ACE HARDWARE CORPORATION

Quarterly report for the period ended July 4, 2015

ACE HARDWARE CORPORATION
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Independent Auditor's Review Report

The Board of Directors
Ace Hardware Corporation

We have reviewed the consolidated financial information of Ace Hardware Corporation and subsidiaries, which comprise the consolidated balance sheets as of July 4, 2015 and June 28, 2014 and the related consolidated statements of income and comprehensive income for the three and six-month periods ended July 4, 2015 and June 28, 2014, and the consolidated statements of equity and cash flows for the six-month periods ended July 4, 2015 and June 28, 2014.

Management's Responsibility for the Financial Statements

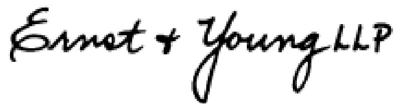
Management is responsible for the preparation and fair presentation of the interim financial information in conformity with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control sufficient to provide a reasonable basis for the preparation and fair presentation of interim financial information in conformity with U.S. generally accepted accounting principles.

Auditor's Responsibility

Our responsibility is to conduct our review in accordance with auditing standards generally accepted in the United States applicable to reviews of interim financial information. A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with auditing standards generally accepted in the United States, the objective of which is the expression of an opinion regarding the financial information. Accordingly, we do not express such an opinion.

Conclusion

Based on our review, we are not aware of any material modifications that should be made to the consolidated financial information referred to above for it to be in conformity with U.S. generally accepted accounting principles.



Chicago, Illinois
August 18, 2015

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

	July 4, 2015	January 3, 2015	June 28, 2014
Assets	**(Unaudited)**	**(Audited)**	**(Unaudited)**
Cash and cash equivalents	$ 35.3	$ 29.8	$ 15.7
Marketable securities	42.8	42.2	55.4
Receivables, net of allowance for doubtful accounts of $7.9, $6.5 and $10.0, respectively	469.5	381.8	487.3
Inventories	807.1	692.9	636.7
Prepaid expenses and other current assets	53.4	54.7	61.2
Total current assets	1,408.1	1,201.4	1,256.3
Property and equipment, net	316.8	323.0	324.1
Notes receivable, net of allowance for doubtful accounts of $9.4, $10.9 and $10.0, respectively	15.8	12.2	21.0
Goodwill and other intangible assets	35.7	35.0	31.9
Other assets	87.2	85.6	76.0
Total assets	$ 1,863.6	$ 1,657.2	$ 1,709.3
Liabilities and Equity			
Current maturities of long-term debt	$ 19.4	$ 41.5	$ 39.8
Accounts payable	799.0	601.6	666.5
Patronage distributions payable in cash	31.6	53.7	34.3
Patronage refund certificates payable	6.6	6.6	-
Accrued expenses	147.7	162.5	145.8
Total current liabilities	1,004.3	865.9	886.4
Long-term debt	282.4	242.2	290.1
Patronage refund certificates payable	42.2	32.3	38.2
Other long-term liabilities	56.8	67.0	65.8
Total liabilities	1,385.7	1,207.4	1,280.5
Member Retailers' Equity:			
Class A voting common stock, $1,000 par value, 10,000 shares authorized, 2,739; 2,751 and 2,756 issued and outstanding, respectively	2.7	2.8	2.8
Class C nonvoting common stock, $100 par value, 6,000,000 shares authorized, 3,847,785; 3,425,232 and 3,495,681 issued and outstanding, respectively	384.8	342.5	349.6
Class C nonvoting common stock, $100 par value, issuable to retailers for patronage distributions, 300,284; 565,068 and 326,665 shares issuable, respectively	30.0	56.5	32.7
Contributed capital	20.7	20.6	20.0
Retained earnings	26.0	15.5	13.1
Accumulated other comprehensive income	1.2	1.7	0.9
Equity attributable to Ace member retailers	465.4	439.6	419.1
Equity attributable to noncontrolling interests	12.5	10.2	9.7
Total equity	477.9	449.8	428.8
Total liabilities and equity	$ 1,863.6	$ 1,657.2	$ 1,709.3

See accompanying notes to the consolidated financial statements.

ACE HARDWARE CORPORATION
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited, in millions)

	Three Months Ended		Six Months Ended	
	July 4, 2015 (13 Weeks)	**June 28, 2014 (13 Weeks)**	**July 4, 2015 (26 Weeks)**	**June 28, 2014 (26 Weeks)**
Revenues:				
Wholesale revenues	$ 1,332.1	$ 1,251.6	$ 2,471.9	$ 2,286.6
Retail revenues	85.4	79.7	131.7	123.4
Total revenues	1,417.5	1,331.3	2,603.6	2,410.0
Cost of revenues:				
Wholesale cost of revenues	1,168.6	1,076.2	2,170.3	1,992.1
Retail cost of revenues	48.3	44.4	72.3	67.4
Total cost of revenues	1,216.9	1,120.6	2,242.6	2,059.5
Gross profit:				
Wholesale gross profit	163.5	175.4	301.6	294.5
Retail gross profit	37.1	35.3	59.4	56.0
Total gross profit	200.6	210.7	361.0	350.5
Distribution operations expenses	33.5	30.3	64.5	57.2
Selling, general and administrative expenses	33.0	38.6	76.3	75.5
Retailer success and development expenses	39.0	46.0	69.7	72.9
Retail operating expenses	25.7	23.8	47.7	46.4
Warehouse facility closure costs	0.2	-	1.7	-
Total operating expenses	131.4	138.7	259.9	252.0
Operating income	69.2	72.0	101.1	98.5
Interest expense	(5.8)	(3.5)	(9.3)	(6.6)
Interest income	0.9	0.9	1.7	1.7
Other income, net	1.6	1.4	3.8	3.2
Income tax expense	(6.0)	(3.9)	(7.5)	(5.5)
Net income	59.9	66.9	89.8	91.3
Less: net income attributable to noncontrolling interests	2.4	0.4	2.4	0.4
Net income attributable to Ace Hardware Corporation	$ 57.5	$ 66.5	$ 87.4	$ 90.9
Patronage distributions accrued	$ 43.1	$ 55.9	$ 76.8	$ 84.2

See accompanying notes to the consolidated financial statements.

ACE HARDWARE CORPORATION
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited, in millions)

	Three Months Ended		Six Months Ended	
	July 4, 2015 (13 Weeks)	**June 28, 2014 (13 Weeks)**	**July 4, 2015 (26 Weeks)**	**June 28, 2014 (26 Weeks)**
Net income	$ 59.9	$ 66.9	$ 89.8	$ 91.3
Other comprehensive income (loss), net of tax:				
Unrealized (loss) gain on investments	(0.4)	0.4	(0.2)	0.6
Unrealized loss on derivative financial instruments	-	(0.2)	(0.3)	-
Total other comprehensive (loss) income, net	(0.4)	0.2	(0.5)	0.6
Comprehensive income	59.5	67.1	89.3	91.9
Less: Comprehensive income attributable to noncontrolling interest	2.4	0.4	2.4	0.4
Comprehensive income attributable to Ace Hardware Corporation	$ 57.1	$ 66.7	$ 86.9	$ 91.5

See accompanying notes to the consolidated financial statements.

