generally based upon product purchases or specific advertising campaigns. Such allowances are accrued when the related revenue is recognized. These cooperative advertising arrangements provide a distinct benefit at fair value, and are accounted for as direct selling expenses.

Sales commissions are expensed when incurred as the related revenue is recognized at a point in time and therefore the amortization period is less than one year. As a result these costs are recorded as direct selling expenses, as incurred.

Shipping and handling activities are considered part of our obligation to transfer the products and therefore are recorded as direct selling expenses, as incurred.

Our reserve for sales returns and allowances amounted to $24.5 million as of June 30, 2019 and $29.4 million as of December 31, 2018.

Fair value measurements. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In determining fair value, we use various methods including market, income and cost approaches. Based upon these approaches, we often utilize certain assumptions that market participants would use in pricing the asset or liability, including assumptions about risk and/or the risks inherent in the inputs to the valuation technique. These inputs can be readily observable, market-corroborated, or unobservable inputs. We utilize valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. Based upon observable inputs used in the valuation techniques, we are required to provide information according to the fair value hierarchy. The fair value hierarchy ranks the quality and reliability of the information used to determine fair values into three broad levels as follows:

Level 1:	Valuations for assets and liabilities traded in active markets from readily available pricing sources for market transactions involving identical assets or liabilities.
Level 2:	Valuations for assets and liabilities traded in less active dealer or broker markets. Valuations are obtained from third-party pricing services for identical or similar assets or liabilities.
Level 3:	Valuations incorporate certain assumptions and projections in determining the fair value assigned to such assets or liabilities.

In instances where the determination of the fair value measurement is based upon inputs from different levels of the fair value hierarchy, the level in the fair value hierarchy within which the entire fair value measurement falls is based upon the lowest level input that is significant to the fair value measurement in its entirety. Our assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment, and considers factors specific to the asset or liability.

The following tables summarize our financial liabilities measured at fair value on a recurring basis as of June 30, 2019 and December 31, 2018 (in thousands):

	Carrying Amount as of June 30, 2019	Fair Value Measurements As of June 30, 2019		
		Level 1	Level 2	Level 3
3.25% convertible senior notes due in 2020	$ 30,503	$ —	$ —	$ 30,503

	Carrying Amount as of December 31, 2018	Fair Value Measurements As of December 31, 2018		
		Level 1	Level 2	Level 3
3.25% convertible senior notes due in 2020	$ 27,974	$ —	$ —	$ 27,974

The following table provides a reconciliation of the beginning and ending balances of liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3) (in thousands):

	2019
Balance at January 1, 2019	$ 27,974
Change in fair value	2,529
Balance at June 30, 2019	$ 30,503

Our accounts receivable, accounts payable and accrued expenses represent financial instruments. The carrying value of these financial instruments is a reasonable approximation of fair value.

In August 2017, we agreed with Oasis Management and Oasis Investments II Master Fund Ltd., (collectively "Oasis") the holder of approximately $21.5 million face amount of our 4.25% convertible senior notes due in 2018 (“2018 Notes”), to exchange and extend the maturity date of these notes to November 1, 2020. In addition, the interest rate was reduced to 3.25% per annum and the conversion rate was increased to 328.0302 shares of our common stock per $1,000 principal amount of notes, among other things. These notes are hereafter referred to as the “3.25% convertible senior notes due in 2020” or “3.25% 2020 Notes.” After execution of a definitive agreement and final approval by the other members of our Board of Directors and Oasis’ Investment Committee, the transaction closed on November 7, 2017. On July 26, 2018, we closed a transaction with Oasis to exchange $8.0 million face amount of the 4.25% convertible senior notes due in August 2018 with convertible senior notes similar to those issued to Oasis in November 2017. The new notes mature on November 1, 2020, accrue interest at an annual rate of 3.25% and are convertible into shares of our common stock at a rate of 322.2688 shares per $1,000 principal amount of the new notes. The conversion price of the 3.25% 2020 notes reset on November 1, 2018 to $2.54 per share and the conversion rate was increased to 393.7008 of our common stock per $1,000 principal amount of notes.

In connection with these transactions, we elected the fair value option of measurement for the 3.25% 2020 Notes under ASC 815 *Derivatives and Hedging*. As a result, these notes are re-measured each reporting period using Level 3 inputs (Monte Carlo simulation model and inputs for stock price, risk-free rate and volatility), with changes in fair value reflected in current period earnings in our condensed consolidated statements of operations. We evaluated our credit risk as of June 30, 2019, and determined that there was no change from December 31, 2018. At June 30, 2019, the 3.25% 2020 Notes had a fair value of $30.5 million.

The fair value of the 4.875% convertible senior notes payable due 2020 as of June 30, 2019 and December 31, 2018 was $102.5 million and $93.2 million, respectively, based upon the most recent quoted market prices. The fair values of the convertible senior notes are considered to be Level 3 measurements on the fair value hierarchy.

For the six months ended June 30, 2019, there was no impairment to the value of the Company’s non-financial assets.

Goodwill and other indefinite-lived intangible assets. Goodwill and indefinite-lived intangible assets are not amortized, but are tested for impairment at least annually at the reporting unit level.

Factors we consider important that could trigger an impairment review include the following:

- significant underperformance relative to expected historical or projected future operating results;
- significant changes in the manner of our use of the acquired assets or the strategy for our overall business; and
- significant negative industry or economic trends.

Due to the subjective nature of the impairment analysis, significant changes in the assumptions used to develop the estimate could materially affect the conclusion regarding the future cash flows necessary to support the valuation of long-lived assets, including goodwill. The valuation of goodwill involves a high degree of judgment. Based upon the assumptions underlying the valuation, impairment is determined by estimating the fair value of a reporting unit and comparing that value to the reporting unit’s book value. If the implied fair value is more than the book value of the reporting unit, an impairment loss is not indicated. If impairment exists, the fair value of the reporting unit is allocated to all of its assets and liabilities excluding goodwill, with the excess amount representing the fair value of goodwill. An impairment loss is measured as the amount by which the book value of the reporting unit’s goodwill exceeds the estimated fair value of that goodwill. Based on our April 1 annual assessment, we determined the fair values of our reporting units were not less than the carrying amounts. No goodwill impairment was determined to have occurred for the six months ended June 30, 2019.

Reserve for Inventory Obsolescence. We value our inventory at the lower of cost or net realizable value. Based upon a consideration of quantities on hand, actual and projected sales volume, anticipated product selling prices and product lines planned to be discontinued, slow-moving and obsolete inventory is written down to its net realizable value.

Failure to accurately predict and respond to consumer demand could result in us under-producing popular items or over-producing less popular items. Furthermore, significant changes in demand for our products would impact management’s estimates in establishing our inventory provision.

Management’s estimates are monitored on a quarterly basis, and a further adjustment to reduce inventory to its net realizable value is recorded as an increase to cost of sales when deemed necessary under the lower of cost or net realizable value standard.

Discrete Items for Income Taxes. The discrete tax expense recorded in the six months ended June 30, 2019 is $0.1 million which is primarily related to excess tax deficiencies fully offset by valuation allowance, return to provision adjustments for foreign jurisdictions, state income taxes, and change in uncertain tax positions. For the comparable period in 2018, a discrete tax benefit was recorded for return to provision adjustments for foreign jurisdictions, change in uncertain tax positions, and excess tax deficiencies fully offset by valuation allowance.

Income taxes and interest and penalties related to income tax payable. We do not file a consolidated return for our foreign subsidiaries. We file federal and state returns and our foreign subsidiaries each file returns as required. Deferred taxes are provided on an asset and liability method, whereby deferred tax assets are recognized as deductible temporary differences and operating loss and tax credit carry-forwards and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some or all of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment.

Management employs a threshold and measurement process for recording in the financial statements uncertain tax positions taken or expected to be taken in a tax return. Tax benefits that are subject to challenge by tax authorities are analyzed and accounted for in the income tax provision.

We accrue a tax reserve for additional income taxes, which may become payable in future years as a result of audit adjustments by tax authorities. The reserve is based upon management's assessment of all relevant information and is periodically reviewed and adjusted as circumstances warrant. As of June 30, 2019 and December 31, 2018, our income tax reserves were approximately $1.5 million and $1.5 million, respectively. The $1.5 million balance primarily relates to the potential tax settlements in Hong Kong and adjustments in the area of withholding taxes. Our income tax reserves are included in income taxes payable on the Condensed Consolidated Balance Sheets and within provision for (benefit from) income taxes on the Condensed Consolidated Statements of Operations and Comprehensive Loss.

Share-Based Compensation**.** We grant restricted stock units and awards to our employees (including officers) and to non-employee directors under our 2002 Stock Award and Incentive Plan (the "Plan"), as amended. The benefits provided under the Plan are share-based payments. We amortize over a requisite service period, the net total deferred restricted stock expense based upon the fair value of the underlying common stock on the date of the grants. In certain instances, the service period may differ from the period in which each award will vest. Additionally, certain groups of grants are subject to performance criteria and/or an expected forfeiture rate calculation.

New Accounting Pronouncements

In May 2014, the FASB issued ASU 2014-09, "Revenue from Contracts with Customers (Topic 606)," which supersedes the revenue recognition requirements in ASC 605, (Topic 605), and most industry-specific guidance. Under the new model, recognition of revenue occurs when a customer obtains control of promised goods or services in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In addition, the new standard requires that reporting companies disclose the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. In August 2015, the FASB issued ASU 2015-14, "Revenue from Contracts with Customers - Deferral of the Effective Date," which defers the effective date of ASU 2014-09 to annual reporting periods beginning after December 15, 2017, and interim periods therein. In 2016, the FASB issued ASU 2016-08, "Principal versus Agent Considerations (Reporting Revenue Gross versus Net)," ASU 2016-10, "Identifying Performance Obligations and Licensing," and ASU 2016-12, "Revenue from Contracts with Customers - Narrow-Scope Improvements and Practical Expedients." Entities have the choice to adopt these updates using either of the following transition methods: (i) a full retrospective approach reflecting the application of the standard in each prior reporting period with the option to elect certain practical expedients, or (ii) a modified retrospective approach with the cumulative effect of these standards recognized at the date of the adoption.

