ACE HARDWARE CORPORATION
2020 Annual Report

ACE HARDWARE CORPORATION
INDEX TO CONSOLIDATED FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Report of Independent Auditors

The Board of Directors
Ace Hardware Corporation

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Ace Hardware Corporation, which comprise the consolidated balance sheets as of January 2, 2021 and December 28, 2019, and the related consolidated statements of income, comprehensive income, equity, and cash flows for each of the three fiscal years in the period ended January 2, 2021, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in conformity with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free of material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Ace Hardware Corporation at January 2, 2021 and December 28, 2019, and the consolidated results of its operations and its cash flows for each of the three fiscal years in the period ended January 2, 2021, in conformity with U.S. generally accepted accounting principles.

Ernst + Young LLP

Chicago, Illinois
February 15, 2021

ACE HARDWARE CORPORATION
CONSOLIDATED BALANCE SHEETS
(In millions, except share data)

	January 2, 2021	December 28, 2019
Assets		
Cash and cash equivalents	$ 28.9	$ 18.2
Marketable securities	63.2	59.5
Receivables, net of allowance for doubtful accounts of $4.8 and $5.4, respectively	527.7	486.5
Inventories	1,133.0	930.8
Prepaid expenses and other current assets	55.1	45.5
Total current assets	1,807.9	1,540.5
Property and equipment, net	423.3	381.7
Operating lease right-of-use assets, net	455.5	-
Finance lease right-of-use assets, net	25.0	-
Goodwill and other intangible assets	100.3	90.5
Other assets	90.9	115.3
Total assets	$ 2,902.9	$ 2,128.0
Liabilities and Equity		
Current maturities of long-term debt	$ 31.7	$ 67.0
Accounts payable	1,109.4	791.8
Patronage distributions payable in cash	112.9	70.4
Patronage refund certificates payable	26.6	17.4
Current operating lease liabilities	64.5	-
Current finance lease liabilities	3.7	-
Accrued expenses	237.5	205.9
Total current liabilities	1,586.3	1,152.5
Long-term debt	24.8	209.9
Patronage refund certificates payable	95.3	107.3
Long-term operating lease liabilities	412.2	-
Long-term finance lease liabilities	20.8	-
Other long-term liabilities	73.6	92.5
Total liabilities	2,213.0	1,562.2
Member Retailers' Equity:		
Class A voting common stock, $1,000 par value, 10,000 shares authorized, 2,689 and 2,691 issued and outstanding, respectively	2.7	2.7
Class C nonvoting common stock, $100 par value, 10,000,000 shares authorized, 5,015,306 and 4,827,851 issued and outstanding, respectively	501.5	482.7
Class C nonvoting common stock, $100 par value, issuable to retailers for patronage distributions, 1,191,050 and 546,146 shares issuable, respectively	119.1	54.6
Contributed capital	19.0	18.8
Retained earnings (accumulated deficit)	32.3	(8.7)
Accumulated other comprehensive income	3.0	0.9
Equity attributable to Ace member retailers	677.6	551.0
Equity attributable to noncontrolling interests	12.3	14.8
Total equity	689.9	565.8
Total liabilities and equity	$ 2,902.9	$ 2,128.0

See accompanying notes to the consolidated financial statements.

ACE HARDWARE CORPORATION
CONSOLIDATED STATEMENTS OF INCOME
(In millions)

	Years Ended		
	January 2, 2021 (53 Weeks)	December 28, 2019 (52 Weeks)	December 29, 2018 (52 Weeks)
Revenues:			
Wholesale revenues	$ 7,011.2	$ 5,564.5	$ 5,341.6
Retail revenues	751.5	506.7	375.4
Total revenues	7,762.7	6,071.2	5,717.0
Cost of revenues:			
Wholesale cost of revenues	6,132.1	4,898.6	4,707.4
Retail cost of revenues	417.1	280.0	214.5
Total cost of revenues	6,549.2	5,178.6	4,921.9
Gross profit:			
Wholesale gross profit	879.1	665.9	634.2
Retail gross profit	334.4	226.7	160.9
Total gross profit	1,213.5	892.6	795.1
Wholesale operating expenses:			
Distribution operations expenses	220.9	178.2	163.7
Selling, general and administrative expenses	210.8	195.1	187.7
Retailer success and development expenses	194.3	166.8	159.1
Retail operating expenses	253.1	201.5	154.4
Retail pre-opening expenses	1.3	8.7	1.7
Goodwill impairment charge	-	8.5	-
Total operating expenses	880.4	758.8	666.6
Operating income	333.1	133.8	128.5
Interest expense	(19.1)	(22.7)	(20.4)
Interest income	3.6	6.9	9.6
Other income, net	4.3	10.8	8.0
Income tax (expense) benefit	(5.0)	11.6	2.5
Net income	316.9	140.4	128.2
Less Net (loss) income attributable to noncontrolling interests	(0.7)	-	0.5
Net income attributable to Ace Hardware Corporation	$ 317.6	$ 140.4	$ 127.7
Patronage distributions accrued	$ 292.9	$ 182.2	$ 141.8
Patronage distributions accrued for third party retailers	$ 275.4	$ 172.5	$ 135.4

See accompanying notes to the consolidated financial statements.

ACE HARDWARE CORPORATION
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(In millions)

	Years Ended		
	January 2, 2021 (53 Weeks)	**December 28, 2019 (52 Weeks)**	**December 29, 2018 (52 Weeks)**
Net income	$ 316.9	$ 140.4	$ 128.2
Other comprehensive income (loss), net of tax:			
Unrealized gain (loss) on investments	1.9	1.5	(6.5)
Unrealized gain (loss) on derivative financial instrument	0.2	(0.8)	1.1
Total other comprehensive income (loss), net	2.1	0.7	(5.4)
Comprehensive income	319.0	141.1	122.8
Less Comprehensive (loss) income attributable to noncontrolling interests	(0.7)	-	0.5
Comprehensive income attributable to Ace Hardware Corporation	$ 319.7	$ 141.1	$ 122.3

See accompanying notes to the consolidated financial statements.

ACE HARDWARE CORPORATION
CONSOLIDATED STATEMENTS OF EQUITY
(In millions)

	Shareholders of Ace Hardware Corporation								
	Capital Stock								
	Class A	Class C	Class C Stock Issuable to Retailers for Patronage Dividends	Additional Stock Subscribed	Contributed Capital	Retained Earnings (Accumulated Deficit)	Accumulated Other Comprehensive Income (Loss)	Noncontrolling Interests	Total Equity
Balances at December 30, 2017	$ 2.7	$ 441.3	$ 48.9	$ -	$ 18.3	$ 33.2	$ 3.5	$ 13.0	$ 560.9
Net income	-	-	-	-	-	127.7	-	0.5	128.2
Other comprehensive loss	-	-	-	-	-	-	(5.4)	-	(5.4)
Net payments on subscriptions	-	-	-	1.2	-	-	-	-	1.2
Stock issued	0.1	49.1	(48.9)	(1.2)	-	-	-	-	(0.9)
Change in noncontrolling interests	-	-	-	-	(0.2)	-	-	0.7	0.5
Stock repurchased	(0.1)	(25.6)	-	-	-	-	-	-	(25.7)
Patronage distributions issuable	-	-	44.0	-	-	-	-	-	44.0
Patronage distributions payable	-	-	-	-	-	(135.4)	-	-	(135.4)
Adoption of accounting standard	-	-	-	-	-	(0.7)	0.7	-	-
Other	-	-	-	-	0.4	-	-	-	0.4
Balances at December 29, 2018	$ 2.7	$ 464.8	$ 44.0	$ -	$ 18.5	$ 24.8	$ (1.2)	$ 14.2	$ 567.8
Net income	-	-	-	-	-	140.4	-	-	140.4
Other comprehensive income	-	-	-	-	-	-	0.7	-	0.7
Net payments on subscriptions	-	-	-	1.1	-	-	-	-	1.1
Stock issued	0.1	43.8	(44.0)	(1.1)	-	-	-	-	(1.2)
Change in noncontrolling interests	-	-	-	-	(0.2)	-	-	0.6	0.4
Stock repurchased	(0.1)	(25.9)	-	-	-	-	-	-	(26.0)
Patronage distributions issuable	-	-	54.6	-	-	-	-	-	54.6
Patronage distributions payable	-	-	-	-	-	(172.5)	-	-	(172.5)
Adoption of accounting standard	-	-	-	-	-	(1.4)	1.4	-	-
Other	-	-	-	-	0.5	-	-	-	0.5
Balances at December 28, 2019	$ 2.7	$ 482.7	$ 54.6	$ -	$ 18.8	$ (8.7)	$ 0.9	$ 14.8	$ 565.8
Net income	-	-	-	-	-	317.6	-	(0.7)	316.9
Other comprehensive income	-	-	-	-	-	-	2.1	-	2.1
Net payments on subscriptions	-	-	-	1.1	-	-	-	-	1.1
Stock issued	0.1	54.3	(54.6)	(1.1)	-	(0.1)	-	-	(1.4)
Change in noncontrolling interests	-	-	-	-	-	-	-	(0.3)	(0.3)
Stock repurchased	(0.1)	(35.5)	-	-	-	-	-	-	(35.6)
Patronage distributions issuable	-	-	119.1	-	-	-	-	-	119.1
Patronage distributions payable	-	-	-	-	-	(275.4)	-	-	(275.4)
Other	-	-	-	-	0.2	(1.1)	-	(1.5)	(2.4)
Balances at January 2, 2021	$ 2.7	$ 501.5	$ 119.1	$ -	$ 19.0	$ 32.3	$ 3.0	$ 12.3	$ 689.9

See accompanying notes to the consolidated financial statements.

ACE HARDWARE CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In millions)

	Years Ended		
	January 2, 2021 (53 Weeks)	December 28, 2019 (52 Weeks)	December 29, 2018 (52 Weeks)
Operating Activities			
Net income	$ 316.9	$ 140.4	$ 128.2
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	64.9	60.1	55.7
Goodwill impairment charge	-	8.5	-
Amortization of deferred financing costs	0.4	0.4	0.5
Loss (gain) on disposal of assets, net	0.9	(5.5)	(4.9)
Credit for doubtful accounts	(0.2)	(0.9)	(0.3)
Other, net	2.5	0.8	1.1
Changes in operating assets and liabilities, exclusive of effect of acquisitions:			
Receivables	(73.2)	(69.7)	(45.2)
Inventories	(194.6)	30.0	(144.6)
Other current assets	(9.6)	4.2	(8.9)
Other long-term assets	9.5	(9.8)	6.7
Accounts payable and accrued expenses	337.3	56.2	66.6
Other long-term liabilities	3.9	12.9	10.9
Deferred taxes	2.5	(13.6)	(2.1)
Net cash provided by operating activities	461.2	214.0	63.7
Investing Activities			
Purchases of marketable securities	(22.2)	(46.5)	(27.8)
Proceeds from sale of marketable securities	20.8	41.4	25.4
Purchases of property and equipment	(99.0)	(76.5)	(61.1)
Cash paid for acquired businesses, net of cash acquired	(21.5)	(22.5)	(18.5)
Proceeds from sale of assets	0.2	22.0	0.1
Other, net	(7.1)	(9.8)	(7.0)
Net cash used in investing activities	(128.8)	(91.9)	(88.9)
Financing Activities			
Net (payments) borrowings under revolving lines of credit	(224.9)	(58.0)	104.8
Principal payments on long-term debt	(10.7)	(10.9)	(11.0)
Payments of debt issuance costs	-	(1.3)	-
Payments of cash portion of patronage distribution	(66.2)	(51.3)	(58.0)
Payments of patronage refund certificates	(9.7)	(5.3)	(6.4)
Repurchase of stock	(4.8)	(3.8)	(2.5)
Purchase of noncontrolling interests	(3.0)	(0.2)	(0.2)
Other, net	(2.4)	1.3	1.1
Net cash (used in) provided by financing activities	(321.7)	(129.5)	27.8
Increase (decrease) in cash and cash equivalents	10.7	(7.4)	2.6
Cash and cash equivalents at beginning of period	18.2	25.6	23.0
Cash and cash equivalents at end of period	$ 28.9	$ 18.2	$ 25.6
Supplemental disclosure of cash flow information:			
Interest paid	$ 16.6	$ 20.2	$ 17.7
Income taxes paid	$ 12.4	$ 1.4	$ 2.1

See accompanying notes to the consolidated financial statements.

(1) Summary of Significant Accounting Policies

The Company and Its Business

Ace Hardware Corporation ("the Company") is a wholesaler of hardware, paint and other related products. The Company also provides to its retail members ("Retailers") value-added services such as advertising, marketing, merchandising and store location and design services. The Company's goods and services are sold predominately within the United States, primarily to retailers that operate hardware stores and with whom the Company has a retail membership agreement. As a retailer-owned cooperative, the Company distributes substantially all of its patronage sourced income in the form of patronage distributions to Retailers based on their volume of merchandise purchases.

Ace Hardware International Holdings, Ltd. ("AIH"), is a majority-owned and controlled subsidiary of the Company with a 20.7 percent noncontrolling interest owned by its international retailers. International retailers do not own shares of stock in the Company nor receive patronage dividends.

Ace Retail Holdings LLC ("ARH") is the owner of the 145 store Westlake Ace Hardware ("Westlake") and the 57 store Great Lakes Ace Hardware, Inc. ("GLA") retail chains. As a result, the Company is also a retailer of hardware, paint and other related products.

