

KOHLS Corp  
Form 10-K  
March 22, 2019  
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934  
For the fiscal year ended February 2, 2019

or

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934  
For the Transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 1-11084

KOHL'S CORPORATION

(Exact name of registrant as specified in its charter)

Wisconsin  
(State or other jurisdiction of incorporation or organization)

39-1630919  
(I.R.S. Employer Identification No.)

N56 W17000 Ridgewood Drive, Menomonee Falls, Wisconsin  
(Address of principal executive offices)

53051  
(Zip Code)

Registrant's telephone number, including area code (262) 703-7000

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

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Title of each class	Name of each exchange on which registered
Common Stock, \$.01 Par Value	New York Stock Exchange
Securities registered pursuant to Section 12(g) of the Act:	None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.  
Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer  Accelerated filer  Non-accelerated filer

Smaller reporting company  Emerging growth company

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

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

At August 3, 2018, the aggregate market value of the voting stock of the Registrant held by stockholders who were not affiliates of the Registrant was approximately \$12.1 billion (based upon the closing price of Registrant's Common Stock on the New York Stock Exchange on such date). At March 13, 2019, the Registrant had outstanding an aggregate of 163,166,004 shares of its Common Stock.

Documents Incorporated by Reference:

Portions of the Proxy Statement for the Registrant's Annual Meeting of Shareholders to be held on May 15, 2019 are incorporated into Part III.



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## PART I

## Item 1. Business

Kohl's Corporation (the "Company," "Kohl's," "we," "our" or "us") was organized in 1988 and is a Wisconsin corporation. As of February 2, 2019, we operated 1,159 Kohl's department stores, a website (www.Kohls.com), 12 FILA outlets, and four Off-Aisle clearance centers. Our Kohl's stores and website sell moderately-priced proprietary and national brand apparel, footwear, accessories, beauty and home products. Our Kohl's stores generally carry a consistent merchandise assortment with some differences attributable to local preferences. Our website includes merchandise that is available in our stores, as well as merchandise that is available only online.

Our merchandise mix includes both national brands and proprietary brands that are available only at Kohl's. Our proprietary portfolio includes well-known established private brands such as Apt. 9, Croft & Barrow, Jumping Beans, SO and Sonoma Goods for Life and exclusive brands that are developed and marketed through agreements with nationally-recognized brands such as Food Network, LC Lauren Conrad, Elle and Simply Vera Vera Wang. National brands generally have higher selling prices, but lower gross margins, than proprietary brands.

The following tables summarize our sales penetration by line of business and brand type over the last three years:

Our fiscal year ends on the Saturday closest to January 31<sup>st</sup> each year. Unless otherwise stated, references to years in this report relate to fiscal years rather than to calendar years. The following fiscal periods are presented in this report.

Fiscal Year Ended		Number of Weeks
2018	February 2, 2019	52
2017	February 3, 2018	53
2016	January 28, 2017	52

For discussion of our financial results, see Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations."

## Distribution

We receive substantially all of our store merchandise at our nine retail distribution centers. A small amount of our merchandise is delivered directly to the stores by vendors or their distributors. The retail distribution centers, which are strategically located throughout the United States, ship merchandise to each store by contract carrier several times a week. Digital sales may be picked up in our stores or are shipped from a Kohl's fulfillment center, retail distribution center or store; by a third-party fulfillment center; or directly by a third-party vendor.





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See Item 2, “Properties,” for additional information about our distribution centers.

### Employees

During 2018, we employed an average of approximately 129,000 associates, including approximately 34,000 full-time and 95,000 part-time associates. The number of associates varies during the year, peaking during the back-to-school and holiday seasons. None of our associates are represented by a collective bargaining unit. We believe our relations with our associates are very good.

### Competition

The retail industry is highly competitive. Management considers style, quality, price and convenience to be the most significant competitive factors in the industry. Merchandise mix, brands, service, loyalty programs, credit availability, and customer experience and convenience are also key competitive factors. Our primary competitors are traditional department stores, mass merchandisers, off-price retailers, specialty stores, internet and catalog businesses and other forms of retail commerce. Our specific competitors vary from market to market.

### Merchandise Vendors

We purchase merchandise from numerous domestic and foreign suppliers. All business partners must meet certain requirements to do business with us. Our Terms of Engagement include provisions regarding laws and regulations, employment practices, ethical standards, environmental and legal requirements, communication, monitoring/compliance, record keeping, subcontracting and corrective action. We expect that all business partners will comply with these Terms of Engagement and quickly remediate any deficiencies, if noted, to maintain our business relationship.

A third-party purchasing agent sources approximately 25% of the merchandise we sell. No vendors individually accounted for more than 10% of our net purchases in 2018. We have no significant long-term purchase commitments or arrangements with any of our suppliers and believe that we are not dependent on any one supplier. We believe we have good working relationships with our suppliers.

### Seasonality

Our business, like that of most retailers, is subject to seasonal influences. The majority of our sales and income are typically realized during the second half of each fiscal year. The back-to-school season extends from August through September and represents approximately 15% of our annual sales. Approximately 30% of our annual sales occur during the holiday season in the months of November and December. Because of the seasonality of our business, results for any quarter are not necessarily indicative of the results that may be achieved for the fiscal year.

### Trademarks and Service Marks

KOHL'S® is a registered trademark owned by one of our wholly-owned subsidiaries. We consider this mark and the accompanying goodwill to be valuable to our business. This subsidiary has over 200 additional registered trademarks, most of which are used in connection with our private brand products.

### Available Information

Our corporate website is <https://corporate.kohls.com>. Through the “Investors” portion of this website, we make available, free of charge, our proxy statements, Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q,

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Current Reports on Form 8-K, SEC Forms 3, 4 and 5 and any amendments to those reports as soon as reasonably practicable after such material has been filed with, or furnished to, the Securities and Exchange Commission (“SEC”).

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The following have also been posted on our website, under the caption "Investors" and sub-caption "Corporate Governance":

- Committee charters of our Board of Directors' Audit Committee, Compensation Committee and Governance & Nominating Committee
- Corporate Governance Guidelines
- Code of Ethics
- Corporate Social Responsibility Report

The information contained on our website is not part of this Annual Report on Form 10-K. Paper copies of any of the materials listed above will be provided without charge to any shareholder submitting a written request to our Investor Relations Department at N56 W17000 Ridgewood Drive, Menomonee Falls, Wisconsin 53051 or via e-mail to [Investor.Relations@Kohls.com](mailto:Investor.Relations@Kohls.com).

### Item 1A. Risk Factors

This Form 10-K contains "forward-looking statements" made within the meaning of the Private Securities Litigation Reform Act of 1995. Words such as "believes," "anticipates," "plans," "may," "intends," "will," "should," "expects" and similar expressions are intended to identify forward-looking statements. Forward-looking statements also include comments about our future sales or financial performance and our plans, performance and other objectives, expectations or intentions, such as statements regarding our liquidity, debt service requirements, planned capital expenditures, future business initiatives, and adequacy of capital resources and reserves. A number of important factors could cause our results to differ materially from those indicated by the forward-looking statements including, among others, those risk factors described below. Forward-looking statements relate to the date made, and we undertake no obligation to update them.

Our sales, gross margin, expenses and operating results could be negatively impacted by a number of factors including, but not limited to those described below. Many of these risk factors are outside of our control. If we are not successful in managing these risks, they could have a negative impact on our sales, gross margin, expenses, and/or operating results.

#### Macroeconomic and Industry Risks

General economic conditions, consumer spending levels and/or other conditions could decline.

Consumer spending habits, including spending for the merchandise that we sell, are affected by many factors including prevailing economic conditions, levels of employment, salaries and wage rates, prevailing interest rates, housing costs, energy and fuel costs, income tax rates and policies, consumer confidence, consumer perception of economic conditions, and the consumer's disposable income, credit availability and debt levels. The moderate-income consumer, which is our core customer, is especially sensitive to these factors. A slowdown in the U.S. economy or an uncertain economic outlook could adversely affect consumer spending habits. As all of our stores are located in the United States, we are especially susceptible to deteriorations in the U.S. economy.

Consumer confidence is also affected by the domestic and international political situation. The outbreak or escalation of war, or the occurrence of terrorist acts or other hostilities in or affecting the United States, could lead to a decrease in spending by consumers.

Our competitors could make changes to their pricing and other practices.

The retail industry is highly competitive. We compete for customers, associates, locations, merchandise, services and other important aspects of our business with many other local, regional and national retailers. Those

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competitors include traditional department stores, mass merchandisers, off-price retailers, specialty stores, internet and catalog businesses, and other forms of retail commerce.

We consider style, quality, price, and convenience to be the most significant competitive factors in our industry. The continuing migration and evolution of retailing to digital channels have increased our challenges in differentiating ourselves from other retailers especially as it relates to national brands. In particular, consumers can quickly and conveniently comparison shop with digital tools, which can lead to decisions based solely on price. Unanticipated changes in the pricing and other practices of our competitors may adversely affect our performance.

Tax and trade policies could adversely change.

Uncertainty with respect to tax and trade policies, tariffs and government regulations affecting trade between the United States and other countries has recently increased. We source the majority of our merchandise from manufacturers located outside of the United States, primarily in Asia. Major developments in tax policy or trade relations, such as the imposition of tariffs on imported products, could have a material adverse effect on our business, results of operations and liquidity.

## Operational Risks

We may be unable to offer merchandise that resonates with existing customers and attracts new customers as well as successfully manage our inventory levels.

Our business is dependent on our ability to anticipate fluctuations in consumer demand for a wide variety of merchandise. Failure to accurately predict constantly changing consumer tastes, preferences, spending patterns and other lifestyle decisions could create inventory imbalances and adversely affect our performance and long-term relationships with our customers. Additionally, failure to accurately predict changing consumer tastes may result in excess inventory, which could result in additional markdowns and adversely affect our operating results.