On January 1, 2018, we adopted the new accounting standard ASC 606, (Topic 606), Revenue from Contracts with Customers and all the related amendments ("new revenue standard") using the modified retrospective method applied to those contracts which were not completed as of January 1, 2018. Results for reporting periods beginning after January 1, 2018 are presented under Topic 606, while prior period amounts are not adjusted and continue to be reported in accordance with our historic accounting under ASC 605, (Topic 605).

There is no impact to our condensed consolidated financial statements resulting from the adoption of Topic 606 as the timing and measurement of revenue remained consistent with Topic 605, although our approach to revenue recognition is now based on the transfer of control. Further, there is no difference in the amounts of the revenue and cost of sales reported in our condensed consolidated statements of operations and comprehensive loss for the three and six months ended June 30, 2019 and 2018 that were recognized pursuant to Topic 606 and those that would have been reported pursuant to Topic 605.

In January 2016, the FASB issued ASU 2016-01, “Financial Instruments - Overall: Recognition and Measurement of Financial Assets and Financial Liabilities,” (“ASU 2016-01”). The new guidance is intended to improve the recognition and measurement of financial instruments. The ASU is effective for fiscal years and interim periods within those years beginning after December 15, 2017. The adoption of this standard did not have an impact on our condensed consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, “Leases.” ASU 2016-02 establishes a right-of-use (“ROU”) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the statement of operations. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted. A modified retrospective transition approach is required, applying the new standard to all leases existing at the date of initial application. An entity may choose to use either (1) its effective date or (2) the beginning of the earliest comparative period presented in the financial statements as its date of initial application. If an entity chooses the second option, the transition requirements for existing leases also apply to leases entered into between the date of initial application and the effective date. The entity must also recast its comparative period financial statements and provide the disclosures required by the new standard for the comparative periods. On January 1, 2019, we adopted the new standard and use the effective date as our date of initial application. Consequently, financial information will not be updated and the disclosures required under the new standard will not be provided for dates and periods before January 1, 2019. The new standard provides a number of optional practical expedients in transition. We elected certain practical expedients, which permits us not to reassess under the new standard our prior conclusions about lease identification, lease classification and initial direct costs. We did not elect the use-of-hindsight or the practical expedient pertaining to land easements; the latter not being applicable to us.

On adoption, we recognized operating lease liabilities of approximately $40.8 million with corresponding ROU assets of $37.6 million based on the present value of the remaining minimum rental payments for existing operating leases. We also derecognized deferred rent liabilities of $4.3 million and prepaid rent of $1.1 million upon the recognition of lease liabilities and ROU assets.

In October 2016, the FASB issued ASU 2016-16, “Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other than Inventory.” The amendments in this ASU reduce the complexity in the accounting standards by allowing the recognition of current and deferred income taxes for an intra-entity asset transfer, other than inventory, when the transfer occurs. Historically, recognition of the income tax consequence was not recognized until the asset was sold to an outside party. This ASU is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017. The adoption of this standard did not have an impact on our condensed consolidated financial statements.

In May 2017, the FASB issued ASU 2017-09, “Compensation - Stock Compensation (Topic 718): Scope of Modification Accounting,” which clarifies when to account for a change to the terms or conditions of a share-based payment award as a modification. Under the new guidance, modification accounting is required only if the fair value, vesting conditions, or the classification of the award (as equity or liability) changes as a result of the change in terms or conditions. ASU 2017-09 is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The adoption of this standard did not have an impact on our condensed consolidated financial statements.

In January 2018, the FASB issued ASU 2018-02, “Income Statement - Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income,” which gives entities the option to reclassify to retained earnings the tax effects resulting from the U.S. Tax Cuts and Jobs Act ("The Act") related to items in Accumulated Other Comprehensive Income (“AOCI”) that the FASB refers to as having been stranded in AOCI. The new guidance may be applied retrospectively to each period in which the effect of the Act is recognized in the period of adoption. We could adopt this guidance for fiscal years beginning after December 15, 2018 and interim periods within those fiscal years. Early adoption is permitted for periods for which financial statements have not yet been issued or made available for issuance, including the period the Act was enacted. The guidance, when adopted, will require new disclosures regarding a company’s accounting policy for releasing the tax effects in AOCI and permit the company the option to reclassify to retained earnings the tax effects resulting from the Act that are stranded in AOCI. We adopted this guidance on January 1, 2019 and the impact was not material.

In March 2018, the FASB issued ASU 2018-03, “Technical Corrections and Improvements to Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities,” which made targeted improvements to address certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. The ASU is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years beginning after June 15, 2018. The adoption of this standard did not have an impact on our condensed consolidated financial statements.

In June 2018, the FASB issued ASU 2018-07, “Improvements to Nonemployee Share-Based Payment Accounting,” which supersedes most of the prior accounting guidance on nonemployee share-based payments, and instead aligns it with existing guidance on employee share-based payments in Topic 718. The new standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years, and early adoption is permitted. The adoption of this standard did not have an impact on our condensed consolidated financial statements.

In August 2018, the FASB issued ASU 2018-13, “Disclosure Framework - Changes to the Disclosure Requirements for Fair Value Measurement,” which improves the effectiveness of the disclosures required under ASC 820 and modifies the disclosure requirements on fair value measurements, including the consideration of costs and benefits. The new standard is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years, and early adoption is permitted. We are currently evaluating the impact of the pending adoption of this new standard on our condensed consolidated financial statements.

In October 2018, the FASB issued ASU 2018-17, "Consolidation: Targeted Improvements to Related Party Guidance for Variable Interest Entities," which improves the accounting for variable interest entities by considering indirect interests held through related parties under common control for determining whether fees paid to decision makers and service providers are variable interests. This new standard is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. The amendments are required to be applied retrospectively with a cumulative-effect adjustment to retained earnings at the beginning of the earliest period presented. Early adoption is permitted. We are currently evaluating the impact of the pending adoption of this new standard on our condensed consolidated financial statements.

Results of Operations

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

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	**2018**	**2019**	**2018**
Net sales	100.0 %	100.0 %	100.0 %	100.0 %
Cost of sales	81.4	73.6	80.7	74.4
Gross profit	18.6	26.4	19.3	25.6
Selling, general and administrative expenses	35.6	37.6	41.6	49.4
Restructuring charge	—	—	0.2	—
Acquisition related and other	2.6	0.3	3.2	0.2
Loss from operations	(19.6)	(11.5)	(25.7)	(24.0)
Income from joint ventures	—	0.3	—	0.1
Other income (expense), net	(0.3)	—	(0.1)	—
Change in fair value of convertible senior notes	(0.1)	(2.3)	(1.5)	(1.7)
Interest income	—	—	—	—
Interest expense	(3.0)	(2.1)	(3.6)	(2.1)
Loss before provision for (benefit from) income taxes	(23.0)	(15.6)	(30.9)	(27.7)
Provision for (benefit from) income taxes	0.6	2.0	0.2	(0.1)
Net loss	(23.6)	(17.6)	(31.1)	(27.6)
Net income (loss) attributable to non-controlling interests	0.1	—	—	—
Net loss attributable to JAKKS Pacific, Inc.	(23.7)%	(17.6)%	(31.1)%	(27.6)%

The following unaudited table summarizes, for the periods indicated, certain statements of operations data by segment (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
Net Sales				
U.S. and Canada	$ 48,502	$ 59,381	$ 105,935	$ 129,916
International	10,293	22,044	20,046	39,343
Halloween	36,387	24,356	40,027	29,526
	95,182	105,781	166,008	198,785
Cost of Sales				
U.S. and Canada	40,271	41,947	84,558	93,589
International	8,547	15,711	17,559	29,536
Halloween	28,618	20,182	31,805	24,760
	77,436	77,840	133,922	147,885
Gross Profit				
U.S. and Canada	8,231	17,434	21,377	36,327
International	1,746	6,333	2,487	9,807
Halloween	7,769	4,174	8,222	4,766
	$ 17,746	$ 27,941	$ 32,086	$ 50,900

Comparison of the Three Months Ended June 30, 2019 and 2018

Net Sales

U.S. and Canada. Net sales of our U.S. and Canada segment were $48.5 million for the three months ended June 30, 2019 compared to $59.4 million for the prior year period, representing a decrease of $10.9 million, or 18.4%. The decrease in net sales was primarily due to lower sales of Incredibles 2 and Squish-Dee-Lish, partially offset by higher sales of Aladdin and Godzilla products, which were not sold in the prior year period.

International. Net sales of our International segment were $10.3 million for the three months ended June 30, 2019 compared to $22.0 million for the prior year period, representing a decrease of $11.7 million, or 53.2%. The decrease in net sales was primarily driven by declines in sales of Incredibles 2, Squish-Dee-Lish and Disney Princess. These declines were partially offset by an increase in sales of Perfectly Cute and Harry Potter, in addition to sales of Aladdin, Godzilla and Who's your Llama products, which were not sold in the prior year period.

Halloween. Net sales of our Halloween segment were $36.4 million for the three months ended June 30, 2019 compared to $24.4 million for the prior year period, representing an increase of $12.0 million, or 49.2%. The increase in net sales was primarily driven by an increase in sales of Toy Story 4 products, which were not sold in the prior year period, in addition to an increase in sales of Disney Princess and Frozen products.

Cost of Sales

U.S. and Canada. Cost of sales of our U.S. and Canada segment was $40.3 million, or 83.1% of related net sales for the three months ended June 30, 2019 compared to $41.9 million, or 70.5% of related net sales for the prior year period, representing a decrease of $1.6 million, or 3.8%. The decrease in dollars is due to lower overall sales in 2019. The increase as a percentage of net sales, year over year, is due to a higher average cost of goods sold rate resulting from a shift in product mix, as well as close-out sales of older brands. Additionally, an increase in average royalty rates due to the change in product mix from the corresponding period in 2018 has also contributed to the percentage increase in cost of goods sold.

International. Cost of sales of our International segment was $8.5 million, or 82.5% of related net sales for the three months ended June 30, 2019 compared to $15.7 million, or 71.4% of related net sales for the prior year period, representing a decrease of $7.2 million, or 45.9%. The decrease in dollars is due to lower overall sales in 2019. The increase as a percent of net sales is due to a higher cost of goods sold rate in 2019 due to a change in product mix, as well as close-out sales of older brands.