Ace Wholesale Holdings LLC ("AWH") owns and operates Emery Jensen Distribution and its related wholesale companies. AWH was formed in 2014 so that the Company could begin making wholesale hardware sales to non-member retailers.

Ace Ecommerce Holdings LLC ("AEH") owns The Grommet, an e-commerce company that operates a website that markets and sells new and innovative products created by independent entrepreneurs.

In September 2019, the Company formed the Ace Services Holdings LLC ("ASH") legal entity. On September 5, 2019, ASH acquired Handyman Matters Inc., a franchisor of home improvement, maintenance and repair services.

Basis of Presentation

The accompanying consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP"). The Company's fiscal year ends on the Saturday nearest December 31. Accordingly, fiscal years 2020, 2019 and 2018 ended on January 2, 2021, December 28, 2019 and December 29, 2018, respectively. Unless otherwise noted, all references herein for the years 2020, 2019 and 2018 represent fiscal years ended January 2, 2021, December 28, 2019 and December 29, 2018, respectively. Fiscal year 2020 consists of 53 weeks. Fiscal years 2019 and 2018 consisted of 52 weeks each.

Subsequent events have been evaluated through February 15, 2021, the date these statements were issued.

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of the Company and its majority-owned subsidiaries. All intercompany transactions have been eliminated.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash, Cash Equivalents and Marketable Securities

In the normal course of business, the Company has outstanding checks that exceed the cash balances in the Company's bank accounts, which create a book overdraft that are recorded as a liability. As of January 2, 2021 and December 28, 2019, the Company had outstanding checks in excess of bank balances totaling $92.4 million and $70.2 million, respectively, which have been included in accounts payable in the accompanying consolidated balance sheets. These outstanding amounts were subsequently funded through cash receipts and borrowings under the Company's debt facilities during the following fiscal year.

The Company classifies all highly liquid investments with original maturities of three months or less as cash equivalents.

The Company determines the appropriate classification of its investments in marketable securities, which are predominately held by the Company's New Age Insurance, Ltd. ("NAIL") subsidiary, at the time of purchase and evaluates such designation at each balance sheet date. All marketable securities have been classified and accounted for as available for sale. The Company may hold debt securities until maturity. In response to changes in the availability of and the yield on alternative investments as well as liquidity requirements, securities are occasionally sold prior to their stated maturities. Debt securities with maturities beyond twelve months are viewed by the Company as available to support current operations and are therefore classified as current assets in the accompanying Consolidated Balance Sheets. Marketable securities are carried at fair value based on quoted market prices, with unrealized gains and losses, net of taxes, reported as a component of Accumulated other comprehensive income ("AOCI"). Realized gains and losses on securities are determined using the specific identification method.

In the normal course of NAIL's operations, standby letters of credit totaling $14.3 million and $11.0 million at January 2, 2021 and December 28, 2019, respectively, were issued in favor of the insurance companies that reinsure a portion of NAIL's loss exposure. At January 2, 2021, NAIL has pledged substantially all of its cash and cash equivalents and marketable securities as collateral for these letters of credit. In fiscal 2019, the Company created a multiemployer welfare association (MEWA) to offer medical insurance and other welfare benefits to employees of the Company and Retailers and their employees at participating Ace retail locations, beginning January 1, 2020. The Company was required to provide a $10.0 million standby letter of credit to the State of Vermont in connection with the MEWA. See Note 12 for more information.

Revenue Recognition

Revenue is recognized when performance obligations under the terms of contracts with our customers are satisfied; generally, this occurs with the transfer of control of merchandise or services. Revenue is measured as the amount of consideration we expect to receive in exchange for transferring goods or providing services. The Company excludes sales and usage-based taxes collected and recognizes revenues net of expected returns. Provisions for sales returns are provided at the time the related sales are recorded based on historic returns activity.

The Company's warehouse merchandise revenue originates with a single performance obligation to ship the products, and therefore the Company's performance obligations are satisfied when control of the products is transferred to the customer per the arranged shipping terms. The customer takes ownership and assumes risk of loss for warehouse merchandise upon delivery. Although products are generally shipped FOB shipping point, the Company effectively retains the responsibilities of ownership until the goods reach the customer. Generally, customer billings for warehouse merchandise occur in bi-weekly intervals subsequent to revenue recognition. The Company considers shipping and handling as activities to fulfill its performance obligation for warehouse merchandise revenues. Billings for freight are accounted for as Revenues and shipping and handling costs are accounted for in Cost of revenues.

The Company has direct shipment arrangements with various vendors to deliver products to its customers without having to physically hold the inventory at the Company's warehouses, thereby increasing efficiency and reducing costs. The Company recognizes revenue for direct shipment arrangements upon delivery to the customer with contract terms that typically specify FOB destination. The Company recognizes the revenue and cost of goods sold from these arrangements on a gross basis as the principal in the transaction. The Company is primarily responsible for fulfilling the promise to customers to provide merchandise at negotiated prices with the vendors, assumes inventory risk if the product is returned by the customers, and assumes all the credit risk for the vendors with the customers. Therefore, the Company concluded it is the principal for these transactions.

Retail revenues from retail locations owned and operated by the Company and e-commerce revenues are recognized when the customer takes ownership of the products sold and assumes the risk of loss. The customer takes ownership and assumes risk of loss generally at the point of sale in our owned retail locations. The Company's e-commerce revenues come from Ace Hardware's website and sales from AEH. For e-commerce transactions, customers choose whether to have merchandise delivered to them (using third-party parcel delivery companies) or to collect their merchandise from one of our stores ("in-store pick up"). For items delivered directly to the customer, control passes and revenue is recognized when delivery has been completed to the customer, as title has passed and we have transferred possession to the customer. For in-store pick up, control passes and revenue is recognized once the customer has taken possession of the merchandise. Any fees charged to customers for delivery are a component of the transaction price and are recognized when delivery has been completed. Payment terms for retail and e-commerce sales are at the point of sale.

Service revenues (advertising activities, brand building initiatives and fees for other services provided primarily to domestic retailers) are recognized when the service is complete as this is when the retailer has the ability to direct the use of and obtain the benefits from the service.

The Company offers its retailers various incentive programs which provide the retailers with certain sales allowances. The Company offers these incentive programs in anticipation of future sales to the retailers that participate in these programs. Since the sales allowances provide future economic benefit to the Company, they are capitalized in Other assets and amortized as a reduction of revenue on a straight-line basis over the period of expected future sales to these retailers, which is generally five years.

(In millions)

The following table provides a summary of revenues by sales category:

	Years Ended	
	January 2, 2021	December 28, 2019
Warehouse merchandise	$ 5,175.2	$ 4,125.2
Direct shipment merchandise	1,337.7	1,136.1
ARH revenues	704.4	466.9
E-commerce	303.8	111.2
Service revenues	267.6	258.9
Amortization of sales allowances under retailer incentive programs	(26.0)	(27.1)
Total revenues	$ 7,762.7	$ 6,071.2

Receivables

Receivables from customers include amounts invoiced for the sale of merchandise, services and equipment used in the operation of customers' businesses.

Notes Receivable

The Company makes available to its Retailers various lending programs whose terms exceed one year. The notes bear interest at various rates based on market rates, the loan program or the Retailer's credit quality and are recorded at face value. Interest is recognized over the life of the note on the effective interest method. Loan origination fees were not material for any period presented.

Allowance for Doubtful Accounts

Management records an allowance for doubtful accounts based on judgments considering a number of factors, primarily historical collection statistics, current customer credit information, the current economic environment, the aging of receivables, the evaluation of compliance with lending covenants and the offsetting amounts due to Retailers for stock, notes, interest and anticipated but unpaid patronage distributions. The Company considers accounts and notes receivable past due if invoices remain unpaid past their due date and provides for the write-off of uncollectible receivables after exhausting all commercially reasonable collection efforts.

Inventories

Wholesale inventories are valued at the lower of cost or net realizable value. Cost is determined primarily using the last-in, first-out ("LIFO") method for all inventories.

Inventories at retail locations operated by ARH and at AEH's warehouse locations are valued at the lower of cost or net realizable value. Inventory cost is determined using the moving average method, which approximates the first-in, first-out ("FIFO") method.

Vendor Funds

The Company receives funds from vendors in the normal course of business principally as a result of purchase volumes, sales, early payments or promotions of vendors' products. Based on the provisions of the vendor agreements in place, management develops accrual rates by estimating the point at which the Company will have completed its performance under the agreement and the amount agreed upon will be earned. Due to the complexity and diversity of the individual vendor agreements, the Company performs analyses and reviews of historical trends throughout the year to ensure the amounts earned are appropriately recorded. As part of these analyses, the Company validates its accrual rates based on actual purchase trends and applies those rates to actual purchase volumes to determine the amount of funds that should be accrued by the Company and receivable from the vendor. Amounts accrued throughout the year could be impacted if actual purchase volumes differ from projected annual purchase volumes, especially in the case of programs that provide for increased funding when graduated purchase volumes are met. At year-end, the accrual reflects actual purchases made throughout the year.

Vendor funds are treated as a reduction of inventory cost, unless they represent a reimbursement of specific, incremental and identifiable costs incurred by the Company to sell the vendor's product, in which case the costs are netted. The majority of the vendor funds that the Company receives do not meet the specific, incremental and identifiable criteria. Therefore, the Company treats a majority of these funds as a reduction in the cost of inventory as the amounts are accrued and recognizes these funds as a reduction of cost of revenues when the inventory is sold.

(In millions)

Property and Equipment

Property and equipment are stated at cost less accumulated depreciation and amortization. Expenditures for maintenance, repairs and renewals of relatively minor items are generally charged to expense. Significant improvements or renewals are capitalized.

Depreciation expense is computed on the straight-line method based on estimated useful lives as follows:

Buildings and improvements	6 – 40 years
Equipment	3 - 20 years

Leasehold improvements are generally amortized on a straight-line basis over the lesser of the lease term or the estimated useful life of the asset.

The Company evaluates long-lived assets, such as property and equipment, for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized in the amount by which the carrying amount of the asset exceeds its fair value.

Goodwill and Other Intangible Assets

Goodwill represents the excess of the cost of an acquired business over the fair value of the net tangible assets acquired and identified intangible assets. Goodwill is not amortized but is tested for impairment at a reporting unit level on an annual basis or more frequently, if circumstances change or an event occurs that would more likely than not reduce the fair value of a reporting unit below its carrying amount. See Note 8 for additional information regarding the Company's annual goodwill impairment testing.

The Company's other intangible assets primarily relate to trademarks, tradenames, customer and vendor relationships and developed technology. The intangibles are amortized over their estimated useful lives. See Note 8 for additional information.

Internal-Use Software

Included in fixed assets is the capitalized cost of internal-use software. The Company capitalizes costs incurred during the application development stage of internal-use software and amortizes these costs over its estimated useful life. Costs incurred related to design or maintenance of internal-use software are expensed as incurred. For fiscal year 2020, 2019 and 2018, the Company capitalized $10.4 million, $10.8 million and $8.1 million, respectively, of software development costs related to internal programming time. Amortization of these capitalized costs was $5.2 million, $4.1 million and $3.0 million for fiscal 2020, 2019 and 2018, respectively. As of January 2, 2021 and December 28, 2019, the Company had $4.4 million and $2.3 million, respectively, of capitalized costs for internal-use software that had not been placed into service.

Leases

The Company leases certain warehouse and distribution space, office space, retail locations, equipment and vehicles. On December 29, 2019, the first day of fiscal 2020, the Company adopted Accounting Standards Update ("ASU") No. 2016-02, "Leases (Topic 842)" which requires these leases to be recognized on the balance sheet (see Note 6 for additional details on the adoption of Topic 842). The Company elected to exclude the recognition requirements for short-term leases in all asset categories.

The Company also elected to use a risk-free discount rate at commencement date based upon the lease term in determining the recognition of the operating and finance lease assets and liabilities. Original terms for the Company's leases are generally between 3 and 25 years. The Company generally does not include options to extend or terminate leases unless it is reasonably certain that the option will be exercised. The Company has lease agreements that contain both lease and non-lease components. The Company elected to not separate non-lease components from lease components for all categories.

Advertising Expense

The Company expenses advertising costs when incurred. Gross advertising expenses amounted to $240.7 million, $209.2 million, and $207.6 million in fiscal 2020, 2019 and 2018, respectively.

Gift Cards

The Company sells gift cards to customers through its Retailers, the Company website and select third parties. The gift cards do not expire. A liability is initially established for the value of the gift card when sold. Gift card breakage income is recognized proportionately as redemption occurs at the approximate monthly redemption rate and represents the balance of gift cards for which the Company believes the likelihood of redemption by the customer is remote. The breakage income calculation takes into account any legal obligation to remit the unredeemed portion to relevant jurisdictions. During fiscal years 2020, 2019 and 2018, the Company recognized gift card breakage income of $3.4 million, $1.1 million and $2.1 million, respectively. The Company does not believe there is a reasonable likelihood that there will be a material change in the future estimates or assumptions that we use to record breakage.

Retirement Plans

The Company sponsors health benefit plans for its retired officers and a limited number of retired non-officer employees. The Company and its subsidiaries also sponsor defined contribution plans for substantially all employees. The Company's contributions under these plans is determined annually by the Board of Directors and charged to expense in the period in which it is earned by employees.