We may be unable to source merchandise in a timely and cost-effective manner.

A third-party purchasing agent sources approximately 25% of the merchandise we sell. The remaining merchandise is sourced from a wide variety of domestic and international vendors. Our ability to find qualified vendors and access products in a timely and efficient manner is a significant challenge which is typically even more difficult for goods sourced outside the United States, substantially all of which are shipped by ocean to ports in the United States. Political or financial instability, trade restrictions, tariffs, currency exchange rates, transport capacity and costs, work stoppages, port strikes, port congestion and delays and other factors relating to foreign trade are beyond our control and could adversely impact our performance.

Increases in the price of merchandise, raw materials, fuel and labor or their reduced availability could increase our cost of merchandise sold. The price and availability of raw materials may fluctuate substantially, depending on a variety of factors, including demand, weather, supply conditions, transportation costs, energy prices, work stoppages, government regulation and policy, economic climates, market speculation and other unpredictable factors. An inability to mitigate these cost increases, unless sufficiently offset with our pricing actions, might cause a decrease in our profitability. Any related pricing actions might cause a decline in our sales volume. Additionally, a reduction in the availability of raw materials could impair our ability to meet our production or purchasing requirements in a timely manner. Both the increased cost and lower availability of merchandise, raw materials, fuel and labor may also have an adverse impact on our cash and working capital needs as well as those of our suppliers.

If any of our significant vendors were to become subject to bankruptcy, receivership or similar proceedings, we may be unable to arrange for alternate or replacement contracts, transactions or business relationships on terms as favorable as current terms, which could adversely affect our sales and operating results.

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Our vendors may not adhere to our Terms of Engagement or to applicable laws.

A substantial portion of our merchandise is received from vendors and factories outside of the United States. We require all of our suppliers to comply with all applicable local and national laws and regulations and our Terms of Engagement for Kohl's Business Partners. These Terms of Engagement include provisions regarding laws and regulations, employment practices, ethical standards, environmental and legal requirements, communication, monitoring/compliance, record keeping, subcontracting and corrective action. From time to time, suppliers may not be in compliance with these standards or applicable laws. Significant or continuing noncompliance with such standards and laws by one or more suppliers could have a negative impact on our reputation and our results of operations.

Our marketing may be ineffective.

We believe that differentiating Kohl's in the marketplace is critical to our success. We design our marketing and loyalty programs to increase awareness of our brands and to build personalized connections with new and existing customers. We believe these programs will strengthen customer loyalty, increase the number and frequency of customers that shop our stores and website and increase our sales. If our marketing and loyalty programs are not successful, our sales and operating results could be adversely affected.

The reputation and brand image of Kohl's and the brands and products we sell could be damaged.

We believe the Kohl's brand name and many of our proprietary brand names are powerful sales and marketing tools. We devote significant resources to develop, promote and protect proprietary brands that generate national recognition. In some cases, the proprietary brands or the marketing of such brands are tied to or affiliated with well-known individuals. We also affiliate the Kohl's brand with third-party national brands that we sell in our store and through our partnerships with companies in pursuit of strategic initiatives. Damage to the reputations (whether or not justified) of the Kohl's brand, our proprietary brand names or any affiliated individuals or companies with which we have partnered, could arise from product failures; concerns about human rights, working conditions and other labor rights and conditions where merchandise is produced; perceptions of our pricing and return policies; litigation; vendor violations of our Terms of Engagement; perceptions of the national vendors and/or third party companies with which we partner; or various other forms of adverse publicity, especially in social media outlets. This type of reputational damage may result in a reduction in sales, earnings, and shareholder value.

There may be concerns about the safety of products that we sell.

If our merchandise offerings do not meet applicable safety standards or our customers' expectations regarding safety, we could experience lost sales, experience increased costs, and/or be exposed to legal and reputational risk. Events that give rise to actual, potential or perceived product safety concerns could expose us to government enforcement action and/or private litigation. Reputational damage caused by real or perceived product safety concerns could have a negative impact on our sales and operating results.

We may be unable to adequately maintain and/or update our information systems.

The efficient operation of our business is dependent on our information systems. In particular, we rely on our information systems to effectively manage sales, distribution, and merchandise planning and allocation functions. We also generate sales through the operations of our Kohls.com website. We frequently make investments that will help maintain and update our existing information systems. We also depend on third parties as it relates to our information systems. In particular, we are currently migrating certain systems and applications to cloud environments that are hosted by third-party service providers. The potential problems and interruptions associated with implementing technology initiatives, the failure of our information systems to perform as designed or the failure to successfully

partner with our third party service providers, such as our cloud platform providers, could disrupt our business and harm our sales and profitability.

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Our information technology projects may not yield their intended results.

We regularly have internal information technology projects in process. Although the technology is intended to increase productivity and operating efficiencies, these projects may not yield their intended results or may deliver an adverse user or customer experience. We may incur significant costs in connection with the implementation, ongoing use, or discontinuation of technology projects, or fail to successfully implement these technology initiatives or achieve the anticipated efficiencies from such projects, any of which could adversely affect our operations, liquidity and financial condition.

Weather conditions and natural disasters could adversely affect consumer shopping patterns and disrupt our operations.

A significant portion of our business is apparel and is subject to weather conditions. As a result, our operating results may be adversely affected by severe or unexpected weather conditions. Frequent or unusually heavy snow, ice or rain storms; natural disasters such as earthquakes, tornadoes, floods, fires, and hurricanes; or extended periods of unseasonable temperatures could adversely affect our performance by affecting consumer shopping patterns and diminishing demand for seasonal merchandise. In addition, these events could cause physical damage to our properties or impact our supply chain, making it difficult or impossible to timely deliver seasonally appropriate merchandise. Although we maintain crisis management and disaster response plans, our mitigation strategies may be inadequate to address such a major disruption event.

We may be unable to successfully execute an omnichannel strategy.

Customer expectations about the methods by which they purchase and receive products or services are evolving. Customers are increasingly using technology and mobile devices to rapidly compare products and prices and to purchase products. Once products are purchased, customers are seeking alternate options for delivery of those products. We must continually anticipate and adapt to these changes in the purchasing process. Our ability to compete with other retailers and to meet our customer expectations may suffer if we are unable to provide relevant customer-facing technology and omnichannel experiences. Our ability to compete may also suffer if Kohl's, our suppliers, or our third-party shipping and delivery vendors are unable to effectively and efficiently fulfill and deliver orders, especially during the holiday season when sales volumes are especially high. Consequently, our results of operations could be adversely affected.

Our business is seasonal in nature, which could negatively affect our revenues, operating results and cash requirements.

Our business is subject to seasonal influences, with a major portion of sales and income historically realized during the second half of the fiscal year, which includes the back-to-school and holiday seasons.

If we do not adequately stock or restock popular products, particularly during the back-to-school and holiday seasons, we may fail to meet customer demand, which could affect our revenue and our future growth. If we overstock products, we may be required to take significant inventory markdowns or write-offs, which could reduce profitability.

We may experience an increase in costs associated with shipping digital orders due to complimentary upgrades, split shipments, and additional long-zone shipments necessary to ensure timely delivery for the holiday season. If too many customers access our website within a short period of time, we may experience system interruptions that make our website unavailable or prevent us from efficiently fulfilling orders, which may reduce the volume of goods we sell and the attractiveness of our products and services. Also, third-party delivery and direct ship vendors may be unable to deliver merchandise on a timely basis.



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This seasonality causes our operating results and cash needs to vary considerably from quarter to quarter. Additionally, any decrease in sales or profitability during the second half of the fiscal year could have a disproportionately adverse effect on our results of operations.

Changes in credit card operations could adversely affect our sales and/or profitability.

Our credit card operations facilitate merchandise sales and generate additional revenue from fees related to extending credit. The proprietary Kohl's credit card accounts are owned by an unrelated third-party, but we share in the net risk-adjusted revenue of the portfolio, which is defined as the sum of finance charges, late fees and other revenue less write-offs of uncollectible accounts. Changes in funding costs related to interest rate fluctuations are shared similar to the revenue when interest rates exceed defined amounts. Though management currently believes that increases in funding costs will be largely offset by increases in finance charge revenue, increases in funding costs could adversely impact the profitability of this program.

Changes in credit card use and applications, payment patterns, credit fraud and default rates may also result from a variety of economic, legal, social and other factors that we cannot control or predict with certainty. Changes that adversely impact our ability to extend credit and collect payments could negatively affect our results.

We may be unable to attract, develop and retain quality associates while controlling costs, which could adversely affect our operating results.

Our performance is dependent on attracting and retaining a large number of quality associates, including our senior management team and other key associates. Many associates are in entry-level or part-time positions with historically high rates of turnover. Many of our strategic initiatives require that we hire and/or develop associates with appropriate experience. Our staffing needs are especially high during the holiday season. Competition for these associates is intense. We cannot be sure that we will be able to attract and retain a sufficient number of qualified personnel in future periods.

Our ability to meet our labor needs while controlling costs is subject to external factors such as unemployment levels, prevailing wage rates, minimum wage legislation, actions by our competitors in compensation levels, potential labor organizing efforts, and changing demographics. Competitive and regulatory pressures have already significantly increased our labor costs. Further changes that adversely impact our ability to attract and retain quality associates could adversely affect our performance and/or profitability. In addition, changes in federal and state laws relating to employee benefits, including, but not limited to, sick time, paid time off, leave of absence, wage-and-hour, overtime, meal-and-break time and joint/co-employment could cause us to incur additional costs, which could negatively impact our profitability.

## Capital Risks

We may be unable to raise additional capital or maintain bank credit on favorable terms, which could adversely affect our business and financial condition.