ACE HARDWARE CORPORATION
CONSOLIDATED STATEMENTS OF EQUITY
(Unaudited, 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 Other Comprehensive Income	Noncontrolling Interests	Total Equity
Balances at December 28, 2013	$ 2.8	$ 315.7	$ 40.9	$ -	$ 20.0	$ 6.3	$ 0.3	$ 8.3	$ 394.3
Net income	-	-	-	-	-	90.9	-	0.4	91.3
Other comprehensive income	-	-	-	-	-	-	0.6	-	0.6
Net payments on subscriptions	-	-	-	0.6	-	-	-	-	0.6
Stock issued	0.1	41.2	(40.9)	(0.6)	-	-	-	-	(0.2)
Sale of noncontrolling interests	-	-	-	-	(0.1)	-	-	1.0	0.9
Stock repurchased	(0.1)	(7.3)	-	-	-	-	-	-	(7.4)
Patronage distributions issuable	-	-	32.7	-	-	-	-	-	32.7
Patronage distributions payable	-	-	-	-	-	(84.1)	-	-	(84.1)
Other	-	-	-	-	0.1	-	-	-	0.1
Balances at June 28, 2014	$ 2.8	$ 349.6	$ 32.7	$ -	$ 20.0	$ 13.1	$ 0.9	$ 9.7	$ 428.8
Balances at January 3, 2015	$ 2.8	$ 342.5	$ 56.5	$ -	$ 20.6	$ 15.5	$ 1.7	$ 10.2	$ 449.8
Net income	-	-	-	-	-	87.4	-	2.4	89.8
Other comprehensive loss	-	-	-	-	-	-	(0.5)	-	(0.5)
Net payments on subscriptions	-	-	-	0.6	-	-	-	-	0.6
Stock issued	-	56.4	(56.5)	(0.6)	-	-	-	-	(0.7)
Redemption of noncontrolling interests	-	-	-	-	0.1	-	-	(0.1)	-
Stock repurchased	(0.1)	(14.1)	-	-	-	-	-	-	(14.2)
Patronage distributions issuable	-	-	30.0	-	-	-	-	-	30.0
Patronage distributions payable	-	-	-	-	-	(76.8)	-	-	(76.8)
Other	-	-	-	-	-	(0.1)	-	-	(0.1)
Balances at July 4, 2015	$ 2.7	$ 384.8	$ 30.0	$ -	$ 20.7	$ 26.0	$ 1.2	$ 12.5	$ 477.9

See accompanying notes to the consolidated financial statements.

ACE HARDWARE CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited, in millions)

	Six Months Ended	
	July 4, 2015 (26 Weeks)	**June 28, 2014 (26 Weeks)**
Operating Activities		
Net income	$ 89.8	$ 91.3
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	25.4	24.7
Amortization of deferred gain on sale leaseback	-	(0.6)
Amortization of deferred financing costs	0.5	0.5
Loss on early extinguishment of debt	2.2	-
(Gain) loss on disposal of assets, net	(0.1)	0.4
Provision for doubtful accounts	2.5	2.4
Other, net	-	0.2
Changes in operating assets and liabilities, exclusive of effect of acquisitions:		
Receivables	(112.9)	(158.5)
Inventories	(110.5)	(103.7)
Other current assets	(1.7)	(15.5)
Other long-term assets	(0.8)	(16.1)
Accounts payable and accrued expenses	182.3	135.3
Other long-term liabilities	(10.6)	(0.3)
Deferred taxes	0.3	(0.2)
Net cash provided by (used in) operating activities	66.4	(40.1)
Investing Activities		
Purchases of marketable securities	(4.4)	(8.4)
Proceeds from sale of marketable securities	3.5	7.9
Purchases of property and equipment	(16.8)	(19.6)
Cash paid for acquired businesses, net of cash acquired	(5.6)	(32.9)
Decrease in notes receivable, net	0.8	1.5
Other	0.1	0.1
Net cash used in investing activities	(22.4)	(51.4)
Financing Activities		
Net borrowings under revolving lines of credit	186.7	132.7
Principal payments on long-term debt	(173.2)	(8.2)
Payments of deferred financing costs	(1.1)	-
Payments of cash portion of patronage distribution	(48.9)	(36.6)
Payments of patronage refund certificates	(0.1)	(0.1)
Proceeds from sale of noncontrolling interests	-	0.9
Repurchase of stock	(2.5)	-
Other	0.6	0.6
Net cash (used in) provided by financing activities	(38.5)	89.3
Increase (decrease) in cash and cash equivalents	5.5	(2.2)
Cash and cash equivalents at beginning of period	29.8	17.9
Cash and cash equivalents at end of period	$ 35.3	$ 15.7
Supplemental disclosure of cash flow information:		
Interest paid	$ 6.1	$ 5.5
Income taxes paid	$ 0.7	$ 3.2

See accompanying notes to the consolidated financial statements.

ACE HARDWARE CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited, in millions)

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 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 member retailers based on their volume of merchandise purchases.

On December 31, 2014, Ace Wholesale Holdings LLC ("AWH") acquired all of the outstanding member units of Jensen-Byrd Co., LLC ("Jensen"), a wholesale hardlines distributor. See Note 2 for additional information.

On February 19, 2014, AWH acquired all of the outstanding shares of capital stock of Emery-Waterhouse ("Emery"), a distributor of hardlines products for independent lumber, paint, industrial and hardware outlets. Immediately following the acquisition, AWH sold a 5 percent noncontrolling interest in Emery to Emery's current Chief Executive Officer. See Note 2 for additional information.

Ace Retail Holdings LLC ("ARH") is the owner of the 90 store Westlake Ace Hardware retail chain. As a result, the Company is also a retailer of hardware, paint and other related products.

The Company's international operations are a stand-alone legal entity with its own management team and board of directors. The entity Ace Hardware International Holdings, Ltd. ("AIH") is a majority-owned and controlled subsidiary of the Company with a noncontrolling interest owned by its international retailers. International retailers do not own shares of stock in the Company nor receive patronage dividends.

Basis of Presentation

The accompanying consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP"). Certain information and note disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted. The unaudited consolidated financial statements and notes should be read in conjunction with the financial statements and notes thereto included in the Company's 2014 Annual Report. The unaudited consolidated financial statements for the three and six months ended July 4, 2015 and June 28, 2014 both cover a 13-week period and a 26-week period, respectively.

Subsequent events have been evaluated through August 18, 2015, the date these statements were available to be issued.

The financial information included herein reflects all adjustments (consisting only of normal recurring adjustments), which, in the opinion of management, are necessary for a fair presentation of the results for the interim periods presented. The results of operations for the three and six months ended July 4, 2015 are not necessarily indicative of the results to be expected for the full fiscal year 2015.

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.