Halloween. Cost of sales of our Halloween segment was $28.6 million, or 78.6% of related net sales for the three months ended June 30, 2019 compared to $20.2 million, or 82.8% of related net sales for the prior year period, representing an increase of $8.4 million, or 41.6%. The increase in dollars is due to an increase in overall unit sales in 2019. The decrease as a percentage of net sales, year-over-year, is primarily due to a lower cost of goods sold rate and average royalty rate due to product mix.

Selling, General and Administrative Expenses

Selling, general and administrative expenses were $33.9 million for the three months ended June 30, 2019 compared to $39.8 million for the prior year period constituting 35.6% and 37.6% of net sales, respectively. Selling, general and administrative expenses decreased by $5.9 million from the prior year period primarily driven by lower payroll expense due, in part, to a Company-wide restructuring initiative, lower marketing expense and a decrease in product development costs from the prior year period.

Restructuring Charge

During the three months ended June 30, 2019, we recognized $22,000 of restructuring charges as a result of a Company-wide restructuring initiative announced in the 2018 fourth quarter.

Acquisition Related and Other

During the three months ended June 30, 2019, we recognized $2.5 million in acquisition related and other charges as a result of our ongoing evaluation and negotiation of a strategic and/or re-financing transaction, including Hong Kong Meisheng Cultural Company Limited's expression of interest in acquiring additional shares of our common stock and the refinancing of our convertible senior notes due in 2020.

Interest Expense

Interest expense was $2.9 million for the three months ended June 30, 2019, as compared to $2.2 million in the prior year period. During the three months ended June 30, 2019, we booked interest expense of $1.6 million related to our convertible senior notes due in 2020, and $1.1 million related to our revolving credit and term loan facilities. During the three months ended June 30, 2018, we booked interest expense of $1.7 million related to our convertible senior notes payable due in 2018 and 2020, $0.2 million related to our revolving credit and term loan facilities.

Provision for (Benefit From) Income Taxes

Our income tax expense, which includes federal, state and foreign income taxes and discrete items, was $0.6 million, or an effective tax rate of (2.7%), for the three months ended June 30, 2019. During the comparable period in 2018, our income tax expense was $2.1 million, or an effective tax rate of (12.7%).

Comparison of the Six Months Ended June 30, 2019 and 2018

Net Sales

U.S. and Canada. Net sales of our U.S. and Canada segment were $105.9 million for the six months ended June 30, 2019 compared to $129.9 million for the prior year period, representing a decrease of $24.0 million, or 18.5%. The decrease in net sales was driven by the liquidation of Toys "R" Us in the U.S. in 2018 with sales declining by approximately $9.5 million in 2019 as well as a decrease in net sales of Incredibles 2 and Squish-Dee-Lish, partially offset by higher sales of Aladdin and Godzilla products, which were not sold in the prior year period.

International. Net sales of our International segment were $20.0 million for the six months ended June 30, 2019 compared to $39.3 million for the prior year period, representing a decrease of $19.3 million, or 49.1%. The decrease in net sales was primarily driven by declines in sales of Incredibles 2, Squish-Dee-Lish and Disney Princess. These declines were partially offset by an increase in sales of Harry Potter products, in addition to an increase in sales of Aladdin, Godzilla and Who’s your Llama products, which were not sold in the prior year period.

Halloween. Net sales of our Halloween segment were $40.0 million for the six months ended June 30, 2019 compared to $29.5 million for the prior year period, representing an increase of $10.5 million, or 35.6%. The increase in net sales was primarily driven by an increase in sales of Toy Story 4 products, which were not sold in the prior year period, in addition to an increase in sales of Disney Princess and a variety of other products in 2019.

Cost of Sales

U.S. and Canada. Cost of sales of our U.S. and Canada segment was $84.6 million, or 79.9% of related net sales for the six months ended June 30, 2019 compared to $93.6 million, or 72.1% of related net sales for the prior year period, representing a decrease of $9.0 million, or 9.6%. The decrease in dollars is due to lower overall sales in 2019. The increase as a percentage of net sales, year over year, is due to a higher average cost of goods sold rate resulting from a shift in product mix, and higher excess and obsolescence charges.

International. Cost of sales of our International segment was $17.6 million, or 88.0% of related net sales for the six months ended June 30, 2019 compared to $29.5 million, or 75.1% of related net sales for the prior year period, representing a decrease of $11.9 million, or 40.3%. The decrease in dollars is due to lower overall sales in 2019. The increase as a percentage of net sales is due to a higher cost of goods sold rate in 2019 due to a change in product mix, and higher excess and obsolescence charges.

Halloween. Cost of sales of our Halloween segment was $31.8 million, or 79.5% of related net sales for the six months ended June 30, 2019 compared to $24.8 million, or 84.1% of related net sales for the prior year period, representing an increase of $7.0 million, or 28.2%. The increase in dollars is due to an increase in overall unit sales in 2019. The decrease as a percentage of net sales, year-over-year, is primarily due to a lower cost of goods sold rate due to product mix.

Selling, General and Administrative Expenses

Selling, general and administrative expenses were $69.1 million for the six months ended June 30, 2019 compared to $98.4 million for the prior year period constituting 41.6% and 49.4% of net sales, respectively. Selling, general and administrative expenses decreased by $29.3 million from the prior year period primarily driven by lower payroll expense due, in part, to a Company-wide restructuring initiative, lower marketing expense, lower product development costs and a bad debt charge of $12.5 million primarily due to the Toys “R” Us liquidation in the U.S. in 2018.

Restructuring Charge

During the six months ended June 30, 2019, we recognized $0.3 million of restructuring charges as a result of a Company-wide restructuring initiative. The restructuring charges are primarily related to employee severance costs.

Acquisition Related and Other

During the six months ended June 30, 2019, we recognized $5.4 million in acquisition related and other charges as a result of our ongoing evaluation and negotiation of a strategic and/or refinancing transaction, including Hong Kong Meisheng Cultural Company Limited's expression of interest in acquiring additional shares of our common stock and the refinancing of our convertible senior notes due in 2020.

Interest Expense

Interest expense was $5.9 million for the six months ended June 30, 2019, as compared to $4.1 million in the prior year period. During the six months ended June 30, 2019, we booked interest expense of $3.2 million related to our convertible senior notes due in 2020, and $1.8 million related to our revolving credit and term loan facilities. During the six months ended June 30, 2018, we booked interest expense of $3.6 million related to our convertible senior notes payable due in 2018 and 2020 and $0.4 million related to our revolving credit and term loan facilities.

Provision for (Benefit From) Income Taxes

Our income tax expense, which includes federal, state and foreign income taxes and discrete items, was $0.3 million, or an effective tax rate of (0.7%), for the six months ended June 30, 2019. During the comparable period in 2018, our income tax benefit was $0.2 million, or an effective tax rate of 0.4%.

Seasonality and Backlog

The retail toy industry is inherently seasonal. Generally, our sales have been highest during the third and fourth quarters, and collections for those sales have been highest during the succeeding fourth and first quarters. Our working capital needs have been highest during the second and third quarters.

While we have taken steps to level sales over the entire year, sales are expected to remain heavily influenced by the seasonality of our toy and Halloween products. The result of these seasonal patterns is that operating results and the demand for working capital may vary significantly by quarter. Orders placed with us are generally cancelable until the date of shipment. The combination of seasonal demand and the potential for order cancellation makes accurate forecasting of future sales difficult and causes us to believe that backlog may not be an accurate indicator of our future sales. Similarly, financial results for a particular quarter may not be indicative of results for the entire year.

Liquidity and Capital Resources

As of June 30, 2019, and taking into consideration the Recapitalization transaction (see Note 19 - Subsequent Event), we had working capital of $70.6 million, compared to $106.0 million as of December 31, 2018. The decrease was primarily attributable to the net loss and a lower accounts receivable balance, partially offset by the reclassification of the GACP term loan from short term to long term.

Operating activities used net cash of $8.9 million in the six months ended June 30, 2019, as compared to a net use of cash of $8.7 million in the prior year period. Net cash during the six months ended June 30, 2019 was primarily impacted by a decrease in accounts receivable and an increase in accounts payable and accrued expenses, partially offset by an increase in prepaid and other assets and a decrease in the reserve for sales returns and allowances. Net cash during the six months ended June 30, 2018 was primarily impacted by a decrease in accounts receivable and an increase in accounts payable, partially offset by an increase in prepaid expenses and other assets. Other than open purchase orders issued in the normal course of business related to shipped product, we have no obligations to purchase inventory from our manufacturers. However, we may incur costs or other losses as a result of not placing orders consistent with our forecasts for product manufactured by our suppliers or manufacturers for a variety of reasons including customer order cancellations or a decline in demand. As part of our strategy to develop and market new products, we have entered into various character and product licenses with royalties generally ranging from 1% to 21% payable on net sales of such products. As of June 30, 2019, these agreements required future aggregate minimum royalty guarantees of $72.9 million, exclusive of $36.8 million in advances already paid. Of this $72.9 million future minimum royalty guarantee, $38.8 million is due over the next twelve months.

Our investing activities used net cash of $5.2 million in the six months ended June 30, 2019, as compared to using net cash of $6.5 million in the prior year period, and consisted primarily of cash paid for the purchase of molds and tooling used in the manufacture of our products.

Our financing activities used net cash of $7.9 million for the six months ended June 30, 2019, primarily consisting of the repayment of credit facility borrowings. Our financing activities provided net cash of $13.4 million in the prior year period, primarily consisting of the net proceeds from our term loan, partially offset by repayment of credit facility borrowings.