We have historically relied on the public debt markets to raise capital to partially fund our operations and growth. We have also historically maintained lines of credit with financial institutions. Changes in the credit and capital markets, including market disruptions, limited liquidity and interest rate fluctuations, may increase the cost of financing or restrict our access to these potential sources of future liquidity. Our continued access to these liquidity sources on favorable terms depends on multiple factors, including our operating performance and maintaining strong debt ratings. If our credit ratings fall below desirable levels, our ability to access the debt markets and our cost of funds for new debt issuances could be adversely impacted. Additionally, if unfavorable capital market conditions exist if and when

we were to seek additional financing, we may not be able to raise sufficient capital on favorable terms and on a timely basis (if at all). If our access to capital was to become significantly constrained or our cost of capital was to increase significantly our financial condition, results of operations and cash flows could be adversely affected.

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Our capital allocation could be inefficient or ineffective.

Our goal is to invest capital to maximize our overall long-term returns. This includes spending on inventory, capital projects and expenses, managing debt levels, and periodically returning value to our shareholders through share repurchases and dividends. To a large degree, capital efficiency reflects how well we manage our other key risks. The actions taken to address other specific risks may affect how well we manage the more general risk of capital efficiency. If we do not properly allocate our capital to maximize returns, we may fail to produce optimal financial results and we may experience a reduction in shareholder value.

## Legal and Regulatory Risks

Regulatory and legal matters could adversely affect our business operations and change financial performance.

Various aspects of our operations are subject to federal, state or local laws, rules and regulations, any of which may change from time to time. The costs and other effects of new or changed legal requirements cannot be determined with certainty. For example, new legislation or regulations may result in increased costs directly for our compliance or indirectly to the extent such requirements increase prices of goods and services, reduce the availability of raw materials or further restrict our ability to extend credit to our customers.

We continually monitor the state and federal legal and regulatory environments for developments that may impact us. Failure to detect changes and comply with such laws and regulations may result in an erosion of our reputation, disruption of business and/or loss of associate morale. Additionally, we are regularly involved in various litigation matters that arise out of the conduct of our business. Litigation or regulatory developments could adversely affect our business operations and financial performance.

Our efforts to protect the security of sensitive or confidential customer, associate or company information could be unsuccessful, which could severely damage our reputation, expose us to risks of litigation and liability, disrupt our operations and harm our business.

As part of our normal course of business, we collect, retain, process and transmit sensitive and confidential customer, associate and company information. We also engage third-party vendors that provide technology, systems and services to facilitate our collection, retention, processing and transmission of this information. The protection of this data is extremely important to us, our associates and our customers. As with other companies, our facilities and systems and those of our third-party vendors are vulnerable to cybersecurity threats, security breaches, system failures, acts of vandalism, fraud, misappropriation, malware and other malicious or harmful code, misplaced or lost data, programming and/or human errors, insider threats, or other similar events. Despite our substantial investments in personnel, training and implementation of programs, procedures, and plans to protect the security, confidentiality, integrity and availability of our information and to prevent, detect, contain and respond to cybersecurity threats, there is no assurance that these measures will be adequate to prevent all such cybersecurity threats, particularly given the ever-evolving and increasingly sophisticated methods of cyber-attack that may be difficult or impossible to anticipate and/or detect. In addition, the regulatory environment related to data privacy and cybersecurity is constantly changing, which may increase our compliance costs and impact our customers' shopping experience. Any data security incident involving the breach, misappropriation, loss or other unauthorized disclosure of sensitive and/or confidential information, whether by us or our vendors, could disrupt our operations, damage our reputation and customers' willingness to shop in our stores or on our website, violate applicable laws, regulations, orders and

agreements, and subject us to additional costs and liabilities which could be material.

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## Item 1B. Unresolved Staff Comments

Not applicable.

## Item 2. Properties

## Stores

As of February 2, 2019, we operated 1,159 Kohl's department stores with 82.6 million selling square feet in 49 states. We also operate four Off-Aisle clearance centers and 12 FILA outlets.

Our typical store lease has an initial term of 20-25 years and four to eight renewal options for consecutive five-year extension terms. Substantially all of our leases provide for a minimum annual rent that is fixed or adjusts to set levels during the lease term, including renewals. Approximately one-fourth of the leases provide for additional rent based on a percentage of sales over designated levels.

The following tables summarize key information about our Kohl's stores as of February 2, 2019:

Number of Stores by State					
Mid-Atlantic Region:		Northeast Region:		South Central Region:	
Delaware	5	Connecticut	22	Arkansas	8
Maryland	23	Maine	5	Kansas	12
Pennsylvania	50	Massachusetts	25	Louisiana	8
Virginia	31	New Hampshire	11	Missouri	27
West Virginia	7	New Jersey	38	Oklahoma	11
		New York	51	Texas	84
		Rhode Island	4		
		Vermont	2		
Total Mid-Atlantic			Total South		
116			Central 150		
Total Northeast		158			
Midwest Region:		Southeast Region:		West Region:	
Illinois	66	Alabama	14	Alaska	1
Indiana	40	Florida	51	Arizona	26
Iowa	18	Georgia	32	California	117
Michigan	46	Kentucky	17	Colorado	24
Minnesota	27	Mississippi	5	Idaho	5
Nebraska	7	North Carolina	31	Montana	3
North Dakota	4	South Carolina	16	Nevada	12
Ohio	59	Tennessee	20	New Mexico	5
South Dakota	4			Oregon	11
Wisconsin	41			Utah	12
				Washington	19
				Wyoming	2
Total Midwest		Total Southeast		Total West	
312		186		237	

Location		Ownership	
Strip centers	780	Owned	412
Community & regional malls	82	Leased	510
Freestanding	297	Ground leased	237

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## Distribution Centers

The following table summarizes key information about each of our distribution centers:

	Year	Square
	Opened	Footage
Store distribution centers:		
Findlay, Ohio	1994	780,000
Winchester, Virginia	1997	450,000
Blue Springs, Missouri	1999	540,000
Corsicana, Texas	2001	540,000
Mamakating, New York	2002	605,000
San Bernardino, California	2002	575,000
Macon, Georgia	2005	560,000
Patterson, California	2006	365,000
Ottawa, Illinois	2008	330,000
Online fulfillment centers:		
Monroe, Ohio	2001	1,225,000
San Bernardino, California	2010	970,000
Edgewood, Maryland	2011	1,450,000
DeSoto, Texas	2012	1,515,000
Plainfield, Indiana	2017	975,000

We own all of the distribution centers except Corsicana, Texas, which is leased.

## Corporate Facilities

We own our corporate headquarters in Menomonee Falls, Wisconsin. We also own or lease additional buildings and office space, which are used by various corporate departments, including our credit operations.

## Item 3. Legal Proceedings

We are not currently a party to any material legal proceedings but are subject to certain legal proceedings and claims from time to time that arise out of the conduct of our business.

## Item 4. Mine Safety Disclosures

Not applicable.

## Item 4A. Executive Officers

Our executive officers as of February 2, 2019 were as follows:

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Name	Age	Position
Michelle Gass	50	Chief Executive Officer
Sona Chawla	51	President
Douglas Howe	58	Chief Merchandising Officer
Bruce Besanko	60	Chief Financial Officer
Marc Chini	60	Senior Executive Vice President, Chief People Officer
Ratnakar Lavu	48	Senior Executive Vice President, Chief Technology Officer
Greg Revelle	41	Senior Executive Vice President, Chief Marketing Officer

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Michelle Gass

Ms. Gass has served as our CEO and as a director since May 2018. Ms. Gass was promoted to CEO-elect in October 2017. She joined the Company in 2013 as Chief Customer Officer and was named Chief Merchandising and Customer Officer in June 2015. Prior to Kohl's, Ms. Gass spent more than 16 years with Starbucks Corporation holding a variety of leadership roles across marketing, global strategy and merchandising, including President, Starbucks Europe, Middle East and Africa. Prior to Starbucks, Ms. Gass was with Procter and Gamble. Ms. Gass has over 25 years of experience in the retail and consumer goods industries. She is currently a director for PepsiCo Inc., a global food and beverage company. From April 2014 to February 2017, Ms. Gass also served as a director of Cigna Corporation, a global health service company.

Sona Chawla

Ms. Chawla has served as President since May 2018. She served as Chief Operating Officer and President-elect from October 2017 to May 2018. Ms. Chawla joined the Company as Chief Operating Officer in November 2015. Prior to joining the Company, Ms. Chawla served on Walgreen Company's senior leadership team in the roles of President, Digital and Chief Marketing Officer from February 2014 to November 2015, President, E-Commerce from 2011 to February 2014 and Senior Vice President, E-Commerce from 2008 to 2011. Prior to Walgreens, Ms. Chawla served as Vice President, Global Online Business with Dell, Inc. (2006-2008) and previously was a key executive at Wells Fargo & Company serving as Executive Vice President, Online Sales, Service and Marketing (2005-2006), Executive Vice President, Web Channel Management (2003-2005) and Senior Vice President, Enterprise Internet Services (2000-2003). Before Wells Fargo, Ms. Chawla worked at Andersen Consulting (now Accenture) and Mitchell Madison Group. Ms. Chawla has 18 years of experience in retail and digital. From 2012 to November 2015, Ms. Chawla served as a director of Express, Inc., a specialty retail apparel chain. She is currently a director of CarMax, Inc., the nation's largest retailer of used vehicles.