Income Taxes

The Company accounts for income taxes using the asset and liability method. Under this approach, deferred taxes are recognized for the future tax consequences of differences between the financial statement and income tax bases of existing assets and liabilities, and measured based upon enacted tax laws and rates.

Self-Insurance

NAIL, the Company's wholly-owned subsidiary, operates as a captive insurance company. NAIL provides the reinsurance of property and casualty insurance policies for some Retailers and is the direct insurer for certain property and casualty insurance policies of the Company. These insurance programs are subject to varying retention levels of self-insurance. Such self-insurance relates to losses and liabilities primarily associated with property, general liability, workers' compensation and auto liability insurance programs. Losses are accrued based upon the Company's estimates of the aggregate liability for claims incurred using certain actuarial assumptions based on Company experience and insurance industry metrics.

Concentration of Credit Risk

Credit risk pertains primarily to the Company's trade and notes receivables. The Company extends credit to its customers as part of its day-to-day operations. Management believes that as no specific receivable or group of receivables comprises a significant percentage of total trade accounts, its concentration of credit risk with respect to trade receivables is limited. Additionally, management believes that its allowance for doubtful accounts is adequate with respect to overall customer credit risks. Also, the Company's certificate of incorporation and by-laws specifically provide that the Company may set-off its obligation to make any payment to a Retailer for such Retailer's stock, notes, interest and declared and unpaid distributions against any obligation owed by the Retailer to the Company. The Company, but not the Retailer, may at its sole discretion exercise these set-off rights when any such funds become due to former Retailers with outstanding accounts and notes receivable owed to the Company and current Retailers with past due receivables owed to the Company.

Impact of New Accounting Standards

Recently issued accounting pronouncements that are not yet effective and that were not discussed in the Company's 2019 Annual Report or below are either inapplicable to the Company or, if applicable, the Company does not expect that they will have a material impact on consolidated results of operations, consolidated financial condition, or consolidated cash flows.

New Accounting Pronouncements – Adopted

In February 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2016-02, "Leases (Topic 842)" along with amendments issued through 2019. The guidance requires that lessees recognize assets and liabilities for leases with lease terms greater than twelve months in the statement of financial position. The guidance also requires improved disclosures to help users of financial statements better understand the amount, timing and uncertainty of cash flows arising from leases.

On December 29, 2019 ("the effective date"), the Company adopted ASU 2016-02 and subsequent updates, collectively referred to as Topic 842, using the modified retrospective approach. In addition, the Company elected the package of practical expedients in transition, which permits the Company to not reassess prior conclusions pertaining to lease identification, lease classification and initial direct costs on leases that commenced prior to the adoption of the new standard. The Company also elected to treat the lease and non-lease components of leases as a single lease component and to exempt leases with an initial term of twelve months or less from balance sheet recognition.

As a result of adopting Topic 842, the Company recognized net operating right-of-use assets and operating lease liabilities of $454.2 million as of December 29, 2019. The adoption of the standard did not have a material impact on the Company's results of operations or cash flows. See Note 6 for additional details of the Company's leases.

(In millions)

New Accounting Pronouncements - Issued

In June 2016, the FASB issued ASU No. 2016-13, "Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments" along with amendments issued in 2018. The guidance requires financial assets measured at amortized cost basis to be presented at the net amount expected to be collected. The amortized cost basis of financial assets should be reduced by expected credit losses to present the net carrying value in the financial statements at the amount expected to be collected. The measurement of expected credit losses is based on past events, historical experience, current conditions and forecasts that affect the collectability of the financial assets. Additionally, credit losses relating to available-for-sale debt securities should be recorded through an allowance for credit losses. ASU 2016-13 is effective for the Company for year-end financial statements and quarterly financial statements in fiscal 2023. The Company is evaluating the impact that ASU 2016-13 will have on the Company's consolidated financial statements.

(2) Acquisitions

During the year ended January 2, 2021, ARH acquired additional retail stores for consideration of $21.8 million, prior to working capital adjustments. These acquisitions resulted in ARH recording $13.4 million of goodwill. Goodwill has an indefinite life and, therefore, is not amortized. The goodwill is expected to be deductible for tax purposes.

(3) Receivables, net

Receivables, net include the following amounts:

	January 2, 2021	December 28, 2019
Trade	$ 395.6	$ 411.1
Other	120.4	64.5
Notes receivable – current portion	16.5	16.3
Less allowance for doubtful accounts	(4.8)	(5.4)
Receivables, net	$ 527.7	$ 486.5

Other receivables are principally amounts due from suppliers for promotional and advertising allowances.

(4) Inventories

Inventories consist of wholesale merchandise inventories held for sale to customers and retail merchandise inventory held for resale at ARH retail locations and at AEH's warehouse locations. Substantially all of the Company's wholesale inventories are valued on the LIFO method. The excess of replacement cost over the LIFO value of inventory was $109.1 million and $104.5 million at January 2, 2021 and December 28, 2019, respectively. Inventories at retail locations operated by ARH and at AEH's warehouses are valued at the lower of cost or net realizable value. Inventory cost is determined using the moving average method, which approximates the FIFO method. The Company regularly reviews its inventory and establishes a reserve for excess and obsolete inventory based on a number of factors, including historical sales, sales forecasts, obsolescence due to technology changes and defective goods.

Inventories consisted of:

	January 2, 2021	December 28, 2019
Wholesale merchandise inventory (LIFO)	$ 973.6	$ 773.9
Retail merchandise inventory at ARH stores and AEH warehouses (FIFO)	159.4	156.9
Inventories	$ 1,133.0	$ 930.8

(In millions)

(5) Property and Equipment, net

Property and equipment, net is summarized as follows:

	January 2, 2021	December 28, 2019
Land	$ 14.7	$ 14.7
Buildings and improvements	297.9	294.6
Warehouse equipment	226.7	186.9
Computer hardware and software and other office equipment	371.2	343.9
Transportation equipment	41.5	39.1
Leasehold improvements	63.1	56.3
Assets under construction	19.6	5.1
Property and equipment, gross	1,034.7	940.6
Accumulated depreciation and amortization	(611.4)	(558.9)
Property and equipment, net	$ 423.3	$ 381.7

Depreciation and amortization expense related to property and equipment for fiscal years 2020, 2019 and 2018 was $60.9 million, $55.1 million and $50.0 million, respectively.

(6) Leases

The Company leases certain warehouse and distribution space, office space, retail locations, equipment and vehicles under finance and operating leases. The Company determines if an arrangement is a lease at inception and recognizes a lease liability and right-of-use (“ROU”) asset in the Company’s Consolidated Balance Sheets upon commencement of a lease. Operating and finance lease assets represent the right to use an underlying asset for the lease term. Operating and finance lease liabilities represent the obligation to make lease payments arising from the lease. These assets and liabilities are recognized based on the present value of future payments over the lease term at commencement date which is the date the Company takes possession or control of the property or equipment. The Company has elected to use a risk-free discount rate at commencement date based upon the lease term.

Original terms for facility-related leases are generally between 5 and 25 years. Original terms for equipment and vehicle leases are generally between 3 and 7 years. The Company generally does not include options to extend or terminate leases unless it is reasonably certain that the option will be exercised.

Real estate operating leases also typically require payment of real estate taxes, common area maintenance and insurance. These components comprise the majority of variable lease costs and are excluded from the present value of lease obligations. Operating lease assets also include prepaid or accrued lease payments and are reduced by lease incentives.

Certain retail lease agreements also provide for contingent rentals based on sales performance in excess of specified minimums or on changes in the consumer price indexes. Contingent rentals, which are based upon future performance or changes in indices, are excluded from the determination of lease payments and were not material. The Company’s lease agreements do not contain any material restrictions, covenants, or any material residual value guarantees.

The components of total lease expense for the twelve months ended January 2, 2021 were as follows:

	Income Statement Classification	January 2, 2021
Finance lease amortization	Cost of revenues	$ 2.9
Finance lease interest	Interest expense	0.1
Operating lease cost, net of sublease income	Cost of revenues, operating expenses	93.4
Short-term lease cost	Cost of revenues, operating expenses	6.6
Variable lease cost	Cost of revenues, operating expenses	20.4
Net lease cost		$ 123.4

(In millions)

The future minimum undiscounted lease payments under operating and finance leases at January 2, 2021 are as follows:

Fiscal Year	Operating Leases	Finance Leases
2021	$ 83.3	$ 4.7
2022	74.5	4.7
2023	67.3	4.6
2024	61.2	4.6
2025	51.5	4.5
Thereafter	170.5	1.8
Total future undiscounted lease payments	508.3	24.9
Less imputed interest	(31.6)	(0.4)
Total reported lease liability	476.7	24.5
Less current portion	(64.5)	(3.7)
Long-term lease liabilities	$ 412.2	$ 20.8

Additionally, the Company has excluded approximately $94.2 million of leases (undiscounted basis) that have not yet commenced. These leases will commence in 2021 with lease terms of up to fifteen years.

Other information related to operating and finance leases for the twelve months ended January 2, 2021, was as follows:

Cash paid for amounts included in the measurement of lease liabilities:	
Operating cash flows from operating leases	$ (93.8)
Operating cash flows from finance leases	$ (3.5)
Lease assets obtained in exchange for new lease liabilities:	
Operating leases	$ 85.8
Finance leases	$ 27.9
Weighted average remaining lease term for operating leases	8.0 years
Weighted average discount rate for operating leases	1.53%
Weighted average remaining lease term for finance leases	5.5 years
Weighted average discount rate for finance leases	0.65%

Prior to the adoption of Topic 842, the Company's operating leases were accounted for under previous lease guidance. The future minimum lease payments under operating leases having initial or remaining non-cancellable lease terms in excess of one year were previously disclosed in our fiscal 2019 Annual Report in Note 15, Commitments and Contingencies and were as follows:

Fiscal Year	As of December 28, 2019
2020	$ 84.2
2021	71.6
2022	60.9
2023	55.3
2024	49.0
Thereafter	200.6
Minimum lease payments	$ 521.6

(In millions)

(7) Notes Receivable, net

The Company makes available to its Retailers various lending programs whose terms exceed one year. At January 2, 2021 and December 28, 2019, the outstanding balance of the notes was $18.9 million and $27.7 million, respectively, of which the current portion of $16.5 million and $16.3 million, respectively, was recorded in Receivables, net.

	January 2, 2021	December 28, 2019
Notes receivable, gross	$ 45.4	$ 43.4
Less estimated patronage applications from 2020 and 2019, respectively	(26.5)	(15.7)
Net	18.9	27.7
Less current portion	(16.5)	(16.3)
Less allowance for doubtful accounts	(1.3)	(1.5)
Notes receivable, net	$ 1.1	$ 9.9

For substantially all of the Company's Notes receivable, the amounts due are generally expected to be collected through the non-cash portion of the annual patronage distribution. In the event a Retailer cancels its membership with the Company, any outstanding loans are transferred from Notes receivable to Accounts receivable and are due immediately. As the non-cash portion of the patronage distribution is used to settle the Notes receivable, there are no loans that are currently past due. The patronage distribution for each Retailer can vary from year to year based on the Company's financial performance as well as the volume of patronage-based merchandise that each Retailer purchases from the Company. The contractual maturities, assuming no patronage deductions, of the Notes receivable are as follows:

	January 2, 2021
0 – 4 years	$ 13.2
5 – 8 years	20.1
9 – 10 years	12.1
Total	$ 45.4

Pursuant to the Company's Amended and Restated Certificate of Incorporation and the Company's by-laws, notes receivable (like all obligations owed to the Company by the Company's Retailers) are secured by the Company stock owned by the Retailers. However, for some Retailers, the redemption value of their stock does not fully cover their obligations.

The Company evaluates risk on its loan portfolio by categorizing each loan into an internal risk category. The Company's risk categories include:

Low – The Retailer possesses a strong financial position, above average payment record to both Ace and other vendors, and the business is well established.

Medium – The Retailer possesses an average financial position, an average payment record to both Ace and other vendors, and the business is somewhat established.

High – The Retailer possesses a weak financial position, a substandard payment record to Ace or other vendors, or the business is somewhat new.

Based upon these criteria, the Company has classified its loan portfolio as follows:

	January 2, 2021	December 28, 2019
Corporate Credit Exposure:		
Low risk	$ 22.3	$ 20.9
Moderate risk	14.8	11.0
High risk	8.3	11.5
Total	$ 45.4	$ 43.4

(In millions)

The Company applies a consistent practice of establishing an allowance for notes that it feels may become uncollectible by monitoring the financial strength of its Retailers. The collectability of certain notes is evaluated on an individual basis while the remaining notes are evaluated on a collective basis. Due to the nature of the notes and the collateral held by the Company, virtually all outstanding notes were collectively evaluated for impairment.