New Accounting Pronouncements - Issued

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09, "Revenue from Contracts with Customers (Topic 606)." The purpose of ASU 2014-09 is to develop a common revenue recognition standard for GAAP and International Financial Reporting Standards. The guidance in this update affects any entity that either enters into contracts with customers to transfer goods or services or enters into contracts for the transfer of nonfinancial assets unless those contracts are within the scope of other standards. The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. ASU 2014-09 allows either full retrospective adoption, meaning the standard is applied to all periods presented, or modified retrospective adoption, meaning the standard is applied only to the most current period presented in the financial statements. In July 2015, the FASB deferred the effective date of ASU 2014-09 which is now effective for the Company for annual reporting periods beginning after December 15, 2018, and interim periods within annual periods beginning after December 15, 2019. The Company is still evaluating the impact that ASU 2014-09 will have on the Company's consolidated financial statements.

In April 2015, the FASB issued ASU No. 2015-03, "Interest – Imputation of Interest (Subtopic 835-30), Simplifying the Presentation of Debt Issuance Costs." ASU 2015-03 requires debt issuance costs to be presented as a deduction from the corresponding debt liability to make the presentation of debt issuance costs consistent with the presentation of debt discounts and premiums. ASU 2015-03 is part of FASB's simplification initiative to reduce the cost and complexity of financial reporting. The recognition and measurement guidance for debt issuance costs are not affected by the amendments in this ASU. ASU 2015-03 is effective for the Company for fiscal years beginning after December 15, 2015 and interim periods within fiscal years beginning after December 15, 2016 with early adoption permitted. The Company is still evaluating the impact that ASU 2015-03 will have on its consolidated financial statements.

In April 2015, the FASB issued ASU No. 2015-05, "Intangibles – Goodwill and Other – Internal-Use Software (Subtopic 350-40): Customer's Accounting for Fees Paid in a Cloud Computing Arrangement." Under ASU 2015-05, if a cloud computing arrangement includes a software license, then the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. If a cloud computing arrangement does not include a software license, the customer should account for the arrangement as a service contract. ASU 2015-05 is effective for the Company for fiscal years beginning after December 15, 2015 and interim periods within fiscal years beginning after December 15, 2016, with early adoption permitted. The provisions of ASU 2015-05 are not expected to have a material effect on the Company's balance sheet or operating results.

(2) Acquisitions

On December 31, 2014, AWH acquired all of the outstanding member units of Jensen, a wholesale hardlines distributor, for $33.4 million. The acquisition has been accounted for as a business combination. The Company recorded the allocation of the purchase price to acquired tangible assets and liabilities assumed based on their fair value at the acquisition date. As a result, the Company recorded $3.1 million of goodwill and $0.4 million for the fair value of a customer relationship intangible asset. Goodwill has an indefinite life and, therefore, is not amortized, while the customer relationship intangible will be amortized over 10 years. The goodwill and customer relationship intangible asset are expected to be deductible for tax purposes.

The following table summarizes the consideration paid for Jensen and the preliminary purchase price allocation at the acquisition date:

Fair value of assets acquired and liabilities assumed:	
Cash	$ 2.9
Receivables	16.9
Inventories	26.6
Other current assets	0.2
Property and equipment	2.0
Goodwill	3.1
Customer relationship intangible	0.4
Current liabilities	(18.7)
	$ 33.4

On February 19, 2014, AWH acquired all of the outstanding shares of capital stock of Emery, a distributor of hardlines products for independent lumber, paint, industrial and hardware outlets, for $33.3 million. Immediately following the acquisition, AWH sold a 5 percent noncontrolling interest in Emery to Emery's current Chief Executive Officer for approximately $1.7 million. The acquisition has been accounted for as a business combination. The Company recorded the allocation of the purchase price to acquired tangible assets and liabilities assumed based on their fair value at the acquisition date. As a result, the Company recorded $5.3 million of goodwill and $2.7 million for the fair value of a customer relationship intangible asset. Goodwill has an indefinite life and, therefore, is not amortized, while the customer relationship intangible will be amortized over 10 years. The goodwill and customer relationship intangible asset are expected to be deductible for tax purposes.

The following table summarizes the consideration paid for Emery and the purchase price allocation at the acquisition date:

Fair value of assets acquired and liabilities assumed:	
Cash	$ 0.8
Receivables	11.6
Inventories	27.7
Other current assets	0.7
Property and equipment	3.8
Goodwill	5.3
Customer relationship intangible	2.7
Current liabilities	(19.3)
	$ 33.3

3) Inventories

Inventories consist of wholesale merchandise inventories held for sale to retailers and retail merchandise inventory held for resale at Company-operated retail locations. Substantially all of the Company's wholesale inventories are valued on the last-in, first-out ("LIFO") method. The excess of replacement cost over the LIFO value of inventory was $94.0 million, $94.0 million and $96.3 million at July 4, 2015, January 3, 2015 and June 28, 2014, respectively. An actual valuation of inventory under the LIFO method can be made only at the end of each year based on the inventory levels and costs at that time. Interim LIFO calculations are based on management's estimates of expected year-end inventory levels and costs, and are subject to the final year-end LIFO inventory valuation. Inventories at retail locations operated by the Company 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.

Inventories consisted of:

	July 4, 2015	January 3, 2015	June 28, 2014
Wholesale merchandise inventory (LIFO)	$ 722.8	$ 623.6	$ 568.6
Retail merchandise inventory at Company-operated stores (FIFO)	84.3	69.3	68.1
Inventories	$ 807.1	$ 692.9	$ 636.7

(4) Debt

On May 29, 2015, the Company amended its secured credit facility which was originally dated April 13, 2012 and previously amended on July 29, 2013. The May 2015 amendment extended the maturity date to May 29, 2020 and lowered the interest rate credit spread by 25 basis points. The amended credit facility consists of a $600.0 million revolving credit facility that is expandable to $750.0 million through a $150.0 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. Borrowings under the amended credit facility bear interest at a rate of either 25 to 100 basis points over the prime rate or 125 to 200 basis points over the London Interbank Offered Rate ("LIBOR") depending on the Company's leverage ratio as defined under the agreement. The amended credit facility was priced at LIBOR plus 150 basis points at July 4, 2015. The amended credit facility requires maintenance of certain financial covenants including a maximum allowable average leverage ratio and a minimum fixed charge coverage ratio. As of July 4, 2015, the Company was in compliance with its covenants and $273.4 million was outstanding under the amended credit facility.

The amended credit facility includes a $175.0 million sublimit for the issuance of standby and commercial letters of credit. As of July 4, 2015, a total of $28.0 million in letters of credit were outstanding. The revolving credit facility requires the Company to pay fees based on the unused portion of the line of credit at a rate of 15 to 30 basis points per annum depending on the Company's leverage ratio.

The amended 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 July 4, 2015, there were no loans or other extensions of credit provided to AIH.