Douglas Howe

Mr. Howe has served as Chief Merchandising Officer since May 2018. Prior to joining the Company, he served in several senior leadership roles with Qurate Retail Group, leading QVC's and HSN's product leadership as Chief Merchandising Officer from December 2017 to April 2018, Executive Vice President of Merchandising from July 2015 to December 2017, Executive Vice President of Merchandising and Planning from 2010 to July 2015, and Executive Vice President of Strategic Multichannel Planning and Merchandising from 2008 to 2010. Prior to joining QVC in 2001 as Vice President of Merchandising, Fashion and Beauty, Mr. Howe previously served as Executive Vice President of Product Design and Development for Old Navy, as well Senior Vice President of Strategy, Design and Development for Walmart. Mr. Howe has over 25 years of experience in the retail industry.

Bruce H. Besanko

Mr. Besanko has served as Chief Financial Officer since July 2017. Prior to joining the Company, he spent four years with Supervalu, Inc. as Executive Vice President, Chief Operating Officer and Chief Financial Officer from October 2015 to July 2017 and Executive Vice President and Chief Financial Officer from 2013 to October 2015. Mr. Besanko served as Executive Vice President, Chief Financial Officer and Chief Administrative Officer at OfficeMax,

Inc. from 2008 to 2013. Mr. Besanko held several finance leadership positions at Circuit City from 2007 to 2008, The Yankee Candle Company, Inc. from 2005 to 2007, Best Buy Co., Inc. from 2002 to 2005, Sears Roebuck & Company from 1996 to 2002 and Atlantic Richfield Company, Inc. from 1992 to 1996. In addition to his business experience, Mr. Besanko served 26 years in the U.S. Air Force where he rose to the rank of Lieutenant Colonel. Mr. Besanko has 23 years of experience in the retail industry. He is currently a director of Diebold Nixdorf, a multinational financial and retail technology company.

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Marc A. Chini

Mr. Chini has served as Senior Executive Vice President – Chief People Officer since November 2018. Prior to joining the Company, he served as Executive Vice President, Chief Human Resources Officer of Synchrony Financial from 2013 to November 2018. Previously, Mr. Chini worked for General Electric Company for more than 30 years, including serving as Vice President of Human Resources GE Corporate Staff (2011-2013), Executive Vice President of Human Resources for NBC Universal (2007-2011), Vice President of Human Resources for GE Infrastructure (2005-2006), GE Aviation & Locomotive (2003-2005), and GE Aviation (1998-2003). Prior to beginning his Human Resources career with General Electric in 1984, Mr. Chini served in various Human Resources roles for McGraw-Edison and Liberty Life.

Ratnakar Lavu

Mr. Lavu has served as Senior Executive Vice President – Chief Technology Officer since April 2018. He served as Executive Vice President – Chief Technology Officer from February 2016 to April 2018 and Executive Vice President – Digital Technology from April 2014 to February 2016. He joined the Company as Senior Vice President – Information Technology, Digital Innovation & Global E-Commerce in 2011. Prior to joining the Company, he served as Chief Technology Officer of Redbox Automated Retail LLC from 2009 to 2011. Prior to that, he served in a variety of management positions at Macys.com from 2000 to 2009, including Group Vice President E-Commerce and Information Technology from 2008 to 2009 and Vice President, Technology for Macys.com and Bloomingdales.com from 2006 to 2008. Mr. Lavu has 18 years of experience in the retail industry.

Greg Revelle

Mr. Revelle has served as Senior Executive Vice President – Chief Marketing Officer since April 2018. He joined the Company in April 2017 as Executive Vice President – Chief Marketing Officer. Prior to joining the Company, he served as Executive Vice President, Chief Marketing Officer & General Manager of Financial Services for Best Buy Co., Inc. from November 2014 to March 2017 and Senior Vice President, Chief Marketing Officer & General Manager of E-Commerce at AutoNation from 2012 to November 2014. Prior to that, he worked at Expedia, Inc. as Vice President & General Manager, Worldwide Online Marketing from 2009 to 2012 and Vice President, Corporate Development and Strategy from 2005 to 2009. Before Expedia, Mr. Revelle worked at Credit Suisse as an Investment Banking Analyst. Mr. Revelle has nine years of experience in the online marketing and retail industries. He is currently a director of Cars.com, a digital automotive platform.

PART II

Item 5. Market for Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Market information

Our Common Stock has been traded on the New York Stock Exchange ("NYSE") since May 19, 1992, under the symbol “KSS.”

On February 27, 2019, our Board of Directors approved a 10% increase in our dividend to \$0.67 per common share. The dividend will be paid on April 3, 2019 to shareholders of record as of March 20, 2019. In 2018, we paid aggregate cash dividends of \$400 million.

#### Holdings

As of March 13, 2019, there were approximately 3,700 record holders of our Common Stock.

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## Performance Graph

The graph below compares our cumulative five-year shareholder return to that of the Standard & Poor's ("S&P") 500 Index and a Peer Group Index that is consistent with the retail peer groups used in the Compensation Discussion & Analysis section of our Proxy Statement for our May 15, 2019 Annual Meeting of Shareholders. The Peer Group Index was calculated by S&P Global, a Standard & Poor's business and includes Bed, Bath & Beyond Inc.; The Gap, Inc.; J.C. Penney Company, Inc.; L Brands, Inc.; Macy's, Inc.; Nordstrom, Inc.; Ross Stores, Inc.; Target Corporation; and The TJX Companies, Inc. The Peer Group Index excludes Sears Holding Corporation as they are in bankruptcy proceedings. The Peer Group Index is weighted by the market capitalization of each component company at the beginning of each period. The graph assumes an investment of \$100 on February 1, 2014 and reinvestment of dividends. The calculations exclude trading commissions and taxes.

	Feb 1, 2014	Jan 31, 2015	Jan 30, 2016	Jan 28, 2017	Feb 3, 2018	Feb 2, 2019
Company / Index	2014	2015	2016	2017	2018	2019
Kohl's Corporation	\$100.00	\$121.26	\$104.25	\$85.43	\$146.53	\$159.40
S&P 500 Index	100.00	114.22	113.46	137.14	168.46	168.36
Peer Group Index	100.00	127.95	121.41	113.11	123.50	130.95

## Recent Sales of Unregistered Securities; Use of Proceeds from Registered Securities

We did not sell any equity securities from 2016 through 2018 that were not registered under the Securities Act.

## Purchases of Equity Securities by the Issuer and Affiliated Purchasers

In 2016, our Board of Directors increased the remaining share repurchase authorization under our existing share repurchase program to \$2.0 billion. Purchases under the repurchase program may be made in the open market, through block trades and other negotiated transactions. We expect to execute the share repurchase program primarily in open market transactions, subject to market conditions. There is no fixed termination date for the repurchase program, and the program may be suspended, discontinued or accelerated at any time.

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The following table contains information for shares repurchased and shares acquired from employees in lieu of amounts required to satisfy minimum tax withholding requirements upon the vesting of the employees' restricted stock during the three fiscal months ended February 2, 2019:

Period	Total Number of Shares Purchased During Period	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate
				Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (Dollars in Millions)
November 4 - December 1, 2018	487,226	\$ 72.16	473,087	\$ 1,291
December 2, 2018 – January 5, 2019	846,310	63.31	817,900	1,239
January 6 - February 2, 2019	514,269	68.25	513,740	1,203
Total	1,847,805	\$ 67.00	1,804,727	1,203



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## Item 6. Selected Consolidated Financial Data

The selected consolidated financial data presented below should be read in conjunction with our consolidated financial statements and related notes included elsewhere in this document.

(Dollars in Millions, Except per Share and per Square Foot Data)	2018	2017		2016 (f)	2015 (f)	2014 (f)
		(e)	(f)			
<b>Net sales</b>						
Dollars	\$19,167	\$19,036	\$18,636	\$19,162	\$18,992	
Net sales increase (decrease)	0.7 %	2.1 %	(2.7 )%	0.9 %	(0.1 )%	
Comparable sales (a)	1.7 %	1.5 %	(2.4 )%	0.7 %	(0.3 )%	
Per selling square foot (b)	\$231	\$229	\$224	\$228	\$226	
Total revenue	\$20,229	\$20,084	\$19,681	\$20,151	\$19,921	
Gross margin as a percent of sales	36.4 %	36.0 %	35.9 %	36.0 %	36.3 %	
<b>Selling, general and administrative expenses ("SG&amp;A")</b>						
Dollars	\$5,601	\$5,501	\$5,430	\$5,399	\$5,248	
As a percent of total revenue	27.7 %	27.4 %	27.6 %	26.8 %	26.3 %	
<b>Operating income</b>						
Dollars						
Reported (GAAP)	\$1,361	\$1,416	\$1,183	\$1,553	\$1,689	
Adjusted (non-GAAP) (c)	\$1,465	\$1,416	\$1,369	\$1,553	\$1,689	
As a percent of total revenue						
Reported (GAAP)	6.7 %	7.1 %	6.0 %	7.7 %	8.5 %	
Adjusted (non-GAAP) (c)	7.2 %	7.1 %	7.0 %	7.7 %	8.5 %	
<b>Net income</b>						
Reported (GAAP)	\$801	\$859	\$556	\$673	\$867	
Adjusted (non-GAAP) (c)	\$927	\$703	\$673	\$781	\$867	
<b>Diluted earnings per share</b>						
Reported (GAAP)	\$4.84	\$5.12	\$3.11	\$3.46	\$4.24	
Adjusted (non-GAAP) (c)	\$5.60	\$4.19	\$3.76	\$4.01	\$4.24	
Dividends per share	\$2.44	\$2.20	\$2.00	\$1.80	\$1.56	
<b>Balance sheet</b>						
Total assets	\$12,469	\$13,389	\$13,623	\$13,660	\$14,393	
Working capital	\$2,105	\$2,671	\$2,264	\$2,352	\$2,710	
Long-term debt	\$1,861	\$2,797	\$2,795	\$2,792	\$2,780	
Capital lease and financing obligations	\$1,638	\$1,717	\$1,816	\$1,916	\$1,968	
Shareholders' equity	\$5,527	\$5,419	\$5,170	\$5,484	\$5,983	
<b>Cash flow</b>						
Net cash provided by operating activities	\$2,107	\$1,691	\$2,153	\$1,484	\$2,027	
Capital expenditures	\$578	\$672	\$768	\$690	\$682	
Free cash flow (d)	\$1,403	\$881	\$1,269	\$681	\$1,237	
<b>Kohl's store information</b>						
Number of stores	1,159	1,158	1,154	1,164	1,162	
Total square feet of selling space (in thousands)	82,620	82,804	82,757	83,810	83,750	

(a)

Kohl's store sales are included in comparable sales after the store has been open for 12 full months. Digital sales and sales at remodeled and relocated Kohl's stores are included in comparable sales, unless square footage has changed by more than 10%. 2018 compares the 52 weeks ended February 2, 2019 and February 3, 2018. 2017 compares the 52 weeks ended January 27, 2018 and January 28, 2017.