The Company has evaluated the collectability of the notes and has established an allowance for doubtful accounts of $1.3 million and $1.5 million at January 2, 2021 and December 28, 2019, respectively. Management records the allowance for doubtful accounts based on the above information as well as judgments made considering a number of factors, primarily historical collection statistics, current Retailer credit information, the current economic environment and the offsetting amounts due to Retailers for stock, notes, interest and declared and unpaid patronage distributions. The components of changes to the Notes receivable allowance for doubtful accounts for 2020 and 2019 were as follows:

	January 2, 2021	December 28, 2019
Allowance for doubtful accounts:		
Beginning balance	$ 1.5	$ 2.8
Provision (Reversal)	0.2	(0.7)
Reclassifications to accounts receivable allowance for doubtful accounts	(0.4)	(0.8)
Reclassifications from accounts receivable allowance for doubtful accounts	-	0.2
Ending balance	$ 1.3	$ 1.5

Notes bear interest at various rates and are recorded at face value. Interest is recognized over the life of the note based on the outstanding balance and stated interest rate, which approximates the effective interest method. During fiscal years 2020, 2019 and 2018, $1.9 million, $2.5 million and $2.0 million respectively, were recorded as interest income related to the notes.

Generally, in the event a Retailer cancels their membership with the Company, any outstanding Notes receivable, and related allowance for doubtful accounts, are transferred to trade receivables and the Retailer is billed for any unpaid principal and interest balances. In fiscal 2020 and 2019, $6.7 million and $9.3 million, respectively, of Notes receivable were transferred to trade receivables as an event occurred which made the notes due immediately. Upon transfer of the Notes receivable to trade receivables, $0.4 million and $0.8 million in fiscal 2020 and 2019, respectively, of the Notes receivable allowance for doubtful accounts was transferred to the Receivables allowance for doubtful accounts to properly match the reserve against the asset on the Consolidated Balance Sheet.

(8) Goodwill and Other Intangible Assets

Changes in the carrying value of goodwill were as follows:

Balance at December 29, 2018	$ 74.0
Acquired goodwill	9.1
Impairment charge	(8.5)
Balance at December 28, 2019	$ 74.6
Acquired goodwill	13.3
Balance at January 2, 2021	$ 87.9

Impairment exists when a reporting unit's carrying value exceeds its fair value. The Company tests reporting units for impairment annually as of the first day of the fourth quarter, or more frequently if events or circumstances indicate it is more likely than not that the fair value of a reporting unit is less than its carrying value.

(In millions)

Identifiable intangible assets were as follows:

	January 2, 2021	December 28, 2019
Trademarks and trade name	$ 10.0	$ 9.9
Customer relationships	8.1	8.1
Maker relationships	7.7	7.7
Developed technology	2.2	2.2
Wholesale relationships	0.6	0.6
Total identifiable intangible assets	28.6	28.5
Less accumulated amortization	(16.2)	(12.6)
Identifiable intangible assets, net	$ 12.4	$ 15.9

The trademarks and trade name are being amortized over 10-20 years. The customer and maker relationships are being amortized over 3-10 years. Developed technology is being amortized over three years. Net amortization expense related to all intangible assets was $3.5 million, $4.3 million and $5.2 million for fiscal years 2020, 2019 and 2018, respectively. The estimated net amortization expense over the next five fiscal years is $8.0 million.

(9) Patronage Distributions and Refund Certificates Payable

The Company operates as a cooperative organization and has paid or may pay patronage distributions to Retailers on a portion of patronage-based income derived from business done with such Retailers. Patronage distributions are allocated in proportion to the volume of purchases by Retailers during the period. The cash portion of the patronage distribution was 40 percent for all years presented.

The accrued patronage distributions composition is summarized as follows:

	Years Ended		
	January 2, 2021	December 28, 2019	December 29, 2018
Cash portion	$ 112.9	$ 70.4	$ 55.0
Class C stock	119.1	54.6	44.0
Patronage refund certificates	15.6	30.0	23.7
Patronage financing deductions	27.8	17.5	12.7
Total patronage distributions accrued for third party Retailers	$ 275.4	$ 172.5	$ 135.4

Patronage distributions are allocated on a fiscal year basis with issuance in the following year.

In those instances where the maximum Class C stock requirements have been met, the non-cash portion of the patronage distribution is distributed in the form of patronage refund certificates with a five-year term and bearing interest at 4 percent.

The patronage refund certificates outstanding at January 2, 2021 are payable as follows:

	Amount
2021	$ 26.6
2022	27.2
2023	23.2
2024	29.3
2025	15.6
Total patronage refund certificates payable	$ 121.9
Less current portion	(26.6)
Long-term patronage refund certificates payable	$ 95.3

(In millions)

(10) Accrued Expenses

Accrued expenses include the following components:

	January 2, 2021	December 28, 2019
Salaries and wages	$ 75.9	$ 62.8
Insurance reserves	18.2	20.9
Deferred income	6.1	3.9
Vendor funds	5.0	7.3
Taxes	23.2	16.3
Profit sharing	23.7	14.4
Gift card	11.5	10.1
Interest	5.7	5.0
Advertising and marketing	27.6	25.1
Other	40.6	40.1
Accrued expenses	$ 237.5	$ 205.9

(11) Debt

The Company has a $700.0 million line of credit facility. The facility is expandable to $1.0 billion through a $300.0 million accordion that is exercisable without the consent of existing lenders provided that the Company is not in default of the credit agreement and further provided that none of the existing lenders are required to provide any portion of the increased facility. At the Company's discretion, borrowings under the credit facility bear interest at a rate of either 0 to 75 basis points over the prime rate or 100 to 175 basis points over the London Interbank Offered Rate ("LIBOR") rate depending on the Company's leverage ratio as defined under the agreement. The credit facility was priced at LIBOR plus 125 basis points at January 2, 2021. The credit facility expires on February 1, 2024 and requires maintenance of certain financial covenants including a maximum allowable average leverage ratio and a minimum fixed charge coverage ratio. As of January 2, 2021, the Company was in compliance with its covenants and $7.9 million was outstanding under the credit facility.

The credit facility includes a $175.0 million sublimit for the issuance of standby and commercial letters of credit. As of January 2, 2021, a total of $19.8 million in letters of credit were outstanding. The credit facility requires the Company to pay fees based on the unused portion of the line of credit at a rate of 12.5 to 25 basis points per annum depending on the Company's leverage ratio.

The credit facility allows the Company to make revolving loans and other extensions of credit to AIH in an aggregate principal amount not to exceed $75.0 million at any time. As of January 2, 2021, there were no loans or other extensions of credit provided to AIH.

The Company was a party to an interest rate swap derivative agreement, which started on March 13, 2017 and expired on May 13, 2020. The swap agreement fixed the LIBOR rate on $150.0 million of the revolving credit facility borrowings at 2.18 percent, plus the then effective margin based on the then current pricing tier per the credit agreement. The swap arrangement was designated as a cash flow hedge and was evaluated to be highly effective throughout the term. As a result, the after-tax change in the fair value of the swap was recorded in AOCI as a gain or loss on derivative financial instruments.

The Company's Westlake subsidiary has a $100.0 million asset-based revolving credit facility ("Westlake Facility"). The Westlake Facility expires on October 24, 2022. Under this facility, Westlake has the right to issue letters of credit up to a maximum of $7.5 million. At Westlake's discretion, borrowings under this facility bear interest at a rate of either the prime rate plus an applicable spread of 25 to 50 basis points or LIBOR plus an applicable spread of 125 to 150 basis points, depending on Westlake's average availability under the Westlake Facility as measured on a trailing 12-month basis. The Westlake Facility was priced at LIBOR plus 125 basis points at January 2, 2021.

The Westlake Facility is collateralized by substantially all of Westlake's personal property and intangible assets. Borrowings under the facility are subject to a borrowing base calculation consisting of certain advance rates applied to eligible collateral balances (primarily consisting of certain receivables and inventories). This agreement requires maintenance of certain financial covenants including a minimum fixed charge coverage ratio. As of January 2, 2021, ARH was in compliance with its covenants and had $20.1 million outstanding under the Westlake Facility. The Westlake Facility includes a lender-controlled cash concentration system that results in all of Westlake's daily available cash being applied to the outstanding borrowings under their facility. Pursuant to FASB Accounting Standards Codification Section 470-10-45, "Classification of Revolving Credit Agreements Subject to Lock-Box

(In millions)

Arrangements and Subjective Acceleration Clauses," the borrowings under the Westlake Facility have been classified as a Current maturity of long-term debt. The GLA Facility was classified under this guidance in prior presented periods.

The Company's GLA subsidiary had a $20.0 million asset-based revolving credit facility ("GLA Facility") that had a maturity date of November 6, 2022. GLA terminated the facility effective August 31, 2020.

Total debt outstanding is comprised of the following:

	January 2, 2021	December 28, 2019
Revolving Credit Facility	$ 7.9	$ 196.5
Westlake Facility	20.1	52.0
GLA Facility	-	4.5
Installment notes with maturities through 2024 at a fixed rate of 6.00%	28.5	23.9
Total debt	56.5	276.9
Less maturities within one year	(31.7)	(67.0)
Long-term debt	$ 24.8	$ 209.9

The aggregate scheduled maturities of total debt at January 2, 2021 are as follows:

Fiscal Year	Amount
2021	$ 31.7
2022	7.9
2023	6.0
2024	10.9
Total debt	$ 56.5

(12) Commitments and Contingencies

Contingencies

The Company has certain contingent liabilities resulting from litigation and claims incident to the ordinary course of business. Management believes that the probable resolution of such contingencies will not materially affect the financial position, results of operations, or liquidity of the Company. The Company expenses legal fees as they are incurred.

Other guarantees

In the normal course of business, the Company enters into commercial commitments including standby letters of credit and guarantees that could become contractual obligations. Letters of credit are issued generally to insurance agencies and financial institutions in direct support of the Company's corporate and Retailer insurance programs as well as to international vendors for imported inventory purchases. As of January 2, 2021, the Company had outstanding standby letters of credit of $14.3 million issued in the normal course of NAIL's operations and commercial letters of credit of $19.8 million issued by the Company's credit facility.

During fiscal 2019 the Company facilitated the adoption of the Ace Hardware Corporation Cooperative Group Health Plan ("AHP"). The AHP is a MEWA that provides medical insurance and other welfare benefits to employees of the Company and their families and employees and families of participating Retailers, beginning January 1, 2020.

The AHP is insured by Ace Group Insurance, Inc. ("AGI"), a newly-formed Vermont-based captive insurance company. AGI is owned by a newly-formed funded welfare trust ("Trust") that serves as the mechanism for the AHP to collect, hold, invest and pay funds deposited with the AHP for the conduct of AHP operations. The Trust is not owned by the Company or any of its subsidiaries.

In order to establish and provide initial capitalization of the AHP, AGI and Trust, NAIL provided a $10 million standby letter of credit in favor of AGI. The letter of credit is held by the Vermont Department of Financial Regulations ("VDFR") and can be drawn upon at VDFR's direction if AGI becomes illiquid. The Company believes that the likelihood of the letter of credit being drawn is remote.

(In millions)

(13) Fair Value

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. There is a three-level hierarchy for disclosure to show the extent and level of judgment used to estimate fair value measurements.

Level 1 – Uses unadjusted quoted prices that are available in active markets for the identical assets or liabilities as of the reporting date.

Level 2 – Uses inputs other than Level 1 that are either directly or indirectly observable as of the reporting date through correlation with market data, including quoted prices for similar assets and liabilities in active markets and quoted prices in markets that are not active. Level 2 also includes assets and liabilities that are valued using models or other pricing methodologies that do not require significant judgment since the input assumptions used in the models, such as interest rates and volatility factors, are corroborated by readily observable data.

Level 3 – Uses inputs that are unobservable and are supported by little or no market activity and reflect the use of significant management judgment. These values are generally determined using pricing models for which the assumptions utilize management's estimates of market participant assumptions.

The tables below set forth, by level, the Company's financial assets, liabilities and derivative instruments that were accounted for at fair value as of January 2, 2021 and of December 28, 2019. The tables do not include cash on hand and also do not include assets and liabilities that are measured at historical cost or any basis other than fair value. The carrying values for other current financial assets and liabilities, such as accounts receivable and accounts payable, approximate fair value due to the short maturity of such instruments. Long-term notes receivable approximate fair value because the Company charges its Retailers an interest rate and a significant portion of the notes have the Company's stock as collateral.

Items measured at fair value on a recurring basis	Carrying Value Measured at Fair Value January 2, 2021	Level 1	Level 2	Level 3
Assets:				
Cash equivalents:				
Money market funds	$ 2.8	$ 2.8	$ -	$ -
Marketable securities:				
Corporate fixed income securities	35.1	-	35.1	-
Mortgage-backed securities	9.9	-	9.9	-
U.S. government notes	17.8	9.8	8.0	-
Other	0.4	-	0.4	-
Total marketable securities	$ 63.2	$ 9.8	$ 53.4	$ -

(In millions)

Items measured at fair value on a recurring basis	Carrying Value Measured at Fair Value December 28, 2019	Level 1	Level 2	Level 3
Assets:				
Cash equivalents:				
Money market funds	$ 3.7	$ 3.7	$ -	$ -
Marketable securities:				
Corporate fixed income securities	31.0	-	31.0	-
Mortgage-backed securities	10.8	-	10.8	-
U.S. government notes	17.0	11.7	5.3	-
Other	0.7	-	0.7	-
Total marketable securities	$ 59.5	$ 11.7	$ 47.8	$ -
Accrued expenses:				
Interest rate swap derivative	$ 0.3	$ -	$ 0.3	$ -

Money market funds and U.S. government notes – The Company's valuation techniques used to measure the fair values of money market funds and U.S. government notes, that were classified as Level 1 in the tables above, are derived from quoted market prices for identical instruments, as active markets for these instruments exist.

