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 March 31, 2022

OR

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

For the transition period from to

Commission File Number 001-40836

Brilliant Earth Group, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**87-1015499**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
300 Grant Avenue, Third Floor San Francisco, CA	**94108**
(Address of principal executive offices)	(Zip Code)

(800) 691-0952

(Registrant's telephone number, including area code)

N/A

(Former name, former address and former fiscal year, if changed since last report)

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

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Class A common stock, $0.0001 par value per share	BRLT	The Nasdaq Global Market

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

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

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

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

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

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

As of May 9, 2022, there were 10,806,956 shares of the registrant's Class A common stock, $0.0001 par value per share, outstanding, 35,285,133 shares of the registrant's Class B common stock, $0.0001 par value per share, outstanding, 49,119,976 shares of the registrant's Class C common stock, $0.0001 par value per share, outstanding and no shares of the registrant's Class D common stock, $0.0001 per share, outstanding.

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CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements. We intend such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in Section 27A of the Securities Act of 1933, as amended (the “Securities Act”), and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). All statements other than statements of historical facts contained in this Quarterly Report on Form 10-Q may be forward-looking statements. Statements regarding our future results of operations and financial position, business strategy, and plans and objectives of management for future operations, including, among others, statements regarding expected growth, future capital expenditures, and debt service obligations, are forward-looking statements. In some cases, you can identify forward-looking statements by terms, such as “anticipate,” “believe,” “contemplates,” “continues,” “could,” “estimate,” “evolve,” “expect,” “intend,” “may,” “plan,” “potential,” “predict,” “seek,” “should,” “strategy,” “target,” “will,” or “would,” or the negative of these terms or other similar expressions. Accordingly, we caution you that any such forward-looking statements are not guarantees of future performance and are subject to risks, assumptions, and uncertainties that are difficult to predict.

We have based these forward-looking statements largely on our current expectations and projections about future events and trends that we believe may affect our financial condition, results of operations, business strategy, short term and long-term business operations and objectives, and financial needs. Although we believe that the expectations reflected in these forward-looking statements are reasonable as of the date made, actual results may prove to be materially different from the results expressed or implied by the forward-looking statements. These forward-looking statements are subject to a number of risks, uncertainties, and assumptions, including, but not limited to: the Company has grown rapidly in recent years and has limited operating experience; the Company may be unable to manage growth effectively; increases in costs of diamonds, other gemstones and precious metals supply shortages; the Company's ability to maintain a low cost of production and distribution; fluctuations in the pricing and supply of diamonds, other gemstones, and precious metals, particularly responsibly sourced natural and lab-grown diamonds and recycled precious metals such as gold, increases in labor costs for manufacturing such as wage rate increases, as well as inflation, and energy prices; the Company’s ability to cost-effectively turn existing customers into repeat customers or to acquire new customers; risks related to the Company’s expansion plans in the U.S.; an overall decline in the health of the economy and other factors impacting consumer spending, such as recessionary conditions, governmental instability, war or the threat of war, and natural disasters may affect consumer purchases; the Company has a history of losses, and may be unable to sustain profitability; competition in the fine jewelry retail industry; the Company’s ability to manage its inventory balances and inventory shrinkage; a decline in sales of Create Your Own rings would negatively affect the Company’s business, financial condition, and results of operations; the Company ability to maintain and enhance its brand; the Company’s marketing efforts to help grow its business may not be effective; environmental, social, and governance matters may impact the Company’s business and reputation; risks related to the Company’s e-commerce and omnichannel business; the Company’s ability to effectively anticipate and respond to changes in consumer preferences and shopping patterns; the Company’s results of operations and operating cash flows could fluctuate on a quarterly and annual basis, which may make it difficult to predict its future performance; the Company’s principal asset is its interest in Brilliant Earth, LLC, and, as a result, the Company depends on distributions from Brilliant Earth, LLC to pay its taxes and expenses; risks related to the Company’s obligations under its Tax Receivable Agreement and its organizational structure; and the other risks, uncertainties and the factors described in the section titled “Risk Factors” in the Company's Annual Report on Form 10-K for the year ended December 31, 2021. Other sections of this Quarterly Report on Form 10-Q include additional factors that could adversely impact our business and financial performance.

Moreover, we operate in a very competitive and rapidly changing environment. New risks emerge from time to time. It is not possible for our management to predict all risks, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements we may make. In light of these risks, uncertainties, and assumptions, the future events and trends discussed in this Quarterly Report on Form 10-Q may not occur and actual results could differ materially and adversely from those anticipated or implied in the forward-looking statements.

You should not rely upon forward-looking statements as predictions of future events. This Quarterly Report on Form 10-Q and the documents that we have filed as exhibits should be read with the understanding that our actual future results, levels of activity, performance and achievements may be materially different from what we expect. We qualify all of our forward-looking statements by these cautionary statements. These forward looking statements speak only as of the date of this Quarterly Report on Form 10-Q. Except as required by applicable law, we undertake no obligation to update or revise any forward-looking statements contained in this Quarterly Report on Form 10-Q, whether as a result of any new information, future events or otherwise.

BASIS OF PRESENTATION

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

- "we," "us," "our," the "Company," "Brilliant Earth," and similar references refer: (1) following the consummation of the Reorganization Transactions (as defined below), including our initial public offering ("IPO") which occurred on September 23, 2021, to Brilliant Earth Group, Inc., and, unless otherwise stated, all of its subsidiaries, including Brilliant Earth, LLC, and (2) prior to the completion of the Reorganization Transactions, including the IPO, to Brilliant Earth, LLC.
- "Brilliant Earth LLC Agreement" refers to Brilliant Earth, LLC's amended and restated limited liability company agreement, which became effective prior to the consummation of the IPO.
- "CAGR" refers to compound annual growth rate.
- "Continuing Equity Owners" refers collectively to holders of LLC Interests and our Class B common stock and Class C common stock immediately following consummation of the Reorganization Transactions, including our Founders (as defined below) and Mainsail (as defined below), who may, exchange at each of their respective options, in whole or in part from time to time, their LLC Interests (along with an equal number of shares of Class B common stock or Class C common stock (and such shares shall be immediately cancelled)), as applicable, for, at our election (determined solely by our independent directors (within the meaning of the Nasdaq rules) who are disinterested), cash or newly-issued shares of our Class A common stock or Class D common stock, as applicable.
- "Founders" refers to Beth Gerstein, our Co-Founder and Chief Executive Officer, Eric Grossberg, our Co-Founder and Executive Chairman, and Just Rocks (as defined below).
- "Just Rocks" refers to Just Rocks, Inc., a Delaware corporation, which is jointly owned and controlled by our Founders.
- "LLC Interests" or "LLC Units" refers to the common units of Brilliant Earth, LLC, including those that we purchased with the net proceeds from the IPO.
- "Original Equity Owners" refers to the owners of LLC Interests in Brilliant Earth, LLC prior to the consummation of the Reorganization Transactions, collectively, which include Mainsail, Just Rocks, and certain executive officers and employees.
- "Mainsail" refers to Mainsail Partners III, L.P., our sponsor and a Delaware limited partnership, and certain funds affiliated with Mainsail Partners III, L.P., including Mainsail Incentive Program, LLC, and Mainsail Co-Investors III, L.P.
- "Reorganization Transactions" refers to the organizational transactions and the IPO, and the application of the net proceeds therefrom.
- "TRA" refers to the Tax Receivable Agreement with Brilliant Earth, LLC and the Continuing Equity Owners that provides for the payment by Brilliant Earth Group, Inc. to the Continuing Equity Owners of 85% of the amount of tax benefits, if any, that Brilliant Earth Group, Inc. actually realizes (or in some circumstances is deemed to realize) related to certain tax basis adjustments and payments made under the TRA.

Part I - Financial Information

Item 1. Financial Statements

Brilliant Earth Group, Inc.
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited and in thousands except share and per share amounts)

	March 31, 2022	December 31, 2021
Assets		
Current assets:		
Cash and cash equivalents	$ 164,890	$ 172,865
Restricted cash	205	205
Inventories, net	28,392	24,743
Prepaid expenses and other current assets	8,560	8,178
Total current assets	202,047	205,991
Property and equipment, net	8,734	6,732
Deferred tax assets	7,840	4,407
Operating lease right of use assets	20,067	—
Other assets	943	601
Total assets	$ 239,631	$ 217,731
Liabilities and equity		
Current liabilities:		
Accounts payable	$ 11,390	$ 14,480
Accrued expenses and other current liabilities	26,429	28,756
Current portion of deferred revenue	23,561	18,818
Current portion of operating lease liabilities	2,779	—
Current portion of long-term debt	41,053	30,789
Total current liabilities	105,212	92,843
Long-term debt, net of debt issuance costs	22,863	32,789
Operating lease liabilities	19,882	—
Deferred rent	—	2,507
Payable pursuant to the Tax Receivable Agreement	6,604	3,775
Other long-term liabilities	3,028	2,979
Total liabilities	157,589	134,893
Commitments and contingencies (Note 11)		
Equity		
Preferred stock, $0.0001 par value per share, 10,000,000 shares authorized, none issued and outstanding at March 31, 2022 and December 31, 2021, respectively	—	—
Class A common stock, $0.0001 par value - 1,200,000,000 shares authorized; 10,708,456 and 9,614,523 shares issued and outstanding at March 31, 2022 and December 31, 2021, respectively	1	1
Class B common stock, $0.0001 par value - 150,000,000 shares authorized; 35,326,696 and 35,658,013 shares issued and outstanding at March 31, 2022 and December 31, 2021, respectively	4	4
Class C common stock, $0.0001 par value - 150,000,000 shares authorized; 49,119,976 and 49,505,250 shares issued and outstanding at March 31, 2022 and December 31, 2021, respectively	5	5
Class D common stock, $0.0001 par value - 150,000,000 shares authorized; none issued and outstanding at March 31, 2022 and December 31, 2021, respectively	—	—
Additional paid-in capital	7,339	6,865
Retained earnings	1,884	1,528
Equity attributable to Brilliant Earth Group, Inc.	9,233	8,403
NCI attributable to Brilliant Earth, LLC	72,809	74,435
Total equity	82,042	82,838
Total liabilities and equity	$ 239,631	$ 217,731

The accompanying notes are an integral part of these condensed consolidated financial statements.

Brilliant Earth Group, Inc.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited and in thousands except share and per share amounts)

	Three months ended March 31, 2022	Three months ended March 31, 2021
Net sales	$ 100,038	$ 70,696
Cost of sales	49,922	38,337
Gross profit	50,116	32,359
Operating expenses:		
Selling, general and administrative	44,816	27,405
Income from operations	5,300	4,954
Interest expense	(1,776)	(1,926)
Other expense, net	(59)	(620)
Income before tax	3,465	2,408
Income tax expense	(96)	—
Net income	3,369	$ 2,408
Net income allocable to non-controlling interest	3,013	
Net income allocable to Brilliant Earth Group, Inc.	$ 356	
Earnings per share:		
Basic	$ 0.04	
Diluted	$ 0.03	
Weighted average shares of common stock outstanding:		
Basic	10,010,798	
Diluted	96,526,843	

The accompanying notes are an integral part of these condensed consolidated financial statements.

Brilliant Earth Group, Inc.
CONDENSED CONSOLIDATED STATEMENTS OF EQUITY AND
CHANGES IN REDEEMABLE CONVERTIBLE PREFERRED UNITS AND EQUITY/ MEMBERS' (DEFICIT)
(Unaudited and in thousands except share amounts)

	Brilliant Earth, LLC							
	Class P Units		Class F		Class M		Class F Units and Class M Units	
	Total Units	Total Amounts	Total Units	Total Amounts	Total Units	Total Amounts	Total Units	Total Amounts
Balance, January 1, 2021	**32,435,595**	**$ 66,327**	**50,232,863**	**$ (85,695)**	**2,537,791**	**$ 300**	**52,770,654**	**$ (85,395)**
Tax distributions to members	—	(29)	—	(46)	—	—	—	(46)
Vested Class M Units	—	—	—	—	325,221	—	325,221	—
Equity-based compensation	—	—	—	—	—	93	—	93
Net income	—	941	—	1,467	—	—	—	1,467
Adjustment of redeemable convertible preferred units to redemption value	—	79,816	—	(79,816)	—	—	—	(79,816)
Balance, March 31, 2021	**32,435,595**	**$ 147,055**	**50,232,863**	**$ (164,090)**	**2,863,012**	**$ 393**	**53,095,875**	**$ (163,697)**

	Brilliant Earth Group, Inc. Stockholders' Equity											
	Class A Common Stock		Class B Common Stock		Class C Common Stock					Non-Controlling Interest		
	Shares	Amount	Shares	Amount	Shares	Amount	Additional Paid-In Capital	Retained Earnings	Stockholders' Equity	Units	Amounts	Total Equity
Balance, January 1, 2022	**9,614,523**	**$ 1**	**35,658,013**	**$ 4**	**49,505,250**	**$ 5**	**$ 6,865**	**$ 1,528**	**$ 8,403**	**85,163,263**	**$ 74,435**	**$ 82,838**
Tax distributions to members	—	—	—	—	—	—	—	—	—	—	(6,874)	(6,874)
Conversion of Class B and Class C to Class A common stock	1,053,914	—	(668,640)	—	(385,274)	—	—	—	—	(1,053,914)	—	—
RSU vesting during period	40,019	—	—	—	—	—	—	—	—	—	—	—
LLC Units vesting during period	—	—	337,323	—	—	—	—	—	—	337,323	—	—
Increase in deferred tax asset from step-up tax basis related to redemption of LLC Units and set-up of TRA liability	—	—	—	—	—	—	605	—	605	—	—	605
Equity-based compensation	—	—	—	—	—	—	2,028	—	2,028	—	76	2,104
Net income	—	—	—	—	—	—	—	356	356	—	3,013	3,369
Rebalancing of controlling and non-controlling interest	—	—	—	—	—	—	(2,159)		(2,159)	—	2,159	—
Balance, March 31, 2022	**10,708,456**	**$ 1**	**35,326,696**	**$ 4**	**49,119,976**	**$ 5**	**$ 7,339**	**$ 1,884**	**$ 9,233**	**84,446,672**	**$ 72,809**	**$ 82,042**

The accompanying notes are an integral part of these condensed consolidated financial statements.

Brilliant Earth Group, Inc.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited and in thousands)

	Three months ended March 31,	
	2022	**2021**
Operating activities		
Net income	$ 3,369	$ 2,408
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	349	164
Equity-based compensation	2,104	93
Non-cash operating lease cost	683	—
Change in fair value of warrants	—	574
Amortization of debt issuance costs	423	423
Other	(14)	(24)
Changes in assets and liabilities:		
Inventories	(3,633)	(2,691)
Prepaid expenses and other current assets	(746)	(24)
Other assets	(342)	(194)
Accounts payable, accrued expenses and other current liabilities	(6,485)	(1,913)
Deferred revenue	4,706	7,815
Operating lease liabilities	(232)	—
Deferred rent	—	240
Net cash provided by operating activities	**182**	**6,871**
Investing activities		
Purchases of property and equipment	(1,283)	(546)
Net cash used in investing activities	**(1,283)**	**(546)**
Financing activities		
Tax distributions to members	(6,874)	(75)
Net cash used in financing activities	**(6,874)**	**(75)**
Net (decrease) increase in cash, cash equivalents and restricted cash	**(7,975)**	**6,250**
Cash, cash equivalents and restricted cash at beginning of period	173,070	66,474
Cash, cash equivalents and restricted cash at end of period	**$ 165,095**	**$ 72,724**
Non-cash investing and financing activities		
Deferred tax assets associated with redemption of LLC Units	$ 3,433	—
TRA Obligation associated with redemption of LLC Units	2,829	—
Purchases of property and equipment included in accounts payable and accrued liabilities	1,068	18
Credit to APIC related to redemption of LLC Units	605	—
Adjustment of redeemable convertible preferred units to redemption value	—	79,816
Supplemental information		
Cash paid for interest	$ 1,341	$ 1,502

The accompanying notes are an integral part of these condensed consolidated financial statements.

Brilliant Earth Group, Inc.
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

NOTE 1. BUSINESS AND ORGANIZATION

Brilliant Earth Group, Inc. was formed as a Delaware corporation on June 2, 2021 for the purpose of facilitating an initial public offering ("IPO") and executing other related organizational transactions to acquire and carry on the business of Brilliant Earth, LLC. Brilliant Earth, LLC was originally incorporated in Delaware on August 25, 2005, and subsequently converted to a limited liability company on November 29, 2012. Brilliant Earth Group, Inc., the sole managing member of Brilliant Earth, LLC, consolidates Brilliant Earth, LLC and both are collectively referred to herein as "the Company."