- (b) Net sales per selling square foot includes in-store and digital merchandise sales.
- (c) Pre-tax adjustments include impairments, store closing and other costs of \$104 million in 2018 and \$186 million in 2016; debt extinguishment losses of \$63 million in 2018 and \$169 million in 2015; and tax settlement and reform benefits of \$156 million in 2017. See GAAP to non-GAAP reconciliation in Results of Operations.
- (d) Free cash flow is a non-GAAP financial measure which we define as net cash provided by operating activities and proceeds from financing obligations less capital expenditures and capital lease and financing obligation payments. See GAAP to non-GAAP reconciliation in Liquidity and Capital Resources.
- (e) Fiscal 2017 was a 53-week year. The impact of the 53<sup>rd</sup> week is approximated as follows: net sales were \$170 million; other revenues were \$10 million; SG&A was \$40 million; interest was \$3 million; net income was \$15 million; and diluted earnings per share were approximately \$0.10.
- (f) Refer to Note 2 of our Consolidated Financial Statements for details on the adoption of the new revenue recognition standard and the impact on previously reported results.

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## Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

## Executive Summary

As of February 2, 2019, we operated 1,159 Kohl's department stores, a website (www.Kohls.com), 12 FILA outlets, and four Off-Aisle clearance centers. Our Kohl's stores and website sell moderately-priced proprietary and national brand apparel, footwear, accessories, beauty and home products. Our Kohl's stores generally carry a consistent merchandise assortment with some differences attributable to local preferences. Our website includes merchandise which is available in our stores, as well as merchandise that is available only online.

Key financial results for 2018 included:

• Sales increased 0.7% to \$19.2 billion reflecting a 1.7% increase in our comparable sales which was partially offset by incremental sales in the 53<sup>rd</sup> week of 2017.

• Gross margin as a percentage of net sales increased 32 basis points as effective inventory management contributed to fewer permanent and promotional markdowns. These increases were partially offset by higher shipping costs resulting from digital sales growth.

• Selling, general and administrative expenses ("SG&A") as a percentage of total revenue increased 30 basis points. The increase was primarily driven by strategic technology investments.

• Net income on a GAAP basis was \$801 million, or \$4.84 per diluted share.

• On a non-GAAP basis, our net income increased 32% to \$927 million and our diluted earnings per share increased 34% to \$5.60.

See "Results of Operations" and "Liquidity and Capital Resources" for additional details about our financial results, how we define comparable sales, and a reconciliation of GAAP to non-GAAP net income and diluted earnings per share.

## 2019 Outlook

Our current expectations for 2019 are as follows:

Comparable sales	Increase 0 - 2%
Gross margin as a percent of sales	Increase up to 10 bps
Selling, general and administrative expenses	Increase 1 - 2%
Depreciation and amortization	\$930 million
Interest expense, net	\$210 million
Effective tax rate	24 - 25%
Earnings per diluted share	\$5.80 - \$6.15
Capital expenditures	\$850 million
Share repurchases	\$400 - \$500 million

This guidance includes the impact of the new lease standard which we are required to adopt in 2019 but excludes any non-recurring charges. For additional details on the lease standard, see Note 1 to our Consolidated Financial Statements.

## Results of Operations

53<sup>rd</sup> Week

Fiscal 2017 was a 53-week year. During the 53<sup>rd</sup> week, net sales were approximately \$170 million; other revenue was approximately \$10 million; SG&A expenses were approximately \$40 million; and interest was approximately \$3 million. The 53<sup>rd</sup> week increased our 2017 net income by approximately \$15 million and our diluted earnings per share by approximately \$0.10. For 2018, comparable sales compare the 52-week periods ended

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February 2, 2019 and February 3, 2018. For 2017, comparable sales compare the 52-week periods ended January 27, 2018 and January 28, 2017.

Net Sales

As an omnichannel retailer, it is often difficult to distinguish between a "store" sale and a "digital" sale. Below is a list of some omnichannel examples:

- Digital customers can choose to have most online orders either shipped to their home or picked up in any of our stores.
  - Approximately 75% of our digital customers also shop in our stores.
  - Digital orders may be shipped from a dedicated E-Commerce fulfillment center, a store, a retail distribution center, third parties or any combination of the above.
  - Stores increase digital sales by providing customers opportunities to view, touch and/or try on physical merchandise before ordering online.
  - Online purchases can easily be returned in our stores.
  - Kohl's Cash coupons and Yes2You rewards can be redeemed online or in store regardless of where they were earned.
  - In-store customers can order from online kiosks in our stores.
  - Customers who utilize our mobile app while in the store may receive mobile coupons to use when they check out.
- Because we do not have a clear distinction between "store" sales and "digital" sales, we do not report them separately.

Kohl's store sales are included in comparable sales after the store has been open for 12 full months. Digital sales and sales at remodeled and relocated Kohl's stores are included in comparable sales unless square footage has changed by more than 10%.

The following graph summarizes net sales dollars and comparable sales (Dollars in Millions):

2018 compared to 2017

Net sales increased \$131 million, or 0.7%, to \$19.2 billion for 2018. The increase was primarily due to a 1.7% increase in comparable sales mostly reflecting higher average transaction values. The increase was partially offset by \$170 million of sales in the 53<sup>rd</sup> week of 2017.

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By line of business, Men's, Children's and Footwear were the strongest categories. Home and Women's also reported positive comparable sales. Accessories was slightly negative.

Geographically, all regions reported higher comparable sales in 2018.

### 2017 compared to 2016

Net sales increased \$400 million, or 2.1%, to \$19.0 billion for 2017. Approximately \$170 million of the increase was due to the 53<sup>rd</sup> week in the fiscal 2017 calendar. The remaining increase was primarily due to a 1.5% increase in comparable sales. The increase in comparable sales reflects higher average transaction values.

By line of business, Home and Footwear were the strongest categories. Men's also outperformed the Company average. Accessories and Children's also reported higher comparable sales. Comparable sales trends in the Women's business improved each quarter, but sales decreased for the year.

Geographically, all regions reported higher comparable sales in 2017.

### Other Revenue

Other revenue includes revenue from credit card operations, third-party advertising on our website, unused gift cards and merchandise return cards (breakage), and other non-merchandise revenue.

The following graph summarizes other revenue (Dollars in Millions):

Other revenue increased \$14 million in 2018 and \$3 million in 2017. The increase in 2018 is due to higher credit card revenue, third-party advertising on our website and breakage. The increase in 2017 is due to \$10 million of revenue earned in the 53<sup>rd</sup> week and higher third-party advertising on our website, partially offset by lower credit card revenue.

### Cost of Merchandise Sold and Gross Margin

Cost of merchandise sold includes the total cost of products sold, including product development costs, net of vendor payments other than reimbursement of specific, incremental and identifiable costs; inventory shrink; markdowns; freight expenses associated with moving merchandise from our vendors to our distribution centers; shipping expenses for digital sales; terms cash discount; and depreciation of product development facilities and equipment. Our cost of merchandise sold may not be comparable with that of other retailers because we include distribution center and buying costs in selling, general and administrative expenses while other retailers may include these expenses in cost of merchandise sold.

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The following graph summarizes cost of merchandise sold and gross margin as a percent of net sales (Dollars in Millions):

Gross margin is calculated as net sales less cost of merchandise sold. Gross margin as a percent of net sales increased 32 basis points in 2018 and 13 basis points in 2017. The increases were driven by effective inventory management which contributed to fewer permanent and promotional markdowns, partially offset by higher shipping costs resulting from digital growth.

Selling, General and Administrative Expenses

SG&A includes compensation and benefit costs (including stores, corporate headquarters, buying and merchandising, and distribution centers); occupancy and operating costs of our retail, distribution and corporate facilities; expenses from our Kohl's credit card operations; freight expenses associated with moving merchandise from our distribution centers to our retail stores and among distribution and retail facilities; marketing expenses, offset by vendor payments for reimbursement of specific, incremental and identifiable costs; and other non-operating revenues and expenses. We do not include depreciation and amortization in SG&A. The classification of these expenses varies across the retail industry.

Many of our expenses, including store payroll and distribution costs, are variable in nature. These costs generally increase as sales increase and decrease as sales decrease. We measure both the change in these variable expenses and the expense as a percent of sales. If the expense as a percent of sales decreased from the prior year, the expense "leveraged". If the expense as a percent of sales increased over the prior year, the expense "deleveraged".

The following graph summarizes the increases and (decreases) in SG&A by expense type (Dollars in Millions):

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SG&A increased \$100 million, or 2%, to \$5.6 billion for 2018. The increase is net of approximately \$40 million of incremental expense in 2017 due to the 53<sup>rd</sup> week in the fiscal 2017 calendar. As a percentage of revenue, SG&A deleveraged by 30 basis points.