Corporate fixed income securities, Mortgage-backed securities and Other – Other securities primarily consist of taxable municipal bonds, corporate asset-backed securities, and U.S. Agency fixed rate notes and bonds. The Company's valuation techniques used to measure the fair values of corporate fixed income securities, mortgage-backed securities and other securities, that were classified as Level 2 in the tables above, are derived from the following: non-binding market consensus prices that are corroborated by observable market data, quoted market prices for similar instruments, or pricing models, such as discounted cash flow techniques, with all significant inputs derived from or corroborated by observable market data.

The fair value of the Company's marketable securities was greater than their cost by $3.7 million at January 2, 2021 and was greater than their cost by $1.3 million at December 28, 2019.

Gross proceeds from the sale of marketable securities and the related realized gains and losses for the fiscal years ended January 2, 2021, December 28, 2019 and December 29, 2018 were as follows:

	Years Ended		
	January 2, 2021	December 28, 2019	December 29, 2018
Gross proceeds	$ 20.8	$ 41.4	$ 25.4
Gross realized gains	0.4	0.8	5.6
Gross realized losses	(0.2)	(0.2)	(0.3)

Gross realized gains and losses were determined using the specific identification method. For the fiscal year ended January 2, 2021, the Company reclassified $0.4 million of unrealized gains and $0.1 million of unrealized losses on marketable securities that were recorded in AOCI as of December 28, 2019 into realized income. These amounts were recorded to Other income, net in the Consolidated Statement of Income.

The following table summarizes the contractual maturity distributions of the Company's debt securities at January 2, 2021. Actual maturities may differ from the contractual or expected maturities since borrowers may have the right to prepay obligations with or without prepayment penalties.

(In millions)

Fair value of available-for-sale debt securities	Due in One Year or Less	Due After One Year through Five Years	Due After Five Years through Ten Years	Due After Ten Years	Total
Corporate fixed income securities	$ 3.7	$ 16.9	$ 8.2	$ 6.3	$ 35.1
Mortgage-backed securities	0.2	0.4	0.8	8.5	9.9
U.S. government notes	3.2	4.3	3.8	6.5	17.8
Other	-	-	0.3	0.1	0.4
Total	$ 7.1	$ 21.6	$ 13.1	$ 21.4	$ 63.2

The Company uses variable-rate LIBOR debt to finance its operations. These debt obligations expose the Company to interest rate volatility risk. The Company has historically attempted to minimize this risk and fix a portion of its overall borrowing costs through the utilization of interest rate swap derivatives. Variable cash flows from outstanding debt are converted to fixed-rate cash flows by entering into receive-variable, pay-fixed interest rate swaps. The Company does not use derivative instruments for trading or speculative purposes, and all derivative instruments are recognized in the Consolidated Balance Sheet at fair value. Hedge ineffectiveness is eliminated by matching all terms of the hedged item and the hedging derivative at inception and on an ongoing basis. The Company does not exclude any terms from consideration when applying the matched terms method.

The Company was a party to an interest rate swap derivative agreement, which started on March 13, 2017 and expired on May 13, 2020. The swap agreement fixed the LIBOR rate on $150.0 million of the revolving credit facility borrowings at 2.18 percent, plus the then effective margin based on the then current pricing tier per the credit agreement – see Note 11 for more information.

Because the interest rate swap was designated as a cash flow hedge and was evaluated to be highly effective, the change in the fair value was recorded in AOCI as a gain or loss on derivative financial instruments. The net of tax amount recorded in AOCI for the fair value adjustment of the interest rate swap was an unrealized loss of $0.2 million as of December 28, 2019. There was no hedge ineffectiveness related to the interest rate swap in fiscal 2020 through the date of expiration.

The Company's debt instruments are recorded at cost on the Consolidated Balance Sheets. The fair value of the Company's debt approximated its carrying value at January 2, 2021. The estimated fair value of long-term debt is based on estimated rates for similar instruments and discounted cash flow analysis using the Company's weighted-average interest rate and is, therefore, classified as Level 3 within the fair value hierarchy.

(14) Income Taxes

Income tax (expense) benefit includes the following components:

	Years Ended		
Current:	January 2, 2021	December 28, 2019	December 29, 2018
Federal	$ 1.4	$ (0.4)	$ 1.6
State	(3.1)	(0.4)	(0.2)
Foreign	(0.9)	(1.1)	(1.1)
Current income tax (expense) benefit	(2.6)	(1.9)	0.3
Deferred:			
Federal	(2.8)	12.0	2.2
State	0.4	1.5	-
Deferred income tax (expense) benefit	(2.4)	13.5	2.2
Total income tax (expense) benefit	$ (5.0)	$ 11.6	$ 2.5

(In millions)

Income tax differs from the amount computed by applying the statutory U.S. Federal income tax rate of 21 percent for fiscal years ended January 2, 2021, December 28, 2019 and December 29, 2018 to pre-tax income because of the effect of the following items:

	Years Ended		
	January 2, 2021	December 28, 2019	December 29, 2018
Expected tax at U.S. Federal income tax rate	$ (67.6)	$ (27.1)	$ (26.4)
Patronage distribution deductions	57.8	36.2	28.4
NOL carryback – tax rate differential	6.3	-	-
Other, net	(1.5)	2.5	0.5
Income tax (expense) benefit	$ (5.0)	$ 11.6	$ 2.5

Under the CARES Act, net operating losses ("NOLs") arising in tax years beginning after December 31, 2017 and ending before January 1, 2021 may be carried back for five years. The Company had NOLs arising in the 2018 and 2019 tax years which, prior to this legislation could only be carried forward into tax years with a federal statutory rate of 21 percent. These NOLs can now be carried back to years prior to 2018 with a federal statutory rate of 35 percent. The Company realized a $6.3 million federal tax benefit resulting from this tax rate differential.

Deferred income taxes reflect the tax effects of temporary differences between the carrying amounts of existing assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's deferred tax assets and liabilities are as follows:

Deferred tax assets:	January 2, 2021	December 28, 2019
Foreign tax credits and other tax credit carryforwards	$ 12.8	$ 11.4
Net operating loss carryforwards	0.3	14.0
Unearned insurance premium and loss reserves	1.0	1.1
Allowance for doubtful accounts	1.1	1.4
Inventory reserves	8.0	4.6
Deferred vendor rebates	16.4	9.7
Accrued compensation and benefits expense	14.7	13.2
Other reserves	10.9	11.8
Total deferred tax assets	65.2	67.2
Less valuation allowance	(9.8)	(8.9)
Deferred tax assets	55.4	58.3
Deferred tax liabilities:		
Depreciation and deferred gains on property and equipment	8.7	8.4
Amortization of intangibles	2.4	2.0
Net unrealized gains	0.3	0.3
Fair market value of leases	-	0.5
Prepaid expenses and deferred income	4.5	4.6
Inventory valuation	16.7	16.6
Deferred tax liabilities	32.6	32.4
Net deferred tax assets	$ 22.8	$ 25.9

Net deferred tax assets are included in Other assets on the Consolidated Balance Sheets.

At January 2, 2021, the Company has state and foreign net operating loss carryforwards of $1.9 million available for offset against future taxable income. For those states not conforming to the indefinite federal carryforward provisions, the post-2018 state net operating losses can, generally, be carried forward through the 2038 and 2039 tax years.

At January 2, 2021, the Company has foreign tax credits of $2.3 million available to offset future tax expense. The foreign tax credits may be carried forward to tax years 2028 through 2030.

At January 2, 2021, the Company has state tax credit carryforwards of $10.5 million available to offset future state income tax expense. The state tax credits may be carried forward to tax years 2021 through 2025. A valuation allowance of $9.8 million has been established against certain state tax credits as it is more likely than not that the benefit of the tax credits will not be realized.

The federal income tax returns of the consolidated group are subject to examination by the Internal Revenue Service ("IRS"), generally for three years after the returns are filed. The 2016 through 2020 tax years remain subject to examination by the IRS. For state purposes, the 2015 through 2020 tax years remain subject to examination.

The Company recognizes interest and penalties related to uncertain tax positions in Income tax expense. Accrued interest and penalties included in the reserve for uncertain tax positions were $0.3 million at January 2, 2021 and December 28, 2019, respectively. The Company recognized immaterial amounts related to interest and penalties within Income tax expense for the years ended January 2, 2021, December 28, 2019 and December 29, 2018. It is reasonably possible that the total amount of unrecognized tax benefits will increase or decrease within the next twelve months. The Company currently estimates that such increases and decreases will not be significant.

(15) Capital Stock

The Company's classes of stock are described below (not in millions):

	Number of Shares at	
	January 2, 2021	December 28, 2019
Class A stock, voting, redeemable at par value:		
Authorized	10,000	10,000
Issued and outstanding	2,689	2,691
Class C stock, nonvoting, redeemable at not less than par value:		
Authorized	10,000,000	6,000,000
Issued and outstanding	5,015,306	4,827,851
Issuable as patronage distributions	1,191,050	546,146

No dividends can be declared on any shares of any class of the Company's stock.

Upon termination of the Company's membership agreement with any retail outlet, all shares of stock of the Company held by the Retailer owning or controlling such outlet must be sold back to the Company, unless a transfer of such shares is made to another party accepted by the Company as a Retailer with respect to the same outlet. A single Class A share is issued to a Retailer only when the share subscribed has been fully paid and Class C shares are issued only when all shares subscribed with respect to a retail outlet have been fully paid. Additional stock subscribed in the accompanying consolidated financial statements represents the paid portion of stock subscribed for stores that have not opened. All shares of stock are currently issued and repurchased at par value.

(16) Retirement Plans

The Company has healthcare plans under which a limited number of qualified retired employees receive certain health care, dental care, life insurance or related benefits. Amounts expensed under these plans were $0.1 million or less in each of the fiscal years 2020, 2019 and 2018.

The Company and its subsidiaries maintain profit sharing and 401k retirement plans for substantially all employees. Amounts expensed under these plans totaled $39.3 million, $28.8 million and $22.8 million during fiscal 2020, 2019 and 2018, respectively.

(17) Supplemental Disclosures of Cash Flow Information

During fiscal 2020, 2019 and 2018, accrued patronage distributions of $29.2 million, $19.1 million and $13.6 million, respectively, were offset against trade receivables and notes receivable owed to the Company by its Retailers with no net impact in the Consolidated Statements of Cash Flows. In addition, the Company had $17.0 million in patronage refund certificates which were included in Accounts payable pending payment in Fiscal 2021 as of January 2, 2021 and had no net impact in the Consolidated Statements of Cash Flows.

During fiscal 2020, 2019 and 2018, non-cash repurchases of stock from Retailers of $30.8 million, $20.7 million and $23.1 million, respectively, were offset against trade receivables of $9.9 million, $5.5 million and $5.2 million, respectively, and notes receivable of $5.6 million, $7.0 million and $6.0 million, respectively. The remaining $15.3 million, $8.2 million and $11.9 million, respectively, were primarily issued as notes payable with no net impact in the Consolidated Statements of Cash Flows.

(In millions)

During fiscal 2020, the Company received $9.4 million of property and equipment prior to year-end and accrued for these items as no cash payments were made. These capital expenditures were not included in the Purchases of property and equipment in the Consolidated Statement of Cash Flows for fiscal year 2020. During fiscal 2020, the Company paid $5.1 million for property and equipment that was purchased and accrued during the year ended December 28, 2019. These capital expenditures were included in the Purchases of property and equipment in the Consolidated Statement of Cash Flows for fiscal year 2020.

(18) Summary of Quarterly Results

The following table provides a summary of quarterly results (unaudited) for the eight quarters prior to and including the quarter ended January 2, 2021:

	2020			
	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Revenues	$ 2,052.7	$ 2,000.5	$ 2,279.1	$ 1,430.4
Gross profit	291.4	328.9	370.6	222.6
Operating expenses	243.5	220.4	232.2	184.3
Net income attributable to Ace Hardware Corporation	43.3	98.9	139.1	36.3

	2019			
	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Revenues	$ 1,475.1	$ 1,530.1	$ 1,687.5	$ 1,378.5
Gross profit	214.3	240.3	247.4	190.6
Operating expenses	213.1	185.2	193.3	167.2
Net income attributable to Ace Hardware Corporation	3.9	60.3	53.7	22.5

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis summarizes the significant factors affecting Ace Hardware Corporation's ("the Company's") consolidated operating results and financial condition during the three-year period ended January 2, 2021 (the Company's fiscal years 2020, 2019 and 2018). Fiscal year 2020 contains 53 weeks of operating results. Fiscal years 2019 and 2018 each contain 52 weeks of operating results. Unless otherwise noted, all references herein for the years 2020, 2019 and 2018 represent fiscal years ended January 2, 2021, December 28, 2019 and December 29, 2018, respectively. This discussion and analysis should be read in conjunction with the consolidated financial statements and the related notes included in this annual report that have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP").

Company Overview

The Company is a wholesaler of hardware and other related products and provides services and best practices for its member retailers ("Retailers"). The overall home improvement industry is estimated to be almost $460 billion and consists of a broad range of products and services, including lawn and garden products, paint and sundries, certain building supplies and general merchandise typically used in connection with home and property improvement, remodeling, repair and maintenance. The industry is fragmented and competition exists between the large home improvement centers, retail hardware stores and other chains offering hardware merchandise. In addition, we face growing competition from online and multichannel retailers.