The Company designs, procures and sells ethically-sourced diamonds, gemstones and jewelry online and through showrooms operated in San Francisco, Los Angeles, Boston, Chicago, San Diego, Washington D.C., Denver, Philadelphia, Atlanta, Seattle, Portland, Austin, Dallas, New York, and Scottsdale. Co-headquarters are located in San Francisco, California and Denver, Colorado.

The Company operates in one operating and reporting segment which is the retail sale of diamonds, gemstones and jewelry. Over 90% of sales are to customers in the United States ("U.S."); sales to non-U.S. customers immediately settle in U.S. dollars and no cash balances are carried in foreign currencies. The Company's chief operating decision maker ("CODM"), the Chief Executive Officer ("CEO"), reviews financial information presented on a consolidated basis for purposes of making operating decisions and assessing financial performance.

In accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") since the members of Brilliant Earth, LLC (the "Continuing Equity Owners") prior to the IPO and merger continue to hold a controlling interest in Brilliant Earth, LLC after the merger (i.e., there was no change in control of Brilliant Earth, LLC) and since Brilliant Earth Group, Inc. was considered a "shell company" which does not meet the definition of a business, the financial statements of the combined entity represent a continuation of the financial position and results of operations of Brilliant Earth, LLC. Accordingly, the historical cost basis of assets, liabilities, and equity of Brilliant Earth, LLC are carried over to the condensed consolidated financial statements of the merged company as a common control transaction. Also, after consummation of the IPO, Brilliant Earth Group, Inc. became subject to U.S. federal, state, and local income taxes with respect to its allocable share of any taxable income of Brilliant Earth, LLC assessed at the prevailing corporate tax rates.

Initial Public Offering and purchase of LLC Interests

On September 27, 2021, the Company completed its IPO of 9,583,332 shares of Class A common stock at an offering price of $12.00 per share, (excluding the underwriting discount), including 1,249,999 shares of Class A common stock issued pursuant to the underwriters' over-allotment option. The Company received $101.6 million in proceeds after a deduction for underwriting discounts and offering costs totaling $13.4 million.

The net proceeds were used to purchase 8,333,333 newly-issued membership units (the "LLC Units" or "LLC Interests") from Brilliant Earth, LLC and 1,249,999 LLC Units in the form of a redemption from the Continuing Equity Owners at a price per unit equal to the IPO price of $11.22 per share after deducting the underwriting discount, and represented a 10.1% economic interest as of the IPO date.

Conversion of Class F, P and M Units at time of IPO

At the time of the IPO, the existing limited liability company agreement of Brilliant Earth, LLC was amended and restated to, among other things, recapitalize all existing Class F, P and M Units in Brilliant Earth, LLC into 86,297,284 common LLC Units after applying a conversion ratio of 1.8588 with a further adjustment for a distribution threshold related to the M Units (which impacted their allocation of value so the economic effect of the exchange was a like-for-like value); the net conversion ratio was 1.8942, 1.9080 and 1.7735 for the Class F Units, P Units and M Units, respectively. The number of Class F, P and M Units presented in these financial statements for periods prior to the IPO have been retroactively adjusted to reflect the conversion ratios (as discussed in the preceding sentence) similar to the presentation of a stock-split.

Summary of the restructuring, offering and other transactions completed in connection with the IPO

In connection with the IPO, Brilliant Earth Group, Inc. and Brilliant Earth, LLC completed a series of transactions that comprise of reorganization, offering and other financing transactions.

The following summarizes the Reorganization Transactions which occurred as of the date of IPO:

- Amended and restated the existing limited liability company agreement of Brilliant Earth, LLC (the "LLC Agreement"), effective prior to the IPO, to, among other things, (1) recapitalize all existing ownership interests in Brilliant Earth, LLC into 86,297,284 LLC Units after applying a conversion ratio of 1.8588, (2) appoint Brilliant Earth Group, Inc. as the sole managing member of Brilliant Earth, LLC upon its acquisition of LLC Units in connection with the IPO, and (3) provide certain redemption rights to the Continuing Equity Owners.

- Amended and restated Brilliant Earth Group, Inc.'s certificate of incorporation to, among other things, provide for four classes of common stock defined as Class A common stock, Class B common stock, Class C common stock and Class D common stock.

- Issued 36,064,421 shares of Class B common stock (prior to the redemption of 522,386 shares pursuant to the exercise of underwriters' overallotment options discussed below) to the Continuing Equity Owners, excluding the founders, Beth Gerstein, Co-Founder and Chief Executive Officer, Eric Grossberg, Co-Founder and Executive Chairman, and Just Rocks, a Delaware corporation which is jointly owned and controlled by the founders (collectively, the "Founders"), which is equal to the number of LLC Units held by such Continuing Equity Owners excluding the Founders, for nominal consideration.

- Issued 50,232,863 shares of Class C common stock (prior to the redemption of 727,613 shares pursuant to the exercise of underwriters' overallotment options discussed below) to the Founders, which is equal to the number of LLC Units held by such Founders, for nominal consideration.

- Entered into a Tax Receivable Agreement (the "TRA") with Brilliant Earth, LLC and the Continuing Equity Owners that will provide for the payment by Brilliant Earth Group, Inc. to the Continuing Equity Owners of 85% of the amount of tax benefits, if any, that Brilliant Earth Group, Inc. actually realizes (or in some circumstances is deemed to realize) related to certain tax basis adjustments and payments made under the TRA.

The organization agreements include a provision for the Continuing Equity Owners, subject to certain exceptions from time to time at each of their option, to require Brilliant Earth, LLC to redeem all or a portion of their LLC Units in exchange for, at the Company's election, newly-issued shares of Class A common stock or Class D common stock, as applicable, on a one-for-one basis, or a cash payment equal to a volume weighted average market price of one share of Class A common stock for each LLC Interest so redeemed, in each case, in accordance with the terms of the Brilliant Earth LLC Agreement.

The following summarizes the IPO and other transactions:

- Issued 9,583,332 shares of Class A common stock, including 1,249,999 shares of Class A common stock from the exercise of the underwriters' overallotment, in exchange for net proceeds of approximately $101.6 million at $12.00 per share, less underwriting discount and offering expenses.

- Used net proceeds from the IPO to purchase 8,333,333 newly issued LLC Units for approximately $93.5 million directly from Brilliant Earth, LLC at a price per unit equal to the initial public offering price per share of Class A common stock less underwriting discount.

- Used net proceeds from the exercise of the underwriters' overallotment to purchase an additional 1,249,999 LLC Units from each of the Continuing Equity Owners in the form of a redemption on a pro rata basis for $14.0 million in aggregate at a price per unit equal to the initial public offering price per share of Class A common stock less the underwriting discount; this purchase of LLC Interests resulted in an obligation under the TRA, including the related set-up of deferred tax assets on the TRA and on the temporary basis difference associated with this purchase.

- Corresponding cancellation of a total of 1,249,999 shares of Class B common stock and Class C common stock resulting from the purchase of 1,249,999 LLC Units from the Continuing Equity Owners.

- Exercise of warrants on convertible preferred units ("Class P Units") with a carrying value of $6.4 million as of September 22, 2021 (after the mark-to-market adjustment as of the date of exercise) into 534,589 newly issued LLC Units on a net settlement basis, elected at the option of the holder.

Risks and Uncertainties – COVID-19

The COVID-19 pandemic remains on-going and continues to impact the global economy. The Company's financial performance could be adversely impacted by the on-going evolution of the pandemic, including any government-imposed pandemic restrictions. The Company cannot predict the full extent of the impacts of the COVID-19 pandemic on its business, operations, or the global economy as a whole. However, the effects could have a material impact on the Company's results of operations.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The unaudited condensed consolidated financial statements for the periods prior to the Reorganization Transactions and IPO have been presented to combine the previously separate entities. These unaudited condensed consolidated financial statements have been prepared in accordance with U.S. GAAP and the requirements of the Securities and Exchange Commission (the "SEC") for interim reporting. As permitted under those rules, certain footnotes or other financial information that are normally required by U.S. GAAP can be condensed or omitted. These interim results are not necessarily indicative of the results to be expected for the fiscal year ending December 31, 2022, or for any other interim period or for any other future year.

In the opinion of management, the unaudited condensed consolidated financial statements reflect all adjustments consisting only of normal recurring adjustments necessary to state fairly the financial position, results of operations and cash flows for the periods presented in conformity with U.S. GAAP applicable to interim periods. The results of operations for the interim periods presented are not necessarily indicative of results for the full year or future periods. These unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and the related notes thereto as of and for the year ended December 31, 2021, as disclosed in the 2021 annual report on Form 10-K.

Principles of Consolidation and Non-Controlling Interest

The unaudited condensed consolidated financial statements include the accounts of the Company and its subsidiary, Brilliant Earth, LLC, which it controls due to ownership of the voting interest or pursuant to variable interest entity ("VIE") accounting guidance. All intercompany balances and transactions have been eliminated in consolidation.

The non-controlling interest on the unaudited condensed consolidated statement of operations represents the portion of earnings or loss attributable to the economic interest in Brilliant Earth, LLC held by the Continuing Equity Owners. The non-controlling interest on the unaudited condensed consolidated balance sheets represent the portion of net assets of the Company attributable to the Continuing Equity Owners, based on the portion of the LLC Interests owned by such unit holders. As of March 31, 2022, the non-controlling interest was 88.7%. At the end of each reporting period, equity related to Brilliant Earth, LLC that is attributable to Brilliant Earth Group, Inc. and Continuing Equity Owners is rebalanced to reflect Brilliant Earth Group, Inc.'s and Continuing Equity Owners' ownership in Brilliant Earth, LLC.

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Estimates are based on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. Some of the more significant estimates include the inventory valuation, allowance for sales returns, estimates of current and deferred income taxes, payable pursuant to the tax receivable agreement, useful lives and depreciation of long-lived assets, fair value of equity-based compensation, and prior to the Reorganization Transactions, the warrants and the redemption of value of the redeemable Class P Units. Actual results could differ materially from those estimates. On an ongoing basis, the Company reviews its estimates to ensure that they appropriately reflect changes in its business or new information available.

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. U.S. GAAP establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. U.S. GAAP prescribes three levels of inputs that may be used to measure fair value:

Level 1 Valuation based on quoted prices (unadjusted) observed in active markets for identical assets or liabilities.
Level 2 Valuation techniques based on inputs that are quoted prices of similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not in active markets; inputs other than quoted prices used in a valuation model that are observable for that instrument; and inputs that are derived from, or corroborated by, observable market data by correlation or other means.
Level 3 Valuation techniques with significant unobservable market inputs.

The Company is required to disclose its estimate of the fair value of material financial instruments, including those recorded as assets or liabilities in its financial statements, in accordance with U.S. GAAP.

At March 31, 2021, Class P Units and warrants on Class P Units were the only financial instruments (assets or liabilities) measured at fair value on a recurring basis.

Through the date of the IPO, the Class P Units and warrants on Class P Units were the only financial instruments (assets or liabilities) measured at fair value on a recurring basis. As discussed in Note 1, *Business and organization*, the securities converted into LLC Interests in connection with the IPO and are now classified as equity. The fair value of the Class P Units and the warrants on Class P Units as of September 22, 2021 just before conversion into common LLC Units were $389.2 million and $6.4 million, respectively; these securities are no longer subject to this fair value disclosure.

The carrying amounts of cash and cash equivalents, restricted cash, accounts payable and accrued expenses and other current liabilities approximate fair value due to their short-term maturities and were classified as Level 1. The carrying value of long-term debt, net of debt issuance costs, also approximates its fair value, which has been estimated by management based on the consideration of applicable interest rates (including certain instruments at variable or floating rates) for similar types of borrowing arrangements. Redeemable Convertible Class P Units and Class P Units underlying warrants were classified as Level 3 until the IPO at which time the securities were converted into LLC Interests.

Comprehensive Income

Comprehensive income is the change in equity of a business enterprise during a period from transactions and all other events and circumstances from non-owner sources. Other comprehensive income may include unrealized gain (loss) on available for sale securities, foreign currency items, and minimum pension liability adjustments. The Company did not have components of other comprehensive income. As a result, comprehensive income is the same as net income.

Cash and Cash Equivalents, and Restricted Cash

All highly liquid investments with an original maturity of three months or less and deposits in transit from banks for payments related to third-party credit and debit card transactions are considered to be cash equivalents. Credit and debit card transactions are short-term and highly liquid in nature.

The following table provides a reconciliation of cash and cash equivalents, and restricted cash from the unaudited condensed consolidated balance sheets to the statements of cash flows for the periods ended March 31, 2022, December 31, 2021, and March 31, 2021 (in thousands):

	March 31, 2022	December 31, 2021	March 31, 2021
Cash and cash equivalents	$ 164,890	$ 172,865	$ 72,519
Restricted cash	205	205	205
Total	**$ 165,095**	**$ 173,070**	**$ 72,724**

Inventories, Net

The Company's diamond, gemstone and jewelry inventories are primarily held for resale and valued at the lower of cost or net realizable value. Cost is primarily determined using the weighted average cost on a first-in, first-out ("FIFO") basis for all inventories, except for unique inventory SKUs (principally independently graded diamonds), where cost is determined using specific identification. Net realizable value is defined as estimated selling price in the ordinary course of business, less reasonably predictable costs of completion, disposal and transportation.

Revenue Recognition

Overview

Net sales primarily consist of revenue from diamond, gemstone and jewelry retail sales and payment is required in full prior to order fulfillment. Delivery is determined to be the time of pickup for orders picked up in showrooms, and for shipped orders, typically within one to two business days after shipment. Credit is not extended to customers except through third-party credit cards or financing offerings. A return policy of 30 days from when the item is picked up or ready for shipment is typically provided; one complimentary resizing for standard ring styles is offered within 60 days of when an order is available for shipment or pickup; a lifetime manufacturing warranty is provided on all jewelry, with the exception of estate and vintage jewelry and center diamonds/gemstones; and a lifetime diamond upgrade program is included on all independently graded natural diamonds. The complimentary resizing, lifetime manufacturing warranty claims and lifetime diamond upgrades have not historically been material. An in-house three-year extended service plan, which provides full inspection, cleaning and certain repairs due to normal wear, is offered for an additional charge. An extended protection plan is also offered through a third party that has different terms ranging from 2 years to lifetime that vary based on the item purchased.

The following table discloses total net sales by geography for the three months ended March 31, 2022 and 2021 (in thousands):

	For the Three Months Ended March 31,	
	2022	2021
United States	$ 93,766	$ 66,000
International	6,272	4,696
Total net sales	$ 100,038	$ 70,696

Revenue Recognition

Revenue is recognized under Financial Accounting Standards Board ("FASB") ASC 606, *Revenue from Contracts with Customers* ("ASC 606"). ASC 606 requires that revenue from customers be recognized as control of the promised goods is transferred to customers, which generally occurs upon delivery if the order is shipped, or at the time the customer picks up the completed product at a showroom. Revenue arrangements generally have one performance obligation and are reported net of estimated sales returns and allowances, which are determined based on historical product return rates and current economic conditions. The Company offers an in-house three-year extended service plan, which gives rise to an additional performance obligation, when purchased by the customer, which is recognized over the course of the plan. The Company also offers an extended protection plan in the capacity of an agent on behalf of a third-party that has different terms ranging from two years to lifetime that vary based on the item purchased. The commission that the Company receives from the third-party is recognized at the time of sale less an estimate of cancellations based on historical experience. There are no additional performance obligations in relation to the third-party plan. Additionally, sales taxes are collected and remitted to taxing authorities, and the Company has elected to exclude sales taxes from revenues recognized under ASC 606.

Contract Balances

Transactions where payment has been received from customers, but control has not transferred, are recorded as customer deposits in deferred revenue and revenue recognition is deferred until delivery has occurred. Deferred revenue also includes payments on the Company's three-year extended service plan that customers have elected to purchase. As of March 31, 2022 and December 31, 2021, total deferred revenue was $23.7 million and $19.0 million, respectively, of which $0.2 million and $0.2 million, respectively, were included within other long-term liabilities in the unaudited condensed consolidated balance sheets. During the three months ended March 31, 2022 and 2021, respectively, the Company recognized $17.6 million and $9.9 million, respectively, of revenue that was deferred as of the last day of the respective prior quarter.

Sales Returns and Allowances

A returns asset account and a refund liabilities account are maintained to record the effects of estimated product returns and sales returns allowance. Returns asset and refund liabilities are updated at the end of each financial reporting period and the effect of such changes are accounted for in the period in which such changes occur.