The increase in technology expenses reflects higher spend as we migrate technology systems to the cloud. Leadership changes drove the increase in corporate expenses. Distribution costs, which exclude payroll related to online originated orders that were shipped from our stores, were \$312 million for 2018 and increased \$9 million due to higher transportation costs. Marketing costs reflect higher digital and personalization spend. In our stores, increases in expenses driven by omnichannel support of ship-from-store and buy online, pick-up in store operations were offset by productivity improvements. Expenses from our credit card operations decreased due to savings in payroll and operating costs.

The following graph summarizes the increases and (decreases) in SG&A by expense type (Dollars in Millions):

SG&A increased \$71 million, or 1%, to \$5.5 billion for 2017. Approximately \$40 million of the increase was due to the 53<sup>rd</sup> week in the fiscal 2017 calendar. As a percentage of revenue, SG&A leveraged by 20 basis points.

The increase in corporate expenses was driven by higher incentive compensation as a result of our strong financial performance in 2017. The increase in technology expenses reflects higher costs as we migrate to the cloud. Distribution costs, which exclude payroll related to online originated orders that were shipped from our stores, were \$303 million for 2017. The increase of \$23 million was due to growth in digital sales and the opening of our fifth E-Commerce facility. In our stores, decreases in controllable expenses were substantially offset by higher store payroll due to on-going wage pressure and omnichannel support of ship-from-store and buy online, pick-up in store operations. Expenses from our credit card operations decreased due to lower operating costs. Marketing costs reflect efficiencies in our non-customer facing spend and the benefit of not repeating a non-productive marketing event.

## Other Expenses

(Dollars in Millions)	2018	2017	2016
Depreciation and amortization	\$964	\$991	\$938
Interest expense, net	256	299	308
Impairments, store closing and other costs	104	—	186
Loss on extinguishment of debt	63	—	—



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The changes in depreciation and amortization reflect the net impact of lower depreciation due to maturing of our stores, higher amortization due to investments in technology, higher depreciation from our fifth E-Commerce fulfillment center which opened in 2017, and a \$22 million write-off in 2017 of information technology projects that no longer fit into our strategic and cloud migration plans.

The decrease in interest expense in 2018 was driven by the benefits of debt reductions in 2018. Higher interest income due to higher yields and investment balances and lower interest on capital leases as the portfolio matures also contributed to the decreases in both periods.

Impairments, store closing and other costs include the following expenses related to closing four stores, consolidating call center locations which support both Kohl's charge and online customers, a voluntary retirement program, and the impairment of certain assets in 2018. In 2016, the costs related to closing 18 stores and the organizational realignment at our corporate office:

(Dollars in Millions)	2018	2017	2016
Severance, early retirement, and other	\$32	\$ —	\$17
Impairments:			
Buildings and other store assets	36	—	53
Intangible and other assets	36	—	23
Store leases:			
Record future obligations	—	—	114
Write-off net obligations	—	—	(21)
Total	\$104	\$ —	\$186

Loss on the extinguishment of debt of \$63 million in 2018 resulted from a \$413 million make whole call and a \$500 million cash tender offer in 2018.

## Income Taxes

(Dollars in Millions)	2018	2017	2016
Provision for income taxes	\$241	\$258	\$319
Effective tax rate	23.2%	23.1%	36.5%

On December 22, 2017, H.R. 1, originally the Tax Cuts & Jobs Act, was signed into law making significant changes to the Internal Revenue Code. Changes include a corporate rate decrease from 35% to 21%, effective January 1, 2018, as well as a variety of other changes including the acceleration of expensing of certain business assets and reductions in the amount of executive pay that could qualify as a tax deduction.

Our effective tax rate in 2018 includes the full year benefit of the decrease in the corporate rate. For 2017, the reduction in the tax rate was prorated, resulting in a statutory federal tax rate of 33.7%. In 2017, we recorded a total tax benefit of \$136 million related to the federal tax rate reduction and the re-measurement of our deferred tax assets and liabilities as well as a \$20 million benefit from the settlement of a significant state tax dispute. These items reduced our 2017 effective tax rate by 10.9 percentage points.



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## Adjusted Net Income and Earnings per Diluted Share

	Income before Taxes	Net Income	Earnings per Diluted Share
(Dollars in Millions, Except per Share Data)			
2018			
GAAP	\$1,042	\$801	\$4.84
Impairments, store closing and other costs	104	78	0.47
Loss on extinguishment of debt	63	48	0.29
Adjusted (non-GAAP)	\$1,209	\$927	\$5.60
2017			
GAAP	\$1,117	\$859	\$5.12
Federal tax reform benefits	—	(136)	(0.81)
State tax settlement	—	(20)	(0.12)
Adjusted (non-GAAP)	\$1,117	\$703	\$4.19
2016			
GAAP	\$875	\$556	\$3.11
Impairments, store closing and other costs	186	117	0.65
Adjusted (non-GAAP)	\$1,061	\$673	\$3.76

We believe adjusted results are useful because they provide enhanced visibility into our results for the periods excluding the impact of unique items such as those included in the table above. However, these non-GAAP financial measures are not intended to replace GAAP measures.

## Inflation

We expect that our operations will continue to be influenced by general economic conditions, including food, fuel and energy prices, higher wages and by costs to source our merchandise. There can be no assurance that our business will not be impacted by such factors in the future.

## Liquidity and Capital Resources

The following table presents our primary cash requirements and sources of funds.

Cash Requirements	Sources of Funds
<ul style="list-style-type: none"> <li>Operational needs, including salaries, rent, taxes and other costs of running our business</li> <li>Capital expenditures</li> <li>Inventory</li> <li>Share repurchases</li> <li>Dividend payments</li> <li>Debt reduction</li> </ul>	<ul style="list-style-type: none"> <li>Cash flow from operations</li> <li>Short-term trade credit, in the form of extended payment terms</li> <li>Line of credit under our revolving credit facility</li> </ul>

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Our working capital and inventory levels typically build throughout the fall, peaking during the November and December holiday selling season.

The following table includes cash balances and changes:

(Dollars in Millions)	2018	2017	2016
Cash and cash equivalents	\$934	\$1,308	\$1,074
Net cash provided by (used in):			
Operating activities	\$2,107	\$1,691	\$2,153
Investing activities	(572 )	(649 )	(756 )
Financing activities	(1,909)	(808 )	(1,030)
Free cash flow (a)	\$1,403	\$881	\$1,269

(a) Non-GAAP financial measure

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### Operating Activities

Net cash provided by operations increased \$416 million to \$2.1 billion in 2018. The increase was primarily attributable to changes in accounts payable and other operating assets and liabilities.

Net cash provided by operations decreased \$462 million to \$1.7 billion in 2017. The decrease was primarily attributable to changes in accounts payable.

### Investing Activities

Net cash used in investing activities decreased \$77 million to \$572 million in 2018. The decrease was primarily due to the timing of technology spending.

Net cash used in investing activities decreased \$107 million to \$649 million in 2017. The decrease was primarily due to the completion of the beauty rollout, corporate improvements, and new stores in 2016.

The following chart summarizes capital expenditures by major category:

We expect total capital expenditures of approximately \$850 million in fiscal 2019. The increase is driven by omnichannel investments as we construct our sixth E-commerce fulfillment center. The total actual amount of our future capital expenditures will depend on store strategies; construction of and renovations to distribution centers; mix of owned, leased or acquired stores; and technology and corporate spending. We do not anticipate that our capital expenditures will be limited by any restrictive covenants in our financing agreements.

### Financing Activities

Net cash used in financing activities increased \$1.1 billion to \$1.9 billion in 2018, primarily due to \$943 million of debt reductions during the year.

Net cash used in financing activities decreased \$222 million to \$808 million in 2017, primarily due to a \$251 million decrease in treasury stock purchases. Share repurchases are discretionary in nature. The timing and amount of repurchases are based upon available cash balances, our stock price and other factors.

We may again seek to retire or purchase our outstanding debt through open market cash purchases, privately negotiated transactions or otherwise. Such repurchases, if any, will depend on prevailing market conditions, our liquidity requirements, contractual restrictions and other factors. The amounts involved could be material.

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As of February 2, 2019, our credit ratings were as follows:

	Moody's	Standard & Poor's	Fitch
Long-term debt	Baa2	BBB-	BBB

During 2018, we paid cash dividends of \$400 million as detailed in the following table:

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Declaration date	February 28	May 16	August 14	November 14
Record date	March 14	June 13	September 12	December 12
Payment date	March 28	June 27	September 26	December 26
Amount per common share	\$ 0.61	\$ 0.61	\$ 0.61	\$ 0.61

On February 27, 2019, our Board of Directors declared a quarterly cash dividend on our common stock of \$0.67 per share, a 10% increase over our prior dividend. The dividend is payable April 3, 2019 to shareholders of record at the close of business on March 20, 2019.

## Free Cash Flow

We generated \$1.4 billion of free cash flow for 2018; an increase of \$522 million, or 59%, over 2017. As discussed above, the increase is primarily the result of changes in operating assets and liabilities. Free cash flow is a non-GAAP financial measure which we define as net cash provided by operating activities and proceeds from financing obligations (which generally represent landlord reimbursements of construction costs) less capital expenditures and capital lease and financing obligation payments. Free cash flow should be evaluated in addition to, and not considered a substitute for, other financial measures such as net income and net cash provided by operating activities. We believe that free cash flow represents our ability to generate additional cash flow from our business operations. See the key financial ratio calculations section below.

## Liquidity Ratios

The following table provides additional measures of our liquidity:

(Dollars in Millions)	2018	2017
Working capital	\$2,105	\$2,671
Current ratio	1.77	1.99

Liquidity measures our ability to meet short-term cash needs. Working capital decreased \$566 million and our current ratio decreased 22 basis points over year-end 2017 primarily due to lower cash balances as a result of debt reductions.