In March 2014, we and our domestic subsidiaries entered into a secured credit facility with General Electric Capital Corporation ("GECC"). The credit facility, as amended and subsequently assigned to Wells Fargo Bank, N.A. ("Wells Fargo") pursuant to its acquisition of GECC, provides for a $75.0 million revolving credit facility subject to availability based on prescribed advance rates on certain domestic accounts receivable and inventory amounts used to compute the borrowing base (the "Credit Facility"). The Credit Facility includes a sub-limit of up to $35.0 million for the issuance of letters of credit. The amounts outstanding under the Credit Facility, as amended, were payable in full upon maturity of the facility on September 27, 2019, except that the Credit Facility would mature on June 15, 2018 if we did not refinance or extend the maturity of the convertible senior notes that mature in 2018, provided that any such refinancing or extension shall have a maturity date that is no sooner than six months after the stated maturity of the Credit Facility (i.e., on or about September 27, 2019). On June 14, 2018, we entered into a Term Loan Agreement with Great American Capital Partners to provide the necessary capital to refinance the 2018 convertible senior notes (see additional details regarding the Term Loan Agreement below). In addition, on June 14, 2018, we revised certain of the Credit Facility documents (and entered into new ones) so that certain of our Hong Kong based subsidiaries became additional parties to the Credit Facility. As a result, the receivables of these subsidiaries can now be included in the borrowing base computation, subject to certain limitations, thereby effectively increasing the amount of funds we can borrow under the Credit Facility. Any additional borrowings under the Credit Facility will be used for general working capital purposes.

The Credit Facility is secured by a security interest in favor of Wells Fargo covering a substantial amount of the consolidated assets and a pledge of the majority of the capital stock of various of our subsidiaries. As of June 30, 2019, there were no outstanding borrowings and the amount of outstanding stand-by letters of credit totaled $9.5 million; the total excess borrowing capacity was $19.3 million. As of December 31, 2018, the amount of outstanding borrowings was $7.5 million and outstanding stand-by letters of credit totaled $12.8 million; the total excess borrowing capacity was $40.7 million. In July 2019, we borrowed $5.0 million under the Credit Facility.

Our ability to borrow under the Credit Facility is also subject to our ongoing compliance with certain financial covenants, including the maintenance of a fixed charge coverage ratio of at least 1.25:1.0 based on the trailing four fiscal quarters in the event minimum excess availability of $10.0 million under the Credit Facility is not maintained. As of June 30, 2019, we were in compliance with the financial covenants under the Credit Facility.

We may borrow funds at LIBOR or at a Base Rate, plus applicable margins of 225 basis point spread over LIBOR and 125 basis point spread on Base Rate loans. The Base Rate is the highest of (i) the Federal Funds Rate plus a margin of 0.50%, (ii) the rate last quoted by The Wall Street Journal as the "Prime Rate," or (iii) the sum of a LIBOR rate plus 1.00%. In addition to standard fees, the Credit Facility has an unused credit line fee, which ranges from 25 to 50 basis points. As of June 30, 2019 and December 31, 2018, the weighted average interest rate on the Credit Facility was approximately 4.77% and 5.53%, respectively.

The Credit Facility also contains customary events of default, including a cross default provision and a change of control provision. In the event of a default, all of our obligations and the obligations of our subsidiaries under the Credit Facility may be declared immediately due and payable. For certain events of default relating to insolvency and receivership, all outstanding obligations become due and payable.

On June 14, 2018, we entered into a Term Loan Agreement, Term Note, Guaranty and Security Agreement and other ancillary documents and agreements (the "Term Loan") with Great American Capital Partners Finance Co., LLC ("GACP"), for itself as a Lender (as defined below) and as the agent (in such capacity, "Agent") for the Lenders from time to time party to the Term Loan (collectively, "Lenders") and the other "Secured Parties" under and as defined therein, with respect to the issuance to us by Lenders of a $20.0 million term loan. To secure our obligations under the Term Loan, we granted to Agent, for the benefit of the Secured Parties, a security interest in a substantial amount of our consolidated assets and a pledge of the majority of the capital stock of various of our subsidiaries. The Term Loan is a secured obligation, second only to the Credit Facility with Wells Fargo, except with respect to certain of our inventory in which GACP has a priority secured position. We may use the funds from the Term Loan to repurchase or retire our outstanding convertible senior notes due August 2018, for working capital, capital expenditures and other general corporate purposes, subject to certain negative covenants set forth in the Term Loan.

The Term Loan requires the repayment of principal in the amount of 10% of the outstanding Term Loan per year (payable monthly) beginning after the first anniversary. All then-outstanding borrowings under the Term Loan are due, and the Term Loan terminates, no later than June 14, 2021, unless sooner terminated in accordance with its terms, which includes the date of termination of the Wells Fargo Credit Facility and the date that is 91 days prior to the maturity of our various convertible senior notes due in 2020. We are permitted, and may be required under certain circumstances as set forth in the Term Loan documents, to prepay the Term Loan, which would require a prepayment fee (i) in year one of up to any unearned and unpaid interest that would have become due and payable in year one had the prepayment not occurred plus 2% of the initial amount of the Term Loan (i.e., $20.0 million), (ii) in year two of 2% of the initial amount of the Term Loan and (iii) in year three of 1% of the initial amount of the Term Loan.

Our ability to continue to borrow the initial Term Loan amount of $20.0 million is based on certain accounts receivable and inventory amounts used to compute the borrowing base. In the event the Term Loan balance exceeds the borrowing base computation, the shortfall would be (i) applied to any excess availability under the Wells Fargo Credit Facility or (ii) prepaid. Similar to the Wells Fargo Credit Facility, we are subject to ongoing compliance with certain financial covenants, including the maintenance of a fixed charge coverage ratio of at least 1.25:1.0 based on the trailing four fiscal quarters in the event minimum excess availability of $10.0 million under the Wells Fargo Credit Facility is not maintained. We must also maintain a minimum amount of liquidity, as defined in the Term Loan, of $10.0 million. As of June 30, 2019, we were in compliance with the financial covenants under the Term Loan.

The Term Loan is accelerated and becomes immediately due and payable (and the Term Loan terminates) in the event of a default under the Term Loan which includes, among other things, breach of certain covenants or representations contained in the Term Loan documents, defaults under other loans or obligations, involvement in bankruptcy proceedings or an occurrence of a change of control (as such terms are defined in the Term Loan). The Term Loan Documents also contain negative covenants which, during the life of the Term Loan, prohibit and/or limit us from, among other things, incurring certain types of other debt, acquiring other companies, making certain expenditures or investments and changing the character of our business.

As of June 30, 2019 and December 31, 2018, the amount outstanding under the Term Loan was $19.8 million and $20.0 million, respectively. Borrowings under the Term Loan accrue interest at LIBOR plus 9.00% per annum. As of June 30, 2019 and December 31, 2018, the weighted average interest rate on the Term Loan was approximately 11.5% and 11.1%, respectively.

Amortization expense classified as interest expense related to the $1.3 million debt issuance costs associated with the transactions that closed on June 14, 2018 (i.e., the amendment of the Wells Fargo Credit Facility and the GACP Term Loan) was nil and $0.4 million for the three and six months ended June 30, 2019 and $0.1 million for the three and six months ended June 30, 2018.

In July 2013, we sold an aggregate of $100.0 million principal amount of 4.25% convertible senior notes due 2018 (the “2018 Notes”). The 2018 Notes, which were senior unsecured obligations, paid interest semi-annually in arrears on August 1 and February 1 of each year at a rate of 4.25% per annum and matured on August 1, 2018. The initial conversion rate for the 2018 Notes was 114.3674 shares of our common stock per $1,000 principal amount of notes, equivalent to an initial conversion price of approximately $8.74 per share of common stock, subject to adjustment in certain events. In 2016, we repurchased and retired an aggregate of approximately $6.1 million principal amount of the 2018 Notes. In 2017, we exchanged and retired $39.1 million principal amount of the 2018 Notes at par for $24.1 million in cash and approximately 2.9 million shares of our common stock. During the second quarter of 2017, we exchanged and retired $12.0 million principal amount of the 2018 Notes at par for $11.6 million in cash and 112,400 shares of our common stock.

In August 2017, we agreed with Oasis Management and Oasis Investments II Master Fund Ltd., (collectively, “Oasis”) the holder of approximately $21.5 million face amount of our 4.25% convertible senior notes due in 2018, to extend the maturity date of these notes to November 1, 2020. In addition, the interest rate was reduced to 3.25% per annum and the conversion rate was increased to 328.0302 shares of our common stock per $1,000 principal amount of notes, among other things. After execution of a definitive agreement for the modification and final approval by the other members of our Board of Directors and Oasis’ Investment Committee the transaction closed on November 7, 2017. On July 26, 2018, we closed a transaction with Oasis to exchange $8.0 million face amount of the 4.25% convertible senior notes due in August 2018 with convertible senior notes similar to those issued to Oasis in November 2017. The new notes mature on November 1, 2020, accrue interest at an annual rate of 3.25% and are convertible into shares of our common stock at an initial rate of 322.2688 shares per $1,000 principal amount of the new notes. The conversion price for the 3.25% convertible senior notes was reset on November 1, 2018 and will be reset on November 1, 2019 (each, a “reset date”) to a price equal to 105% above the 5-day Volume Weighted Average Price ("VWAP") preceding the reset date; provided, however, among other reset restrictions, that if the conversion price resulting from such reset is lower than 90 percent of the average VWAP during the 90 calendar days preceding the reset date, then the reset price shall be the 30-day VWAP preceding the reset date. The conversion price of the 3.25% 2020 Notes reset on November 1, 2018 to $2.54 per share and the conversion rate was increased to 393.7008 shares of our common stock per $1,000 principal amount of notes.

The remaining $13.2 million 2018 Notes were redeemed at par at maturity on August 1, 2018.

In June 2014, we sold an aggregate of $115.0 million principal amount of 4.875% convertible senior notes due 2020 (the “2020 Notes”). The 2020 Notes are senior unsecured obligations paying interest semi-annually in arrears on June 1 and December 1 of each year at a rate of 4.875% per annum and will mature on June 1, 2020. The initial and still current conversion rate for the 2020 Notes is 103.7613 shares of our common stock per $1,000 principal amount of notes, equivalent to an initial conversion price of approximately $9.64 per share of common stock, subject to adjustment in certain events. Upon conversion, the 2020 Notes will be settled in shares of our common stock. Holders of the 2020 Notes may require that we repurchase for cash all or some of their notes upon the occurrence of a fundamental change (as defined in the 2020 Notes). In January 2016, we repurchased and retired an aggregate of $2.0 million principal amount of the 2020 Notes.