The Company estimates anticipated product returns in the form of a refund liability based on historical return percentages and current period sales levels, and accrues a related returns asset for goods expected to be returned in salable condition less any expected costs to recover such goods, including return shipping costs that the Company may incur.

As of March 31, 2022 and December 31, 2021, refund liabilities balances were $1.6 million and $2.3 million, respectively, and are included as a provision for sales returns and allowances within accrued expenses and other current liabilities in the unaudited condensed consolidated balance sheets. As of March 31, 2022 and December 31, 2021, returns asset balances were $0.7 million and $1.1 million, respectively, and are included within prepaid expenses and other current assets in the unaudited condensed consolidated balance sheets. See Note 5, *Accrued Expenses and Other Current Liabilities*, for further discussion.

Fulfillment Costs

The Company generally does not bill customers separately for shipping and handling charges. Any fulfillment costs incurred by the Company when shipping to customers is reflected in cost of sales in the unaudited condensed consolidated statements of operations.

Consignment Inventory Sales

Sales of consignment inventory are presented on a gross sales basis as control of the merchandise is maintained through the point of sale. The Company also provides independent advice, guidance and after-sales service to customers. Consigned products are selected at the discretion of the Company, and the determination of the selling price as well as responsibility of the physical security of the products is maintained by the Company. The products sold from consignment inventory are similar in nature to other products that the Company sells to customers and are sold on the same terms.

Cost of Sales

The Company purchases diamonds and gemstones from suppliers and utilizes third-party manufacturing suppliers for the production and assembly of substantially all jewelry sold by the Company. Cost of sales includes merchandise costs, inbound freight charges, costs of shipping orders to customers, costs and reserves for disposal of obsolete, slow-moving or defective items and shrinkage.

Marketing, Advertising and Promotional Costs

Marketing, advertising and promotional costs are expensed as incurred and totaled approximately $20.0 and $14.4 million, for the three months ended March 31, 2022 and 2021, respectively.

Equity-Based Compensation

Equity-based compensation is accounted for as an expense in accordance with ASC Topic 718, *Compensation - Stock Compensation*, with the fair value recognition and measurement provisions of U.S. GAAP which requires compensation cost for the grant-date fair value of equity-based awards to be recognized over the requisite service period. The Company uses the straight-line method to amortize all stock awards granted over the requisite service period of the award. The Company accounts for forfeitures when they occur, and any compensation expense previously recognized on unvested equity-based awards will be reversed when forfeited.

The fair value of awards of restricted LLC Units is based on the fair value of the member unit underlying the awards as of the date of grant. The fair value of the underlying member units (referred to as Class M Units prior to conversion to common LLC Units in the IPO on a value-for-value basis) for grants prior to the Company's IPO in September 2021 was determined by considering a number of objective, subjective and highly complex factors including independent third-party valuations of the Company's member units, operating and financial performance, the lack of liquidity of member units and general and industry specific economic outlook among other factors.

The fair value of restricted stock units ("RSUs") is based on the fair value of the Class A common stock at the time of grant.

The fair value of option-based awards is estimated using the Black-Scholes valuation model. The Black-Scholes model requires the use of highly subjective and complex assumptions, including the option's expected term and the price volatility of the underlying stock. For inputs into the Black-Scholes model, the expected stock price volatility for the common stock is estimated by taking the average historic price volatility for industry peers based on daily price observations over a period equivalent to the expected term of the stock option grants. Industry peers consist of several public companies in the Company's industry which are of similar size, complexity and stage of development. The risk-free interest rate for the expected term of the option is based on the U.S. Treasury implied yield at the date of grant. The Company has elected to use the "simplified method" to determine the expected term, which is the midpoint between the vesting date and the end of the contractual term, because it has insufficient history upon which to base an assumption about the term; the Company believes the simplified method approximates a term if it were to be based on expected life. The expected dividend yield is nil as the Company has not paid and does not anticipate paying dividends on its common stock.

Income Taxes

Interim Periods

In calculating the provision for interim income taxes, in accordance with ASC 740, *Income Taxes* an estimated annual effective tax rate is applied to year-to-date ordinary income. At the end of each interim period, the Company estimates the effective tax rate expected to be applicable for the full fiscal year. This differs from the method utilized at the end of an annual period.

Annual Reporting

For annual periods, income taxes are accounted for using the asset and liability method. Under this method, deferred tax assets and liabilities are recognized for the estimated future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. In assessing the realizability of deferred tax assets, management considers whether it is more-likely-than-not that the deferred tax assets will be realized. Deferred tax assets and liabilities are calculated by applying existing tax laws and the rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in the year of the enacted rate change.

Uncertainty in income taxes is accounted for using a recognition and measurement threshold for tax positions taken or expected to be taken in a tax return, which are subject to examination by federal and state taxing authorities. The tax benefit from an uncertain tax position is recognized when it is more likely than not that the position will be sustained upon examination by taxing authorities based on the technical merits of the position. The amount of the tax benefit recognized is the largest amount of the benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. The effective tax rate and the tax basis of assets and liabilities reflect management’s estimates of the ultimate outcome of various tax uncertainties. The Company recognizes penalties and interest related to uncertain tax positions within the provision (benefit) for income taxes line in the unaudited condensed consolidated statements of operations. As of March 31, 2022, no uncertain tax positions have been recorded. The Company will continue to monitor this position each interim period.

Recent Accounting Pronouncements

Recently adopted accounting pronouncements

In February 2016, the Financial Accounting Standards Board (“FASB”) issued ASU 2016-02 – *Leases*, and also issued subsequent amendments to the initial guidance, ASC 2018-10, ASC 2018-11, ASU 2019-10, ASU 2020-02 and ASU 2020-05 (collectively, “ASC 842”). ASC 842 introduces a lessee model that brings most leases on the balance sheet and, among other changes, eliminates the requirement in current GAAP for an entity to use bright-line tests in determining lease classification. ASC 842 allows for several practical expedients which permit the following: no reassessment of lease classification or initial direct costs; use of the standard’s effective date as the date of initial application; and no separation of non-lease components from the related lease components and, instead, to account for those components as a single lease component if certain criteria are met. The Company adopted this guidance by applying the modified retrospective approach effective January 1, 2022, and no cumulative effect adjustment was required to be recorded. See Note 6, *Leases*, for further discussion.

In December 2019, the FASB issued ASU 2019-12, Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes (“ASU 2019-12”), which modifies ASC 740 to reduce complexity while maintaining or improving the usefulness of the information provided to users of financial statements. ASU 2019-12 is effective for the Company for interim and annual reporting periods beginning after December 15, 2021. The Company adopted this guidance on January 1, 2022 and did not have a material impact on the Company's unaudited condensed consolidated financial statements.

Accounting pronouncements recently issued but not yet adopted

Other recent accounting pronouncements not yet adopted are not expected to have a material impact on the Company's unaudited condensed consolidated financial statements.

NOTE 3. EARNINGS PER SHARE

Basic earnings per share is computed by dividing net income applicable to Brilliant Earth Group, Inc. by the weighted average shares of Class A common stock outstanding (and Class D common stock if outstanding) during the period. Diluted earnings per share is computed by adjusting the net income available to Brilliant Earth Group, Inc. and the weighted average shares outstanding to give effect to potentially dilutive securities. Shares of Class B and Class C common stock are not entitled to receive any distributions or dividends and are therefore excluded from this presentation since they are not participating securities.

All earnings prior to September 23, 2021, the date of the IPO, were entirely allocable to the non-controlling interest and, as a result, earnings per share information is not applicable for reporting periods prior to this date. Consequently, earnings per share for net income for periods prior to September 22, 2021 are not presented.

Basic and diluted earnings per share of common stock for the three months ended March 31, 2022 have been computed as follows (in thousands, except share and per share amounts):

Numerator:		
Net income attributable to Brilliant Earth Group, Inc., BASIC	$	356
Add: Net income impact from assumed redemption of all LLC Units to common stock		3,013
Less: Income tax expense on net income attributable to NCI		(753)
Net income attributable to Brilliant Earth Group, Inc., after adjustment for assumed conversion, DILUTED	$	2,616
Denominator:		
Weighted average shares of common stock outstanding, BASIC		10,010,798
Dilutive effects of:		
Vested LLC Units that are exchangeable for common stock		84,858,932
LLC Units, RSUs and stock options		1,657,113
Weighted average shares of common stock outstanding, DILUTED		96,526,843
BASIC earnings per share	$	0.04
DILUTED earnings per share	$	0.03

Net income attributable to the non-controlling interest added back to net income in the fully dilutive computation has been adjusted for income taxes which would have been expensed had the income been recognized by Brilliant Earth Group, Inc., a taxable entity. The weighted average common shares outstanding in the diluted computation per share assumes all outstanding LLC Units are converted and the Company will elect to issue shares of common stock upon redemption rather than cash-settle.

For the three months ended March 31, 2022, the dilutive impact of LLC Units convertible into common stock were included in the computation of diluted earnings per share under the if-converted method; the dilutive impact of unvested LLC Units, RSUs and stock options were included using the treasury stock method.

NOTE 4. INVENTORIES, NET

Inventories, net consist of the following (in thousands):

	March 31, 2022	December 31, 2021
Loose diamonds	$ 8,367	$ 9,013
Fine jewelry and other	20,269	15,990
Allowance for inventory obsolescence	(244)	(260)
Total inventories, net	**$ 28,392**	**$ 24,743**

The allowance for inventory obsolescence consists of the following (in thousands):

	March 31, 2022	March 31, 2021
Balance at beginning of period	$ (260)	$ (242)
Change in allowance for inventory obsolescence	16	24
Balance at end of period	**$ (244)**	**$ (218)**

As of March 31, 2022 and December 31, 2021, the Company had $21.3 million and $16.9 million, respectively, in consigned inventory held on behalf of suppliers which is not recorded in the unaudited condensed consolidated balance sheets.

NOTE 5. ACCRUED EXPENSES AND OTHER CURRENT LIABILITIES

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

	March 31, 2022	December 31, 2021
Accrued vendor expenses	$ 8,608	$ 9,563
Inventory received not billed	6,500	4,648
Accrued payroll expenses	1,901	4,498
Sales and other tax payable accrual	2,890	4,229
Provision for sales returns and allowances	1,583	2,338
Other	4,947	3,480
Total accrued expenses and other current liabilities	**$ 26,429**	**$ 28,756**

Included in accrued expenses and other current liabilities is a provision for sales returns and allowances. Returns are estimated based on past experience and current expectations and are recorded as an adjustment to revenue. Activity for the three months ended March 31, 2022 and 2021 was as follows (in thousands):

	March 31, 2022	March 31, 2021
Balance at beginning of period	$ 2,338	$ 2,341
Provision	5,277	4,893
Returns and allowances	(6,032)	(6,014)
Balance at end of period	**$ 1,583**	**$ 1,220**

NOTE 6. LEASES

The Company leases its executive offices, retail showrooms, office and operational locations under operating leases. The fixed, non-cancelable terms of our real estate leases are generally 5- 10 years and typically include renewal options. Most of the real estate leases require payment of real estate taxes, insurance and certain common area maintenance costs in addition to future minimum lease payments.

The Company elected the package of practical expedients permitted under the transition guidance within ASC 842 which, among other items, allowed the Company to carry forward historical lease classifications. As such, the Company applied the modified retrospective approach as of the adoption date to those lease contracts for which it had taken possession of the property as of December 31, 2021. In addition to the aforementioned practical expedient, the Company has elected to:

- Adopt the short-term lease exception for leases with terms of twelve months or less and account for them as if they were operating leases under ASC 840; and
- Apply the practical expedient of combining lease and non-lease components.

The Company determines if an arrangement is a lease at inception. Right of use ("ROU") assets represent the Company's right to use an underlying asset for the lease term while lease liabilities represent the Company's obligation to make lease payments for the lease term. All leases greater than 12 months' result in the recognition of a ROU asset and liability at the lease commencement date based on the present value of the lease payments over the lease term. The present value of the lease payments is calculated using the applicable weighted-average discount rate. The weighted-average discount rate is based on the discount rate implicit in the lease, or if the implicit rate is not readily determinable from the lease, then the Company estimates an applicable incremental borrowing rate. The incremental borrowing rate is estimated using the currency denomination of the lease, the contractual lease term and the Company's applicable borrowing rate. The incremental borrowing rate represents the rate that would approximate the rate to borrow funds on a collateralized (or secured) basis over a similar term and in a similar economic environment.

The Company accounts for lease components separately from non-lease components. Generally, the real estate leases have initial terms ranging from five to ten years and typically include a five-year renewal option. Renewal options are typically not included in the lease term as it is not reasonably certain at commencement date that the Company would exercise the options to extend the lease. The exercise of the lease renewal options is at the Company's discretion and are included in the determination of the ROU asset and lease liability when the option is reasonably certain of being exercised.

As of March 31, 2022, no renewal option periods were included in the estimated minimum lease terms as the options were not deemed to be reasonably certain to be exercised. The Company expends cash for leasehold improvements to build out and equip for its leased premises. Generally, a portion of the leasehold improvements costs are reimbursed by the landlords as tenant improvement allowances pursuant to agreed-upon terms in the lease agreements. Tenant improvement allowances are recorded as part of the lease liability on the unaudited condensed consolidated balance sheet and are amortized on a straight-line basis over the lease term. Operating leases with fixed minimum rent payments are recognized on a straight-line basis over the lease term starting on the date the Company takes possession of the leased property.

Total operating lease ROU assets and lease liabilities were as follows (in thousands):

Assets	**Classification**		**As of March 31, 2022**
Operating ROU assets at cost	Operating lease right of use assets	$	20,750
Accumulated amortization	Operating lease right of use assets		(683)
Net book value		**$**	**20,067**

Liabilities	**Classification**		**As of March 31, 2022**
Current:			
Operating leases	Current portion of operating lease liabilities	$	2,779
Noncurrent:			
Operating leases	Operating lease liabilities		19,882
Total lease liabilities		**$**	**22,661**

Total operating lease costs were as follows (in thousands):

	Classification		**For the three months ended March 31, 2022**
Operating lease costs	Selling, general and administrative expense	$	924

The maturity analysis of the operating lease liabilities under long-term non-cancelable operating leases, where the Company has taken physical possession of or has control of the physical use of these leased properties, as of March 31, 2022 was as follows (in thousands):

		Amount
For the nine months ending December 31, 2022	$	2,645
Years ending December 31,		
2023		4,164
2024		3,995
2025		3,930
2026		3,564
2027		2,089
Thereafter		6,304
Total minimum lease payments		26,691
Less: imputed interest		(4,030)
Net present value of operating lease liabilities		**22,661**
Less: current portion		(2,779)
Long-term portion	**$**	**19,882**

The following table summarizes the weighted-average remaining lease term and weighted-average discount rate on long-term leases as of March 31, 2022 (in thousands):

Weighted-average remaining lease term - operating leases		5.8 years
Weighted-average discount rate - operating leases		4.2 %
ROU assets and lease obligations recognized upon adoption of ASC 842 on January 1, 2022:		
ROU assets	$	19,173
Operating lease obligations	$	(21,316)
Supplemental cash flow information related to operating leases as of March 31, 2022 is as follows:		
Cash paid for amounts included in lease liabilities for the three months ended March 31, 2022:		
Operating cash flows from operating leases	$	1,005
ROU assets obtained in exchange for new operating lease liabilities	$	1,577

NOTE 7. LONG-TERM DEBT

The following table summarizes the net carrying amount of the Term Loan (as defined below) as of March 31, 2022 and December 31, 2021, net of debt issuance costs (in thousands):

	March 31, 2022			December 31, 2021		
	Outstanding principal	**Debt issuance costs**	**Net carrying amount**	**Outstanding principal**	**Debt issuance costs**	**Net carrying amount**
Term loan	$ 65,000	$ (1,084)	$ 63,916	$ 65,000	$ (1,422)	$ 63,578
Total debt	$ 65,000	$ (1,084)	$ 63,916	$ 65,000	$ (1,422)	$ 63,578
Current portion	$ 41,053	$ —	$ 41,053	$ 30,789	$ —	$ 30,789
Long term	23,947	(1,084)	22,863	34,211	(1,422)	32,789
Total debt	$ 65,000	$ (1,084)	$ 63,916	$ 65,000	$ (1,422)	$ 63,578

The Company entered into a Loan and Security Agreement (the “Term Loan Agreement”) on September 30, 2019 with Runway Growth Credit Fund Inc. (the “Lender”) for a $40.0 million term loan, of which $35.0 million was defined as the First Tranche Term Loan and $5.0 million was the Second Tranche Term Loan. The $35.0 million First Tranche Term Loan was drawn on September 30, 2019. Payments were interest only through October 15, 2021 (first scheduled amortization payment) after which equal monthly payments of principal were due through April 15, 2023 (maturity date). Interest was at a variable rate equal to LIBOR (floor of 2.15%) plus 8.25%.