In order to reduce the risk of interest rate volatility, the Company entered into an interest rate swap derivative agreement in June 2012, which expires on March 13, 2017. This swap agreement fixes the LIBOR rate on a portion of the revolving credit facility at 1.13%, resulting in an effective rate of 2.63% after adding the 1.50% margin based on the current pricing tier per the credit agreement. The notional amount of the derivative agreement decreases by $5.0 million each quarter through expiration of the interest rate swap derivative agreement in March 2017. As of July 4, 2015, the notional amount of the interest rate swap agreement remaining was $160.0 million. The Company entered into a forward interest rate swap derivative agreement in June 2015 to reduce the risk of interest rate volatility for the remaining term of the amended credit facility. The forward interest rate swap starts on March 13, 2017 and expires on May 13, 2020. The forward swap agreement fixes the LIBOR rate on $150.0 million of the revolving credit facility at 2.18%, resulting in an effective rate of 3.68% after adding the 1.50% margin based on the current pricing tier per the credit agreement. The swap arrangements have been designated as cash flow hedges and have been evaluated to be highly effective. As a result, the after-tax change in the fair value of the swaps are recorded in Accumulated other comprehensive income ("AOCI") as a gain or loss on derivative financial instruments.

The Company's ARH subsidiary has a $60.0 million asset-based revolving credit facility ("ARH Facility"). The ARH Facility matures on June 28, 2019 and is expandable to $85.0 million under certain conditions. In addition, the Company has the right to issue letters of credit up to a maximum of $7.5 million. At the Company's discretion, borrowings under this facility bear interest at a rate of either the prime rate plus an applicable spread of 35 basis points to 75 basis points or LIBOR plus an applicable spread of 135 basis points to 175 basis points, depending on the Company's availability under the ARH Facility as measured on a quarterly basis.

The ARH Facility is collateralized by substantially all of ARH'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 July 4, 2015, ARH was in compliance with its covenants. At the end of the second quarter of 2015, ARH had $13.3 million in loans outstanding under its Facility.

The ARH Facility requirements include a lender-controlled cash concentration system that results in all of ARH's daily available cash being applied to the outstanding borrowings under this facility. Pursuant to 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 ARH Facility have been classified as a Current maturity of long-term debt as of July 4, 2015.

Total debt outstanding is comprised of the following:

	July 4, 2015	January 3, 2015	June 28, 2014
Term Loan Facility	$ -	$ 170.0	$ 182.5
Revolving Credit Facility	273.4	84.5	121.6
ARH Facility	13.3	15.5	11.1
Installment notes with maturities through 2018 at a fixed rate of 6.00%	15.1	13.7	14.7
Total debt	301.8	283.7	329.9
Less: maturities within one year	(19.4)	(41.5)	(39.8)
Long-term debt	$ 282.4	$ 242.2	$ 290.1

(5) Fair Value

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 July 4, 2015, January 3, 2015 and June 28, 2014. 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.

Items measured at fair value on a recurring basis	Carrying Value Measured at Fair Value July 4, 2015	Level 1	Level 2	Level 3
Assets:				
Cash equivalents:				
Money market funds	$ 9.0	$ 9.0	$ -	$ -
Marketable securities:				
Corporate fixed income securities	12.6	-	12.6	-
Fixed income and equity mutual fund securities	11.9	11.9	-	-
Mortgage-backed securities	6.0	-	6.0	-
U.S. government notes	11.4	11.4	-	-
Other	0.9	-	0.9	-
Total marketable securities	$ 42.8	$ 23.3	$ 19.5	$ -
Other long-term liabilities:				
Interest rate swap derivatives	$ 1.6	$ -	$ 1.6	$ -

Items measured at fair value on a recurring basis	Carrying Value Measured at Fair Value January 3, 2015	Level 1	Level 2	Level 3
Assets:				
Cash equivalents:				
Money market funds	$ 10.8	$ 10.8	$ -	$ -
Marketable securities:				
Corporate fixed income securities	13.3	-	13.3	-
Fixed income and equity mutual fund securities	11.7	11.7	-	-
Mortgage-backed securities	6.6	-	6.6	-
U.S. government notes	10.2	10.2	-	-
Other	0.4	-	0.4	-
Total marketable securities	$ 42.2	$ 21.9	$ 20.3	$ -
Other long-term liabilities:				
Interest rate swap derivatives	$ 1.1	$ -	$ 1.1	$ -

Items measured at fair value on a recurring basis	Carrying Value Measured at Fair Value June 28, 2014	Level 1	Level 2	Level 3
Assets:				
Cash equivalents:				
Money market funds	$ 2.4	$ 2.4	$ -	$ -
Marketable securities:				
Corporate fixed income securities	13.2	-	13.2	-
Fixed income and equity mutual fund securities	25.3	25.3	-	-
Mortgage-backed securities	7.1	-	7.1	-
U.S. government notes	9.5	9.5	-	-
Other	0.3	-	0.3	-
Total marketable securities	$ 55.4	$ 34.8	$ 20.6	$ -
Other long-term liabilities:				
Interest rate swap derivative	$ 1.9	$ -	$ 1.9	$ -

Money market funds, Fixed income and equity mutual fund securities and U.S. government notes - The Company's valuation techniques used to measure the fair values of money market funds, fixed income and equity mutual fund securities 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 and Mortgage-backed securities - The Company's valuation techniques used to measure the fair values of corporate fixed income securities and mortgage-backed 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.

There were no material differences between the fair value and cost basis of the Company's marketable securities at July 4, 2015 and June 28, 2014, respectively. Gross proceeds from the sale of marketable securities and the related realized gains and losses for the three and six months ended July 4, 2015 and June 28, 2014 were as follows:

	Three Months Ended		**Six Months Ended**	
	July 4, 2015	June 28, 2014	July 4, 2015	June 28, 2014
Gross proceeds	$ 1.9	$ 4.5	$ 3.5	$ 7.9
Gross realized gains	-	0.3	0.1	0.4
Gross realized losses	-	(0.1)	-	(0.1)

Gross realized gains and losses were determined using the specific identification method. As of the six months ended July 4, 2015, the Company reclassified $0.1 million of unrealized gains and an immaterial amount of unrealized losses on marketable securities that were recorded in AOCI as of January 3, 2015 into realized income. These amounts were recorded to Other income, net in the Consolidated Statements of Income.

The following table summarizes the contractual maturity distributions of the Company's debt securities at July 4, 2015. Actual maturities may differ from the contractual or expected maturities since borrowers may have the right to prepay obligations with or without prepayment penalties.

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	$ 0.9	$ 4.8	$ 4.9	$ 2.0	$ 12.6
Mortgage-backed securities	-	-	0.2	5.8	6.0
U.S. government notes	-	6.2	3.2	2.0	11.4
Other	-	0.3	0.1	0.5	0.9
Total	$ 0.9	$ 11.3	$ 8.4	$ 10.3	$ 30.9

The Company uses variable-rate LIBOR debt to finance its operations. These debt obligations expose the Company to interest rate volatility risk. The Company attempts 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 Sheets 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.

On June 5, 2012, the Company entered into an interest rate swap agreement, which expires on March 13, 2017, with an amortizing notional amount of $200.0 million. This instrument is being used to fix the LIBOR rate on a portion of the revolving credit facility at 1.13%, resulting in an effective rate of 2.63% after adding the 1.50% margin based on the current pricing tier per the credit agreement. As of July 4, 2015, the notional amount of the interest rate swap agreement remaining was $160.0 million. The Company entered into a forward interest rate swap derivative agreement in June 2015, which starts on March 13, 2017 and expires on May 13, 2020. The forward swap agreement fixes the LIBOR rate on $150.0 million of the revolving credit facility at 2.18%, resulting in an effective rate of 3.68% after adding the 1.50% margin based on the current pricing tier per the credit agreement.