The Company's retailers generally compete in the $62 billion "convenience hardware" segment which is characterized by purchases primarily of products related to home improvement and repair, including paint and related products, lawn and garden equipment, and those products less focused on large-scale building, renovation and remodeling projects. The Company believes that the following competitive strengths distinguish it from its peers and contribute to its success in the convenience hardware market: (1) strong consumer recognition of the Ace Brand; (2) well-regarded for exceptional customer service and convenience; (3) strength of distribution operations; (4) consolidated purchasing power; (5) differentiated and localized product and service offerings; and (6) a diversified network of independent retailers.

The Company strives to be the best provider of products, services and operating methods for convenience hardware retailers. The four main drivers that support that goal and the Company's efforts to grow the business are improving the store model, accelerating new store openings, increasing store projects that drive store sales and profitability and reducing the number of store closings.

Ace Hardware International Holdings, Ltd. ("AIH") is a majority-owned and controlled subsidiary of the Company with a 20.7 percent noncontrolling interest owned by its international retailers. AIH has wholesale distribution capabilities in Ningbo, China; Colon, Panama; and Dubai, United Arab Emirates. AIH customers operate 816 stores located in approximately 65 countries.

Ace Retail Holdings LLC ("ARH") is the owner of the 145 store Westlake Ace Hardware retail chain. In March 2019, ARH acquired the remaining 58 percent of the outstanding stock of Great Lakes Ace Hardware, Inc. ("GLA") that it did not already own. GLA is the owner of the 57 store Great Lakes Ace retail chain. As a result, the Company is also a retailer of hardware, paint and other related products.

Ace Wholesale Holdings LLC ("AWH") owns and operates Emery Jensen Distribution and its related wholesale companies. AWH was formed in 2014 so that the Company could begin making wholesale hardware sales to non-member retailers.

Ace Ecommerce Holdings LLC ("AEH") owns The Grommet, an e-commerce company that operates a website that markets and sells new and innovative products created by independent entrepreneurs.

In September 2019, the Company formed the Ace Services Holdings LLC ("ASH") legal entity. On September 5, 2019, ASH acquired Handyman Matters Inc., a franchisor of home improvement, maintenance and repair services.

Worldwide Store Count

The number of worldwide Ace retail outlets during the past three fiscal years is summarized as follows:

	Fiscal Years		
	2020	2019	2018
Retail outlets at beginning of period	5,366	5,253	5,121
New retail outlets	201	208	257
Retail outlet cancellations	(104)	(95)	(125)
Retail outlets at end of period	5,463	5,366	5,253

Results of Operations

Comparison of the Year Ended January 2, 2021 to the Year Ended December 28, 2019

The following data summarizes the Company's performance in 2020 as compared to 2019 (in millions):

	2020		2019		Favorable/ (Unfavorable)	
	$	% of Revenues*	$	% of Revenues*	$	%
Revenues:						
Wholesale revenues	7,011.2	90.3%	5,564.5	91.7%	1,446.7	26.0%
Retail revenues	751.5	9.7%	506.7	8.3%	244.8	48.3%
Total revenues	7,762.7	100.0%	6,071.2	100.0%	1,691.5	27.9%
Gross profit:						
Wholesale gross profit	879.1	12.5%	665.9	12.0%	213.2	32.0%
Retail gross profit	334.4	44.5%	226.7	44.7%	107.7	47.5%
Total gross profit	1,213.5	15.6%	892.6	14.7%	320.9	36.0%
Operating expenses:						
Wholesale operating expenses	626.0	8.9%	540.1	9.7%	(85.9)	(15.9%)
Retail operating expenses	253.1	33.7%	201.5	39.8%	(51.6)	(25.6%)
Retail pre-opening expenses	1.3	0.2%	8.7	1.7%	7.4	85.1%
Goodwill impairment	-	0.0%	8.5	1.7%	8.5	100.0%
Total operating expenses	880.4	11.3%	758.8	12.5%	(121.6)	(16.0%)
Operating income	333.1	4.3%	133.8	2.2%	199.3	149.0%
Interest expense	(19.1)	(0.2%)	(22.7)	(0.4%)	3.6	15.9%
Other income, net	3.6	0.0%	29.3	0.5%	(25.7)	(87.7%)
Net income attributable to Ace Hardware Corporation	317.6	4.1%	140.4	2.3%	177.2	126.2%

*Wholesale gross profit and expenses are shown as a percentage of wholesale revenues. Retail gross profit and expenses are shown as a percentage of retail revenues. Non-operating items are shown as a percentage of total revenues.

A reconciliation of consolidated revenues follows (in millions):

	Amount	% Change vs. 2019
2019 Revenues	$ 6,071.2	
Wholesale Merchandise Revenues change based on new and cancelled domestic Ace stores:		
Revenues increase from new stores added since January 2019	204.1	3.4%
Revenues decrease from stores cancelled since January 2019	(38.9)	(0.6%)
Increase in wholesale merchandise revenues to comparable domestic Ace stores	1,176.5	19.4%
Increase in AWH revenues	25.8	0.4%
Decrease in AIH revenues	(36.0)	(0.6%)
Increase in ARH revenues	237.9	3.9%
Increase in AEH retail revenues	6.4	0.1%
Increase in Acehardware.com revenues	186.5	3.1%
Other revenue changes, net (primarily elimination of increased wholesale revenue to ARH)	(70.8)	(1.2%)
2020 Revenues	$ 7,762.7	27.9%

Consolidated revenues for the year ended January 2, 2021 totaled $7.8 billion, an increase of $1.7 billion, or 27.9 percent, as compared to the prior year. Fiscal 2020 consisted of 53 weeks compared to 52 weeks in fiscal 2019. The 53rd week added $99.9 million in sales. Excluding the 53rd week, sales increased $1.6 billion or 26.2 percent compared to fiscal 2019.

Total wholesale revenues were $7.0 billion for fiscal 2020, an increase of $1.5 billion, or 26.0 percent, as compared to the prior year. New domestic Ace stores are defined as stores that were activated from January 2019 through December 2020. In 2020, the Company had an increase in wholesale merchandise revenues from new domestic Ace stores of $204.1 million. This increase was partially offset by a decrease in wholesale merchandise revenues due to domestic Ace store cancellations of $38.9 million. As a result, the Company realized a net increase in wholesale merchandise revenues of $165.2 million related to the impact of both new Ace stores affiliated with the Company and from stores that cancelled their membership in 2019 and 2020. Wholesale merchandise revenues to comparable domestic Ace stores increased $1.2 billion compared to the prior year. Increases were noted across all departments with grilling, paint, power tools and outdoor power equipment showing the largest gains. Warehouse sales represented 80.2 percent of wholesale merchandise revenue in 2020 compared to 78.9 percent in 2019, while direct ship sales were 19.8 percent, down from 21.1 percent in 2019.

AWH wholesale revenues were $406.9 million during fiscal 2020. This is an increase of $25.8 million from fiscal 2019, which was primarily due to higher sales to e-commerce customers and traditional hardware stores.

AIH wholesale revenues were $217.1 million during fiscal 2020. This is a decrease of $36.0 million from fiscal 2019, as the global pandemic caused temporary store closures at AIH's largest customers.

Total retail revenues were $751.5 million, an increase of $244.8 million, or 48.3 percent, as compared to the prior year. Retail revenues from ARH were $704.4 million during fiscal 2020, an increase of $237.9 million or 51.0 percent. Westlake experienced a 24.7 percent increase in same-store-sales while GLA grew same-store-sales by 32.7 percent during fiscal 2020. The eleven new California stores opened by Westlake in 2019 contributed $87.2 million of the increase. Retail revenues from AEH were $47.1 million during fiscal 2020. This was an increase of $6.4 million from fiscal 2019, primarily driven by new customer acquisitions.

Wholesale gross profit for fiscal 2020 was $879.1 million, an increase of $213.2 million from fiscal 2019. The wholesale gross margin percentage was 12.5 percent of wholesale revenues in fiscal 2020, an increase from the fiscal 2019 gross margin percentage of 12.0 percent. The increase in wholesale gross margin percentage was due to the increased volume, which led to higher vendor funds earned.

Retail gross profit for fiscal 2020 was $334.4 million, an increase of $107.7 million from fiscal 2019. The retail gross margin percentage was 44.5 percent of retail revenues in fiscal 2020, down slightly from 44.7 percent in fiscal 2019. For ARH, retail gross profit as reported in the Ace financial statements is based on the Ace wholesale acquisition cost of product, not ARH's acquisition cost which includes a markup from the Company.

Wholesale operating expenses increased $85.9 million, or 15.9 percent in fiscal 2020, as compared to fiscal 2019. The increase is due to higher distribution costs resulting from higher wholesale revenues and an increase in advertising expenses. As a percentage of wholesale revenues, wholesale operating expenses decreased to 8.9 percent in fiscal 2020 from 9.7 percent in fiscal 2019.

Retail operating expenses increased $51.6 million, or 25.6 percent in fiscal 2020, as compared to fiscal 2019. This increase was primarily driven by compensation and operating costs to support the increase in retail revenues along with expenses related to the eleven new California stores. Retail operating expenses as a percentage of retail revenue decreased to 33.7 percent in fiscal 2020 from 39.8 percent in fiscal 2019.

Retail pre-opening expenses decreased $7.4 million in fiscal 2020 due to expenses related to the eleven new California stores which opened in 2019.

During fiscal 2019, the Company recorded a non-cash impairment charge of $8.5 million to fully eliminate the carrying amount of goodwill in the AEH subsidiary.

Interest expense decreased $3.6 million or 15.9 percent compared to fiscal 2019 due a significant decrease in LIBOR rates during fiscal 2020.

Other income, net decreased $25.7 million compared to fiscal 2019 primarily due to a $16.6 million increase in income tax expense in fiscal 2020 compared to fiscal 2019 due to increased taxable income from non-patronage sources. Additionally, Other income, net decreased as a result of the $4.9 million gain recorded in fiscal 2019 on the sale of the Company's Prince George RSC and decreased gains on equity investments.

Comparison of the Year Ended December 28, 2019 to the Year Ended December 29, 2018

The following data summarizes the Company's performance in 2019 as compared to 2018 (in millions):

	2019		**2018**		**Favorable/ (Unfavorable)**	
	$	% of Revenues*	$	% of Revenues*	$	%
Revenues:						
Wholesale revenues	5,564.5	91.7%	5,341.6	93.4%	222.9	4.2%
Retail revenues	506.7	8.3%	375.4	6.6%	131.3	35.0%
Total revenues	6,071.2	100.0%	5,717.0	100.0%	354.2	6.2%
Gross profit:						
Wholesale gross profit	665.9	12.0%	634.2	11.9%	31.7	5.0%
Retail gross profit	226.7	44.7%	160.9	42.9%	65.8	40.9%
Total gross profit	892.6	14.7%	795.1	13.9%	97.5	12.3%
Operating expenses:						
Wholesale operating expenses	540.1	9.7%	510.5	9.6%	(29.6)	(5.8%)
Retail operating expenses	201.5	39.8%	154.4	41.1%	(47.1)	(30.5%)
Retail pre-opening expenses	8.7	1.7%	1.7	0.5%	(7.0)	(411.8%)
Goodwill impairment	8.5	1.7%	-	-%	(8.5)	(100.0%)
Total operating expenses	758.8	12.5%	666.6	11.7%	(92.2)	(13.8%)
Operating income	133.8	2.2%	128.5	2.2%	5.3	4.1%
Interest expense	(22.7)	(0.4%)	(20.4)	(0.4%)	(2.3)	(11.3%)
Other income, net	29.3	0.5%	19.6	0.4%	9.7	49.5%
Net income attributable to Ace Hardware Corporation	140.4	2.3%	127.7	2.2%	12.7	9.9%

*Wholesale gross profit and expenses are shown as a percentage of wholesale revenues. Retail gross profit and expenses are shown as a percentage of retail revenues. Non-operating items are shown as a percentage of total revenues.

A reconciliation of consolidated revenues follows (in millions):

	Amount	% Change vs. 2018
2018 Revenues	$ 5,717.0	
Wholesale Merchandise Revenues change based on new and cancelled domestic Ace stores:		
Revenues increase from new stores added since January 2018	186.0	3.3%
Revenues decrease from stores cancelled since January 2018	(42.7)	(0.8%)
Increase in wholesale merchandise revenues to comparable domestic Ace stores	155.1	2.7%
Decrease in AWH revenues	(11.5)	(0.2%)
Decrease in AIH revenues	(6.4)	(0.1%)
Increase in ARH revenues	136.8	2.4%
Decrease in AEH retail revenues	(5.0)	(0.1%)
Other revenue changes, net (primarily elimination of wholesale revenue to ARH)	(58.1)	(1.0%)
2019 Revenues	$ 6,071.2	6.2%

Consolidated revenues for the year ended December 28, 2019 totaled $6.1 billion, an increase of $354.2 million, or 6.2 percent, as compared to the prior year. Total wholesale revenues were $5.6 billion for fiscal 2019, an increase of $222.9 million, or 4.2 percent, as compared to the prior year. The categories with the largest revenue gains were grilling, hand and power tools and outdoor power equipment. New domestic Ace stores are defined as stores that were activated from January 2018 through December 2019. In 2019, the Company had an increase in wholesale merchandise revenues from new domestic Ace stores of $186.0 million. This increase was partially offset by a decrease in wholesale merchandise revenues due to domestic Ace store cancellations of $42.7 million. As a result, the Company realized a net increase in wholesale merchandise revenues of $143.3 million related to the impact of both new Ace stores affiliated with the Company and from stores that cancelled their membership in 2018 and 2019. Wholesale merchandise revenues to comparable domestic Ace stores increased $155.1 million compared to the prior year. This net increase was partially offset by the elimination of $56.2 million of sales to GLA which became a wholly-owned subsidiary and was fully consolidated beginning in the first quarter of 2019. This elimination was not required in 2018. Warehouse sales represented 78.9 percent of wholesale merchandise revenue in 2019 compared to 79.2 percent in 2018, while direct ship sales were 21.1 percent, up from 20.8 percent in 2018.