The Term Loan (the “Term Loan”) under the Term Loan Agreement is secured by substantially all assets of the Company, and the Company is required to comply with certain covenants, including a covenant that requires the Company to reach certain minimum liquidity requirements of cash and cash equivalents as defined in the Term Loan Agreement. The Company was in compliance with all covenants as of March 31, 2022. Prepayment fees of 3.00% declining to 0.00% were provided based on the anniversary date of payment.

Debt issuance costs of $2.6 million were capitalized and are being amortized to interest expense as an adjustment to yield using the effective interest method. Included in the debt issuance costs is the present value of a $1.6 million final payment due on April 15, 2023 (the "Final Payment"), which is being accreted to full value over the term and is recorded in other long-term liabilities in the unaudited condensed consolidated balance sheets.

In connection with the origination of the Term Loan Agreement, a warrant for 333,333 Class P Units was issued. The fair value of the warrant was $0.1 million at the time of issuance which was accounted for as a debt origination cost (contra-liability). The warrants had a carrying value of $6.4 million as of September 22, 2021 (after the mark-to-market adjustment as of the date of exercise) and were converted upon exercise into 534,589 newly issued LLC Units on a net settlement basis, elected at the option of the holder.

On December 17, 2020, the Company entered into a First Amendment to the Term Loan Agreement with the Lender (the "First Amendment") to expand the Second Tranche Term Loan from $5.0 million to $30.0 million for a total commitment of $65.0 million. Up to $30.0 million of the proceeds from the Second Tranche Term Loan could be distributed to the holders of the equity interests within 90 days of closing. Other modifications in the First Amendment include:

- Closing fee of $0.3 million related to this new facility;
- Reduction in the LIBOR Floor on the entire facility from 2.15% to 1.00% (effective interest rate reduced from 10.40% to 9.25% based on LIBOR);
- Extension of the maturity to October 15, 2023;
- Extension of the interest-only period by six months (first scheduled amortization payment on April 15, 2022);
- Allowance of quarterly tax distributions to members;
- Extension of the prepayment term trigger dates by six months;
- Modification of the Final Payment, as defined, to include the present value of an additional $1.4 million, which represents the incremental increase in the Final Payment due to the increase in the Term Loan principal, and an additional $0.2 million, which are included in the debt issuance costs, and are being accreted to full value as an adjustment to the interest rate in other long-term liabilities in the unaudited condensed consolidated balance sheets; and
- Issuance of 25,000 new warrants to the Lender with an exercise price of $10.00 per Unit with a term of ten years. These warrants were accounted for using a similar methodology to the valuation of the original warrants discussed above, and the fair value was determined to be less than $0.1 million. The warrants were converted into LLC Units at the time of the IPO.

The accreted Final Payments recorded in other long-term liabilities were $2.9 million and $2.8 million as of March 31, 2022 and December 31, 2021, respectively.

On August 6, 2021, a second amendment was executed primarily to allow for contributions to the Brilliant Earth Foundation. On August 29, 2021, a third amendment was executed to among other matters, permit the Reorganization Transactions that were consummated by the Company in connection with the Up-C structure of the IPO transaction and reduce the variable interest rate from 8.25% to 7.75%; and the LIBOR Floor from 1.00% to 0.50%. The amendments were treated as debt modifications for accounting purposes.

The effective interest rate was 11.08% and 12.02% for the three months ended March 31, 2022 and 2021, respectively. Interest expense was $1.4 million, and $1.5 million; and the amortization of deferred issuance costs was $0.4 million and $0.4 million for the three months ended March 31, 2022 and 2021, respectively.

As of March 31, 2022, the aggregate future principal payments under the Term Loan, including the Final Payment payable to the lender, are as follows (in thousands):

	Principal	Final payment	Total
Years ending December 31,			
2022	$ 41,053	$ —	$ 41,053
2023	23,947	3,151	27,098
Total aggregate future principal payments	$ 65,000	$ 3,151	$ 68,151

NOTE 8. STOCKHOLDERS' AND MEMBERS' EQUITY

Summary Capitalization

The following summarizes the capitalization and voting rights of the Company's classes of equity as of March 31, 2022 and December 31, 2021:

		March 31, 2022	December 31, 2021		
	Authorized	**Issued & Outstanding**		**Votes per share**	**Economic Rights**
Preferred stock	10,000,000	None	None		
Common stock:					
Class A	1,200,000,000	10,708,456	9,614,523	1	Yes
Class B	150,000,000	35,326,696	35,658,013	1	No
Class C	150,000,000	49,119,976	49,505,250	10	No
Class D	150,000,000	None	None	10	Yes
Common stock reserved for issuances:					
Conversion of LLC Units		84,446,672	85,163,263		
Unvested LLC Units		1,074,874	1,901,977		
Unvested RSUs		2,462,868	1,377,728		
Stock options		1,449,181	1,449,181		
Common LLC Units		84,446,672	85,163,263	No	Yes

The Board of Directors is authorized to direct the Company to issue shares of preferred stock in one or more series and the discretion to determine the number and designation of such series and the powers, rights, preferences, privileges and restrictions, including voting rights, dividend rights, conversion rights, redemption privileges and liquidation preferences, of each series of preferred stock. Through March 31, 2022, no series of preferred stock have been issued.

Shares of Class B and Class C common stock are not entitled to receive any distributions or dividends other than in connection with a liquidation and have no rights to convert into Class A common stock or

Class D common stock, separate from an exchange or redemption of the LLC Interests corresponding to such shares of Class B common stock or Class C common stock, as applicable, as discussed below under *Brilliant Earth, LLC*. When a common unit is redeemed for cash or Class A or D common stock by a Continuing Equity Owner who holds shares of Class B common stock or Class C common stock, such Continuing Equity Owner will be required to surrender a share of Class B common stock or Class C common stock, as applicable, which will be cancelled for no consideration.

The Company must, at all times, maintain (i) a one-to-one ratio between the number of shares of Class A common stock issued to Brilliant Earth Group, Inc. and the number of LLC Interests owned by Brilliant Earth Group, Inc., and (ii) maintain a one-to-one ratio between the number of shares of Class B and Class C common stock owned by the Continuing Equity Owners and the number of LLC Interests owned by them.

The different classes of common stock as of March 31, 2022, are held as follows:

- 10,708,456 shares of Class A common stock were issued in the IPO, and through subsequent conversion of LLC Units and vesting of RSUs;

- 35,326,696 shares of Class B common stock are held by the Continuing Equity Owners excluding the Founders; and

- 49,119,976 shares of Class C common stock are held by the Founders.

Class C and D common stock may only be held by the Founders and their respective permitted transferees. No shares of Class D common stock are outstanding, but may be issued in connection with an exchange by the Founders of their LLC Interests (along with an equal number of shares of Class C common stock and such shares shall be immediately cancelled).

Brilliant Earth, LLC

As of March 31, 2022, Brilliant Earth Group, Inc. holds a 11.3% economic interest in Brilliant Earth, LLC through its ownership of 10,708,456 LLC Units, but consolidates Brilliant Earth, LLC as sole managing member. The remaining 84,446,672 LLC Units representing an 88.7% interest are held by the Continuing Equity Owners and presented in the condensed consolidated financial statements as a non-controlling interest.

The organization agreements include a provision for the Continuing Equity Owners, subject to certain exceptions from time to time at each of their option, to require Brilliant Earth, LLC to redeem all or a portion of their LLC Units in exchange for, at the Company’s election, newly-issued shares of Class A common stock or Class D common stock, as applicable, on a one-for-one basis or, at the Company's election, a cash payment equal to a volume weighted average market price of one share of Class A common stock for each LLC Interest so redeemed, in each case, in accordance with the terms of the Brilliant Earth LLC Agreement. The redemption feature is not bifurcated from the underlying LLC Unit.

Issuance of Additional LLC Units

Under the LLC Agreement, the Company is required to cause Brilliant Earth, LLC to issue additional LLC Interests to the Company when the Company issues additional shares of Class A common stock. Other than as it relates to the issuance of Class A common stock in connection with an equity incentive program, the Company must contribute to Brilliant Earth, LLC net proceeds and property, if any, received by the Company with respect to the issuance of such additional shares of Class A common stock. The Company must cause Brilliant Earth, LLC to issue a number of LLC Interests equal to the number of shares of Class A common stock issued such that, at all times, the number of LLC Interests held by the Company equals the number of outstanding shares of Class A common stock.

For the three months ended March 31, 2022, the Company caused Brilliant Earth, LLC to issue to the Company a vested total of 40,019 LLC Units for RSUs. The Company also caused Brilliant Earth Group, Inc. to issue 337,323 shares of Class B common stock to the Continuing Equity Owners associated with LLC units which vested during the period. There were 668,640 shares of Class B and 385,274 shares of Class C common stock converted to Class A common stock related to the Continuing Equity Owners. No stock options were exercised during the period.

Distributions to Members Related to Their Income Tax Liabilities

As a limited liability company treated as a partnership for income tax purposes, Brilliant Earth, LLC does not incur significant federal, state or local income taxes, as these taxes are primarily the obligations of its members. Under the LLC Agreement, Brilliant Earth, LLC is required to distribute cash, to the extent that Brilliant Earth, LLC has cash available, on a pro rata basis to its members to the extent necessary to cover the members' tax liabilities, if any, with respect to each member's share of Brilliant Earth, LLC taxable earnings. Brilliant Earth, LLC makes such tax distributions to its members quarterly, based on an estimated tax rate and projected year-to-date taxable income, with a final accounting once actual taxable income or loss has been determined. Such distributions totaled approximately $6.9 million and $0.1 million respectively, for the three months ended March 31, 2022 and March 31, 2021.

NOTE 9. EQUITY-BASED COMPENSATION

Overview

At the time of the IPO on September 23, 2021, the 2021 Incentive Award Plan and the 2021 Employee Stock Purchase Plan (the "2021 Plans") were adopted to attract, retain, and motivate selected employees, consultants, and directors through the granting of equity-based compensation awards and cash-based performance bonus awards. The compensation committee or its approved designees, as defined, administer the 2021 Plans. Subject to the terms and conditions of the 2021 Plans, the administrator has the authority to select the persons to whom awards are to be made, to determine the number of shares to be subject to awards and the terms and conditions of awards, and to make all other determinations and to take all other actions necessary or advisable for the administration of the 2021 Plans.

Under the 2021 Incentive Award Plan, 10,923,912 shares of common stock were reserved for issuance pursuant to a variety of equity-based compensation awards, including stock options, stock appreciation rights, or SARs, restricted stock awards, restricted stock unit awards, and other equity-based awards. In addition, 1,638,586 shares of Class A common stock were reserved for issuance under our Employee Stock Purchase Plan. The number of shares initially reserved for issuance or transfer pursuant to awards under the 2021 Incentive Award Plan will be increased by an annual increase on the first day of each fiscal year beginning in 2022 and ending in 2031, equal to the lesser of (A) 5% of the shares of common stock outstanding (on an as converted basis) on the last day of the immediately preceding fiscal year and (B) such smaller number of shares of stock as determined by the board of directors; provided, however, that no more than 81,929,342 shares of stock may be issued upon the exercise of incentive stock options. As of March 31, 2022, 9,391,642 shares of common stock are available for future grant under the 2021

Incentive Award Plan. All of the shares of Class A common stock reserved for issuance remain available. Vesting is subject to certain change in control provisions as provided in the award agreements.

Prior to the IPO, Class M Units were granted to certain employees at the Company's discretion in consideration of services provided by employees. The agreements generally provide for 25% vesting on the first anniversary from the date of grant (or a shorter period at the Company's board of directors' discretion), with the remainder vesting monthly over the subsequent three years. Compensation cost related to these Class M Units was measured as of the grant date based on the fair value of the award and is being expensed ratably over the service period. Class M Units were issued and outstanding as of the date of grant. As discussed in Note 1, *Business and organization*, under *Conversion of Class F, P and M units at time of IPO,* at the time of the IPO, the LLC Agreement was amended and restated to recapitalize all 2,006,212 unvested Class M Units into 2,046,008 unvested LLC Units after applying a conversion ratio of 1.8588 with a further adjustment for a distribution threshold (which impacted their allocation of value) so the economic effect of the exchange was a like-for-like value. The unamortized compensation and remaining vesting period for these awards prior to the IPO has been carried forward after the IPO without adjustment. The number of unvested Class M Units presented in these financial statements for periods prior to the IPO have been retroactively adjusted to reflect the conversion ratio similar to the presentation of a stock-split.

Grants of Restricted Stock Units

RSUs have a time-based vesting requirement (based on continuous employment). Upon vesting, the RSUs convert into Class A common stock; unvested RSUs are not considered outstanding shares of Class A common stock. The agreements generally provide for 25% vesting at the first anniversary of the date of the grant (or a shorter period at the Company's board of director's discretion), with the remainder vesting quarterly over the following three years.

The following table summarizes the activity related to the Company's RSUs for the three months ended March 31, 2022:

	Number of Restricted Stock Units	Weighted Average Grant Date Fair Value
Balance as of December 31, 2021, unvested	1,377,728	$ 13.15
Granted	1,192,805	$ 11.08
Vested	(40,019)	$ 12.00
Forfeited	(67,646)	$ 13.32
Balance as of March 31, 2022, unvested	2,462,868	$ 12.16

The fair value of the RSUs was based on the fair value of a Class A share of common stock at the time of grant. Total compensation expense for RSUs was approximately $1.4 million for the three months ended March 31, 2022, and is included in selling, general and administrative expenses in the unaudited condensed consolidated statements of operations. No tax benefit was associated with the equity-based compensation expense for RSUs.

The unamortized compensation cost related to RSUs of $28.0 million as of March 31, 2022 is expected to be recognized over a weighted-average period of approximately 3.7 years.

Grants of Stock Options

On September 22, 2021, options to purchase 1,618,064 shares of Class A common stock with a strike price of $12.00 (per share underlying the option) were granted to certain executives, employees and members of the Board with the number of shares underlying the options determined based on the number of Class M Units reduced in the conversion of LLC Units. The awards have a time-based vesting requirement (based on continuous employment). Upon vesting, the stock options are exercisable into Class A common stock. Vesting is generally over four years from the date of grant of the related Class M Units and options may be exercised up to 10.0 years from the date of issuance.

The following table summarizes the activity related to the outstanding and exercisable stock options:

	Number of options	Weighted Average Grant Date Fair Value
Outstanding as of December 31, 2021	1,612,133	$ 4.28
Forfeited	(468,189)	$ 4.29
Outstanding as of March 31, 2022	1,143,944	$ 4.29
Vested and exercisable as of March 31, 2022	458,008	$ 4.26
Unvested as of March 31, 2022	685,936	$ 4.29
Vested and expected to vest as of March 31, 2022	1,143,944	$ 4.28

As of March 31, 2022, the vested stock options did not have an aggregated intrinsic value as the exercise price exceeded the estimated fair market value of the stock options. The stock option awards have weighted average remaining contractual terms of 9.5 years.

Since options represent equity awards, such awards are fair valued as of the grant date for the purposes of measurement and recognition under U.S. GAAP. To measure the fair value of an option, the Black Scholes valuation model was utilized. The value of the common stock underlying the award is based on the fair value of a share of Class A common stock. The valuation model requires the input of other highly subjective assumptions. Inputs to model for awards granted on September 22, 2021 are as follows:

Expected volatility	35.0 %
Expected dividend yield	Nil
Expected term (in years)	5.0 to 6.3 Years
Risk free interest rate	0.9 %

Total compensation expense for stock options was approximately $0.6 million for the three months ended March 31, 2022, and is included in selling, general and administrative expenses in the unaudited condensed consolidated statements of operations.

As of March 31, 2022, total compensation cost related to unvested option awards not yet recognized was $2.9 million and the weighted-average period over which the compensation is expected to be recognized is 2.9 years.

Outstanding Restricted LLC Units (formerly M Units)

As discussed above, restricted LLC Units were granted to certain executives, employees and members of the Board prior to the IPO and have been retroactively adjusted as described in Note 1, *Business and Organization, Conversion of Class F, P and M Units at Time of IPO*. The awards have a time-based vesting requirement (based on continuous employment). Upon grant, the awards are issued and outstanding common LLC Units but subject to forfeiture in the event of a termination of service; unvested awards are outstanding LLC units. Vesting is generally over four years from the date of grant.