As discussed in the Current Report on Form 8-K dated August 9, 2019, we entered into and consummated multiple, binding definitive agreements (collectively, the “Recapitalization”) among Wells Fargo Bank, National Association, Oasis Investments II Master Fund Ltd. and an ad hoc group of holders of the 4.875% convertible senior notes due 2020 to recapitalize our balance sheet, including the extension to the Company of incremental liquidity and three-year extensions of substantially all of our outstanding convertible debt obligations and revolving credit facility. Our term loan agreement entered into with Great American Capital Partners has been paid in full in connection with the Recapitalization transaction (see Note 5 - Credit Facilities and Note 6 - Convertible Senior Notes for additional information).

As of June 30, 2019 and December 31, 2018, we held cash and cash equivalents, including restricted cash, of $37.0 million and $58.2 million, respectively. Cash, and cash equivalents, including restricted cash held outside of the United States in various foreign subsidiaries totaled $21.8 million and $33.9 million as of June 30, 2019 and December 31, 2018, respectively. The cash and cash equivalents, including restricted cash balances in our foreign subsidiaries have either been fully taxed in the U.S. or tax has been accounted for in connection with the Tax Cuts and Jobs Act, or may be eligible for a full foreign dividends received deduction under such Act, and thus would not be subject to additional U.S. tax should such amounts be repatriated in the form of dividends or deemed distributions. Any such repatriation may result in foreign withholding taxes, which we expect would not be significant as of June 30, 2019.

Our primary sources of working capital are cash flows from operations and borrowings under our credit facility (see Note 5 - Credit Facilities in the accompanying notes to the condensed consolidated financial statements for additional information).

Typically, cash flows from operations are impacted by the effect on sales of (1) the appeal of our products, (2) the success of our licensed brands, (3) the highly competitive conditions existing in the toy industry, (4) dependency on a limited set of large customers, and (5) general economic conditions. A downturn in any single factor or a combination of factors could have a material adverse impact upon our ability to generate sufficient cash flows to operate the business. In addition, our business and liquidity are dependent to a significant degree on our vendors and their financial health, as well as the ability to accurately forecast the demand for products. The loss of a key vendor, or material changes in support by them, or a significant variance in actual demand compared to the forecast, can have a material adverse impact on our cash flows and business. Given the conditions in the toy industry environment in general, vendors, including licensors, may seek further assurances or take actions to protect against non-payment of amounts due to them. Changes in this area could have a material adverse impact on our liquidity.

Cash and cash equivalents, including restricted cash, projected cash flow from operations, and borrowings under our credit facility, as well as taking into account the August 2019 Recapitalization transaction noted above, should be sufficient to meet working capital and capital expenditure requirements for the next 12 months. Our ability to fund operations and retire debt when due is dependent on a number of factors, some of which are beyond our control and/or inherently difficult to estimate, including our future operating performance and the factors mentioned above, among other risks and uncertainties. To the extent we are unable to fund our operations or retire debt when due, no assurances can be given that we will have the financial resources required to obtain, or that the conditions of the capital markets will support, any future debt or equity financings which could have a material adverse impact on our business, results of operations and financial condition.

As of June 30, 2019, off-balance sheet arrangements include letters of credit issued by Wells Fargo of $9.5 million.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Interest Rate Risk

As of June 30, 2019, we have outstanding convertible senior notes payable of $113.0 million principal amount due June 2020 with a fixed interest rate of 4.875% per annum, and $29.5 million principal amount due November 2020 with a fixed interest rate of 3.25% per annum if paid in cash. As the interest rates on the notes are at fixed rates, we are not generally subject to any direct risk of loss related to these notes arising from changes in interest rates.

Our exposure to market risk includes interest rate fluctuations in connection with our revolving credit facility and term loan facility (see Note 5 - Credit Facilities in the accompanying notes to the condensed consolidated financial statements for additional information). Borrowings under the revolving credit facility bear interest at a variable rate based on Base Rate or LIBOR Rate at the option of the Company. For Base Rate loans, the interest rate is equal to a margin of 1.25% plus the highest of (i) the Federal Funds Rate plus a margin of 0.50%, (ii) the rate last quoted by The Wall Street Journal as the “Prime Rate,” or (iii) the sum of a LIBOR rate plus 1.00%. For LIBOR rate loans, the interest rate is equal to a LIBOR rate plus a margin of 2.25%. Borrowings under the term loan facility bear interest at LIBOR plus 9% per annum. Borrowings under the revolving credit facility and term loan facility are therefore subject to risk based upon prevailing market interest rates. Interest rate risk may result from many factors, including governmental monetary and tax policies, domestic and international economic and political considerations and other factors that are beyond our control. During the six months ended June 30, 2019, the maximum amount borrowed under the revolving credit facility was $7.5 million and the average amount of borrowings outstanding was $1.6 million. As of June 30, 2019, the amount of total borrowings outstanding under the revolving credit facility and term loan was $19.8 million. If the prevailing market interest rates relative to these borrowings increased by 10%, our interest expense during the six months period ended June 30, 2019 would have increased by approximately $0.1 million.

Foreign Currency Risk

We have wholly-owned subsidiaries in Hong Kong, China, the United Kingdom, Germany, France, Canada and Mexico. Sales are generally made by these operations on FOB China or Hong Kong terms and are denominated in U.S. dollars. However, purchases of inventory and Hong Kong operating expenses are typically denominated in Hong Kong dollars and local operating expenses in the United Kingdom, Germany, France, Canada, Mexico and China are denominated in local currency, thereby creating exposure to changes in exchange rates. Changes in the U.S. dollar exchange rates may positively or negatively affect our results of operations. 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 these exchange rates, if any, will result in a material effect on our future earnings, fair values or cash flows. 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 these foreign currencies.

Item 4. Controls and Procedures

Our Chief Executive Officer and Chief Financial Officer, after evaluating the effectiveness of our disclosure controls and procedures as of the end of the period covered by this Report, have concluded that as of that date, our disclosure controls and procedures were effective. There has been no change in our internal control over financial reporting identified in connection with the evaluation required by Exchange Act Rule 13a-15(d) that occurred during the period covered by this Report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II – OTHER INFORMATION

Item 1. Legal Proceedings

We are a party to, and certain of our property is the subject of, various pending claims and legal proceedings that routinely arise in the ordinary course of our business. We accrue for losses when the loss is deemed probable and the liability can reasonably be estimated. Where a liability is probable and there is a range of estimated loss with no best estimate in the range, we record the minimum estimated liability related to the claim. As additional information becomes available, we assess the potential liability related to our pending litigation and revise our estimates.

In the normal course of business, we may provide certain indemnifications and/or other commitments of varying scope to a) our licensors, customers and certain other parties, including against third party claims of intellectual property infringement, and b) our officers, directors and employees, including against third party claims regarding the periods in which they serve in such capacities with us. The duration and amount of such obligations is, in certain cases, indefinite. Our director's and officer's liability insurance policy may, however, enable us to recover a portion of any future payments related to our officer, director or employee indemnifications. For the past five years, costs related to director and officer indemnifications have not been significant. Other than certain liabilities recorded in the normal course of business related to royalty payments due our licensors, no liabilities have been recorded for indemnifications and/or other commitments.

Item 1A. *Risk Factors*

From time to time, including in this Quarterly Report on Form 10-Q, we publish forward-looking statements, as disclosed in our Disclosure Regarding Forward-Looking Statements beginning immediately following the Table of Contents of this Report. We note that a variety of factors could cause our actual results and experience to differ materially from the anticipated results or other expectations expressed or anticipated in our forward-looking statements. The factors listed below are risks and uncertainties that may arise and that may be detailed from time to time in our public announcements and our filings with the Securities and Exchange Commission, such as on Forms 8-K, 10-Q and 10-K. We undertake no obligation to make any revisions to the forward-looking statements contained in this Report to reflect events or circumstances occurring after the date of the filing of this report.

Our inability to redesign, restyle and extend our existing core products and product lines as consumer preferences evolve, and to develop, introduce and gain customer acceptance of new products and product lines, may materially and adversely impact our business, financial condition and results of operations.

Our business and operating results depend largely upon the appeal of our products. Our continued success in the toy industry will depend upon our ability to redesign, restyle and extend our existing core products and product lines as consumer preferences evolve, and to develop, introduce and gain customer acceptance of new products and product lines. Several trends in recent years have presented challenges for the toy industry, including:

- *the phenomenon of children outgrowing toys at younger ages, particularly in favor of interactive and high technology products;*
- *increasing use of technology;*
- *shorter life cycles for individual products; and*
- *higher consumer expectations for product quality, functionality and value.*

We cannot assure you that:

- *our current products will continue to be popular with consumers;*
- *the products that we introduce will achieve any significant degree of market acceptance;*
- *the life cycles of our products will be sufficient to permit us to recover our inventory costs, and licensing, design, manufacturing, marketing and other costs associated with those products; or*
- *our inclusion of new technology will result in higher sales or increased profits.*

Any or all of the foregoing factors may adversely affect our business, results of operations and financial condition.

There are risks associated with our license agreements.

- *Our current licenses require us to pay minimum royalties*

Sales of products under trademarks or trade or brand names licensed from others account for substantially all of our net sales. Product licenses allow us to capitalize on characters, designs, concepts and inventions owned by others or developed by toy inventors and designers. Our license agreements generally require us to make specified minimum royalty payments, even if we fail to sell a sufficient number of units to cover these amounts. In addition, under certain of our license agreements, if we fail to achieve certain prescribed sales targets, we may be unable to retain or renew these licenses which may adversely impact our business, results of operations and financial condition.

- *Some of our licenses are restricted as to use and include other restrictive provisions*

Under the majority of our license agreements, the licensors have the right to review and approve our use of their licensed products, designs or materials before we may make any sales. If a licensor refuses to permit our use of any licensed property in the way we propose, or if their review process is delayed, our development or sale of new products could be impeded. Our licensing agreements include other restrictive provisions, such as limitations of the time period in which we have to sell existing inventory upon expiration of the license, requiring licensor approval of contract manufacturers and approval of marketing and promotional materials, limitations on channels of distribution, including internet sales, change of ownership clauses that require licensor approval of such change and may require a fee to be paid under certain circumstances and various other provisions that may have an adverse impact on our business, results of operations and financial condition.

