

KROGER CO
Form 10-K/A
April 18, 2005

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K/A

Amendment No. 1

(Mark One)

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

For the Fiscal year ended January 29, 2005.

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 1-303

THE KROGER CO.

(Exact name of registrant as specified in its charter)

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Ohio
(State or other jurisdiction of
incorporation or organization)

31-0345740
(I.R.S. Employer
Identification No.)

1014 Vine Street, Cincinnati, OH 45202
(Address of principal executive offices)

45202
(Zip Code)

Registrant's telephone number, including area code (513) 762-4000

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

<u>Title of each class</u>	<u>Name of each exchange on which registered</u>
Common Stock \$1 par value 728,772,101 shares outstanding on April 8, 2005	New York Stock Exchange

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

NONE

(Title of class)

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Exchange Act Rule 12b-2).

Yes No

The aggregate market value of the Common Stock of The Kroger Co. held by non-affiliates as of April 8, 2005: \$11,616,627,274

Documents Incorporated by Reference:

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Proxy statement to be filed pursuant to Regulation 14A of the Exchange Act on or before May 31, 2005, incorporated by reference into Parts II and III of Form 10-K.

EXPLANATORY NOTE:

This Amendment No. 1 to Form 10-K is filed solely to insert a conformed signature to the Report of Independent Registered Public Accounting Firm appearing in Item 8, which conformed signature inadvertently was omitted from the original filing.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Report of Independent Registered Public Accounting Firm

To the Shareowners and Board of Directors of The Kroger Co.:

We have completed an integrated audit of The Kroger Co.'s January 29, 2005 consolidated financial statements and of its internal control over financial reporting as of January 29, 2005 and audits of its January 31, 2004 and February 1, 2003 consolidated financial statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Our opinions, based on our audits, are presented below.

Consolidated financial statements

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, cash flows and changes in shareowners' equity present fairly, in all material respects, the financial position of The Kroger Co. and its subsidiaries at January 29, 2005 and January 31, 2004, and the results of their operations and their cash flows for each of the three years in the period ended January 29, 2005 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit of financial statements includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in note 19 to the consolidated financial statements, the Company adopted the provisions of Statement of Financial Accounting Standards No. 145, Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections, as of February 2, 2003. As discussed in notes 1 and 5 to the consolidated financial statements, the Company also adopted the provisions of Statement of Financial Accounting Standards No. 142, Goodwill and Other Intangible Assets, as of February 3, 2002, and Emerging Issues Task Force Issue No. 02-16, Accounting by a Customer (including a Reseller) for Certain Consideration Received from a Vendor, as of January 1, 2003.

Internal control over financial reporting

Also, we have audited management's assessment, included in the accompanying Management's Annual Report on Internal Control Over Financial Reporting appearing in Item 9A, that The Kroger Co. did not maintain effective internal controls over financial reporting as of January 29, 2005, because the Company did not maintain effective control over the determination of deferred income tax balances related to a business combination, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations (COSO). The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express opinions on management's assessment and on the effectiveness of the Company's internal control over financial reporting based on our audit.

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We conducted our audit of internal control over financial reporting in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. An audit of internal control over financial reporting includes obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we consider necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

A material weakness is a control deficiency, or combination of control deficiencies, that results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected. The following material weakness has been identified and included in management's assessment. As of January 29, 2005, the Company did not maintain effective controls over the determination of deferred income tax balances related to a business combination. Specifically, controls over the processes and procedures in calculating deferred income tax liabilities related to a business combination were not effective to ensure that the deferred income tax liabilities and allocated goodwill were fairly stated in accordance with generally accepted accounting principles. This deficiency resulted in a year-end audit adjustment affecting deferred income tax liabilities, goodwill and the goodwill impairment charge. Therefore, the Company concluded that this control deficiency constitutes a material weakness. This material weakness was considered in determining the nature, timing, and extent of audit tests applied in our audit of the January 29, 2005 consolidated financial statements, and our opinion regarding the effectiveness of the Company's internal control over financial reporting does not affect our opinion on those consolidated financial statements.

In our opinion, management's assessment that The Kroger Co. did not maintain effective internal control over financial reporting as of January 29, 2005, is fairly stated, in all material respects, based on *Internal Control - Integrated Framework* issued by the COSO. Also, in our opinion, because of the effect of the material weakness described above on the achievement of the objectives of the control criteria, The Kroger Co. has not maintained effective internal control over financial reporting as of January 29, 2005, based on *Internal Control - Integrated Framework* issued by the COSO.