The following table summarizes the activity related to the unvested LLC Units for the three months ended of each period:

	Number of LLC Units	Weighted average grant date fair value
Balance, December 31, 2020, unvested	1,485,946	$ 0.29
Granted	1,187,852	$ 0.21
Forfeited	(17,733)	$ 0.30
Vested	(325,211)	$ 0.29
Balance, March 31, 2021, unvested	2,330,854	$ 0.25

	Number of LLC Units	Weighted average grant date fair value
Balance, December 31, 2021, unvested	1,901,977	$ 0.52
Forfeited	(489,780)	$ 0.21
Vested	(337,323)	$ 0.42
Balance, March 31, 2022, unvested	1,074,874	$ 0.68

The fair value of restricted LLC Units was based on the fair value of an unrestricted LLC Unit at the date of grant. Total compensation expense for unvested LLC Units recorded in selling, general and administrative expenses in the unaudited condensed consolidated statements of operations were approximately $0.1 million and $0.1 million, for the three months ended March 31, 2022 and 2021, respectively.

The unamortized LLC Unit compensation cost of $0.7 million as of March 31, 2022 is expected to be recognized over a weighted-average period of approximately 2.7 years.

NOTE 10. INCOME TAXES AND TAX RECEIVABLE AGREEMENT

Overview of Income Taxes

Brilliant Earth Group, Inc. is taxed as a subchapter C corporation and is subject to federal and state income taxes. Brilliant Earth Group, Inc.'s sole material asset is its ownership interest in Brilliant Earth, LLC, which is a limited liability company that is taxed as a partnership for U.S. federal and certain state and local income tax purposes. Brilliant Earth, LLC's net taxable income or loss and related tax credits are passed through to its members on a pro-rata basis and included in the member's tax returns. The income tax burden on the earnings taxed to the non-controlling interest holders is not reported by the Company in its unaudited condensed consolidated financial statements under U.S. GAAP.

The Company files U.S. federal and certain state income tax returns. The income tax returns of the Company are subject to examination by U.S. federal and state taxing authorities for various time periods, depending on those jurisdictions' rules, generally after the income tax returns are filed.

Tax Provision and Deferred Tax Asset

In calculating the provision for interim income taxes in accordance with ASC Topic 740, *Income Taxes*, an estimated annual effective tax rate is applied to year-to-date ordinary income. At the end of each interim period, Brilliant Earth Group, Inc. estimates the effective tax rate expected to be applicable for the full fiscal year. This differs from the method utilized at the end of an annual period. The Company's effective tax rate of 2.8% for the quarter ended March 31, 2022, differs from the U.S. federal statutory tax rate of 21% primarily due to income associated with the non-controlling interest, state tax expense and other permanent items.

The Company recorded net increases in deferred tax assets of $3.4 million during the three months ended March 31, 2022, with a corresponding increase to additional paid in capital, resulting from changes in the outside basis difference on Brilliant Earth's investment in LLC. The Company has determined it is more-likely-than-not that it will be able to realize this deferred tax asset in the future. The Company's income tax provision was $0.1 million for the three months ended March 31, 2022. As the IPO occurred during the quarter ended September 30, 2021, and the Company had no business transactions or activities prior to the IPO, no amounts related to the provision for income taxes were recognized for the three months ended March 31, 2021.

On September 23, 2021, the Company recorded a deferred tax asset related to the outside basis difference between U.S. GAAP and reporting for income tax purposes of the Company's investment in Brilliant Earth, LLC of $4.4 million. The basis difference resulted from the step-up in basis allowed under Section 743(b) and 197 of the Internal Revenue Code related to the purchase of 1,249,999 LLC Units from the Continuing Equity Owners discussed in Note 1, *Business and organization,* which is expected to be amortized over the useful lives of the underlying assets. In assessing the realizability of deferred tax assets, management determined that it was more likely than not that the deferred tax assets will be realized. No deferred taxes were provided on the inside basis difference resulting from the direct purchase of 8,333,333 newly-issued membership units from Brilliant Earth, LLC since such difference is subject to the indefinite reversal criteria of ASC 740, *Income taxes.*

Tax receivable agreement

As each of the Continuing Equity Owners elect to convert their LLC Interests into Class A common stock or Class D common stock, as applicable, Brilliant Earth Group, Inc. will succeed to their aggregate historical tax basis which will create a net tax benefit to the Company. These tax benefits are expected to be amortized over 15.0 years pursuant to Sections 743(b) and 197 of the Code. The Company will only recognize a deferred tax asset for financial reporting purposes when it is "more-likely-than-not" that the tax benefit will be realized.

In addition, as part of IPO, the Company entered into a TRA with the Continuing Equity Owners to pay 85% of the tax savings from the tax basis adjustment to them as such savings are realized. Amounts payable under the TRA are contingent upon, among other things, generation of sufficient future taxable income during the term of the TRA.

The Company has recorded a liability under the tax receivable agreement of $6.6 million as of March 31, 2022. The tax receivable agreement provides for the payment of 85% of the amount of the tax benefits, if any, that Brilliant Earth is deemed to realize as a result of increases in the tax basis of its ownership in LLC related to exchanges of non-controlling interest for Class A common stock. $0.1 million expected to be paid within the next 12 months.

NOTE 11. COMMITMENTS AND CONTINGENCIES

Legal Proceedings

In the ordinary course of business, the Company may be subject from time to time to various proceedings, lawsuits, disputes or claims. In addition, the Company is regularly audited by various tax authorities. Although the Company cannot predict with assurance the outcome of any litigation or audit, it does not believe there are currently any such actions that, if resolved unfavorably, would have a material impact on the Company's financial condition, results of operations or cash flows. The Company accrues for loss contingencies when losses become probable and are reasonably estimable. If the reasonable estimate of the loss is a range and no amount within the range is a better estimate, the minimum amount of the range is recorded as a liability. The Company does not accrue for contingent losses that, in its judgment, are considered to be reasonably possible, but not probable; however, to the extent possible, the Company discloses the range of such reasonably possible losses.

On August 26, 2021, Plaintiff Anna Lerman filed a complaint against the Company in California Superior Court for Ventura County. The complaint alleges, on behalf of a putative class, that the Company recorded telephone calls between the Company's customers and its customer service representatives without the customers' consent, in violation of the California Invasion of Privacy Act Sections 631 and 632.7. The plaintiff seeks statutory damages, injunctive relief, attorneys' fees and costs, and other unspecified damages. The Company has obtained an extension of time to file a response, the time to file such response has not yet passed, and as of the date of this Quarterly Report on Form 10-Q, the Company has not responded to the complaint. The Company believes these claims have no merit, and intends to vigorously defend against this lawsuit, though there can be no assurance regarding its ultimate outcome. At this time, any liability related to the alleged claims is not currently probable or reasonably estimable.

Non-Income Related Taxes

The Company collects and remits sales and use taxes in a variety of jurisdictions across the U.S. The amounts payable to relevant sales and use tax authorities are accrued in the period incurred and presented on the balance sheet as a component of accrued expenses and other current liabilities.

Purchase Obligations

From time to time in the normal course of business, the Company will enter into agreements with suppliers or service providers. As of March 31, 2022, unconditional future minimum payments under agreements to purchase services primarily related to software maintenance and marketing and advertising spending. The Company does not have a material amount of purchase obligations from contracts with a remaining term in excess of 12 months.

Capital Commitments

The Company may enter into commitments to expand various locations, which generally include design, store construction and improvements. As of March 31, 2022, these commitments totaled $3.2 million related to the opening of new locations.

Letter of Credit

As of March 31, 2022, the Company has an unused letter of credit in the amount of $0.2 million, which was issued in lieu of a security deposit at one of its showroom locations. The certificate of deposit used to secure this letter of credit is recorded as restricted cash on the Company's unaudited condensed consolidated balance sheets.

401K Plan

The Company maintains a qualified defined contribution plan under Section 401(k) of the Internal Revenue Code, which provides for voluntary contributions from the Company and its employees. Contributions from the Company were $0.3 million and $0.2 million, for the three months ended March 31, 2022 and 2021, respectively.

NOTE 12. SUBSEQUENT EVENTS

The Company entered into 3 new lease agreements in additional locations in the U.S. for showrooms, where the Company had not yet taken physical possession of nor had control of the physical use of these leased properties, with future minimum aggregate rent payments totaling approximately $3.9 million.

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

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the information presented in the unaudited condensed consolidated financial statements and related notes included elsewhere in this Quarterly Report on Form 10-Q, as well as our audited consolidated financial statements and related notes as disclosed in our 2021 Form 10-K filed with the Securities and Exchange Commission ("SEC"), March 22, 2022. The following discussion and analysis reflects the historical results of operations and financial position of Brilliant Earth, LLC prior to the Reorganization Transactions on September 22, 2021 and that of Brilliant Earth Group, Inc. and its consolidated subsidiary, Brilliant Earth, LLC, following the completion of the Reorganization Transactions. In addition to historical information, the following discussion contains forward-looking statements, such as statements regarding our expectation for future performance, liquidity and capital resources, that involve risks, uncertainties and assumptions that could cause actual results to differ materially from our expectations. Our actual results may differ materially from those contained in or implied by any forward-looking statements. Factors that could cause such differences include those identified below and those described in "Cautionary Note Regarding Forward-Looking Statements," and "Risk Factors" in this Quarterly Report on Form 10-Q. We assume no obligation to update any of these forward-looking statements.

Company Overview

Brilliant Earth is an innovative, digital-first jewelry company, and a global leader in ethically sourced fine jewelry. We offer exclusive designs with superior craftsmanship and supply chain transparency, delivered to customers through a highly personalized omnichannel experience. We operate in one operating and reporting segment, the retail sale of diamonds, gemstones, and jewelry.

Our mission is to create a more transparent, sustainable, compassionate, and inclusive jewelry industry, and we are proud to offer customers distinctive and thoughtfully designed products that they can truly feel good about wearing. Our core values resonate strongly across many demographics and particularly with values-driven Millennial and Gen Z consumers.

Our extensive collection of premium-quality diamond engagement and wedding rings, gemstone rings, and fine jewelry is conceptualized by our leading in-house design studio and then brought to life by expert jewelers. From our award-winning jewelry designs to our responsibly sourced materials, at Brilliant Earth we aspire to exceptional standards in everything we do.

We were founded in 2005 as an e-commerce company with an ambitious mission and a single showroom in San Francisco. We have rapidly scaled our business while remaining focused on our mission and elevating the omnichannel customer experience. Through our intuitive digital commerce platform and personalized individual appointments in our showrooms, we cater to the shopping preferences of tech-savvy next-generation consumers. We create an educational, joyful, and approachable experience that is unique in the jewelry industry. As of March 31, 2022, Brilliant Earth has sold to consumers in over 50 countries.

Throughout our history, we have invested in technology to create a seamless customer experience, inform our data-driven decision-making, improve efficiencies, and advance our mission. Our technology enables dynamic product visualization, augmented reality try-on, blockchain-enabled transparency, and rapid fulfillment of our flagship Create Your Own product, a custom design process. We leverage powerful data capabilities to improve our marketing and operational efficiencies, personalize the customer experience, curate showroom inventory and merchandising, inform real estate decisions, and develop new product designs that reflect consumer preferences. We believe the Brilliant Earth digital experience drives higher satisfaction, engagement, and conversion both online and in-showroom.

We have achieved strong financial performance and rapid growth since our founding with minimal outside funding, and believe we are in the early stages of realizing our potential in a significant market opportunity.

Below is a summary of our performance for the three months ended March 31, 2022:

- Net sales of $100.0 million, up 41.5% from $70.7 million for the three months ended March 31, 2021;
- Net income of $3.4 million, up 39.9% from $2.4 million for the three months ended March 31, 2021;
- Net income margin of 3.4%, compared to 3.4% for the three months ended March 31, 2021;
- Adjusted EBITDA of $8.4 million, up 28.8% from $6.5 million for the three months ended March 31, 2021; and
- Adjusted EBITDA margin of 8.4%, compared to 9.2% for the three months ended March 31, 2021.

We operate in one operating and reporting segment, the retail sale of diamonds, gemstones, and jewelry.

Initial Public Offering and Purchase of LLC Interests

On September 27, 2021, we completed our IPO of 9,583,332 shares of Class A common stock at an offering price of $12.00 per share, (excluding the underwriting discount), including 1,249,999 shares of Class A common stock issued pursuant to the underwriters' over-allotment option. We received $101.6 million in proceeds after a deduction for underwriting discounts and offering costs totaling $13.4 million.

The net proceeds were used to purchase 8,333,333 newly-issued membership units (the “LLC Units” or “LLC Interests”) from Brilliant Earth, LLC and 1,249,999 LLC Units in the form of a redemption from the Continuing Equity Owners at a price per unit equal to the IPO price of $11.22 per share after deducting the underwriting discount, which represented a 10.1% economic interest as of the IPO date.

Conversion of Class F, P and M Units at Time of IPO

At the time of the IPO, the existing limited liability company agreement of Brilliant Earth, LLC was amended and restated to, among other things, recapitalize all existing Class F, P and M Units in Brilliant Earth, LLC into 86,297,284 common LLC Units after applying a conversion ratio of 1.8588 with a further adjustment for a distribution threshold related to the M Units (which impacted their allocation of value so the economic effect of the exchange was a like-for-like value); the net conversion ratio was 1.8942, 1.9080 and 1.7735 for the Class F Units, P Units and M Units, respectively. The number of Class F, P and M Units presented in these unaudited condensed consolidated financial statements for periods prior to the IPO have been retroactively adjusted to reflect the conversion ratios (as discussed in the preceding sentence) similar to the presentation of a stock-split.

Summary of the Restructuring, Offering and Other Transactions Completed in Connection with the IPO

In connection with the IPO, Brilliant Earth Group, Inc. and Brilliant Earth, LLC completed a series of transactions that comprise of reorganization, offering and other financing transactions.

The following summarizes the Reorganization Transactions which occurred as of the date of IPO:

- Amended and restated the existing limited liability company agreement of Brilliant Earth, LLC (the "LLC Agreement"), effective prior to the IPO, to, among other things, (1) recapitalize all existing ownership interests in Brilliant Earth, LLC into 86,297,284 LLC Units after applying a conversion ratio of 1.8588, (2) appoint Brilliant Earth Group, Inc. as the sole managing member of Brilliant Earth, LLC, upon its acquisition of LLC Units in connection with the IPO, and (3) provide certain redemption rights to the Continuing Equity Owners.

- Amended and restated Brilliant Earth Group, Inc.'s certificate of incorporation to, among other things, provide for four classes of common stock defined as Class A common stock, Class B common stock, Class C common stock and Class D common stock.

- Issued 36,064,421 shares of Class B common stock (prior to the redemption of 522,386 shares pursuant to the exercise of underwriters' overallotment options discussed below) to the Continuing Equity Owners, excluding the Founders, which is equal to the number of LLC Units held by such Continuing Equity Owners excluding the Founders, for nominal consideration.

- Issued 50,232,863 shares of Class C common stock (prior to the redemption of 727,613 shares pursuant to the exercise of underwriters' overallotment options discussed below) to the Founders, which is equal to the number of LLC Units held by such Founders, for nominal consideration.

- Entered into a TRA with Brilliant Earth, LLC and the Continuing Equity Owners that provides for the payment by Brilliant Earth Group, Inc. to the Continuing Equity Owners of 85% of the amount of tax benefits, if any, that Brilliant Earth Group, Inc. actually realizes (or in some circumstances is deemed to realize) related to certain tax basis adjustments and payments made under the TRA.

The organization agreements include a provision for the Continuing Equity Owners, subject to certain exceptions from time to time at each of their option, to require Brilliant Earth, LLC to redeem all or a portion of their LLC Units in exchange for, at the Company's election, newly-issued shares of Class A common stock or Class D common stock, as applicable, on a one-for-one basis, or a cash payment equal to a volume weighted average market price of one share of Class A common stock for each LLC Interest so redeemed, in each case, in accordance with the terms of the Brilliant Earth LLC Agreement.

The following summarizes the IPO and other transactions:

- Issued 9,583,332 shares of Class A common stock, including 1,249,999 shares of Class A common stock from the exercise of the underwriters' overallotment option, in exchange for net proceeds of approximately $101.6 million at $12.00 per share, less underwriting discount and offering expenses.

- Used net proceeds from the IPO to purchase 8,333,333 newly issued LLC Units for approximately $93.5 million directly from Brilliant Earth, LLC at a price per unit equal to the initial public offering price per share of Class A common stock less underwriting discount.