The fair value of the Company's interest rate swaps are estimated using Level 2 inputs, which are based on model-derived valuations in which all significant inputs and significant value drivers are observable in active markets. The Company also considers counterparty credit-risk and bilateral or "own" credit risk adjustments in estimating fair value, in accordance with the requirements of GAAP. As of July 4, 2015, the fair values of the interest rate swap and forward interest rate swap were liability balances of $1.3 million and $0.3 million, respectively. The Company classifies derivative liabilities as Other long-term liabilities in the Consolidated Balance Sheets.

Because the interest rate swaps have been designated as cash flow hedges and have been evaluated to be highly effective, the change in the fair value is recorded in AOCI as a gain or loss on derivative financial instruments. The amount in AOCI is reclassified to earnings if the derivative instruments are sold, extinguished or terminated, or at the time they become expected to be sold, extinguished or terminated. As of July 4, 2015, the net of tax amount recorded in AOCI for the fair value adjustment of the interest rate swaps was an unrealized loss of $1.0 million. This unrealized loss is not expected to be reclassified into interest expense within the next 12 months. The impact of any ineffectiveness is recognized in earnings. However, there was no hedge ineffectiveness related to the interest rate swaps for the three and six months ended July 4, 2015.

The Company's debt instruments are recorded at cost in the Consolidated Balance Sheets. The fair value of long-term debt was approximately $305.8 million at July 4, 2015, compared to the carrying value, including accrued interest, of $302.3 million.

(6) Commitments and Contingencies

The Company has certain contingencies resulting from litigation and claims incident to the ordinary course of business. During the period ended July 4, 2015, the Company received a settlement related to the resolution of a gain contingency which was recorded as a $10.0 million reduction of Selling, general and administrative expenses.

(7) Income Taxes

Income tax differs from the amount computed by applying the statutory U.S. Federal income tax rate of 35% to income before income taxes because of the effect of the following items:

	Three Months Ended		Six Months Ended	
	July 4, 2015	June 28, 2014	July 4, 2015	June 28, 2014
Expected tax at U.S. Federal income tax rate	$ (23.1)	$ (24.8)	$ (34.1)	$ (33.9)
Patronage distribution deductions	15.1	19.6	26.9	29.5
Annual effective tax rate timing adjustment	1.4	1.7	(0.4)	(0.4)
Other, net	0.6	(0.4)	0.1	(0.7)
Income tax expense	$ (6.0)	$ (3.9)	$ (7.5)	$ (5.5)

(8) Supplemental Disclosures of Cash Flow Information

During the six months ended July 4, 2015 and June 28, 2014, current year accrued patronage distributions of $5.2 million and $7.3 million, respectively, were offset against receivables owed to the Company by its member retailers with no net impact in the Consolidated Statements of Cash Flows.

During the six months ended July 4, 2015 and June 28, 2014, repurchases of stock from retailers of $11.7 million and $7.4 million, respectively, were offset against current receivables of $4.4 million and $2.5 million, respectively, and notes receivable of $2.8 million and $1.5 million, respectively. An additional $4.5 million and $3.4 million, respectively, were primarily issued as notes payable with no net impact in the Consolidated Statements of Cash Flows.

During fiscal 2012, the Company entered into an interest rate swap derivative dated June 5, 2012. In June 2015, the Company entered into a forward interest rate swap derivative agreement, which starts on March 13, 2017 and expires on May 13, 2020. The fair value adjustments for the interest rate swap derivatives were recorded as Other long-term liabilities of $1.6 million and $1.9 million as of July 4, 2015 and June 28, 2014. The Company offset these adjustments in fair value, net of tax, against AOCI with no net impact in the Consolidated Statements of Cash Flows.

During the six months ended July 4, 2015, the Company received $0.5 million of property and equipment prior to quarter 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 the six months ended July 4, 2015.

(9) Warehouse Facility Closure Costs

During the three and six months ended July 4, 2015, the Company recorded additional charges of $0.2 million and $1.7 million, respectively, related to the settlement of a withdrawal liability for the multi-employer pension fund that covers the former union employees at the closed Retail Support Center in Toledo, Ohio. The Company paid $6.4 million to settle its obligation with the multi-employer pension fund during the second quarter of 2015.

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

The following discussion and analysis summarizes the significant factors affecting the Company's consolidated operating results and financial condition during the three- and six-month periods ended July 4, 2015 and June 28, 2014. This discussion and analysis should be read in conjunction with the Company's 2014 Annual Report, as well as the consolidated financial statements (unaudited) and notes thereto contained in this report that have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP"). Results of the interim periods presented are not necessarily indicative of the results to be expected for the full fiscal year due to seasonal and other factors.

Results of Operations

Comparison of the Three Months Ended July 4, 2015 to the Three Months Ended June 28, 2014

The following data summarizes the Company's performance in 2015 as compared to 2014 (in millions):

	2015		2014		Increase/(decrease)	
	$	% of Revenues*	$	% of Revenues*	$	%
Revenues:						
Wholesale revenues	1,332.1	94.0%	1,251.6	94.0%	80.5	6.4%
Retail revenues	85.4	6.0%	79.7	6.0%	5.7	7.2%
Total revenues	1,417.5	100.0%	1,331.3	100.0%	86.2	6.5%
Gross profit:						
Wholesale gross profit	163.5	12.3%	175.4	14.0%	(11.9)	(6.8%)
Retail gross profit	37.1	43.4%	35.3	44.3%	1.8	5.1%
Total gross profit	200.6	14.2%	210.7	15.8%	(10.1)	(4.8%)
Operating expenses:						
Distribution operations expenses	33.5	2.5%	30.3	2.4%	3.2	10.6%
Selling, general and administrative expenses	33.0	2.5%	38.6	3.1%	(5.6)	(14.5%)
Retailer success and development expenses	39.0	2.9%	46.0	3.7%	(7.0)	(15.2%)
Retail operating expenses	25.7	30.1%	23.8	29.9%	1.9	8.0%
Warehouse facility closure costs	0.2	0.0%	-	-	0.2	100.0%
Total operating expenses	131.4	9.3%	138.7	10.4%	(7.3)	(5.3%)
Operating income	69.2	4.9%	72.0	5.4%	(2.8)	(3.9%)
Interest expense	(5.8)	(0.4%)	(3.5)	(0.3%)	(2.3)	(65.7%)
Other	(5.9)	(0.4%)	(2.0)	(0.1%)	(3.9)	(195.0%)
Net income	57.5	4.1%	66.5	5.0%	(9.0)	(13.5%)

*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.