AWH revenues were $391.2 million during fiscal 2019. This is a decrease of $11.5 million from fiscal 2018 and was the result of the decision to reduce the number of products available for sale to certain customers due to low profitability.

AIH revenues were $253.1 million during fiscal 2019. This is a decrease of $6.4 million from fiscal 2018 and was driven by lower sales to customers in St. Maarten, UAE, Indonesia, Puerto Rico, Ecuador and Israel, partially offset by increased sales to customers in Saudi Arabia and the Philippines.

Total retail revenues were $506.7 million, an increase of $131.3 million, or 35.0 percent, as compared to the prior year. Retail revenues from ARH were $466.5 million during fiscal 2019, an increase of $136.8 million or 41.5 percent. A significant portion of this increase was due to the inclusion of GLA, which contributed $94.8 million of this increase. The remaining increase was the result of twelve new retail stores added by the Westlake retail chain since January 2018, including eleven in California. Retail revenues from AEH were $40.7 million during fiscal 2019, compared to $45.7 million during fiscal 2018. This was a decrease of $5.0 million from fiscal 2018 which was the result of a reduction in new customer acquisitions.

Wholesale gross profit for fiscal 2019 was $665.9 million, an increase of $31.7 million from fiscal 2018. The wholesale gross margin percentage was 12.0 percent of wholesale revenues in fiscal 2019, up slightly from 11.9 percent in fiscal 2018.

Retail gross profit for fiscal 2019 was $226.7 million, an increase of $65.8 million from fiscal 2018. The retail gross margin percentage was 44.7 percent of retail revenues in fiscal 2019, up from 42.9 percent in fiscal 2018. The increase in retail gross margin percentage was primarily a result of an increase in vendor income earned and the inclusion of GLA results in fiscal 2019 which carried a higher margin. For ARH, retail gross profit as reported in the Ace financial statements is based on the Ace wholesale acquisition cost of product, not ARH's acquisition cost which includes a markup from the Company.

Wholesale operating expenses increased $29.6 million, or 5.8 percent in fiscal 2019, as compared to fiscal 2018. The increase is primarily due to higher distribution costs associated with the increased volume. As a percentage of wholesale revenues, wholesale operating expenses increased slightly to 9.7 percent in fiscal 2019 from 9.6 percent in fiscal 2018.

Retail operating expenses increased $47.1 million, or 30.5 percent in fiscal 2019, as compared to fiscal 2018. ARH's retail operating expenses increased $49.8 million, or 41.9 percent, in fiscal 2019 as compared to fiscal 2018. Approximately $33.4 million of the increase was due to the inclusion of GLA operating expenses as a result of consolidating GLA results beginning in the first quarter of 2019. The remainder of the ARH increase was driven by expenses from twelve new retail stores added by Westlake in 2019. Retail operating expenses as a percentage of retail revenue decreased to 39.8 percent in fiscal 2019 from 41.1 percent in fiscal 2018.

Retail pre-opening expenses of $8.7 million were incurred in fiscal 2019 primarily related to one-time, start-up costs from eleven new stores in California opened by Westlake during fiscal 2019.

During fiscal 2019, the Company recorded a non-cash impairment charge of $8.5 million to fully eliminate the carrying amount of goodwill in the AEH subsidiary.

Interest expense increased $2.3 million or 11.3 percent compared to fiscal 2018 due to an increase in the Company's average revolver balance during fiscal 2019 and higher rates. In addition, an increase in patronage refund certificates outstanding throughout the year contributed to the increase.

Other income, net increased $9.7 million primarily due to a $4.9 million gain on the sale of the Company's former distribution center in Prince George, Virginia in fiscal 2019 and an increased tax benefit from losses incurred by certain of the Company's tax paying subsidiaries.

Liquidity and Capital Resources

The Company believes that existing cash balances, along with the existing lines of credit and long-term financing, will be sufficient to finance the Company's working capital requirements, debt service, patronage distributions, capital expenditures, share redemptions from Retailer cancellations and growth initiatives for at least the next 12 months.

The Company's borrowing requirements have historically arisen from, and are expected to continue to arise from, seasonal working capital needs, debt service, capital improvements and acquisitions, patronage distributions and other general corporate purposes. In the past, the Company has met its operational cash needs using cash flows from operating activities and funds from its revolving credit facilities. The Company currently estimates that its cash flows from operating activities and working capital, together with its lines of credit, will be sufficient to fund its short-term liquidity needs. Actual liquidity and capital funding requirements depend on numerous factors, including operating results, general economic conditions and the cost of capital.

The Company has a $700.0 million line of credit that is expandable to $1.0 billion through a $300.0 million accordion that is exercisable without the consent of existing lenders provided that the Company is not in default of the credit agreement and further provided that none of the existing lenders are required to provide any portion of the increased facility. At the Company's discretion, borrowings under the credit facility bear interest at a rate of either 0 to 75 basis points over the prime rate or 100 to 175 basis points over the London Interbank Offered Rate ("LIBOR") depending on the Company's leverage ratio as defined under the agreement. The credit facility was priced at LIBOR plus 125 basis points at January 2, 2021. The credit facility expires on February 1, 2024 and requires maintenance of certain financial covenants including a maximum allowable average leverage ratio and a minimum fixed charge coverage ratio. As of January 2, 2021, the Company was in compliance with its covenants and $7.9 million was outstanding under the credit facility.

The credit facility includes a $175.0 million sublimit for the issuance of standby and commercial letters of credit. As of January 2, 2021, a total of $19.8 million in letters of credit were outstanding. The credit facility requires the Company to pay fees based on the unused portion of the line of credit at a rate of 12.5 to 25 basis points per annum depending on the Company's leverage ratio.

The credit facility allows the Company to make revolving loans and other extensions of credit to AIH in an aggregate principal amount not to exceed $75.0 million at any time. As of January 2, 2021, there were no loans or other extensions of credit provided to AIH.

The Company was a party to an interest rate swap derivative agreement, which started on March 13, 2017 and expired on May 13, 2020. The swap agreement fixed the LIBOR rate on $150.0 million of the revolving credit facility borrowings at 2.18 percent, plus the then effective margin based on the then current pricing tier per the credit agreement. The swap arrangement was designated as a cash flow hedge and was evaluated to be highly effective throughout the term. As a result, the after-tax change in the fair value of the swap was recorded in Accumulated other comprehensive income as a gain or loss on derivative financial instruments.

The Company's Westlake subsidiary has a $100.0 million asset-based revolving credit facility ("Westlake Facility"). The Westlake Facility expires on October 24, 2022. Under this facility, Westlake has the right to issue letters of credit up to a maximum of $7.5 million. At Westlake's discretion, borrowings under this facility bear interest at a rate of either the prime rate plus an applicable spread of 25 basis points to 50 basis points or LIBOR plus an applicable spread of 125 basis points to 150 basis points, depending on the Company's average availability under the Westlake Facility as measured on a trailing 12-month basis. The Westlake Facility was priced at LIBOR plus 125 basis points at January 2, 2021.

The Westlake Facility is collateralized by substantially all of Westlake's personal property and intangible assets. Borrowings under the facility are subject to a borrowing base calculation consisting of certain advance rates applied to eligible collateral balances (primarily consisting of certain receivables and inventories). This agreement requires maintenance of certain financial covenants including a minimum fixed charge coverage ratio. As of January 2, 2021, ARH was in compliance with its covenants and had $20.1 million in loans outstanding under the Westlake Facility.

The Company's GLA subsidiary had a $20.0 million asset-based revolving credit facility ("GLA Facility") that had a maturity date of November 6, 2022. GLA terminated the facility effective August 31, 2020. Borrowings under the terminated GLA Facility had been subject to a borrowing base calculation consisting of certain advance rates applied to eligible receivables and inventory. The interest rate was based on either the lender's prime rate plus 100 basis points or LIBOR plus 200 basis points.

The Westlake Facility includes a lender-controlled cash concentration system that results in all of Westlake's daily available cash being applied to the outstanding borrowings under their facility. Pursuant to Financial Accounting Standards Board ("FASB") Accounting Standards Codification Section 470-10-45, "Classification of Revolving Credit Agreements Subject to Lock-Box Arrangements and Subjective Acceleration Clauses," the borrowings under the Westlake Facility have been classified as a Current maturity of long-term debt. The GLA Facility was classified under this guidance in prior presented periods.

Total debt, the majority of which is comprised of the $28.0 million borrowed on lines of credit, was $56.5 million as of January 2, 2021, compared to $276.9 million as of December 28, 2019.

Cash Flows

The Company had $28.9 million and $18.2 million of cash and cash equivalents at January 2, 2021 and December 28, 2019, respectively. Following is a summary of the Company's cash flows from operating, investing and financing activities for fiscal years 2020 and 2019, respectively (in millions):

	2020	2019
Cash provided by operating activities before changes in assets and liabilities	$ 385.4	$ 203.8
Net changes in assets and liabilities	75.8	10.2
Net cash provided by operating activities	461.2	214.0
Net cash used in investing activities	(128.8)	(91.9)
Net cash used in financing activities	(321.7)	(129.5)
Net change in cash and cash equivalents	$ 10.7	$ (7.4)

The Company's operating activities generated $461.2 million of cash in fiscal 2020 compared to $214.0 million in fiscal 2019. Excluding the impact of net changes in assets and liabilities, cash provided by operating activities increased from $203.8 million in fiscal 2019 to $385.4 million in fiscal 2020. This $181.6 million increase was primarily the result of a $176.5 million increase in net income in 2020.

The net change in assets and liabilities provided $75.8 million of cash in fiscal 2020 compared to $10.2 in fiscal 2019. This $65.6 million increase in net working capital was primarily driven by the intentional buildup of inventory to improve fill rates. Cash flows used by receivables and inventories were a combined $267.8 million in fiscal 2020 compared to a combined use of cash of only $39.7 million in fiscal 2019. Offsetting this use of cash were cash flows from accounts payable and accrued expenses of $337.3 million in fiscal 2020 compared to $56.2 million in fiscal 2019. During fiscal 2019, cash flows from accounts payable and accrued expenses were $56.2 million which was consistent with the $39.7 million of cash flows used by receivables and inventories during that period. However, during 2020, cash flows from accounts payable and accrued expenses were $337.3 million compared to $267.8 million of cash flows used by receivables and inventories during that period. This $337.3 million of cash flows from accounts payable and accrued expenses was primarily the result of a $317.6 million increase in accounts payable that occurred as a result of the 26.0 percent increase in wholesale revenues during 2020. Because the Company generally has 60-day payments terms with its vendors, the substantial increase in wholesale revenues in 2020 resulted in a greater percentage of the inventory sold during the fourth quarter of 2020 not having been paid for at the end of the year as compared to 2019.

Net cash used for investing activities was $128.8 million in fiscal 2020 compared to $91.9 million in fiscal 2019. Investing activities in fiscal 2020 consisted of $99.0 million in capital expenditures and $21.5 million paid for the acquisition of additional retails stores by ARH. Investing activities in fiscal 2019 consisted of $76.5 million in capital expenditures which were partially offset by $22.0 million in proceeds from sale of assets, primarily from the sale of the Prince George RSC. There was also $22.5 million paid for the acquisition of GLA, Handyman Matters Inc., and additional retail stores by ARH.

Net cash used in financing activities was $321.7 million in fiscal 2020 compared to $129.5 million in fiscal 2019. During fiscal 2020, the Company had $224.9 million of net payments under the revolving lines of credit, paid $66.2 million for the cash portion of the 2019 patronage distributions, paid $9.7 million on patronage refund certificates and had $10.7 million in payments on long-term debt. During 2019, the Company had $58.0 million of net payments under the revolving lines of credit, paid $51.3 million for the cash portion of the 2018 patronage distributions, paid $5.3 million on patronage refund certificates and had $10.9 million in payments on long-term debt.

Off-balance sheet arrangements

The Company has certain other guarantees, as further described in the Notes to the Consolidated Financial Statements – Note 12 – Commitments and Contingencies. The Company believes the likelihood of any such payment under these guarantees is remote.

Application of Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses in the consolidated financial statements. On an ongoing basis, the Company evaluates its estimates and judgments based on historical experience and various other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates, and these estimates would vary under different assumptions or conditions. Management believes these estimates and assumptions are reasonable.

The Company annually reviews its financial reporting and disclosure practices and accounting policies to ensure that they provide accurate and comprehensive information relative to the current economic and business environment. The Company's significant accounting policies are described in the Notes to the Consolidated Financial Statements. The following represents those critical accounting policies which involve a relatively higher degree of judgment, estimation and complexity and where materially different amounts could be reported under different conditions or using different assumptions.