/s/ PricewaterhouseCoopers LLP

Cincinnati, Ohio

April 15, 2005

THE KROGER CO.
CONSOLIDATED BALANCE SHEETS

(In millions)	January 29, 2005	January 31, 2004
ASSETS		
Current assets		
Cash and temporary cash investments	\$ 144	\$ 159
Deposits In-Transit	506	579
Receivables	661	674
Receivables - Taxes	167	66
FIFO Inventory	4,729	4,493
LIFO Credit	(373)	(324)
Prefunded employee benefits	300	300
Prepaid and other current assets	272	251
Total current assets	<u>6,406</u>	<u>6,198</u>
Property, plant and equipment, net	11,497	11,178
Goodwill, net	2,191	3,134
Fair value interest rate hedges		6
Other assets	397	247
Total Assets	<u>\$ 20,491</u>	<u>\$ 20,763</u>
LIABILITIES		
Current liabilities		
Current portion of long-term debt including obligations under capital leases and financing obligations	\$ 71	\$ 248
Accounts payable	3,778	3,637
Accrued salaries and wages	659	547
Deferred income taxes	267	138
Other current liabilities	1,541	1,595
Total current liabilities	<u>6,316</u>	<u>6,165</u>
Long-term debt including obligations under capital leases and financing obligations		
Face value long-term debt including obligations under capital leases and financing obligations	7,830	8,012
Adjustment to reflect fair value interest rate hedges	70	104
Long-term debt including obligations under capital leases and financing obligations	<u>7,900</u>	<u>8,116</u>
Deferred income taxes	939	974
Other long-term liabilities	1,796	1,523
Total Liabilities	<u>16,951</u>	<u>16,778</u>
Commitments and Contingencies		
SHAREOWNERS EQUITY		
Preferred stock, \$100 par, 5 shares authorized and unissued		
Common stock, \$1 par, 1,000 shares authorized: 918 shares issued in 2004 and 913 shares issued in 2003	918	913
Additional paid-in capital	2,432	2,382
Accumulated other comprehensive loss	(202)	(124)
Accumulated earnings	3,541	3,641
Common stock in treasury, at cost, 190 shares in 2004 and 170 shares in 2003	(3,149)	(2,827)

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Total Shareowners' Equity	<u>3,540</u>	<u>3,985</u>
Total Liabilities and Shareowners' Equity	<u>\$ 20,491</u>	<u>\$ 20,763</u>

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

THE KROGER CO.

CONSOLIDATED STATEMENTS OF OPERATIONS

Years Ended January 29, 2005, January 31, 2004, and February 1, 2003

(In millions, except per share amounts)	2004 (52 weeks)	2003 (52 weeks)	2002 (52 weeks)
Sales	\$ 56,434	\$ 53,791	\$ 51,760
Merchandise costs, including advertising, warehousing, and transportation, excluding items shown separately below	42,140	39,637	37,810
Operating, general and administrative	10,611	10,354	9,618
Rent	680	657	660
Depreciation and amortization	1,256	1,209	1,087
Goodwill impairment charge	900	444	
Asset impairment charges		120	
Restructuring charges			15
Merger-related costs			1
Operating Profit	847	1,370	2,569
Interest expense	557	604	619
Earnings before income tax expense and cumulative effect of accounting change	290	766	1,950
Income tax expense	390	454	732
Earnings (loss) before cumulative effect of accounting change	(100)	312	1,218
Cumulative effect of an accounting change, net of income tax benefit of \$10 in 2002			(16)
Net earnings (loss)	\$ (100)	\$ 312	\$ 1,202
Earnings (loss) per basic common share:			
Earnings (loss) before cumulative effect of accounting change	\$ (0.14)	\$ 0.42	\$ 1.56
Cumulative effect of an accounting change, net of income tax benefit			(0.02)
Net earnings (loss)	\$ (0.14)	\$ 0.42	\$ 1.54
Average number of common shares used in basic calculation	736	747	779
Earnings (loss) per diluted common share:			
Earnings (loss) before cumulative effect of accounting change	\$ (0.14)	\$ 0.41	\$ 1.54
Cumulative effect of an accounting change, net of income tax benefit			(0.02)
Net earnings (loss)	\$ (0.14)	\$ 0.41	\$ 1.52
Average number of common shares used in diluted calculation	736	754	791