- Used net proceeds from the exercise of the underwriters' overallotment option to purchase an additional 1,249,999 LLC Units from each of the Continuing Equity Owners in the form of a redemption on a pro rata basis for $14.0 million in aggregate at a price per unit equal to the initial public offering price per share of Class A common stock less the underwriting discount; this purchase of LLC Interests resulted in an obligation under the TRA, including the related set-up of deferred tax assets on the TRA and on the temporary basis difference associated with this purchase.

- Corresponding cancellation of a total of 1,249,999 shares of Class B common stock and Class C common stock resulting from the purchase of 1,249,999 LLC Units from the Continuing Equity Owners.

- Exercise of warrants on Class P Units with a carrying value of $6.4 million as of September 22, 2021 (after the mark-to-market adjustment as of the date of exercise) into 534,589 newly issued LLC Units on a net settlement basis, elected at the option of the holder.

Key Factors Affecting Our Performance

Our Ability to Increase Brand Awareness

Increasing brand awareness and growing favorable brand equity have been and remain key to our growth. We have a significant opportunity to continue to grow our brand awareness, broaden our customer reach, and maximize lifetime value through brand and performance marketing. We have made significant investments to strengthen the Brilliant Earth brand through our dynamic marketing strategy, which includes brand marketing campaigns across email, digital, social media, earned media, and media placements and with key influencers. In order to compete effectively and increase our share of the jewelry market, we must maintain our strong customer experience, produce compelling products, and continue our mission of creating a more transparent, sustainable, compassionate and inclusive jewelry industry. Our performance will also depend on our ability to increase the number of consumers aware of Brilliant Earth and our product assortment. We believe our brand strength will enable us to continue to expand across categories and channels, to deepen relationships with consumers, and to expand our presence in U.S. and international markets.

Cost-Effective Acquisition of New Customers and Retention of Existing Customers.

We have historically had attractive customer acquisition economics, including substantial first order profitability. To continue to grow our business, we must continue to acquire new customers and retain existing customers in a cost-effective manner. The success of our customer acquisition strategy depends on a number of factors, including the level and pattern of consumer spending in the product categories in which we operate, and our ability to cost-effectively drive traffic to our website and showrooms and to convert these visitors to customers. With our strong brand resonance and passionate customer base, we generate significant earned and organic traffic, impressions, and media placements. We continually evolve our dynamic marketing strategies, optimizing our messaging, creative assets, and spending across channels. We also believe our expanded fine jewelry assortment and strategic customer acquisition will continue to drive fine jewelry orders from new customers and repeat orders from existing customers.

Our Ability to Continue Expansion of our Omnichannel Strategy

Our ability to expand our omnichannel presence to new markets and locations is key to our success. Historically, we have been successful in every new geographic market we have entered, and we are in the early stages of expanding our premium showroom footprint nationwide. We intend to continue leveraging our marketing strategy and growing brand awareness to drive increased qualified consumer traffic to and sales from our website and premium showrooms.

We believe expanding our number of showrooms will drive accelerated growth by increasing our average order value (“AOV”) compared to e-commerce orders, improving conversion in the showrooms’ metro regions compared to pre-opening conversion, and raising our brand awareness. As of March 31, 2022, we have 15 showroom locations. We intend to strategically open showrooms in the future, and we believe we can achieve broad national showroom coverage with far fewer locations than many traditional retailers. We rely on this highly efficient showroom model to complement our digital strategy and to continue to drive growth and profitability.

Our Ability to Successfully Introduce New Products

Product expansion allows us significant opportunity to drive new and repeat purchases by expanding purchase occasions beyond engagement and bridal. We intend to leverage our in-house design capabilities and nimble data-driven product development to expand product assortment for special occasions and self-purchase. In addition, we will have more opportunity to enhance and leverage our customer relationship management (“CRM”) and data-segmentation capabilities to increase repeat purchases and lifetime value. We have consistently invested in technology to create a seamless customer experience, including dynamic visualization, augmented reality try-on, and automated, rapid fulfillment, and we intend to continue investing in technology to enhance the digital and showroom experience and help drive conversion. Expanding affiliations and brand collaborations will also broaden our existing assortment, reinforce our brand ethos, and feature like-minded designers, which will help to drive both new and repeat purchases.

International Expansion

We are in the early stages of expanding globally, and a larger geographic footprint will help drive future growth. Our early proof-points from localizing our website for Canada, Australia, and the United Kingdom, and our sales to customers from over 50 countries, provide encouraging signs for future global expansion. We see strong potential in launching e-commerce in new overseas markets and new showrooms in countries where we have already established a localized digital presence. We plan to drive brand awareness through localized marketing channels and expect our data-driven technology platform to continue providing insights for product recommendations and inventory management.

Operational and Marketing Efficiency

We have a unique, asset-light operating model with attractive working capital dynamics, capital-efficient showrooms, and a vast virtual inventory of premium natural and lab-grown diamonds that allows us to offer over 150,000 diamonds with significant value, while keeping our balance sheet inventory low. This has driven attractive inventory turns and allows us to operate with negative working capital, which we define as our current assets less cash minus our current liabilities. Our showroom strategy avoids the inefficiencies of traditional, retail-first jewelers. Our showrooms are appointment-driven with large catchment regions, so we are less reliant on expensive high foot traffic retail locations. We also curate showroom inventory for scheduled visits and require limited inventory in each location. Our tech-enabled jewelry specialist team supports online customers when not in appointment, maximizing workforce utilization. As we continue to scale our business, our future success is dependent on maintaining this capital efficient operating model and driving continued operational improvement as we expand to new locations both in the U.S. and internationally.

Costs of Operating as a Public Company

We anticipate that the costs of operating as a public company will be significant as we are now subject to the reporting, listing, and compliance requirements of various governing bodies and applicable securities laws and regulations that we were previously not subjected to as a privately-held company. These costs have been rapidly increasing over time, and we expect these rules and regulations to increase our legal, financial, and technology compliance costs, and to make some activities more difficult, time-consuming, and costly. Remaining compliant and satisfying our obligations as a public company, while maintaining forecasted gross margins and operating results, and attracting and retaining qualified persons to serve on our board of directors, our board committees, or as our executive officers will be critical to our future success.

Macroeconomic Trends

We believe we are well-positioned at the intersection of key macro-level trends impacting our industry. Consumers are increasingly becoming more conscious of the products they purchase, seeking brands that stand for sustainability, supply chain transparency, and social and environmental responsibility. This has contributed to our strong brand affinity and loyalty, and further differentiates us from our competitors. Consumers are increasingly favoring seamless omnichannel shopping experiences, and we believe our model is well-suited to satisfy these consumer preferences. Changes in inflation and macro-level consumer spending trends, including as a result of the COVID-19 pandemic, could result in fluctuations in our operating results.

Effects of COVID-19 on Our Business

The COVID-19 pandemic remains on-going and continues to impact the global economy. Our financial performance could be adversely impacted by the on-going evolution of the pandemic, including any government-imposed pandemic restrictions. We cannot predict the full extent of the impacts of the COVID-19 pandemic on our business, our operations, or the global economy as a whole. However, the effects could have a material impact on our results of operations.

Key Metrics

We monitor the key business metrics set forth below to help us evaluate our business and growth trends, establish budgets, measure the effectiveness of our sales and marketing efforts, and assess operational efficiencies. The calculation of the key metrics discussed below may differ from other similarly titled metrics used by other companies, securities analysts or investors.

The following table sets forth our key performance indicators for the periods presented (amounts in thousands, except for total orders and AOV):

	Three months ended March 31,			
	2022	**2021**	**Change**	**% Change**
Net Sales	$ 100,038	$ 70,696	29,342	41.5 %
Total Orders	32,372	21,555	10,817	50.2 %
AOV	$ 3,090	$ 3,280	$ (190)	(5.8)%

Net Sales

Net sales is defined below in "Components of Results of Operations".

Total Orders

We define total orders as the total number of customer orders delivered less total orders returned in a given period (excluding those repair, resize, and other orders which have no revenue). We view total orders as a key indicator of the velocity of our business and an indication of the desirability of our products to our customers. Total orders, together with AOV, is an indicator of the net sales we expect to recognize in a given period. Total orders may fluctuate based on the number of visitors to our website and showrooms, and our ability to convert these visitors to customers. We believe that total orders is a measure that is useful to investors and management in understanding our ongoing operations and in an analysis of ongoing operating trends.

Average Order Value

We define average order value, or AOV, as net sales in a given period divided by total orders in that period. We believe that AOV is a measure that is useful to investors and management in understanding our ongoing operations and in an analysis of ongoing operating trends. AOV varies depending on the product type and number of items per order. AOV may also fluctuate as we expand into and increase our presence in additional product lines and price points, and open additional showrooms.

Components of Results of Operations

Net Sales

Our sales are recorded net of estimated sales returns and allowances and sales taxes collected from customers. Our net sales primarily consist of revenue from diamond, jewelry, and gemstone retail sales through our website and dedicated jewelry specialists via chat, phone, email, virtual appointment, or in our showrooms. Our net sales are derived primarily in the U.S., but we also sell products to customers outside the U.S. Our website platform allows us to sell to a worldwide customer base, even in markets where we do not have a physical presence. Payment for all our sales occurs prior to fulfillment. Customers pick up the items in our showrooms, or we deliver purchases to customers, with delivery typically within one to two business days after shipment. We recognize revenue upon pick-up or delivery if an order is shipped. We also offer third-party financing options.

We allow for certain returns within 30 days of when an order is available for shipment or pickup. We also provide one complimentary resizing for standard ring styles within 60 days of when an order is available for shipment or pickup, a lifetime manufacturing warranty (except on estate and vintage jewelry and center diamonds/gemstones), and a lifetime diamond upgrade program on all independently-graded natural diamonds. For an additional charge, we offer an in-house three-year extended service plan, which provides full inspection, cleaning, and certain repairs due to normal wear. We also offer an extended protection plan through a third-party that has terms ranging from two years to lifetime that vary based on the item purchased.

Revenue is deferred on transactions where payment has been received from the customer, but control has not yet transferred. Revenue related to customer purchases of our in-house extended service plan are deferred and recognized ratably over the service plan term.

Cost of Sales

Cost of sales consists primarily of merchandise costs for the purchase of diamonds and gemstones from our global base of diamond and gemstone suppliers, and the cost of jewelry production from our third-party jewelry manufacturing suppliers. Cost of sales includes merchandise costs, inbound freight charges, and costs of shipping orders to customers. Our cost of sales includes reserves for disposal of obsolete, slow-moving or defective items, and shrinkage, which we estimate and record on a periodic basis.

Selling, General and Administrative Expenses

Selling, general and administrative (“SG&A”) expenses consist primarily of marketing, advertising, and promotional expenses; payroll and related benefit costs for our employees, including equity-based compensation expense; merchant processing fees; certain facility-related costs; customer service; technology; and depreciation and amortization expenses, as well as professional fees, other general corporate expenses, and charitable donations in connection with establishing and funding the Brilliant Earth Foundation, a donor advised fund, to support our charitable giving efforts.

Results of Operations Data

The results of operations data in the following tables for the periods presented have been derived from the unaudited condensed consolidated financial statements included elsewhere in this Quarterly Report on Form 10-Q.

Comparison of Three Months Ended March 31, 2022 and 2021

The following table sets forth our statements of operations for the three months ended March 31, 2022 and 2021, including amounts and percentages of net sales for each period and the period-to-period change in dollars and percent (amounts in thousands):

	Three months ended March 31,					
	2022		2021		Period change	
	Amount	Percent	Amount	Percent	Amount	Percent
Condensed consolidated statements of operations data:						
Net sales	$ 100,038	100.0 %	$ 70,696	100.0 %	$ 29,342	41.5 %
Cost of sales	49,922	49.9 %	38,337	54.2 %	11,585	30.2 %
Gross profit	50,116	50.1 %	32,359	45.8 %	17,757	54.9 %
Operating expenses:						
Selling, general and administrative	44,816	44.8 %	27,405	38.8 %	17,411	63.5 %
Income from operations	5,300	5.3 %	4,954	7.0 %	346	7.0 %
Interest expense	(1,776)	(1.8)%	(1,926)	(2.7)%	150	(7.8)%
Other expense, net	(59)	(0.1)%	(620)	(0.9)%	561	(90.5)%
Net income before tax	3,465	3.5 %	2,408	3.4 %	1,057	43.9 %
Income tax expense	(96)	(0.1)%	—	— %	(96)	*nm
Net income	3,369	3.4 %	$ 2,408	3.4 %	961	39.9 %
Net income allocable to non-controlling interest	3,013	3.0 %				
Net income allocable to Brilliant Earth Group, Inc.	$ 356	0.4 %				

Amounts may not sum due to rounding

*nm - Not meaningful

Net Sales

Net sales for the three months ended March 31, 2022 increased by $29.3 million, or 41.5%, compared to the three months ended March 31, 2021. We experienced increases in net sales across our products, and in both domestic and international markets, primarily driven by a 50.2% increase in order volumes due to:

- continued efficiency of our customer acquisition and conversion activities;
- an increase in orders driven by strong omnichannel performance across the Company's products and new product collection releases; and
- the opening of new showrooms in Seattle (second quarter of 2021), Portland, Austin, Dallas and New York (third quarter of 2021) and Scottsdale (fourth quarter of 2021).

The increase in net sales was partially offset by a decline of 5.8% in AOV driven by an increase in sales of lower price point fine jewelry.

Gross Profit

Gross profit for the three months ended March 31, 2022 increased by $17.8 million, or 54.9%, compared to the three months ended March 31, 2021. Gross margin, expressed as a percentage and calculated as gross profit divided by net sales, increased by 432 basis points for the three months ended March 31, 2022 compared to the three months ended March 31, 2021, primarily driven by our premium brand and differentiated product offerings, enhancements to our pricing engine and procurement efficiencies. Gross margin improvements were also due to reduced average platinum spot prices of 11.5%, partially offset by higher average gold spot prices of 4.9% for the period ended March 31, 2022 as compared to the three months ended March 31, 2021.

Selling, General and Administrative Expenses

Selling, general and administrative ("SG&A") expenses for the three months ended March 31, 2022 increased by $17.4 million, or 63.5%. SG&A expenses as a percentage of net sales increased by 603 basis points for the period ended March 31, 2022 compared to the period ended March 31, 2021. The increase in SG&A expenses was driven by an increase in employment expense, marketing expenses and other general and administrative expenses, which increased by $7.4 million, $5.6 million and $4.4 million, respectively, from the period ended March 31, 2021 to the period ended March 31, 2022. The increase in employment expenses was driven by a $5.4 million increase in salaries and wages, payroll taxes and other benefits expense due to the addition of corporate and showroom staff and a $2.0 million increase in equity-based compensation. The increase in marketing expenses was driven by increased investments in marketing and advertising to increase brand awareness and support strategic growth initiatives. The increase in other general and administrative expenses was principally driven by a $1.2 million increase in public company operating costs, $1.0 million in merchant bank fees, packaging supplies and other variable expenses due to revenue growth, and $0.8 million additional rent and pre-opening expenses from the opening of new showrooms.

Interest Expense

Interest expense for the three months ended March 31, 2022 decreased by $0.2 million, or 7.8%, primarily due to a decrease in the interest rate during the first quarter of 2022 as compared to the first quarter of 2021 pursuant to the third amendment of the Term Loan Agreement which reduced the variable interest rate from 8.25% to 7.75%; and the LIBOR floor from 1.00% to 0.50% .

Other Expense, net

Other expense, net for the three months ended March 31, 2022 decreased by $0.6 million, or 90.5% due to a $0.6 million expense related to the change in the fair market value of warrants recognized during the first quarter of 2021.

Seasonality

Our business is subject to seasonal fluctuation with a typical increase in sales around the holiday season, with the fourth quarter historically representing approximately 30% of annual net sales and a high percentage of annual net income.

Non-GAAP Financial Measures

We report our financial results in accordance with GAAP. However, management believes that certain non-GAAP financial measures provide users of our financial information with additional useful information in evaluating our performance and liquidity, as applicable, and to more readily compare these financial measures between past and future periods. There are limitations to the use of the non-GAAP financial measures presented in this Quarterly Report on Form 10-Q. For example, our non-GAAP financial measures may not be comparable to similarly titled measures of other companies. Other companies, including companies in our industry, may calculate non-GAAP financial measures differently than we do, limiting the usefulness of those measures for comparative purposes.