- *New licenses are difficult and expensive to obtain*

Our continued success will substantially depend upon our ability to obtain additional licenses. Intense competition exists for desirable licenses in our industry. We cannot assure you that we will be able to secure or renew significant licenses on terms acceptable to us. In addition, as we add licenses, the need to fund additional capital expenditures, royalty advances and guaranteed minimum royalty payments may strain our cash resources.

- *A limited number of licensors account for a large portion of our net sales*

We derive a significant portion of our net sales from a limited number of licensors, one of which accounts for over 50% of our net sales. If one or more of these licensors were to terminate or fail to renew our license or not grant us new licenses, our business, results of operation and financial condition could be adversely affected.

The failure of our character-related and theme-related products to become and/or remain popular with children may materially and adversely impact our business, results of operations and financial condition.

The success of many of our character-related and theme-related products depends upon the popularity of characters in movies, television programs, live sporting exhibitions, and other media and events. We cannot assure you that:

- *media associated with our character-related and theme-related product lines will be released at the times we expect or will be successful;*
- *the success of media associated with our existing character-related and theme-related product lines will result in substantial promotional value to our products;*
- *we will be successful in renewing licenses upon expiration of terms that are favorable to us; or*
- *we will be successful in obtaining licenses to produce new character-related and theme-related products in the future.*

Our failure to achieve any or all of the foregoing benchmarks may cause the infrastructure of our operations to fail, thereby adversely affecting our business, results of operations and financial condition.

A limited number of customers account for a large portion of our net sales, so that if one or more of our major customers were to experience difficulties in fulfilling their obligations to us, cease doing business with us, significantly reduce the amount of their purchases from us or return substantial amounts of our products, it could have a material adverse effect on our business, results of operations and financial condition.

Our two largest customers, Wal-Mart and Target, accounted for 47.0% of our net sales for the six months ended June 30, 2019. Except for outstanding purchase orders for specific products, we do not have written contracts with or commitments from any of our customers and pursuant to the terms of certain of our vendor agreements, even some purchase orders may be cancelled without penalty up until delivery. A substantial reduction in or termination of orders from any of our largest customers would adversely affect our business, results of operations and financial condition. In addition, pressure by large customers seeking price reductions, financial incentives and changes in other terms of sale or for us to bear the risks and the cost of carrying inventory could also adversely affect our business, results of operations and financial condition. For example, the recent bankruptcy and liquidation of Toys “R” Us (“TRU”) in the United States, and in certain other jurisdictions around the world, had a material, adverse impact on the toy industry and our business, results of operations and financial condition. In 2017, TRU was our third largest customer with net sales of $69.5 million. In 2018, net sales to TRU declined by over 76.1% to $16.6 million. In addition to the reduction in net sales, we also recorded significant bad debt charges in 2017 and 2018 as a result of the TRU bankruptcy and liquidation.

If one or more of our major customers were to experience difficulties in fulfilling their obligations to us resulting from bankruptcy or other deterioration in their financial condition or ability to meet their obligations; cease doing business with us; significantly reduce the amount of their purchases from us; or return substantial amounts of our products, it could have a material adverse effect on our business, results of operations and financial condition.

Restrictions under or the loss of availability under our term loan and revolving credit line could adversely impact our business and financial condition.

In August 2019, we amended, extended and executed a $60.0 million revolving credit line. In August 2019, we entered into a term loan (i) to refinance $103.8 million of certain of our outstanding convertible senior notes due June 2020 (excluding accrued but unpaid interest which will also be added to the term loan principal) and (ii) to borrow $30.0 million of cash. Amounts borrowed under the revolving credit line and term loan are senior secured obligations. All outstanding borrowings under the revolving credit line and term loan are accelerated and become immediately due and payable (and the revolving credit line and term loan terminate) in the event of a default, which includes, among other things, failure to comply with certain financial covenants or breach of representations contained in the credit line and term loan documents, defaults under other loans or obligations, involvement in bankruptcy proceedings, an occurrence of a change of control or an event constituting a material adverse effect on us (as such terms are defined in the credit line and term loan documents). We are also subject to negative covenants which, during the life of the credit line and term loan, prohibit and/or limit us from, among other things, incurring certain types of other debt, acquiring other companies, making certain expenditures or investments, and changing the character of our business. Our failure to comply with such covenants or any other breach of the credit line or term loan agreements could cause a default and we may then be required to repay borrowings under our credit line and term loan with capital from other sources. We could also be blocked from future borrowings or obtaining letters of credit under the revolving credit line, and the credit line agreement and the term loan could be terminated by the lenders. Under these circumstances, other sources of capital may not be available or may be available only on unfavorable terms. In the event of a default, it is possible that our assets and certain of our subsidiaries’ assets may be attached or seized by the lenders. Any (i) failure by us to comply with the covenants or other provisions of the credit line and term loan, (ii) difficulty in securing any required future financing, or (iii) any such seizure or attachment of assets could have a material adverse effect on our business and financial condition. Our revolving credit line and term loan mature in August 2022 and February 2023, respectively.

We may not have the funds necessary to purchase our outstanding convertible senior notes upon a fundamental change or other purchase date, as required by the indenture governing the notes.

In June 2014, we sold an aggregate of $115.0 million principal amount of 4.875% convertible senior notes due on June 1, 2020, of which $113.0 million are currently outstanding (the “4.875% 2020 Notes”). As of August 9 2019, approximately $2 million of the 4.875% 2020 Notes remain outstanding. In July 2013, we sold an aggregate of $100.0 million principal amount of 4.25% convertible senior notes due on August 1, 2018, of which no amounts are currently outstanding, but $29.5 million were exchanged for new notes that mature on November 1, 2020 (the “3.25% 2020 Notes” and collectively with the 4.875% 2020 Notes, the “Notes”). In August 2019, the 3.25% 2020 Notes were amended and, among other changes, now mature on the earlier of (i) 91 days after the repayment in full of the newly issued secured term loan that matures in February 2023 or (ii) July 2023 (the “3.25% 2023 Notes”). In addition, a portion of the 4.875% 2020 Notes was exchanged for the 3.25% 2023 Notes. As of August 2019, approximately $37.5 million of the 3.25% 2023 Notes are outstanding. Holders of the Notes may require us to repurchase for cash all or some of their notes upon the occurrence of a fundamental change (as defined in the Notes). Holders of the Notes may convert their notes upon the occurrence of specified events. Upon conversion, the Notes will be settled in shares of our common stock and/or in cash. Restrictions on borrowings under or loss of our revolving credit line could result in our not having the funds necessary to pay the Notes upon a fundamental change or other purchase date, as required by the indenture governing the Notes.

The agreement governing our outstanding preferred stock includes terms and conditions that may adversely impact our business and cash flows.

In August 2019, we issued a series of preferred stock with a face amount of $20.0 million. The preferred stock (i) is senior to our common stock, (ii) not convertible into common stock, (iii) earns a dividend at an annual rate of 6% (which may or may not be paid in cash), (iv) includes a liquidation preference of up to 150% of the accrued amount, and (v) includes the right to elect two members to the Company’s Board of Directors, among other rights, terms and conditions. In addition, the series of preferred stock includes other protective rights and provisions, such as amendments to the Company’s bylaws to restrict changes that may adversely impact the rights of the preferred stockholders, engaging in businesses that are not permitted businesses, as defined, limitations on assets dispositions and entering into a change of control transaction without the approval of the preferred stockholders. Some of these rights, restrictions and other terms and conditions may prevent us from taking advantageous actions with respect to our business, result in our inability to respond effectively to competitive pressures and industry developments, and/or adversely affect our cash flows or operations.

We depend upon our Chief Executive Officer and any loss or interruption of his services could adversely affect our business, results of operations and financial condition.

Our success has been largely dependent upon the experience and continued services of Stephen G. Berman, our President and Chief Executive Officer. We cannot assure you that we would be able to find an appropriate replacement for Mr. Berman should the need arise, and any loss or interruption of the services of Mr. Berman could adversely affect our business, results of operations and financial condition.

Market conditions and other third-party conduct could negatively impact our margins and implementation of other business initiatives.

Economic conditions, such as decreased consumer confidence or a recession, may adversely impact our business, results of operations and financial condition. In addition, general economic conditions were significantly and negatively affected by the September 11th terrorist attacks and could be similarly affected by any future attacks. Such a weakened economic and business climate, as well as consumer uncertainty created by such a climate, could adversely affect our sales and profitability. Other conditions, such as the unavailability of electronic components, for example, may impede our ability to manufacture, source and ship new and continuing products on a timely basis. Significant and sustained increases in the price of oil, for example, could adversely impact the cost of the raw materials used in the manufacture of certain of our products, such as plastic.

Our business is seasonal and therefore our annual operating results will depend, in large part, on our sales during the relatively brief holiday shopping season. This seasonality is exacerbated by retailers' quick response to inventory management techniques.

Sales of our products at retail are extremely seasonal, with a majority of retail sales occurring during the period from September through December in anticipation of the holiday season. Further, ecommerce is growing significantly and accounts for a higher portion of the ultimate sales of our products. Ecommerce retailers tend to hold less inventory and take inventory closer to the time of sale to consumers than traditional retailers. As a result, customers are timing their orders so that they are being filled by suppliers, such as us, closer to the time of purchase by consumers. For our products, a majority of retail sales for the entire year generally occur in the fourth quarter, close to the holiday season. As a consequence, the majority of our sales to our customers occur in the third and fourth quarters, as our customers do not want to maintain large on-hand inventories throughout the year, ahead of consumer demand. While these techniques reduce a retailer's investment in inventory, they increase pressure on suppliers like us to fill orders promptly and thereby shift a significant portion of inventory risk and carrying costs to the supplier. The level of inventory carried by retailers may also reduce or delay retail sales resulting in lower revenues for us. If we or our customers determine that one of our products is more popular at retail than was originally anticipated, we may not have sufficient time to produce and ship enough additional products to fully meet consumer demand. Additionally, the logistics of supplying more and more product within shorter time periods increases the risk that we will fail to achieve tight and compressed shipping schedules and quality control, which also may reduce our sales and harm our results of operations. This seasonal pattern requires significant use of working capital, mainly to manufacture or acquire inventory during the portion of the year prior to the holiday season, and it requires accurate forecasting of demand for products during the holiday season in order to avoid losing potential sales of popular products or producing excess inventory of products that are less popular with consumers. Our failure to accurately predict and respond to consumer demand, resulting in under-producing popular items and/or overproducing less popular items, could significantly reduce our total sales, negatively impact our cash flows, increase the risk of inventory obsolescence, and harm our results of operations and financial condition. 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.