Consolidated revenues for the three months ended July 4, 2015 totaled $1.4 billion, an increase of $86.2 million, or 6.5%, as compared to the prior year. A reconciliation of consolidated revenues follows (in millions):

	Amount	% Change vs. 2014
2014 Revenues	$ 1,331.3	
Wholesale Merchandise Revenues change based on new and cancelled domestic stores:		
Revenues increase from new stores added since January 2014**	23.3	1.8%
Net decrease from stores cancelled since January 2014**	(12.0)	(0.9%)
Increase in wholesale merchandise revenues to comparable domestic stores**	38.5	2.9%
Decrease in wholesale merchandise revenues due to non-recurring Paint Studio sales	(13.1)	(1.0%)
Increase in Ace Wholesale Holdings LLC revenues	46.2	3.5%
Increase in Ace Retail Holdings LLC revenues	5.7	0.4%
Other wholesale revenue changes, net	(2.4)	(0.2%)
2015 Revenues	$ 1,417.5	6.5%

**Year-over-year changes exclude the impact of non-recurring Paint Studio equipment revenue.

Total wholesale revenues were $1.3 billion, an increase of $80.5 million, or 6.4%, as compared to the prior year. Increases were noted across almost all departments with outdoor living, electrical and lawn and garden showing the largest increases. Excluding the non-recurring revenues related to the rollout of the new Paint Studio equipment in 2014, wholesale revenues increased by $93.6 million, or 7.1%, in the second quarter of 2015 compared to the prior year.

New stores are defined as stores that were activated from January 2014 through June 2015. Wholesale merchandise revenues from new domestic stores were $23.3 million in the second quarter of 2015. This increase was partially offset by a decrease in wholesale merchandise revenues of $12.0 million due to domestic store cancellations. As a result, the Company realized a net increase in wholesale merchandise revenues of $11.3 million related to the impact of both new stores affiliated with the Company and from stores that cancelled their membership in 2014 and 2015. Wholesale merchandise revenues to comparable domestic stores increased $38.5 million in the second quarter of 2015 compared to the prior year period. The new store, cancelled store and comparable store numbers all exclude the impact of non-recurring Paint Studio equipment revenues.

The number of the Company's domestic member retailer outlets is summarized as follows:

	Three Months Ended	
	July 4, 2015	June 28, 2014
Retailer outlets at beginning of period	4,252	4,220
New retailer outlets added	31	33
Retailer outlet cancellations	(27)	(27)
Retailer outlets at end of period	4,256	4,226

Revenues from the Ace Wholesale Holdings LLC ("AWH") subsidiary were $93.8 million during the three months ended July 4, 2015. This is an increase of $46.2 million from the second quarter of 2014. AWH began operations on February 19, 2014 and was expanded to include the acquisition of Jensen-Byrd Co., LLC ("Jensen") in December 2014. Jensen added $43.2 million of the $46.2 million increase during the second quarter.

Retail revenues were $85.4 million during the second quarter of 2015. This is an increase of $5.7 million or 7.2%. Average ticket price increased 3.1% and customer count increased 0.9% as compared to the prior year. Same-store-sales increased 3.9% compared to the second quarter of 2014 with the largest increases in lawn and garden and electrical.

Wholesale gross profit for the second quarter of 2015 was $163.5 million, a decrease of $11.9 million from the second quarter of 2014. Wholesale gross margin percentage was 12.3% of wholesale revenues, a decrease from 2014's unusually high second quarter wholesale gross margin percentage of 14.0%. The second quarter of 2014 gross margin rate was higher than normal due to incentives received from vendors.

Retail gross profit for the second quarter of 2015 was $37.1 million, an increase of $1.8 million from the second quarter of 2014. Retail gross margin percentage was 43.4% of retail revenues in 2015, down from 44.3% in the prior year. The decrease in the retail gross margin percentage was primarily the result of product mix and an increase in promotional discounting. Retail gross profit as reported in the Ace financial statements is based on the Ace wholesale acquisition cost of product rather than the ARH acquisition cost which includes Ace's normal markup from cost.

Wholesale operating expenses decreased $9.4 million, or 8.2%, for the second quarter of 2015 as compared to the second quarter of 2014. The decrease was primarily driven by the settlement of a gain contingency of $10.0 million. The additional operating expenses caused by the AWH acquisition of Jensen in December 2014 were offset by lower advertising expenses due to the timing of promotional spending. As a percentage of wholesale revenues, wholesale operating expenses decreased from 9.2% of wholesale revenues in the second quarter of 2014 to 7.9% of wholesale revenues in the second quarter of 2015.

Retail operating expenses of $25.7 million increased $1.9 million, or 8.0%, in the second quarter of 2015 as compared to the second quarter of 2014. The increase was driven by higher payroll expense and other store operating expenses primarily due to the addition of five retail outlets during the second quarter as well as the timing of advertising expenses. Retail operating expenses as a percent of retail revenues remained relatively constant at 30.1% of retail revenues versus 29.9% of retail revenues in the second quarter of 2015 and 2014, respectively.

In the second quarter of 2015, the Company recorded an additional charge of $0.2 million related to the final settlement of the withdrawal liability for the multi-employer pension fund that covers the former union employees at the closed Retail Support Center in Toledo, Ohio.

Interest expense increased $2.3 million compared to the second quarter of 2014. During the second quarter of 2015 the Company refinanced its debt with its existing lenders. The previous $400 million revolving credit facility and $165 million amortizing term loan were replaced with a $600 million revolving credit facility that expires in May of 2020. The interest rate on the facility was also reduced by 25 basis points. Because of the refinancing, the Company was required to write-off $2.2 million of deferred financing fees related to the old credit facility and term loan. This write-off was recorded as additional interest expense.

Other income and expense showed an increase in expense of $3.9 million primarily from increases in income tax expense and net income attributable to noncontrolling interests. The increase in income tax expense is primarily the result of taxes that were recorded on the settlement of the gain contingency, which is taxable to the Company.

Comparison of the Six Months Ended July 4, 2015 to the Six Months Ended June 28, 2014

The following data summarizes the Company's performance in 2015 as compared to 2014 (in millions):

	2015		**2014**		**Increase/(decrease)**	
	$	% of Revenues*	$	% of Revenues*	$	%
Revenues:						
Wholesale revenues	2,471.9	94.9%	2,286.6	94.9%	185.3	8.1%
Retail revenues	131.7	5.1%	123.4	5.1%	8.3	6.7%
Total revenues	2,603.6	100.0%	2,410.0	100.0%	193.6	8.0%
Gross profit:						
Wholesale gross profit	301.6	12.2%	294.5	12.9%	7.1	2.4%
Retail gross profit	59.4	45.1%	56.0	45.4%	3.4	6.1%
Total gross profit	361.0	13.9%	350.5	14.5%	10.5	3.0%
Operating expenses:						
Distribution operations expenses	64.5	2.6%	57.2	2.5%	7.3	12.8%
Selling, general and administrative expenses	76.3	3.1%	75.5	3.3%	0.8	1.1%
Retailer success and development expenses	69.7	2.8%	72.9	3.2%	(3.2)	(4.4%)
Retail operating expenses	47.7	36.2%	46.4	37.6%	1.3	2.8%
Warehouse facility closure costs	1.7	0.1%	-	0.0%	1.7	100.0%
Total operating expenses	259.9	10.0%	252.0	10.5%	7.9	3.1%
Operating income	101.1	3.9%	98.5	4.0%	2.6	2.6%
Interest expense	(9.3)	(0.3%)	(6.6)	(0.3%)	(2.7)	(40.9%)
Other	(4.4)	(0.2%)	(1.0)	0.1%	(3.4)	(340.0%)
Net income	87.4	3.4%	90.9	3.8%	(3.5)	(3.9%)

*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.