## Return on Investment Ratios

The following table provides additional measures of our return on investments:

2018	2017	2016
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Return on assets ("ROA")	6.1 %	6.4 %	4.1 %
Return on gross investment ("ROI") (a)	13.4%	14.0%	12.6%
Excluding non-recurring items (a)			
ROA	7.0 %	5.2 %	4.9 %
ROI	14.0%	14.0%	13.6%

(a) Non-GAAP financial measures

Changes in earnings drove changes in our return on investment ratios.

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We believe that ROI is a useful financial measure in evaluating our operating performance. When analyzed in conjunction with our net earnings and total assets and compared with the return on assets, it provides investors with a useful tool to evaluate our ongoing operations and our management of assets from period to period. ROI is a non-GAAP financial measure which we define as earnings before interest, taxes, depreciation, amortization and rent (“EBITDAR”) divided by average gross investment. Our ROI calculation may not be comparable to similarly titled measures reported by other companies. ROI should be evaluated in addition to, and not considered a substitute for, other financial measures such as return on assets. See the key financial ratio calculations below for our ROI and ROA and ROI excluding non-recurring items calculations.

## Capital Structure Ratios

The following table provides additional measures of our capital structure:

	2018	2017
Debt/capitalization	38.8%	45.4%
Adjusted debt to adjusted EBITDAR (a)	2.16	2.54

(a) Non-GAAP financial measure

The decreases in our capital structure ratios are primarily due to debt reductions in 2018.

Adjusted Debt to EBITDAR is a non-GAAP financial measure which we define as our adjusted outstanding debt balance divided by adjusted EBITDAR. We believe that our debt levels are best analyzed using this measure. Our current goals are to maintain a ratio that demonstrates our commitment to an investment grade rating and allows us to operate with an efficient capital structure for our size, growth plans and industry. Our Adjusted Debt to EBITDAR calculation may not be comparable to similarly-titled measures reported by other companies. Adjusted Debt to EBITDAR should be evaluated in addition to, and not considered a substitute for, other financial measures such as debt/capitalization. See the key financial ratio calculations section below for our Adjusted Debt to EBITDAR calculation.

Our debt agreements contain various covenants including limitations on additional indebtedness and a maximum permitted debt ratio. As of February 2, 2019, we were in compliance with all debt covenants and expect to remain in compliance during 2019. See the key financial ratio calculations section below for our debt covenant calculation.

## Key Financial Ratio Calculations

The following tables include our ROA and ROI calculations. All ratios except ROA are non-GAAP financial measures.

(Dollars in Millions)	2018	2017	2016
Net income	\$801	\$859	\$556



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Impairments, store closing and other costs	78	-	117
Loss on extinguishment of debt	48	-	-
Federal tax reform benefits	-	(136 )	-
State tax settlement	-	(20 )	-
Adjusted net income	927	703	673
Average total assets (a)	\$13,161	\$13,467	\$13,637
ROA (b)	6.1	% 6.4	% 4.1
Adjusted ROA (b)	7.0	% 5.2	% 4.9

(a) Represents average of five most recent quarter-end balances.

(b) Net income or adjusted net income, as applicable, divided by average total assets.

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(Dollars in Millions)	2018	2017	2016
Operating income	\$1,361	\$1,416	\$1,183
Depreciation and amortization	964	991	938
Rent expense	301	293	276
EBITDAR	2,626	2,700	2,397
Impairments, store closing and other costs	104	-	186
Adjusted EBITDAR	\$2,730	\$2,700	\$2,583
Average: (a)			
Total assets	\$13,161	\$13,467	\$13,637
Cash equivalents and long-term investments (b)	(753 )	(629 )	(476 )
Other assets	(33 )	(32 )	(35 )
Accumulated depreciation and amortization	7,812	7,217	6,558
Accounts payable	(1,580 )	(1,548 )	(1,515 )
Accrued liabilities	(1,235 )	(1,213 )	(1,252 )
Other long-term liabilities	(658 )	(674 )	(620 )
Capitalized rent (c)	2,831	2,767	2,654
Gross investment ("AGI")	\$19,545	\$19,355	\$18,951
ROI (d)	13.4 %	14.0 %	12.6 %
Adjusted ROI (d)	14.0 %	14.0 %	13.6 %

(a) Represents average of five most recent quarter-end balances

(b) Represents excess cash not required for operations

(c) Represents ten times store rent and five times equipment/other rent

(d) EBITDAR or adjusted EBITDAR, as applicable, divided by gross investment

The following table reconciles net cash provided by operating activities (a GAAP measure) to free cash flow (a non-GAAP measure):

(Dollars in Millions)	2018	2017	2016
Net cash provided by operating activities	\$2,107	\$1,691	\$2,153
Acquisition of property and equipment	(578 )	(672 )	(768 )
Capital lease and financing obligation payments	(126 )	(138 )	(127 )
Proceeds from financing obligations	-	-	11
Free cash flow	\$1,403	\$881	\$1,269

The following table includes our debt/capitalization and Adjusted Debt to Adjusted EBITDAR calculations:

(Dollars in Millions)	2018	2017
Capital lease and financing obligations	\$1,638	\$1,717
Long-term debt	1,861	2,797
Debt	3,499	4,514
Equity	5,527	5,419
Capitalization	\$9,026	\$9,933
Debt/capitalization	38.8 %	45.4 %
Total debt	\$3,499	\$4,514

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Rent x 8	2,408	2,344
Adjusted debt	\$5,907	\$6,858
Operating income	\$1,361	\$1,416
Depreciation and amortization	964	991
Rent expense	301	293
EBITDAR	2,626	2,700
Impairments, store closing and other costs	104	-
Adjusted EBITDAR	\$2,730	\$2,700
Adjusted debt to adjusted EBITDAR	2.16	2.54

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The following table includes our debt ratio calculation, as defined by our debt agreements:

(Dollars in Millions)	2018
Included Indebtedness	
Consolidated indebtedness	\$3,511
Permitted exclusions for L/C obligations	-
Permitted exclusions for unamortized debt discount	(2 )
Subtotal	3,509
Rent x 8	2,408
Included indebtedness	\$5,917
Debt Compliance EBITDAR	
Net income	\$801
Impairments, store closing and other costs	104
Interest charges	256
Income taxes	241
Depreciation and amortization	964
Loss on extinguishment of debt	63
Capital losses from the disposition of fixed assets	-
Other non-cash expenses reducing net income	100
Subtotal	2,529
Non-cash items increasing net income	(7 )
Capital gains from the disposition of fixed assets	(1 )
Subtotal	2,521
Rent	301
Consolidated EBITDAR	\$2,822
Debt ratio (a)	2.10
Maximum permitted debt ratio	3.75

(a) Included Indebtedness divided by Consolidated EBITDAR

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## Contractual Obligations

Our contractual obligations as of February 2, 2019 were as follows:

(Dollars in Millions)	Maturing in:				
	Total	2019	2020 and 2021	2022 and 2023	2024 and after
<b>Recorded contractual obligations:</b>					
Outstanding long-term debt	\$ 1,873	\$—	\$—	\$534	\$ 1,339
Capital lease and financing obligations	1,157	103	218	170	666
	3,030	103	218	704	2,005
<b>Unrecorded contractual obligations:</b>					
<b>Interest payments:</b>					
Long-term debt	1,169	89	177	171	732
Capital lease and financing obligations	2,054	157	286	250	1,361
Operating leases (a)	4,977	275	535	498	3,669
Other (b)	856	386	275	142	53
	9,056	907	1,273	1,061	5,815
<b>Total</b>	<b>\$ 12,086</b>	<b>\$ 1,010</b>	<b>\$ 1,491</b>	<b>\$ 1,765</b>	<b>\$ 7,820</b>

(a) Our leases typically require that we pay taxes, insurance and maintenance costs in addition to the minimum rental payments included in the table above. Such costs vary from period to period and totaled \$183 million for 2018, \$184 million for 2017, and \$179 million for 2016. The lease term includes cancelable option periods where failure to exercise such options would result in an economic penalty.

(b) Other includes royalties, legally binding minimum lease and interest payments for stores opening in 2019 or later, as well as payments associated with technology and marketing agreements.

## Off-Balance Sheet Arrangements

We have not provided any financial guarantees as of year-end 2018.

We have not created, and are not party to, any special-purpose or off-balance sheet entities for the purpose of raising capital, incurring debt or operating our business. We do not have any arrangements or relationships with entities that are not consolidated into the financial statements that are reasonably likely to materially affect our financial condition, liquidity, results of operations or capital resources.

## Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires us to make estimates and assumptions that affect the reported amounts. Management has discussed the development, selection and disclosure of these estimates and assumptions with the Audit Committee of our Board of Directors. There have been no significant changes in the critical accounting policies and estimates discussed in our 2018 Form 10-K.

### Retail Inventory Method and Inventory Valuation

Merchandise inventories are valued at the lower of cost or market using the retail inventory method (“RIM”). Under RIM, the valuation of inventory at cost and the resulting gross margins are calculated by applying a cost-to-retail ratio to the retail value of inventory. RIM is an averaging method that has been widely used in the retail industry due to its practicality. The use of RIM will result in inventory being valued at the lower of cost or market since permanent markdowns are taken as a reduction of the retail value of inventories. We would record an additional reserve if the future estimated selling price is less than cost.

RIM inherently requires management judgment and estimates, such as the amount and timing of permanent markdowns to clear unproductive or slow-moving inventory, which may impact the ending inventory valuation as well

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as gross margin. Factors considered in the determination of permanent markdowns include current and anticipated demand, customer preferences, age of the merchandise, fashion trends and weather conditions.