We depend upon third-party manufacturers, and if our relationship with any of them is harmed or if they independently encounter difficulties in their manufacturing processes, we could experience product defects, production delays, unplanned costs or higher product costs, or the inability to fulfill orders on a timely basis, any of which could adversely affect our business, results of operations and financial condition.

We depend upon many third-party manufacturers who develop, provide and use the tools, dyes and molds that we generally own to manufacture our products. However, we have limited control over the manufacturing processes themselves. As a result, any difficulties encountered by the third-party manufacturers that result in product defects, production delays, cost overruns or the inability to fulfill orders on a timely basis, could adversely affect our business, results of operations and financial condition.

We do not have long-term contracts with our third-party manufacturers. Although we believe we could secure other third-party manufacturers to produce our products, our operations would be adversely affected if we lost our relationship with any of our current suppliers or if our current suppliers' operations or sea or air transportation with our overseas manufacturers were disrupted or terminated even for a relatively short period of time. Our tools, dyes and molds are located at the facilities of our third-party manufacturers.

Although we do not purchase the raw materials used to manufacture our products, we are potentially subject to variations in the prices we pay our third-party manufacturers for products, depending upon what they pay for their raw materials. We may also incur costs or other losses as a result of not placing orders consistent with our forecasts for product manufactured by our suppliers or manufacturers for a variety of reasons including customer order cancellations or a decline in demand.

The toy industry is highly competitive and our inability to compete effectively may materially and adversely impact our business, results of operations and financial condition.

The toy industry is highly competitive. Globally, certain of our competitors have financial and strategic advantages over us, including:

- *greater financial resources;*
- *larger sales, marketing and product development departments;*
- *stronger name recognition;*
- *longer operating histories; and*
- *greater economies of scale.*

In addition, the toy industry has no significant barriers to entry. Competition is based primarily upon the ability to design and develop new toys, procure licenses for popular characters and trademarks, and successfully market products. Many of our competitors offer similar products or alternatives to our products. Our competitors have obtained and are likely to continue to obtain licenses that overlap our licenses with respect to products, geographic areas and markets. We cannot assure you that we will be able to obtain adequate shelf space in retail stores to support our existing products, expand our products and product lines or continue to compete effectively against current and future competitors.

We have substantial sales and manufacturing operations outside of the United States, subjecting us to risks common to international operations.

We sell products and operate facilities in numerous countries outside the United States. Sales to our international customers comprised approximately 12.1% of our net sales for the six months ended June 30, 2019 and approximately 19.8% of our net sales for the six months ended June 30, 2018. We expect our sales to international customers to account for a greater portion of our revenues in future fiscal periods. Additionally, we use third-party manufacturers, located principally in China, and are subject to the risks normally associated with international operations, including:

- *currency conversion risks and currency fluctuations;*
- *limitations, including taxes, on the repatriation of earnings;*
- *political instability, civil unrest and economic instability;*
- *greater difficulty enforcing intellectual property rights and weaker laws protecting such rights;*
- *complications in complying with laws in varying jurisdictions and changes in governmental policies;*
- *greater difficulty and expenses associated with recovering from natural disasters, such as earthquakes, hurricanes and floods;*
- *transportation delays and interruption;*
- *work stoppages;*
- *the potential imposition of tariffs; and*
- *the pricing of intercompany transactions may be challenged by taxing authorities in both foreign jurisdictions and the United States, with potential increases in income and other taxes.*

Our reliance upon external sources of manufacturing can be shifted, over a period of time, to alternative sources of supply, should such changes be necessary. However, if we were prevented from obtaining products or components for a material portion of our product line due to regulatory, political, labor or other factors beyond our control, our operations would be disrupted while alternative sources of products were secured. Also, the imposition of trade sanctions by the United States against a class of products imported by us from, or the loss of "normal trade relations" status by, China could significantly increase our cost of products imported from that nation. Because of the importance of international sales and international sourcing of manufacturing to our business, our results of operations and financial condition could be significantly and adversely affected if any of the risks described above were to occur.

Legal proceedings may harm our business, results of operations, and financial condition.

We are a party to lawsuits and other legal proceedings in the normal course of our business. Litigation and other legal proceedings can be expensive, lengthy, and disruptive to normal business operations. Moreover, the results of complex legal proceedings are difficult to predict. We cannot provide assurance that we will not be a party to additional legal proceedings in the future. To the extent legal proceedings continue for long time periods or are adversely resolved, our business, results of operations, and financial condition could be significantly harmed.

Our business is subject to extensive government regulation and any violation by us of such regulations could result in product liability claims, loss of sales, diversion of resources, damage to our reputation, increased warranty costs or removal of our products from the market, and we cannot assure you that our product liability insurance for the foregoing will be sufficient.

Our business is subject to various laws, including the Federal Hazardous Substances Act, the Consumer Product Safety Act, the Flammable Fabrics Act and the rules and regulations promulgated under these acts. These statutes are administered by the Consumer Product Safety Commission ("CPSC"), which has the authority to remove from the market products that are found to be defective and present a substantial hazard or risk of serious injury or death. The CPSC can require a manufacturer to recall, repair or replace these products under certain circumstances. We cannot assure you that defects in our products will not be alleged or found. Any such allegations or findings could result in:

- *product liability claims;*
- *loss of sales;*
- *diversion of resources;*
- *damage to our reputation;*
- *increased warranty and insurance costs; and*
- *removal of our products from the market.*

Any of these results may adversely affect our business, results of operation and financial condition. There can be no assurance that our product liability insurance will be sufficient to avoid or limit our loss in the event of an adverse outcome of any product liability claim.

We depend upon our proprietary rights, and our inability to safeguard and maintain the same, or claims of third-parties that we have violated their intellectual property rights, could have a material adverse effect on our business, results of operations and financial condition.

We rely upon trademark, copyright and trade secret protection, nondisclosure agreements and licensing arrangements to establish, protect and enforce our proprietary rights in our products. The laws of certain foreign countries may not protect intellectual property rights to the same extent or in the same manner as the laws of the United States. We cannot assure you that we or our licensors will be able to successfully safeguard and maintain our proprietary rights. Further, certain parties have commenced legal proceedings or made claims against us based upon our alleged patent infringement, misappropriation of trade secrets or other violations of their intellectual property rights. We cannot assure you that other parties will not assert intellectual property claims against us in the future. These claims could divert our attention from operating our business or result in unanticipated legal and other costs, which could adversely affect our business, results of operations and financial condition.

Restructuring our workforce can be disruptive and harm our results of operations and financial condition.

We have in the past restructured or made other adjustments to our workforce in response to the economic environment, performance issues, acquisitions, and other internal and external considerations. Restructurings can among other things result in a temporary lack of focus, reductions in net sales and reduced productivity. In addition, we may be unable to realize the anticipated cost savings from our previously announced restructuring efforts or may incur additional and/or unexpected costs in order to realize the anticipated savings. The amounts of anticipated cost savings and anticipated expenses-related restructurings are based on our current estimates, but they involve risks, uncertainties, assumptions and other factors that may cause actual results, performance or achievements to be materially different from those previously planned. These impacts, among others, could occur in connection with previously announced restructuring efforts, or related to future acquisitions and other restructurings and, as a result, our results of operations and financial condition could be negatively affected.

The inability to successfully defend claims from taxing authorities or the adoption of new tax legislation could adversely affect our results of operations and financial condition.

We conduct business in many countries, which requires us to interpret the income tax laws and rulings in each of those jurisdictions. Due to the complexity of tax laws in those jurisdictions as well as the subjectivity of factual interpretations, our estimates of income tax liabilities may differ from actual payments or assessments. Claims from tax authorities related to these differences could have an adverse impact on our results of operations and financial condition. In addition, legislative bodies in the various countries in which we do business may from time to time adopt new tax legislation that could have a material adverse effect on our business, results of operations and financial condition.

We may not be able to sustain or manage our product line growth, which may prevent us from increasing our net revenues.

Historically, we experienced growth in our product lines through acquisitions of businesses, products and licenses. This growth in product lines has contributed significantly to our total revenues over the last few years. Even though we have had no significant acquisitions since 2012, comparing our future period-to-period operating results may not be meaningful and results of operations from prior periods may not be indicative of future results. We cannot assure that we will continue to experience growth in, or maintain our present level of, net sales.

Our growth strategy calls for us to continuously develop and diversify our toy business by acquiring other companies, entering into additional license agreements, refining our product lines and expanding into international markets, which will place additional demands upon our management, operational capacity and financial resources and systems. The increased demand upon management may necessitate our recruitment and retention of qualified management personnel. We cannot assure that we will be able to recruit and retain qualified personnel or expand and manage our operations effectively and profitably. To effectively manage future growth, we must continue to expand our operational, financial and management information systems and to train, motivate and manage our work force. There can be no assurance that our operational, financial and management information systems will be adequate to support our future operations. Failure to expand our operational, financial and management information systems or to train, motivate or manage employees could have a material adverse effect on our business, results of operations and financial condition.

In addition, implementation of our growth strategy is subject to risks beyond our control, including competition, market acceptance of new products, changes in economic conditions, our ability to obtain or renew licenses on commercially reasonable terms, our ability to identify acquisition candidates and conclude acquisitions on acceptable terms, and our ability to obtain the required consents from certain lenders and finance increased levels of accounts receivable and inventory necessary to support our sales growth, if any. Accordingly, we cannot assure that our growth strategy will be successful.

We rely extensively on information technology in our operations, and any material failure, inadequacy, interruption, or security breach of that technology could have a material adverse impact on our business.