Consolidated revenues for the six months ended July 4, 2015 totaled $2.6 billion, an increase of $193.6 million, or 8.0%, as compared to the prior year. A reconciliation of consolidated revenues follows (in millions):

	Amount	% Change vs. 2014
2014 Revenues	$ 2,410.0	
Wholesale Merchandise Revenues change based on new and cancelled domestic stores:		
Revenues increase from new stores added since January 2014**	61.7	2.6%
Net decrease from stores cancelled since January 2014**	(22.1)	(0.9%)
Increase in wholesale merchandise revenues to comparable domestic stores**	84.3	3.5%
Decrease in wholesale merchandise revenues due to non-recurring Paint Studio sales	(41.4)	(1.7%)
Increase in Ace Wholesale Holdings LLC revenues	103.6	4.3%
Increase in Ace Retail Holdings LLC revenues	8.3	0.2%
Other wholesale revenue changes, net	(0.8)	0.0%
2015 Revenues	$ 2,603.6	8.0%

**Year-over-year changes exclude the impact of non-recurring Paint Studio equipment revenue.

Total wholesale revenues were $2.5 billion, an increase of $185.3 million, or 8.1%, as compared to the prior year. Increases were noted across all departments, while outdoor living, electrical, and lawn and garden had the largest increases. Excluding the non-

recurring revenues related to the rollout of the new Paint Studio equipment in 2014, wholesale revenues increased by $226.7 million, or 9.5%, in the first six months of 2015 compared to the prior year.

New stores are defined as stores that were activated from January 2014 through June 2015. In 2015, the Company had wholesale merchandise revenues from new domestic stores of $61.7 million. This increase was partially offset by a decrease in wholesale merchandise revenues of $22.1 million due to domestic store cancellations. As a result, the Company realized a net increase in wholesale merchandise revenues of $39.6 million related to the impact of both new stores affiliated with the Company and from stores that cancelled their membership in 2014 and 2015. Wholesale merchandise revenues to comparable domestic stores increased $84.3 million. The new store, cancelled store and comparable store numbers all exclude the impact of non-recurring Paint Studio equipment revenues.

The number of the Company's domestic member retailer outlets is summarized as follows:

	Six Months Ended	
	July 4, 2015	June 28, 2014
Retailer outlets at beginning of period	4,251	4,171
New retailer outlets added	64	111
Retailer outlet cancellations	(59)	(56)
Retailer outlets at end of period	4,256	4,226

Revenues from the AWH subsidiary were $171.9 million during the six months ended July 4, 2015. This is an increase of $103.6 million from the first six months of 2014. AWH began operations on February 19, 2014 and was expanded to include the acquisition of Jensen in December 2014. Jensen added $82.1 million of the $103.6 million increase during the six months ended July 4, 2015.

Retail revenues were $131.7 million during the six months ended July 4, 2015. Same store sales growth primarily drove the increase of $8.3 million or 6.7% from the six months ended June 28, 2014. With increases in the majority of departments, lawn and garden, electrical, and paint showed the largest increases. Increases were seen in average ticket and customer count as compared to the prior year.

Wholesale gross profit for the first six months of 2015 was $301.6 million, an increase of $7.1 million from the six months ended June 28, 2014. The wholesale gross margin percentage was 12.2% of wholesale revenues in the first six months of 2015, a decrease from the 2014 gross margin percentage of 12.9%. The decrease in wholesale gross margin percentage was primarily driven by lower service revenues due to timing and lower paint profitability resulting from reduced sales, unfavorable product mix and increased consumer promotions.

Retail gross profit for the six months ended July 4, 2015 was $59.4 million, an increase of $3.4 million from the six months ended June 28, 2014. Retail gross margin percentage was 45.1% of retail revenues in 2015, down from 45.4% in the prior year. The decrease in the retail gross margin percentage was primarily the result of product mix and an increase in promotional discounting. Retail gross profit as reported in the Ace financial statements is based on the Ace wholesale acquisition cost of product rather than the ARH acquisition cost which includes Ace's normal markup from cost.

Wholesale operating expenses increased $4.9 million, or 2.4%, for the six months ended July 4, 2015 as compared to the six months ended June 28, 2014. The increase was primarily driven by additional operating expenses from the AWH acquisitions of Emery-Waterhouse in February 2014 and Jensen in December 2014 and higher warehouse wages from the increase in sales, partially offset by the settlement of a gain contingency of $10.0 million. As a percentage of wholesale revenues, wholesale operating expenses decreased from 9.0% of wholesale revenues in 2014 to 8.5% of wholesale revenues in 2015.

Retail operating expenses of $47.7 million increased $1.3 million, or 2.8%, for the six months ended July 4, 2015 as compared to the six months ended June 28, 2014. The increase was primarily driven by higher payroll and other store operating expenses due to the acquisition of five new retail outlets in 2015 and the timing of advertising expenses. Retail operating expenses as a percent of retail revenues decreased from 37.6% of retail revenues in the six months ended June 28, 2014 to 36.2% of retail revenues in the six months ended July 4, 2015.

In the six months ended July 4, 2015, the Company recorded an additional charge of $1.7 million related to the final settlement of the withdrawal liability for the multi-employer pension fund that covers the former union employees at the closed Retail Support Center in Toledo, Ohio.

Interest expense increased $2.7 million compared to the six months ended June 28, 2014. During the six months ended July 4, 2015, the Company refinanced its debt with its existing lenders. The previous $400 million revolving credit facility and $165 million amortizing term loan were replaced with a $600 million revolving credit facility that expires in May of 2020. The interest rate on the facility was also reduced by 25 basis points. Because of the refinancing, the Company was required to write-off $2.2 million of deferred financing fees related to the old credit facility and term loan. This write-off was recorded as additional interest expense. Additionally, the Company had higher average outstanding balances under its revolving lines of credit during the six months ended July 4, 2015.

Other income and expense showed an increase in expense of $3.4 million primarily from increases in income tax expense and net income attributable to noncontrolling interests. The increase in income tax expense is primarily the result of taxes that were recorded on the settlement of the gain contingency, which is taxable to the Company.

Liquidity and Capital Resources

The Company believes that existing cash balances, along with the existing line 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, 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 facility. The Company currently estimates that its cash flows from operating activities and working capital, together with its line 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.