Inventory shrinkage is estimated as a percent of sales for the period between the last physical inventory count and the balance sheet date. Shrink is the difference between the recorded amount of inventory and the physical inventory. We perform an annual physical inventory count at the majority of our stores and distribution centers. The shrinkage rate from the most recent physical inventory, in combination with current events and historical experience, is used as the standard for the shrinkage accrual rate for the next inventory cycle. Historically, our actual physical inventory count results have shown our estimates to be reliable.

### Vendor Allowances

We frequently receive allowances from our vendors for discounts that we have taken in order to sell the vendor's merchandise and/or to support gross margins earned on those sales. This markdown support generally relates to sold inventory or permanent markdowns and, accordingly, is reflected as a reduction to cost of merchandise sold. Markdown support related to merchandise that has not yet been sold is recorded in inventory.

We also receive support from vendors for marketing and other costs that we have incurred to sell the vendors' merchandise. To the extent the reimbursements are for specific, incremental and identifiable costs incurred to sell the vendor's products and do not exceed the costs incurred, they are recognized as a reduction of selling, general, and administrative expenses. If these criteria are not met, the support is recorded in inventory and reflected as a reduction of costs of merchandise sold when the related merchandise is sold.

### Insurance Reserve Estimates

We are primarily self-insured for costs related to workers' compensation, general liability, and employee-related health care benefits. We use a third-party actuary to estimate the liabilities associated with these risks. The actuary considers historical claims experience, demographic and severity factors, health care trends, and actuarial assumptions to estimate the liabilities associated with these risks. Historically, our actuarial estimates have not been materially different from actual results.

### Impairment of Long-Lived Assets

We review our long-lived assets for impairment when events or changes in circumstances, such as decisions to close a store or significant operating losses, indicate the carrying value of the asset may not be recoverable. All long-lived assets are reviewed for impairment at least annually.

If our evaluations, which are performed on an undiscounted cash flow basis, indicate that the carrying amount of the asset may not be recoverable, the potential impairment is measured as the excess of carrying value over the fair value of the impaired asset.

Identifying impaired assets and quantifying the related impairment loss, if any, requires significant estimates by management. The most significant of these estimates is the cash flow expected to result from the use and eventual disposition of the asset. When determining the stream of projected future cash flows associated with an individual store, management estimates future store performance including sales, gross margin, and controllable expenses, such as store payroll and occupancy expense. Projected cash flows must be estimated for future periods throughout the remaining life of the property, which may be as many as 40 years in the future. The accuracy of these estimates will be impacted by a number of factors including general economic conditions, changes in competitive landscape and our ability to effectively manage the operations of the store.

Other than stores which we have closed and the trademark that was impaired in the fourth quarter of 2018, we have not historically experienced any significant impairment of long-lived assets. Additionally, impairment of an

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individual building and related improvements, net of accumulated depreciation, would not generally be material to our financial results.

### Store Closure Reserve

In 2016, we closed numerous leased stores prior to their scheduled lease expiration. In addition to future rent obligations, the closed store reserve includes estimates for operating and other expenses expected to be incurred over the remaining lease term, some of which extend through January 2030.

### Income Taxes

We regularly evaluate the likelihood of realizing the benefit for income tax positions we have taken in various federal and state filings by considering all relevant facts, circumstances and information available to us. If we believe it is more likely than not that our position will be sustained, we recognize a benefit at the largest amount which we believe is cumulatively greater than 50% likely to be realized.

Unrecognized tax benefits require significant management judgment regarding applicable statutes and their related interpretation, the status of various income tax audits and our particular facts and circumstances. Also, as audits are completed or statutes of limitations lapse, it may be necessary to record adjustments to our taxes payable, deferred tax assets, tax reserves or income tax expense. Although we believe we have adequately reserved for our uncertain tax positions, no assurance can be given that the final tax outcome of these matters will not be different.

### Leases

Accounting for leased properties requires compliance with technical accounting rules and significant judgment by management. Application of these accounting rules and assumptions made by management will determine whether we are considered the owner for accounting purposes or whether the lease is accounted for as a capital or operating lease.

If we are considered the owner for accounting purposes or the lease is considered a capital lease, we record the property and related financing or capital lease obligation on our balance sheet. The asset is then depreciated over its expected lease term. Rent payments for these properties are recognized as interest expense and a reduction of the financing or capital lease obligation.

If the lease is considered an operating lease, it is not recorded on our balance sheet and rent expense is recognized on a straight-line basis over the expected lease term.

The most significant estimates used by management in accounting for property leases and the impact of these estimates are as follows:

**Expected lease term**—Our expected lease term includes both contractual lease periods and cancelable option periods where failure to exercise such options would result in an economic penalty. The expected lease term is used in determining whether the lease is accounted for as an operating lease or a capital lease. A lease is considered a capital lease if the lease term exceeds 75% of the leased asset's useful life. The expected lease term is also used in determining the depreciable life of the asset or the straight-line rent recognition period. Increasing the expected lease term will increase the probability that a lease will be considered a capital lease and will generally result in higher rent expense for an operating lease and higher interest and depreciation expenses for a leased property recorded on our balance sheet.

**Incremental borrowing rate**—We estimate our incremental borrowing rate using treasury rates for debt with maturities comparable to the expected lease term plus our credit spread. The incremental borrowing rate is primarily used in

determining whether the lease is accounted for as an operating lease or a capital lease. A lease is considered a capital lease if the net present value of the lease payments is greater than 90% of the

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fair market value of the property. Increasing the incremental borrowing rate decreases the net present value of the lease payments and reduces the probability that a lease will be considered a capital lease. For leases which are recorded on our balance sheet with a related capital lease or financing obligation, the incremental borrowing rate, subject to certain limitations, is also used in allocating our rental payments between interest expense and a reduction of the outstanding obligation.

**Fair market value of leased asset**—The fair market value of leased retail property is generally estimated based on comparable market data as provided by third-party appraisers or consideration received from the landlord. Fair market value is used in determining whether the lease is accounted for as an operating lease or a capital lease. A lease is considered a capital lease if the net present value of the lease payments is greater than 90% of the fair market value of the property. Increasing the fair market value reduces the probability that a lease will be considered a capital lease. Fair market value is also used in determining the amount of property and related financing obligation to be recognized on our balance sheet for certain leased properties which are considered owned for accounting purposes.

**Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

All of our long-term debt at year-end 2018 is at fixed interest rates and, therefore, is not affected by changes in interest rates. When our long-term debt instruments mature, we may refinance them at the existing market interest rates, which may be more or less than interest rates on the maturing debt.

We share in the net risk-adjusted revenue of the Kohl's credit card portfolio as defined by the sum of finance charges, late fees and other revenue less write-offs of uncollectible accounts. We also share the costs of funding the outstanding receivables as interest rates exceed defined rates. As a result, our share of profits from the credit card portfolio may be negatively impacted by increases in interest rates. The reduced profitability, if any, will be impacted by various factors, including our ability to pass higher funding costs on to the credit card holders and the outstanding receivable balance. Recent increases in interest rates have not had a material impact on our financial results. The impact of future increases, if any, cannot be reasonably estimated at this time.

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## Item 8. Financial Statements and Supplementary Data

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Schedules have been omitted as they are not applicable.

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and the Board of Directors of Kohl's Corporation

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of Kohl's Corporation (the "Company") as of February 2, 2019 and February 3, 2018, the related consolidated statements of income, changes in shareholders' equity and cash flows, for each of the three years in the period ended February 2, 2019, and the related notes (collectively referred to as the "consolidated financial statements"). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company at February 2, 2019 and February 3, 2018, and the results of its operations and its cash flows for each of the three years in the period ended February 2, 2019, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the Company's internal control over financial reporting as of February 2, 2019, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) and our report dated March 22, 2019 expressed an unqualified opinion thereon.

Adoption of ASU No. 2014-09

As discussed in Note 2 to the consolidated financial statements, the Company changed its method of accounting for revenue recognition in each of the three years in the period ended February 2, 2019 due to the adoption of ASU No. 2014-09, Revenue from Contracts with Customers.

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ Ernst & Young LLP

We have served as the Company's auditor since 1986.

Milwaukee, Wisconsin

March 22, 2019



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## KOHL'S CORPORATION

## CONSOLIDATED BALANCE SHEETS

	February 2, February 3,	
(Dollars in Millions)	2019	2018
		As Adjusted (a)
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$934	\$1,308
Merchandise inventories	3,475	3,542
Other	426	530
Total current assets	4,835	5,380
Property and equipment, net	7,428	7,773
Other assets	206	236
Total assets	\$12,469	\$13,389
<b>Liabilities and Shareholders' Equity</b>		
Current liabilities:		
Accounts payable	\$1,187	\$1,271
Accrued liabilities	1,364	1,213
Income taxes payable	64	99
Current portion of capital lease and financing obligations	115	126
Total current liabilities	2,730	2,709
Long-term debt	1,861	2,797
Capital lease and financing obligations	1,523	1,591
Deferred income taxes	184	211
Other long-term liabilities	644	662
Shareholders' equity:		
Common stock - 374 and 373 million shares issued	4	4
Paid-in capital	3,204	3,078
Treasury stock, at cost, 211 and 205 million shares	(11,076)	(10,651)
Accumulated other comprehensive loss	—	(11)
Retained earnings	13,395	12,999
Total shareholders' equity	\$5,527	\$5,419
Total liabilities and shareholders' equity	\$12,469	\$13,389

(a) Refer to Note 2 for details on the adoption of the new revenue recognition accounting standard and the impact on previously reported results.

See accompanying Notes to Consolidated Financial Statements

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KOHL'S CORPORATION

CONSOLIDATED STATEMENTS OF INCOME

(Dollars in Millions, Except per Share Data)	2018	2017	2016
		As Adjusted (a)	As Adjusted (a)
Net sales	\$ 19,167	\$ 19,036	