We rely extensively on information technology systems across our operations, including for management of our supply chain, sale and delivery of our products and services, reporting our results of operations, collection and storage of consumer data, data of customers, employees and other stakeholders, and various other processes and transactions. Many of these systems are managed by third-party service providers. We use third-party technology and systems for a variety of reasons, including, without limitation, encryption and authentication technology, employee email, content delivery to customers, back-office support, and other functions. A small and growing volume of our consumer products and services are web-based, and some are offered in conjunction with business partners or such third-party service providers. We, our business partners and third-party service providers may collect, process, store and transmit consumer data, including personal information, in connection with those products and services. Failure to follow applicable regulations related to those activities, or to prevent or mitigate data loss or other security breaches, including breaches of our business partners’ technology and systems, could expose us or our customers to a risk of loss or misuse of such information, which could adversely affect our results of operations, result in regulatory enforcement, other litigation and csuld be a potential liability for us, and otherwise significantly harm our business. Our ability to effectively manage our business and coordinate the production, distribution, and sale of our products and services depends significantly on the reliability and capacity of these systems and third-party service providers.

Although we have developed systems and processes that are designed to protect customer information and prevent data loss and other security breaches, including systems and processes designed to reduce the impact of a security breach at a third-party provider, such measures cannot provide absolute security. We have exposure to similar security risks faced by other large companies that have data stored on their information technology systems. To our knowledge, we have not experienced any material breach of our cybersecurity systems. If our systems or our third-party service providers' systems fail to operate effectively or are damaged, destroyed, or shut down, or there are problems with transitioning to upgraded or replacement systems, or there are security breaches in these systems, any of the aforementioned could occur as a result of natural disasters, human error, software or equipment failures, telecommunications failures, loss or theft of equipment, acts of terrorism, circumvention of security systems, or other cyber-attacks, including denial-of-service attacks, we could experience delays or decreases in product sales, and reduced efficiency of our operations. Additionally, any of these events could lead to violations of privacy laws, loss of customers, or loss, misappropriation or corruption of confidential information, trade secrets or data, which could expose us to potential litigation, regulatory actions, sanctions or other statutory penalties, any or all of which could adversely affect our business, and cause it to incur significant losses and remediation costs.

If we are unable to acquire and integrate companies and new product lines successfully, we will be unable to implement a significant component of our growth strategy.

Our growth strategy depends, in part, upon our ability to acquire companies and new product lines. Future acquisitions, if any, may succeed only if we can effectively assess characteristics of potential target companies and product lines, such as:

- *attractiveness of products;*
- *suitability of distribution channels;*
- *management ability;*
- *financial condition and results of operations; and*
- *the degree to which acquired operations can be integrated with our operations.*

We cannot assure you that we can identify attractive acquisition candidates or negotiate acceptable acquisition terms, and our failure to do so may adversely affect our results of operations and our ability to sustain growth. Our acquisition strategy involves a number of risks, each of which could adversely affect our operating results, including:

- *difficulties in integrating acquired businesses or product lines, assimilating new facilities and personnel and harmonizing diverse business strategies and methods of operation;*
- *diversion of management attention from operation of our existing business;*
- *loss of key personnel from acquired companies;*
- *failure of an acquired business to achieve targeted financial results; and*
- *limited capital to finance acquisitions.*

Our stock price has been volatile over the past several years and could decline in the future, resulting in losses for our investors.

All the factors discussed in this section, disclosures made in other parts of this Quarterly Report on Form 10-Q, or any other material announcements or events could affect our stock price. In addition, quarterly fluctuations in our operating results, changes in investor and analyst perception of the business risks and conditions of our business, our ability to meet earnings estimates and other performance expectations of financial analysts or investors, unfavorable commentary or downgrades of our stock by research analysts, fluctuations in the stock prices of our peer companies or in stock markets in general, and general economic or political conditions could also cause the price of our stock to change. A significant drop in the price of our stock could expose us to the risk of securities class action lawsuits, which could result in substantial costs and divert management's attention and resources, adversely affecting our business.

If our stock price continues to remain below $1.00, our common stock may be subject to delisting from The NASDAQ Stock Market. On June 24, 2019, we received a written notice from NASDAQ stating that we no longer comply with NASDAQ Marketplace Rule 5450(a)(1) because the bid price of our common stock closed below the required minimum $1.00 per share for the previous 30 consecutive business days. The notice also indicated that, in accordance with Marketplace Rule 5810(c)(3)(A), we have a period of 180 calendar days, until December 23, 2019, to regain compliance with Rule 5450(a)(1). If at any time before December 23, 2019 the bid price of our common stock closes at $1.00 per share or more for a minimum of 10 consecutive business days, NASDAQ will notify us that we have regained compliance with Rule 5450(a)(1). In the event we do not regain compliance with Rule 5450(a)(1) prior to the expiration of the 180-day period, NASDAQ will notify us that our common stock is subject to delisting. We may appeal the delisting determination to a NASDAQ hearing panel and the delisting will be stayed pending the panel's determination. At such hearing, we would present a plan to regain compliance and NASDAQ would then subsequently render a decision. We are currently evaluating our alternatives to resolve the listing deficiency. To the extent we are unable to resolve the listing deficiency, there is a risk that our common stock may be delisted from NASDAQ, which would adversely impact the liquidity of our common stock and potentially result in even lower bid prices for our common stock.

We have a valuation allowance on the deferred taxes on our books since their future realization is uncertain.

Deferred tax assets are realized by prior and future taxable income of appropriate character. Current accounting standards require that a valuation allowance be recorded if it is not likely that sufficient taxable income of appropriate character will be generated to realize the deferred tax assets. We currently believe that based on the available information, it is more likely than not that our deferred tax assets will not be realized, and accordingly we have recorded a valuation allowance against our U.S. federal and state deferred tax assets. Certain of our net operating losses and tax credit carry-forwards can expire if unused, and the utilization of our net operating losses and tax credit carry-forwards could be substantially limited in the event of an "ownership change," as defined in Section 382 of the Internal Revenue Code of 1986, as amended, or the Internal Revenue Code.

We have a material amount of goodwill which, if it becomes impaired, would result in a reduction in our net earnings.

Goodwill is the amount by which the cost of an acquisition exceeds the fair value of the net assets we acquire. Goodwill is not amortized and is required to be evaluated for impairment at least annually. At June 30, 2019, $35.1 million, or 10.7%, of our total assets represented goodwill. Declines in our profitability may impact the fair value of our reporting units, which could result in a write-down of our goodwill and consequently harm our results of operations. We did not record any goodwill impairment charges during 2018 and 2019. In the future, if we do not achieve our profitability and growth targets the carrying value of our goodwill may become further impaired, resulting in additional impairment charges.

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

Issuer Purchases of Equity Securities

During the second quarter of 2019, the Company did not purchase any of its common stock.

Item 6. Exhibits

Number	Description
3.1	Amended and Restated Certificate of Incorporation of the Company (1)
3.1.1	Certificate of Designations of Series A Senior Preferred Stock (2)
3.2	Second Amended and Restated By-laws of the Company (2)
31.1	Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer (3)
31.2	Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer (3)
32.1	Section 1350 Certification of Chief Executive Officer (3)
32.2	Section 1350 Certification of Chief Financial Officer (3)
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

(1) Filed previously as Appendix 2 to the Company's Schedule 14A Proxy Statement filed August 23, 2002 and incorporated herein by reference.

(2) Filed previously as an exhibit to the Company's Current Report on Form 8-K filed August 9, 2019 and incorporated herein by reference.

(3) Filed herewith.

SIGNATURES

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

JAKKS PACIFIC, INC.

Date: August 9, 2019	By:	/s/ Brent Novak
		Brent Novak
		Executive Vice President and Chief Financial Officer
		(Duly Authorized Officer and Principal Financial Officer)

Exhibit Index

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(2) Filed previously as an exhibit to the Company's Current Report on Form 8-K filed August 9, 2019 and incorporated herein by reference.

(3) Filed herewith.

Exhibit 31.1

CERTIFICATIONS

I, Stephen G. Berman, Chief Executive Officer, certify that:

I have reviewed this quarterly report on Form 10-Q of JAKKS Pacific, Inc. (“Company”);

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 quarterly report;

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

The Company’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 Company 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 Company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly 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 Company’s disclosure controls and procedures and presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this quarterly report based on such evaluation; and

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

The Company’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Company’s auditors and the Audit Committee of the Company’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 Company’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 Company’s internal control over financial reporting.

By: /s/ Stephen G. Berman

Stephen G. Berman

Chief Executive Officer

Date: August 9, 2019

Exhibit 31.2

CERTIFICATIONS

I, Brent Novak, Chief Financial Officer, certify that:

I have reviewed this quarterly report on Form 10-Q of JAKKS Pacific, Inc. (“Company”);

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 quarterly report;

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

The Company’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 Company 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 Company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly 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 Company’s disclosure controls and procedures and presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this quarterly report based on such evaluation; and

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

The Company’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Company’s auditors and the Audit Committee of the Company’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 Company’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 Company’s internal control over financial reporting.

By: /s/ Brent Novak

Brent Novak

Chief Financial Officer

Date: August 9, 2019

Exhibit 32.1

Written Statement of the Chief Executive Officer Pursuant to 18 U.S.C. Section 1350

Pursuant to 18 U.S.C. Section 1350, the undersigned officer of JAKKS Pacific, Inc. (“Registrant”) hereby certifies that the Registrant’s Quarterly Report on Form 10-Q for the six months ended June 30, 2019 (the “Report”) fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934 and that the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Registrant.

/s/ Stephen G. Berman

Stephen G. Berman
Chief Executive Officer

Date: August 9, 2019

Exhibit 32.2

Written Statement of the Chief Financial Officer Pursuant to 18 U.S.C. Section 1350

Pursuant to 18 U.S.C. Section 1350, the undersigned officer of JAKKS Pacific, Inc. (“Registrant”) hereby certifies that the Registrant’s Quarterly Report on Form 10-Q for the six months ended June 30, 2019 (the “Report”) fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934 and that the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Registrant.

/s/ Brent Novak

Brent Novak

Chief Financial Officer

Date: August 9, 2019