Valuation of Inventories When necessary, the Company provides allowances to adjust the carrying value of inventories to the lower of cost or market, including costs to sell or dispose of surplus or damaged/obsolete inventory, and for estimated shrinkage. Estimates of the future demand for the Company's products are key factors used by management in assessing the net realizable value of the inventories. While management believes that the estimates used are appropriate, an unanticipated decline in revenues at retail outlets or a significant decline in demand for products in selected product categories could result in valuation adjustments.

Vendor Funds The Company receives funds from vendors in the normal course of business principally as a result of purchase volumes, revenues or promotions of vendors' products. Based on the provisions of the vendor agreements in place, management develops accrual rates by estimating the point at which the Company will have completed its performance under the agreement and the amount agreed upon will be earned. Due to the complexity and diversity of the individual vendor agreements, the Company performs analyses and reviews of historical trends throughout the year to ensure the amounts earned are appropriately recorded. As part of these analyses, the Company validates its accrual rates based on actual purchase trends and applies those rates to actual purchase volumes to determine the amount of funds that should be accrued by the Company and receivable from the vendor. Amounts accrued throughout the year could be impacted if actual purchase volumes differ from projected annual purchase volumes, especially in the case of programs that provide for increased funding when graduated purchase volumes are met. At year-end, the accrual reflects actual purchases made throughout the year.

Vendor funds are treated as a reduction of inventory cost, unless they represent a reimbursement of specific, incremental and identifiable costs incurred by the customer to sell the vendor's product, in which case the costs would be netted. The majority of the vendor funds that the Company receives do not meet the specific, incremental and identifiable criteria. Therefore, the Company treats a majority of these funds as a reduction in the cost of inventory as the amounts are accrued and recognized as a reduction of cost of revenues when the inventory is sold.

Allowance for Doubtful Accounts The allowance for doubtful accounts reflects management's estimate of the future amount of accounts and notes receivable that will not be collected. Management records allowances for doubtful accounts based on judgments made considering a number of factors, primarily historical collection statistics, current retailer credit information, the current economic environment, the aging of receivables, the evaluation of compliance with lending covenants and the offsetting amounts due to Retailers for stock, notes, interest and anticipated but unpaid patronage distributions. While the Company believes it has appropriately considered known or expected outcomes, its customers' ability to pay their obligations, including those to the Company, could be adversely affected by declining revenues at retail resulting from such factors as contraction in the economy or competitive conditions in the wholesale and retail industry including increased competition from omni-channel retailers, discount stores, chain stores and other mass merchandisers.

The Company's allowance for doubtful accounts at January 2, 2021 and December 28, 2019 was $6.1 million and $6.9 million, respectively. Actual credit losses could vary materially from the Company's estimates.

Insurance Reserves Insurance reserves for claims related to the Company's self-insured property, general liability, workers' compensation and auto liability insurance programs are dependent on assumptions used in calculating such amounts. These assumptions include projected ultimate losses and confidence levels of the reserve requirement and consider historical loss levels and other factors. While management believes that the assumptions used are appropriate, differences in actual claims experience or changes in assumptions may affect the Company's insurance reserves.

Goodwill Goodwill represents the excess of the cost of an acquired business over the fair value of net tangible assets acquired and identified intangible assets. Goodwill is not amortized but is tested for impairment at a reporting unit level on an annual basis or more frequently, if circumstances change or an event occurs that would more likely than not reduce the fair value of a reporting unit below its carrying amount.

Qualitative factors may be assessed to determine whether it is more likely than not that the fair value of the reporting unit is less than its carrying amount. If an election is made to not perform the qualitative assessment, or the qualitative assessment indicates that the carrying amount is more likely than not higher than the fair value, goodwill is tested for impairment. If the fair value of a reporting unit exceeds its carrying amount, goodwill of the reporting unit is considered not impaired. If the carrying amount of a reporting unit exceeds its fair value, an impairment loss shall be recognized in an amount equal to that excess.

Significant judgment is applied when goodwill is assessed for impairment. This judgment includes developing cash flow projections, selecting appropriate discount rates, identifying relevant market comparables, incorporating general economic and market conditions and selecting an appropriate control premium. The income approach is based on discounted cash flows, which are derived from internal forecasts and economic expectations for each respective reporting unit.

The Company tests reporting units for impairment annually as of the first day of the fourth quarter, or more frequently if events or circumstances indicate it is more likely than not that the fair value of a reporting unit is less than its carrying value. No goodwill impairment charge was recorded during fiscal years 2020 and 2018. The Company recorded an impairment charge of $8.5 million in fiscal 2019.

Impact of New Accounting Standards

New Accounting Pronouncements – Adopted

In February 2016, the FASB issued Accounting Standards Update ("ASU") No. 2016-02, "Leases (Topic 842)" along with amendments issued through 2019. The guidance requires that lessees recognize assets and liabilities for leases with lease terms greater than twelve months in the statement of financial position. The guidance also requires improved disclosures to help users of financial statements better understand the amount, timing and uncertainty of cash flows arising from leases.

On December 29, 2019 ("the effective date"), the Company adopted ASU 2016-02 and subsequent updates, collectively referred to as Topic 842, using the modified retrospective approach. In addition, the Company elected the package of practical expedients in transition, which permits the Company to not reassess prior conclusions pertaining to lease identification, lease classification and initial direct costs on leases that commenced prior to the adoption of the new standard. The Company also elected to treat the lease and non-lease components of leases as a single lease component and to exempt leases with an initial term of twelve months or less from balance sheet recognition.

As a result of adopting Topic 842, the Company recognized net operating right-of-use assets and operating lease liabilities of \$454.2 million as of December 29, 2019. The adoption of the standard did not have a material impact on the Company's results of operations or cash flows. See Note 6 for additional details of the Company's leases.

New Accounting Pronouncements – Issued

In June 2016, the FASB issued ASU No. 2016-13, "Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments" along with amendments issued in 2018. The guidance requires financial assets measured at amortized cost basis to be presented at the net amount expected to be collected. The amortized cost basis of financial assets should be reduced by expected credit losses to present the net carrying value in the financial statements at the amount expected to be collected. The measurement of expected credit losses is based on past events, historical experience, current conditions and forecasts that affect the collectability of the financial assets. Additionally, credit losses relating to available-for-sale debt securities should be recorded through an allowance for credit losses. ASU 2016-13 is effective for the Company for year-end financial statements and quarterly financial statements in fiscal 2023. The Company is evaluating the impact that ASU 2016-13 will have on the Company's consolidated financial statements.

Qualitative and Quantitative Disclosure About Market Risk

Inflation and Changes in Prices The Company's business is not generally governed by contracts that establish prices substantially in advance of the receipt of goods or services. As vendors increase or decrease their prices for merchandise supplied to the Company, the Company generally increases or decreases the price to its customers in an equal amount plus the normal handling charge on such amounts. In the past, these increases and decreases have provided adequate gross profit to offset the impact of inflation.

Foreign Currency Although the Company has international operating entities, its exposure to foreign currency rate fluctuations is not significant to its financial condition and results of operations.

Customer Credit Risk The Company is exposed to the risk of financial non-performance by customers. The Company's ability to collect on sales to its customers is dependent on the liquidity of its customer base. Volatility in credit markets may reduce the liquidity of the Company's customer base. To manage customer credit risk, the Company monitors historical collection statistics, current Retailer credit information, the current economic environment, the aging of receivables, the evaluation of compliance with lending covenants and the offsetting amounts due to Retailers for stock, notes, interest and anticipated but unpaid patronage distributions. From certain customers, the Company also obtains collateral as considered necessary to reduce risk of loss. The Company does not believe the loss of any single customer would have a material adverse effect on its results of operations.

Interest Rate Volatility The Company has exposure to fluctuations in interest rates on its floating rate debt. In order to reduce the risk of interest rate volatility, the Company has historically entered into interest rate swap agreements to fix the LIBOR rate on a portion of its revolving credit facility. The Company was party to an interest rate derivative agreement, which started on March 13, 2017 and expired on May 13, 2020. The Company has no plans to replace or supplement it. The Company believes that its exposure to interest rate fluctuations is not significant to its financial condition and results of operations.

Disclosure Regarding Forward-Looking Statements

This document includes certain forward-looking statements about the expectations of the Company. Although the Company believes these statements are based on reasonable assumptions, actual results may vary materially from stated expectations. Such forward-looking statements may be identified by the use of forward-looking words or phrases such as "anticipate," "believe," "expect," "intend," "may," "planned," "potential," "should," "will," "would," "project," "estimate," "ultimate," or similar phrases. Actual results may differ materially from those indicated in the Company's forward-looking statements and undue reliance should not be placed on such statements.

Factors that could cause materially different results include, but are not limited to, weather conditions; natural disasters; fair value accounting adjustments; inventory valuation; health care costs; insurance costs or recoveries; legal costs; borrowing needs; interest rates; credit conditions; economic and market conditions; accidents, leaks, equipment failures, service interruptions, and other operating risks; legislative actions; tax rulings or audit results; asset sales; significant unplanned capital needs; changes in accounting principles, interpretations, methods, judgments or estimates; performance of major customers, transporters, suppliers and contractors; labor relations; civil unrest; pandemics; and acts of terrorism.

Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date of this report. The Company undertakes no obligation to publicly release any revision to these forward-looking statements to reflect events or circumstances after the date of this report.

In March 2020, the World Health Organization declared the outbreak of a novel coronavirus a global pandemic. The pandemic is having a significant effect on overall economic conditions and the preventative and protective measures taken by governments are resulting in global business disruptions, including the Company's customers and vendors. Some of the Company's customers have seen a temporary reduction of operating hours for their stores, as well as temporary store closures where government mandated. While the impact of the pandemic is currently expected to be temporary, there is uncertainty around the severity and duration of the disruption. Although the Company continues to see significant increases in revenues, the possibility still exists that the pandemic may negatively affect its future operating results, financial position and cash flow. However, the financial impacts cannot be reasonably estimated at this time. The Company is monitoring its working capital, including its accounts receivable and inventory, closely for signs of deterioration due to late payments, bad debts and reduced demand.

The Company continues to monitor its operations and government recommendations and has made modifications to its normal operations because of the pandemic. These modifications vary by location depending on local conditions and government mandates. While the measures the Company has taken serve to reduce the possibility of transmission of the virus within its workplaces, they do not assure that the Company's employees will not contract the virus or bring it into the workplace. If the Company were forced to close any of its warehouses for an extended period of time, the Company's operations would be significantly disrupted resulting in a material adverse effect on the Company's business, financial condition, results of operations and liquidity.

FIVE YEAR SUMMARY OF EARNINGS AND DISTRIBUTIONS

	Years Ended				
	January 2, 2021 (53 Weeks)	December 28, 2019 (52 Weeks)	December 29, 2018 (52 Weeks)	December 30, 2017 (52 Weeks)	December 31, 2016 (52 Weeks)
Revenues	$ 7,762.7	$ 6,071.2	$ 5,717.0	$ 5,388.4	$ 5,125.5
Cost of revenues	6,549.2	5,178.6	4,921.9	4,634.1	4,412.7
Gross profit	1,213.5	892.6	795.1	754.3	712.8
Total operating and other expenses, net	895.9	752.2	667.4	607.7	551.9
Net income attributable to Ace Hardware Corporation	$ 317.6	$ 140.4	$ 127.7	$ 146.6	$ 160.9
Distribution of net income:					
Patronage distributions to third party Retailers	$ 275.4	$ 172.5	$ 135.4	$ 150.6	$ 152.8
Net income (loss) of non-patronage activities	42.2	(32.1)	(7.7)	(4.0)	8.1
Net income attributable to Ace Hardware Corporation	$ 317.6	$ 140.4	$ 127.7	$ 146.6	$ 160.9

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL STATEMENTS

The consolidated financial statements presented in this Annual Report have been prepared with integrity and objectivity and are the responsibility of the management of Ace Hardware Corporation. These consolidated financial statements have been prepared in conformity with U.S. generally accepted accounting principles and properly reflect certain estimates and judgments based upon the best available information.

The Company maintains a system of internal accounting controls, which is supported by an internal audit program and is designed to provide reasonable assurance, at an appropriate cost, that the Company's assets are safeguarded and transactions are properly recorded. This system is continually reviewed and modified in response to changing business conditions and operations and as a result of recommendations by the internal and external auditors. In addition, the Company has distributed to employees its policies for conducting business affairs in a lawful and ethical manner.

The consolidated financial statements of the Company have been audited by Ernst & Young LLP, independent accountants. Their accompanying report is based upon audits conducted in accordance with auditing standards generally accepted in the United States of America.

The Audit Committee of the Board of Directors meets periodically with the independent auditors and with the Company's internal auditors, both privately and with management present, to review accounting, auditing, internal control and financial reporting matters. The Audit Committee recommends to the full Board of Directors the selection of the independent auditors and regularly reviews the internal accounting controls, the activities of the outside auditors and internal auditors and the financial condition of the Company. Both the Company's independent auditors and the internal auditors have free access to the Audit Committee.

February 15, 2021

/s/ John Venhuizen
John Venhuizen
President and Chief Executive Officer

/s/ William M. Guzik
William M. Guzik
Executive Vice President,
Chief Financial Officer and Chief Risk Officer

/s/ Steven G. Locanto
Steven G. Locanto
Vice President, Controller

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