On May 29, 2015, the Company amended its secured credit facility which was originally dated April 13, 2012 and previously amended on July 29, 2013. The May 2015 amendment extended the maturity date to May 29, 2020 and lowered the interest rate credit spread by 25 basis points. The amended credit facility consists of a $600.0 million revolving credit facility that is expandable to $750.0 million through a $150.0 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. Borrowings under the amended credit facility bear interest at a rate of either 25 to 100 basis points over the prime rate or 125 to 200 basis points over the London Interbank Offered Rate ("LIBOR") depending on the Company's leverage ratio as defined under the agreement. The amended credit facility was priced at LIBOR plus 150 basis points at July 4, 2015. The amended credit facility requires maintenance of certain financial covenants including a maximum allowable average leverage ratio and a minimum fixed charge coverage ratio. As of July 4, 2015, the Company was in compliance with its covenants and $273.4 million was outstanding under the amended credit facility.

The amended credit facility includes a $175.0 million sublimit for the issuance of standby and commercial letters of credit. As of July 4, 2015, a total of $28.0 million in letters of credit were outstanding. The revolving credit facility requires the Company to pay fees based on the unused portion of the line of credit at a rate of 15 to 30 basis points per annum depending on the Company's leverage ratio.

The amended 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 July 4, 2015, there were no loans or other extensions of credit provided to AIH.

In order to reduce the risk of interest rate volatility, the Company entered into an interest rate swap derivative agreement in June 2012, which expires on March 13, 2017. This swap agreement fixes the LIBOR rate on a portion of the revolving credit facility at 1.13%, resulting in an effective rate of 2.63% after adding the 1.50% margin based on the current pricing tier per the credit agreement. The notional amount of the derivative agreement decreases by $5.0 million each quarter through expiration of the interest rate swap derivative agreement in March 2017. As of July 4, 2015, the notional amount of the interest rate swap agreement remaining was $160.0 million. The Company entered into a forward interest rate swap derivative agreement in June 2015 to reduce the risk of interest rate volatility for the remaining term of the amended credit facility. The forward interest rate swap starts on March 13, 2017 and expires on May 13, 2020. The forward swap agreement fixes the LIBOR rate on $150.0 million of the revolving credit facility at 2.18%, resulting in an effective rate of 3.68% after adding the 1.50% margin based on the current pricing tier per the credit agreement. The swap arrangements have been designated as cash flow hedges and have been evaluated to be highly effective. As a result, the after-tax change in the fair value of the swaps are recorded in Accumulated other comprehensive income ("AOCI") as a gain or loss on derivative financial instruments.

The Company's ARH subsidiary has a $60.0 million asset-based revolving credit facility ("ARH Facility"). The ARH Facility matures on June 28, 2019 and is expandable to $85.0 million under certain conditions. In addition, the Company has the right to issue letters of credit up to a maximum of $7.5 million. At the Company's discretion, borrowings under this facility bear interest at a rate of either the prime rate plus an applicable spread of 35 basis points to 75 basis points or LIBOR plus an applicable spread of 135 basis points to 175 basis points, depending on the Company's availability under the ARH Facility as measured on a quarterly basis.

The ARH Facility is collateralized by substantially all of ARH'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 July 4, 2015, ARH was in compliance with its covenants. At the end of the second quarter of 2015, ARH had $13.3 million in loans outstanding under its Facility.

The ARH Facility requirements include a lender-controlled cash concentration system that results in all of ARH's daily available cash being applied to the outstanding borrowings under this facility. Pursuant to 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 ARH Facility have been classified as a Current maturity of long-term debt as of July 4, 2015.

Total debt was $301.8 million as of July 4, 2015, compared to $283.7 million and $329.9 million as of January 3, 2015 and June 28, 2014, respectively.

Cash Flows

The Company had $35.3 million and $15.7 million of cash and cash equivalents at July 4, 2015 and June 28, 2014, respectively. Following is a summary of the Company's cash flows from operating, investing and financing activities for the first six months of 2015 and 2014 (in millions):

	2015	2014
Cash provided by operating activities before changes in assets and liabilities	$ 120.3	$ 118.9
Net changes in assets and liabilities	(53.9)	(159.0)
Net cash provided by (used in) operating activities	66.4	(40.1)
Net cash used in investing activities	(22.4)	(51.4)
Net cash (used in) provided by financing activities	(38.5)	89.3
Net change in cash and cash equivalents	$ 5.5	$ (2.2)

The Company's operating activities provided $66.4 million of cash in 2015 compared to using $40.1 million in 2014. Excluding the impact of net changes in assets and liabilities, cash provided by operating activities increased from $118.9 million in 2014 to $120.3 million in 2015.

The net change in assets and liabilities was a $159.0 million use of cash in 2014 compared to a $53.9 million use of cash in 2015. In the first six months of 2015, receivables increased $112.9 million due to seasonal dating programs and inventories increased $110.5 million for the intentional build-up of LED lighting inventories for planned resets and promotions, the seasonal inventory build and higher inventory levels to support higher sales volumes. Increases in receivables and inventories were offset by a $182.3 million increase in accounts payable and accrued expenses. The decrease in other long-term liabilities primarily resulted from $6.4 million of payments related to the settlement of a withdrawal liability for the multi-employer pension fund that covers the former union employees at the closed Retail Support Center in Toledo, Ohio. In the first six months of 2014, receivables increased $158.5 million due to seasonal dating programs as well as product shipments for the Paint Studio initiative. Inventories increased $103.7 million in 2014 as a result of seasonal inventory build, increased revenues and the addition of Valspar-branded paint at all Company warehouses. Offsetting these increases was the increase in accounts payable of $135.3 million, which corresponded with the planned increase in inventories.

Net cash used in investing activities was $22.4 million in the first six months of 2015 compared to $51.4 million in 2014. Investing activities in 2015 primarily consisted of $16.8 million in capital expenditures and $5.6 million paid for acquired businesses primarily related to the acquisition of five retail stores by ARH. Investing activities in the first six months of 2014 primarily consisted of the $32.9 million in net cash paid for Emery-Waterhouse along with $19.6 million in capital expenditures.

Net cash provided by financing activities was $89.3 million in the first six months of 2014 compared to a $38.5 million use of cash in 2015. During 2015, the Company decreased long-term debt by $173.2 million and paid $48.9 million for the cash portion of patronage distributions. This was partially offset by net borrowings under the revolving lines of credit of $186.7. During 2014, the Company borrowed $132.7 million under revolving lines of credit. This was offset slightly by payments of the cash portion of patronage distributions of $36.6 million and $8.2 million in principal payments on long-term debt.

Contractual Obligations and Commitments

For the six months ended July 4, 2015, there have been no significant changes to the Company's contractual obligations and commitments as disclosed in its 2014 Annual Report.

Application of Critical Accounting Policies and Estimates

For a description of the Company's critical accounting policies and estimates, please see the Application of Critical Accounting Policies and Estimates section in the Management's Discussion and Analysis of Financial Condition and Results of Operations section of the Company's 2014 Annual Report.

Qualitative and Quantitative Disclosure About Market Risk

The Company is exposed to market risk in the normal course of its business operations, including the risk of loss from inflation and changes in price, foreign currency, interest rates and customer credit risk.

There has been no material change in the Company's exposure to market risk from what was disclosed in the 2014 Annual Report.

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; 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.

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL STATEMENTS

The consolidated financial statements presented in this Quarterly 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 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.

August 18, 2015

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

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

/s/ Steven G. Locanto
Steven G. Locanto
Corporate Controller

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