Adjusted EBITDA and Adjusted EBITDA Margin

Adjusted EBITDA and Adjusted EBITDA margin are included in this Quarterly Report on Form 10-Q because they are non-GAAP financial measures used by management and our board of directors to assess our financial performance. We define Adjusted EBITDA as net income excluding interest expense, income taxes, depreciation expense, amortization of cloud-based software implementation costs, equity-based compensation expense, showroom pre-opening expense, certain non-operating expenses and income, and other unusual and/or infrequent costs, which we do not consider in our evaluation of ongoing operating performance. We define Adjusted EBITDA margin as Adjusted EBITDA calculated as a percentage of net sales. These non-GAAP financial measures provide users of our financial information with useful information in evaluating our operating performance and exclude certain items from net income that may vary substantially in frequency and magnitude from period to period. These non-GAAP financial measures are not meant to be considered as indicators of performance in isolation from or as a substitute for net income prepared in accordance with GAAP and should be read only in conjunction with financial information presented on a GAAP basis. Reconciliations of each of Adjusted EBITDA and Adjusted EBITDA margin to its most directly comparable GAAP financial measure, net income and net income margin, are presented below. We encourage you to review the reconciliations in conjunction with the presentation of the non-GAAP financial measures for each of the periods presented. In future periods, we may exclude similar items, may incur income and expenses similar to these excluded items, and may include other expenses, costs and non-recurring items.

The following table presents a reconciliation of net income and net income margin, the most comparable GAAP financial measures, to Adjusted EBITDA and Adjusted EBITDA margin, respectively, for the periods presented (amounts in thousands):

	Three months ended March 31,	
	2022	**2021**
Net income	**$ 3,369**	**$ 2,408**
Interest expense	1,776	1,926
Income tax expense	96	—
Depreciation expense	349	164
Showroom pre-opening expense	475	163
Equity-based compensation expense	2,104	93
Other expense, net (1)	59	620
Transaction costs and other expense (2)	146	1,129
Adjusted EBITDA	**$ 8,374**	**$ 6,503**
Net income margin	**3.4 %**	**3.4 %**
Adjusted EBITDA margin	**8.4 %**	**9.2 %**

(1) Other expense, net for the three months ended March 31, 2021 consisted primarily of the change in fair value of the warrant liability necessary to mark our warrants to fair market value. Additionally, these expenses for all periods presented include losses on exchange rates on consumer payments, partially offset by interest and other miscellaneous income.

(2) These expenses are those that we did not incur in the normal course of business. These expenses for all periods presented include professional fees in connection with the evaluation and preparation for operations as a public company. Additionally, the expense also includes one-time costs associated with the opening of a new operations facility for the period ended March 31, 2021.

Liquidity and Capital Resources

Overview

Our primary requirements for liquidity and capital are for purchases of inventory, payment of operating expenses, tax distributions to LLC members, debt service, and capital expenditures. Historically, these cash requirements have been met through cash provided by operating activities, cash and cash equivalents, and borrowings under our Term Loan. We have historically had negative working capital driven by our high inventory turns and typical collection of payment from customers prior to payment of suppliers. As of March 31, 2022, we had a cash balance, excluding restricted cash, of $164.9 million, working capital, excluding cash, of ($68.1) million, and a Term Loan with a principal balance of $65.0 million, excluding unamortized debt issuance costs of $1.1 million, of which $23.9 is classified as long-term.

We lease our showrooms and headquarters office space under operating leases pursuant to which $2.6 million is due in the year ending December 31, 2022. Total future lease payments as of March 31, 2022 are $26.7 million.

In the three months ended March 31, 2022, the Company declared and paid $6.9 million of distributions to, or on behalf of, members associated with their estimated income tax obligations. We are committed to continue to make quarterly distributions in connection with member estimated income tax obligations which we expect to fund with cash flow from operations.

Notwithstanding our obligations under the TRA discussed below, we believe that our current sources of liquidity, which include cash, and net cash provided by operating activities, will be sufficient to meet our projected operating, debt service, and tax distribution requirements for at least the next 12 months. We have capital commitments of $3.2 million related to the opening of new locations as of March 31, 2022, and we have $41.1 million of principal repayments due in 2022 and $23.9 million of principal due in 2023 on our Term Loan. As further described below, we have an additional final payment of $3.2 million due in 2023 on our Term Loan.

Additional future liquidity needs may include public company costs, payments under the TRA, and state and federal taxes to the extent not offset by our deferred income tax assets, including those arising as a result of purchases or exchanges of common units for Class A and Class D common stock. Although the actual timing and amount of any payments that may be made under the TRA will vary, we expect that the payments that we will be required to make to the Continuing Equity Owners will be significant. Any payments made by us to the Continuing Equity Owners under the TRA will generally reduce the amount of overall cash flow that might have otherwise been available to us or to Brilliant Earth, LLC, and, to the extent that we are unable to make payments under the TRA for any reason, the unpaid amounts generally will be deferred and will accrue interest until paid by us; provided, however, that nonpayment for a specified period may constitute a material breach of a material obligation under the TRA and therefore may accelerate payments due under the TRA.

To the extent that our current liquidity is insufficient to fund future activities, we may need to raise additional funds, such as attempts to raise additional capital through the sale of equity securities or through debt financing arrangements. If we raise additional funds by issuing equity securities, the ownership of our existing stockholders will be diluted. The incurrence of additional debt financing would result in debt service obligations, and any future instruments governing such debt could provide for operating and financing covenants that could restrict our operations. We cannot ensure that we could obtain refinancing or additional financing on favorable terms or at all.

Cash Flows from Operating, Investing, and Financing Activities

The following table summarizes our cash flows for the three months ended March 31, 2022 and 2021 (in thousands):

	Three months ended March 31,	
	2022	**2021**
Net cash provided by operating activities	$ 182	$ 6,871
Net cash used in investing activities	(1,283)	(546)
Net cash used in financing activities	(6,874)	(75)
Net (decrease) increase in cash, cash equivalents and restricted cash	**(7,975)**	**6,250**
Cash, cash equivalents and restricted cash at beginning of period	173,070	66,474
Cash, cash equivalents and restricted cash at end of period	**$ 165,095**	**$ 72,724**

Operating Activities

Net cash provided by operating activities was $0.2 million for the three months ended March 31, 2022, consisting of $3.4 million in net income adjusted for $3.5 million in non-cash expense addbacks, primarily comprised of equity based compensation, depreciation, non-cash operating lease cost and amortization of debt issuance costs, offset by a $6.7 million decrease from changes in assets and liabilities related to operating activities. The change in assets and liabilities related to operating activities, which is the result of our revenue growth, primarily reflects a $4.7 million increase in deferred revenue, and offset by $11.4 million decrease in accounts payable, accrued expenses and other current liabilities, operating lease liabilities and an increase in inventories, prepaid expenses and other current assets and other assets.

Net cash provided by operating activities was $6.9 million for the three months ended March 31, 2021, consisting of a net income of $2.4 million adjusted for $1.2 million in non-cash addbacks, plus a $3.2 million increase from changes in assets and liabilities related to operating activities. The change in assets and liabilities related to operating activities primarily reflects a $8.1 million increase resulting from an increase in deferred revenue and deferred rent, offset by $4.8 million decrease in accounts payable and accrued expenses and other current liabilities and an increase in inventories, other assets and prepaid expenses and other current assets.

Investing Activities

Net cash used in investing activities was $1.3 million for the three months ended March 31, 2022, which primarily consisted of purchases of property and equipment related to new facilities leased during the period.

Net cash used in investing activities was $0.5 million for the three months ended March 31, 2021, which primarily consisted of purchases of property and equipment related to new facilities leased during the period.

Financing Activities

Net cash used in financing activities was $6.9 million for the three months ended March 31, 2022 related to tax distributions pursuant to the LLC Agreement.

Net cash used in financing activities was $0.1 million for the three months ended March 31, 2021 due to the tax paid distributions to members prior to the Reorganization Transactions.

Term Loan Agreement

On September 30, 2019, we entered into a Loan and Security Agreement with Runway Growth Finance Corp. (f/k/a Runway Growth Credit Fund Inc.) (“Runway”) which provided for a first tranche of loans in an aggregate principal amount up to $35.0 million available immediately and a second tranche of loans in an aggregate principal amount up to $5.0 million (“Original Term Loan”). On December 17, 2020, the Original Term Loan was amended to add a commitment for supplemental second tranche loans in the aggregate amount of up to $30.0 million (the “First Amendment”). On August 6, 2021, the Original Term Loan was amended to permit (1) a transfer of $1.0 million to the Brilliant Earth Foundation, and (2) additional amounts up to 5.00% of our annual net profits thereafter provided that there is not an event of default that has not been cured (the “Second Amendment”). On August 29, 2021, the Original Term Loan was amended to, among other matters, permit the Reorganization Transactions to be consummated by us in connection with the Up-C structure, and reduce the interest rate of the Term Loan (the “Third Amendment”, and the Original Term Loan, as amended by the First Amendment, the Second Amendment, and the Third Amendment, the “Term Loan”). The maturity date of the Term Loan is October 15, 2023, and as of March 31, 2022, we complied with all covenants under the Term Loan.

The Term Loan carries an interest rate equal to LIBOR, with a floor of 0.50%, plus 7.75%, unless LIBOR becomes no longer available or ceases to accurately or fairly cover or reflect the costs of the lender, in which case the applicable interest rate shall be Prime Rate, with a floor of 3.35%, plus 4.90%. We are required to make interest-only payments on the Term Loan through April 15, 2022 (the "Amortization Date"). The Term Loan will begin amortizing on the Amortization Date, with equal monthly payments of principal, which would fully amortize the principal amount of the Term Loan by October 15, 2023, plus interest being made by us to Runway in consecutive monthly installments until October 15, 2023. The Term Loan carries a prepayment fee of 3.00% declining to 0.00% based on the anniversary date of payment; and, a final payment fee equal to 4.50% of the principal amount repaid upon maturity or prepayment, plus $0.2 million. In the event that we choose to partially prepay the Term Loan, we are obligated to make a partial final payment on the date of such prepayment.

The Term Loan is secured by substantially all of the assets of the Company and requires us to comply with various affirmative and negative debt covenants. The affirmative covenants include meeting reporting requirements, such as monthly financial statements and compliance certificates, board observer rights, annual operating budget and financial projections, annual audited financial statements, federal tax returns, and other requirements. The negative covenants contain requirements that restrict our ability to create, incur, assume, or be liable for any indebtedness, incur liens, make distributions, make investments, dispose of assets, engage in mergers or acquisitions, or effect a change in business, management, ownership, or business locations, and other restrictive requirements. In addition, the financial covenants require us to reach the minimum liquidity requirements of cash and cash equivalents in deposit accounts secured in favor of Runway in an amount not less than the sum of (a) projected negative cash flow from operations (including interest payments due in respect of any indebtedness) for the immediately following six (6) months, plus (b) projected capital expenditures on property and/or equipment, including any leasing expenditures and principal repayments in respect of any indebtedness, for the immediately following six (6) months, as determined monthly on the last day of each month. For additional information regarding our long-term debt activity, see Note 7, *Long-Term Debt* to the unaudited condensed consolidated financial statements included elsewhere in this Quarterly Report on Form 10-Q.

Additional Liquidity Requirements after Completion of Offering

We are a holding company and have no material assets other than our ownership of LLC Interests. We have no independent means of generating revenue. The Brilliant Earth LLC Agreement in effect since the time of the IPO provides for the payment of certain distributions to the Continuing Equity Owners and to us in amounts sufficient to cover the income taxes imposed on such members with respect to the allocation of taxable income from Brilliant Earth, LLC as well as to cover our obligations under the TRA and other administrative expenses.

Regarding the ability of Brilliant Earth, LLC to make distributions to us, the terms of their financing arrangements, including the Term Loan Agreement, contain covenants that may restrict Brilliant Earth, LLC from paying such distributions, subject to certain exceptions. Further, Brilliant Earth, LLC is generally prohibited under Delaware law from making a distribution to a member to the extent that, at the time of the distribution, after giving effect to the distribution, liabilities of Brilliant Earth, LLC (with certain exceptions), as applicable, exceed the fair value of its assets.

In addition, under the TRA, we are required to make cash payments to the Continuing Equity Owners equal to 85% of the tax benefits, if any, that we actually realize (or in certain circumstances are deemed to realize), as a result of (1) increases in our allocable share of the tax basis of Brilliant Earth, LLC's assets resulting from (a) our purchase of LLC Interests from each Continuing Equity Owner; (b) future redemptions or exchanges of LLC Interests for Class A common stock or cash; and (c) certain distributions (or deemed distributions) by Brilliant Earth, LLC; and (2) certain tax benefits arising from payments made under the TRA. We expect the amount of the cash payments that we will be required to make under the TRA will be significant. The actual amount and timing of any payments under the TRA will vary depending upon a number of factors, including the timing of redemptions or exchanges by the Continuing Equity Owners, the amount of gain recognized by the Continuing Equity Owners, the amount and timing of the taxable income we generate in the future, and the federal tax rates then applicable. Any payments made by us to the Continuing Equity Owners under the TRA will generally reduce the amount of overall cash flow that might have otherwise been available to us.

Additionally, in the event we declare any cash dividends, we intend to cause Brilliant Earth, LLC to make distributions to us in amounts sufficient to fund such cash dividends declared by us to our shareholders. Deterioration in the financial condition, earnings, or cash flow of Brilliant Earth, LLC for any reason could limit or impair their ability to pay such distributions.

If we do not have sufficient funds to pay taxes or other liabilities or to fund our operations, we may have to borrow funds, which could materially adversely affect our liquidity and financial condition and subject us to various restrictions imposed by any such lenders. To the extent that we are unable to make payments under the TRA for any reason, such payments generally will be deferred and will accrue interest until paid; provided, however, that nonpayment for a specified period may constitute a material breach of a material obligation under the TRA and therefore accelerate payments due under the TRA. In addition, if Brilliant Earth, LLC does not have sufficient funds to make distributions, our ability to declare and pay cash dividends will also be restricted or impaired.

Contractual Obligations and Commitments

There have been no material changes to our contractual obligations from those described in the Annual Report.

Critical Accounting Policies and Estimates

In preparing our unaudited condensed consolidated financial statements and the related notes thereto included elsewhere in this Quarterly Report on Form 10-Q in conformity with U.S. GAAP, we must make decisions that impact the reported amounts of assets, liabilities, revenues, expenses, and related disclosures. Such decisions include the selection of the appropriate accounting principles to be applied and the assumptions on which to base accounting estimates. In reaching such decisions, we apply judgments based on our understanding and analysis of the relevant circumstances, historical experience, and business valuations. Actual amounts could differ from those estimated at the time the unaudited condensed consolidated financial statements are prepared.

Our critical accounting policies are described under the heading “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Critical Accounting Policies and Estimates” in the 2021 annual report on Form 10-K and the notes to the audited consolidated financial statements appearing elsewhere in the 2021 annual report on form 10-K. During the three months ended March 31, 2022, there were no material changes to our critical accounting policies from those discussed in our 2021 annual report on Form 10-K.

Revenue Recognition

Net sales primarily consists of revenue from the sale of inventory, and we recognize revenue as control of promised goods is transferred to customers, which generally occurs upon delivery if the order is shipped, or at the time the customer picks up the completed product at a showroom. Revenue arrangements generally have one performance obligation and are reported net of estimated sales returns and allowances, which are determined based on historical product return rates and current economic conditions. We offer a three-year extended in-house service plan, which gives rise to an additional performance obligation that is recognized over the course of the service plan. We maintain a returns asset account, less any expected costs to recover, and a refund liabilities account to record the effects of estimated product returns and sales returns and allowances, which are updated at the end of each financial reporting period with the effect of such changes accounted for in the period in which such changes occur. Our sales returns and allowance accounts are based on historical return experience and current period sales levels.

Equity-Based Compensation

Equity-based compensation is accounted for as an expense in accordance with the fair value recognition and measurement provisions of U.S. GAAP which requires compensation cost for the grant-date fair value of equity-based awards to be recognized over the requisite service period. We account for a forfeiture when it occurs, and any compensation expense previously recognized on unvested equity-based awards will be reversed when forfeited.

The fair value of awards of restricted LLC Units is based on the fair value of the member unit underlying the awards as of the date of grant. The fair value of the underlying member units (referred to as Class M Units prior to conversion to common LLC Units in the IPO on a value-for-value basis) for grants prior to our IPO in September 2021 was determined by considering a number of objective, subjective and highly complex factors including independent third-party valuations of our member units, operating and financial performance, the lack of liquidity of member units and general and industry specific economic outlook among other factors. We do not anticipate issuing any new restricted LLC Units.

The fair value of RSUs, all of which were granted at the time of the IPO or thereafter, is based on the fair value of the Class A common stock at the time of grant.

The fair value of option-based awards is estimated using the Black-Scholes valuation model. The Black-Scholes model requires the use of highly subjective and complex assumptions, including the option's expected term and the price volatility of the underlying stock. For inputs into the Black-Scholes model, the expected stock price volatility for the common stock is estimated by taking the average historic price volatility for industry peers based on daily price observations over a period equivalent to the expected term of the stock option grants. Industry peers consist of several public companies in our industry which are of similar size, complexity and stage of development. The risk-free interest rate for the expected term of the option is based on the U.S. Treasury implied yield at the date of grant.

We have elected to use the “simplified method” to determine the expected term which is the midpoint between the vesting date and the end of the contractual term because it has insufficient history upon which to base an assumption about the term; we believe the simplified method approximates a term if it were to be based on expected life. The expected dividend yield is nil as we have not paid and do not anticipate paying dividends on our common stock.

Deferred Tax Asset and Tax Receivable Agreement

We may receive a deferred tax benefit resulting from the step-up in basis which occurs in the event that we redeem LLC interests from the Continuing Equity Owners. Pursuant to a TRA entered into by Brilliant Earth, LLC and the Continuing Equity Owners, we will make payments to the Continuing Equity Owners of 85% of the amount of tax benefits, if any, that Brilliant Earth Group, Inc. actually realizes (or in some circumstances is deemed to realize) as a result of (1) increases in Brilliant Earth Group, Inc.'s allocable share of the tax basis of Brilliant Earth, LLC's assets resulting from (a) Brilliant Earth Group, Inc.'s purchase of LLC Interests from each Continuing Equity Owner, (b) future redemptions or exchanges of LLC Interests for Class A common stock or cash, and (c) certain distributions (or deemed distributions) by Brilliant Earth, LLC; and (2) certain tax benefits arising from payments made under the TRA.

We expect that payments under the TRA will be significant. We will account for the income tax effects and corresponding TRA's effects resulting from future taxable purchases or redemptions of LLC Interests of the Continuing LLC Owners by us or Brilliant Earth, LLC by recognizing an increase in our deferred tax assets, based on enacted tax rates at the date of the purchase or redemption, and assessment of the book basis of the redeemed LLC interests at the time of redemption. Further, we will evaluate the likelihood that we will realize the benefit represented by the deferred tax asset and, to the extent that we estimate that it is more likely than not that we will not realize the benefit, we will reduce the carrying amount of the deferred tax asset with a valuation allowance.

The amounts to be recorded for both the deferred tax asset and the liability for our obligations under the TRA will be estimated at the time of any purchase or redemption as a reduction to shareholders' equity, and the effects of changes in any of our estimates after this date will be included in net income. Similarly, the effect of subsequent changes in the enacted tax rates will be included in net income. We currently believe that all deferred tax assets will be recovered based upon the projected profitability of our operations. Judgement is required in assessing the future tax consequences of events that have been recognized in Brilliant Earth Group, Inc.'s financial statements. A change in the assessment of such consequences, such as realization of deferred tax assets, changes in tax laws or interpretations thereof could materially impact our results.

Recent Accounting Pronouncements

For information regarding recent accounting pronouncements, see Note 2, *Recent accounting pronouncements* in these unaudited condensed consolidated financial statements and related notes thereto.

JOBS Act

We qualify as an “emerging growth company” pursuant to the provisions of the JOBS Act, enacted on April 5, 2012. Section 102 of the JOBS Act provides that, among other reporting exemptions, an “emerging growth company” can take advantage of the extended transition period provided in Section 7(a)(2) (B) of the Securities Act for complying with new or revised accounting standards. We are electing to delay the adoption of new or revised accounting standards, and as a result, we may not comply with new or revised accounting standards on the relevant dates on which adoption of such standards is required for non-emerging growth companies. As a result, our unaudited condensed consolidated financial statements may not be comparable to companies that comply with new or revised accounting pronouncements as of public company effective dates.

The exemptions afforded to emerging growth companies will apply until we no longer meet the requirements of being an emerging growth company. We will remain an emerging growth company until the earlier of (a) the last day of the fiscal year (i) following the fifth anniversary of the completion of our IPO (December 31, 2026), (ii) in which we have total annual gross revenue of at least $1.07 billion or (iii) in which we are deemed to be a large accelerated filer, which means the market value of our common stock that is held by non-affiliates exceeds $700.0 million as of the last business day of our prior second fiscal quarter, and (b) the date on which we have issued more than $1.07 billion in non-convertible debt during the prior three-year period.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Market risk is the risk of economic losses due to adverse changes in financial market prices and rates. Our primary market risk has been interest rate, foreign currency, inflation and commodity risk.

Interest Rate Fluctuation Risk

Our cash and cash equivalents consist of cash and money market funds in government securities. The primary objective of our investment activities is to preserve principal while increasing income without significantly increasing risk. Because our cash and cash equivalents have a relatively short maturity, our portfolio's fair value is relatively insensitive to interest rate changes. We do not believe that an increase or decrease in interest rates of 10% would have a material effect on our operating results or financial condition. In future periods, we will continue to evaluate our investment policy in order to ensure that we continue to meet our overall objectives.

Interest on our term loan is based on a fixed rate of 7.75% plus LIBOR with a floor of 0.50% per annum. A 10.00% change in interest rates would not result in a material change to the annual interest expense.

Foreign Currency Risk

Over 90% of sales are to customers in the United States ("U.S."); sales to non-U.S. customers immediately settle in U.S. Dollars and no cash balances are carried in foreign currencies.

We do not believe that fluctuations in exchange rates have had a material effect on our historical operating results or financial condition. In future periods, we will continue to evaluate fluctuations in currency exchange rates and the requirements of currency control regulations, which might impact the conversion of other currencies into U.S. Dollars.

Inflation and Commodity Risk

Our results are subject to risks associated with inflation including to the cost of inventory, compensation expenses, and other costs.

Our results are also subject to fluctuations in the supply and market pricing of diamonds, gold, platinum and certain other precious metals and gemstones, all of which are key raw material components of our products. We manage exposure to market risk through certain operating activities. We do not currently deploy the use of financial derivatives as a hedge against fluctuations in precious metal pricing.

Item 4. Controls and Procedures

Limitations on effectiveness of control and procedures

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

Evaluation of disclosure controls and procedures

Our management, with the participation of our principal executive officer and principal financial officer, conducted an evaluation of the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on this evaluation, our principal executive officer and principal financial officer concluded that, as of March 31, 2022, our disclosure controls and procedures were effective at the reasonable assurance level.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the quarter ended March 31, 2022 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Part II - Other Information

Item 1. Legal Proceedings

We are, from time to time, party to various claims and legal proceedings arising out of our ordinary course of business, but we do not believe that any of these claims or proceedings will have a material effect on our business, unaudited condensed consolidated financial condition or results of operations.

On August 26, 2021, Plaintiff Anna Lerman filed a complaint against the Company in California Superior Court for Ventura County. The complaint alleges, on behalf of a putative class, that the Company recorded telephone calls between the Company's customers and its customer service representatives without the customers' consent, in violation of the California Invasion of Privacy Act Sections 631 and 632.7. The plaintiff seeks statutory damages, injunctive relief, attorneys' fees and costs, and other unspecified damages. The Company has obtained an extension of time to file a response, the time to file such response has not yet passed, and as of the date of this Quarterly Report on Form 10-Q, the Company has not responded to the complaint. We believe these claims have no merit, and intends to vigorously defend against this lawsuit, though there can be no assurance regarding its ultimate outcome. At this time, any liability related to the alleged claims is not currently probable or reasonably estimable.

Item 1A. Risk Factors

There have been no material changes to our risk factors as previously disclosed in Item 1A of Part I of our Annual Report on Form 10-K for the year ended December 31, 2021 filed with the Securities and Exchange Commission on March 22, 2022.

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

Recent Sales of Unregistered Securities; Purchases of Equity Securities by the Issuer or Affiliated Purchaser

On September 22, 2021, the Company issued (i) 35,542,035 shares of Class B common stock of the Company, par value $0.0001 per share, to Mainsail Partners III, L.P., a Delaware limited partnership, Mainsail Incentive Program, LLC, a Delaware limited liability company, Mainsail Co-Investors III, L.P., a Delaware Limited Partnership and the Members (as defined in the Amended and Restated Limited Liability Company Agreement of Brilliant Earth, LLC, dated September 22, 2021), on a one-to-one basis equal to the number of common membership interests of the LLC it owns, in exchange for nominal consideration and (ii) 49,119,976 shares of Class C common stock of the Company, par value $0.0001 per share, to Just Rocks, Inc., a Delaware corporation, on a one-to-one basis equal to the number of common membership interests of the LLC it owns, in exchange for nominal consideration (the "Exchange").

No underwriters were involved in the issuance and sale of the shares of Class B common stock or the issuance of shares of Class C common stock pursuant to the Exchange. The shares of Class B common stock and Class C common stock were issued in reliance upon an exemption from registration pursuant to Section 4(a)(2) of the Securities Act on the basis that the transaction did not involve a public offering.

Use of Proceeds

On September 27, 2021, we completed the IPO of shares of our Class A common stock, in which we issued and sold 9,583,332 shares of our Class A common stock, including the full exercise by the underwriters of the offering of their option to purchase 1,249,999 shares, at a price to the public of $12.00 per share. We raised net proceeds to us of approximately $101.6 million, after deducting the underwriting discount and offering expenses of $13.4 million. All shares sold were registered pursuant to a registration statement on Form S-1 (File No. 333- 259164), as amended (the “Registration Statement”), declared effective by the SEC on September 22, 2021. J.P. Morgan Securities LLC, Credit Suisse Securities (USA) LLC, Jefferies LLC and Cowen and Company, LLC acted as representatives of the underwriters for the offering. The offering terminated after the sale of all securities registered pursuant to the Registration Statement. No payments for expenses were made directly or indirectly to (i) any of our officers or directors or their associates, (ii) any persons owning 10% or more of any class of our equity securities or (iii) any of our affiliates. The net proceeds of the IPO were used to purchase 8,333,333 LLC Units from Brilliant Earth, LLC and 1,249,999 LLC Units in the form of a redemption from the Continuing Equity Owners at a price per unit equal to the IPO price of $11.22 per share after deducting the underwriting discount. There has been no material change in the expected use of the net proceeds from our initial public offering as described in our Prospectus dated September 22, 2021.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

Item 6. Exhibits

		Incorporated by Reference				
Exhibit Number	Exhibit Description	Form	File No.	Exhibit	Filing Date	Filed / Furnished Herewith
3.1	Amended and Restated Certificate of Incorporation of Brilliant Earth Group, Inc.	8-K	001-40836	3.1	9/27/2021	
3.2	Amended and Restated Bylaws of Brilliant Earth Group, Inc.	8-K	001-40836	3.2	9/27/2021	
4.1	Specimen Stock Certificate evidencing shares of Class A Common Stock	S-1/A	001-40836	4.1	9/14/2021	
10.1	Amended and Restated Limited Liability Company Agreement of Brilliant Earth, LLC, dated as of September 22, 2021.	8-K	001-40836	10.1	9/27/2021	
10.2	Tax Receivable Agreement, dated as of September 22, 2021, by and among Brilliant Earth Group, Inc., Brilliant Earth LLC and its Members.	8-K	001-40836	10.2	9/27/2021	
10.3	Registration Rights Agreement, dated September 22, 2021, by and among Brilliant Earth Group, Inc., Brilliant Earth LLC and its Original Equity Owners.	8-K	001-40836	10.3	9/27/2021	
10.4	Stockholders Agreement, dated September 22, 2021, by and among Brilliant Earth Group, Inc., Brilliant Earth LLC and the Original Members.	8-K	001-40836	10.4	9/27/2021	
10.5	Offer letter, dated as of September 22, 2021, by and between Brilliant Earth Group, Inc. and Beth Gerstein.	8-K	001-40836	10.5	9/27/2021	
10.6	Offer letter, dated as of September 22, 2021, by and between Brilliant Earth Group, Inc. and Eric Grossman.	8-K	001-40836	10.6	9/27/2021	
10.7	Offer letter, dated as of September 22, 2021, by and between Brilliant Earth Group, Inc. and Jeffrey Kuo.	8-K	001-40836	10.7	9/27/2021	
10.8	Brilliant Earth Group, Inc. 2021 Incentive Award Plan.	S-8	333-259736	99.1	9/23/2021	
10.9	Brilliant Earth Group, Inc. 2021 Employee Stock Purchase Plan.	S-8	333-259736	99.2	9/23/2021	
10,10	Form of Brilliant Earth, LLC Unit Restriction Agreement (Class M Units).	S-1/A	001-40836	10.9	9/14/2021	
10.11	Form of Stock Option Grant Notice and Stock Option Agreement under the 2021 Incentive Award Plan.	S-1/A	001-40836	10.11	9/14/2021	
10.12	Form of Restricted Stock Unit Award Grant Notice and Restricted Stock Unit Award Agreement under the 2021 Incentive Award Plan.	S-1/A	001-40836	10.12	9/14/2021	
10.13	Non-Employee Director Compensation Program.	S-1/A	001-40836	10.14	9/14/2021	
10.14	Form of Indemnification Agreement.	S-1/A	001-40836	10.15	9/14/2021	
10.15†	Second Amendment to Loan and Security Agreement, dated as of August 6, 2021, by and among Brilliant Earth, LLC, the Lenders party thereto and Runway Growth Credit Fund Inc., as Agent.					
10.16†	Third Amendment to Loan and Security Agreement, dated as of August 29, 2021, by and among Brilliant Earth, LLC, the Lenders party thereto and Runway Growth Finance Corp. (f/k/a Runway Growth Credit Fund Inc.), as Agent.	S-1/A	001-40836	10.4	9/14/2021	
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a)/15d-14(a).					*
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a)/15d-14(a).					*

32.1	Certificati3on of Chief Executive Officer pursuant to 18 U.S.C. Section 1350.	**
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350.	**
101.INS	Inline XBRL Instance Document - the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document.	*
101.SCH	Inline XBRL Taxonomy Extension Schema Document	*
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase Document	*
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase Document	*
101.LAB	Inline XBRL Taxonomy Extension Label Linkbase Document	*
101.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase Document	*
104	Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101)	*

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*	Filed herewith.
**	Furnished herewith.
†	Schedules and exhibits to this Exhibit omitted pursuant to Regulation S-K Item 601(b)(2). Brilliant Earth agrees to furnish supplementally a copy of any omitted schedule or exhibit to the SEC upon request.

Signatures

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

Brilliant Earth Group, Inc.

May 12, 2022 By:/s/ Jeffrey Kuo
Jeffrey Kuo
Chief Financial Officer
(Principal Financial Officer and Principal Accounting Officer)

Exhibit 31.1

CERTIFICATION

I, Beth Gerstein, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Brilliant Earth Group, Inc.;

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

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

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

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

   (b) [Omitted];

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

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

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

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

Date: May 12, 2022 By: /s/ Beth Gerstein

Name: Beth Gerstein
Title: Chief Executive Officer

Exhibit 31.2

CERTIFICATION

I, Jeffrey Kuo, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Brilliant Earth Group, Inc.;

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

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

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

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

   (b) [Omitted];

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

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

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

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

Date: May 12, 2022 By: /s/ Jeffrey Kuo
Name: Jeffrey Kuo
Title: Chief Financial Officer

Exhibit 32.1

Certification of CEO Pursuant to 18 U.S.C. Section 1350,
As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

In connection with the quarterly report of Brilliant Earth Group, Inc. (the “Company”) on Form 10-Q for the period ended March 31, 2022 (the “Report”), as filed with the Securities and Exchange Commission on the date hereof, I, the undersigned, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to the best of my knowledge, that:
(1) The Report fully complies with the requirements of Section 13(a) or Section 15(d) of the Securities Exchange Act of 1934; and
(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: May 12, 2022

By: /s/ Beth Gerstein
Name: Beth Gerstein
Title: Chief Executive Officer

Exhibit 32.2

Certification of CFO Pursuant to 18 U.S.C. Section 1350,
As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

In connection with the quarterly report Brilliant Earth Group, Inc. (the “Company”) on Form 10-Q for the period ended March 31, 2022 (the “Report”), as filed with the Securities and Exchange Commission on the date hereof, I, the undersigned, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to the best of my knowledge, that:
(1) The Report fully complies with the requirements of Section 13(a) or Section 15(d) of the Securities Exchange Act of 1934; and
(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: May 12, 2022

By: /s/ Jeffrey Kuo
Name: Jeffrey Kuo
Title: Chief Financial Officer