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

THE KROGER CO.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years Ended January 29, 2005, January 31, 2004 and February 1, 2003

<u>(In millions)</u>	<u>2004</u> <u>(52 weeks)</u>	<u>2003</u> <u>(52 weeks)</u>	<u>2002</u> <u>(52 weeks)</u>
Cash Flows From Operating Activities:			
Net earnings (loss)	\$ (100)	\$ 312	\$ 1,202
Adjustments to reconcile net earnings (loss) to net cash provided by operating activities:			
Cumulative effect of an accounting change, net of income tax benefit of \$10 in 2002			16
Depreciation and amortization	1,256	1,209	1,087
LIFO charge (credit)	49	34	(50)
Merger-related costs			1
Goodwill impairment charge	857	444	
Asset impairment charges		120	
Item-cost conversion			91
EITF 02-16 adoption			28
Deferred income taxes	230	329	468
Other	59	22	38
Changes in operating assets and liabilities net of effects from acquisitions of businesses:			
Store deposits in-transit	73	(363)	77
Inventories	(236)	(20)	(62)
Receivables	13	3	2
Prepaid expenses	(31)	5	(34)
Accounts payable	167	44	282
Accrued expenses	104	224	(4)
Income taxes receivable (payable)	(86)	(62)	(11)
Contribution to company sponsored pension plans	(35)	(100)	
Other	10	14	52
Net cash provided by operating activities	2,330	2,215	3,183
Cash Flows From Investing Activities:			
Capital expenditures, excluding acquisitions	(1,615)	(2,000)	(1,891)
Capital expenditures, lease-financing transactions	(6)		
Capital expenditures, sale-leaseback transactions	(13)		
Proceeds from sale of assets	86	68	90
Payments for acquisitions, net of cash acquired	(25)	(87)	(126)
Other	(35)	(7)	20
Net cash used by investing activities	(1,608)	(2,026)	(1,907)
Cash Flows From Financing Activities:			
Proceeds from issuance of long-term debt	616	347	1,353
Proceeds from lease-financing transactions	6		
Reductions in long-term debt	(1,010)	(487)	(1,757)
Debt prepayment costs	(25)	(17)	(14)
Financing charges incurred	(5)	(3)	(16)
Proceeds from issuance of capital stock	25	39	41

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Treasury stock purchases	(319)	(301)	(785)
Cash received from interest rate swap terminations		114	
Increase (decrease) in book overdrafts	(25)	107	(88)
	<u> </u>	<u> </u>	<u> </u>
Net cash used by financing activities	(737)	(201)	(1,266)
Net increase (decrease) in cash and temporary cash investments	(15)	(12)	10
Cash and temporary cash investments:			
Beginning of year	159	171	161
	<u> </u>	<u> </u>	<u> </u>
End of year	\$ 144	\$ 159	\$ 171
	<u> </u>	<u> </u>	<u> </u>
Disclosure of cash flow information:			
Cash paid during the year for interest	\$ 590	\$ 589	\$ 585
Cash paid during the year for income taxes	\$ 206	\$ 139	\$ 268
Non-cash changes related to purchase acquisitions:			
Fair value of inventory acquired	\$	\$ 8	\$ 4
Fair value of other assets acquired	\$ 20	\$ 71	\$ 120
Goodwill recorded	\$ 6	\$ 9	\$ 9
Liabilities assumed	\$ (1)	\$ (1)	\$ (7)

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

THE KROGER CO.

CONSOLIDATED STATEMENT OF CHANGES IN SHAREOWNERS EQUITY

Years Ended January 29, 2005, January 31, 2004 and February 1, 2003

(In millions)	Common Stock		Additional Paid-In Capital	Treasury Stock		Accumulated Other Comprehensive Gain (Loss)	Accumulated Earnings	Total
	Shares	Amount		Shares	Amount			
Balances at February 2, 2002	901	\$ 901	\$ 2,217	106	\$(1,730)	\$ (33)	\$ 2,127	\$ 3,482
Issuance of common stock:								
Stock options and warrants exercised	6	6	35					41
Restricted stock issued	1	1	15					16
Treasury stock purchases, at cost								
Treasury stock purchases, at cost				43	(785)			(785)
Stock options and restricted stock exchanged				1	(6)			(6)
Tax benefits from exercise of stock options and warrants			50					50
Other comprehensive loss, net of income tax of \$102						(173)		(173)
Net earnings							1,202	1,202
Balances at February 1, 2003	908	908	2,317	150	(2,521)	(206)	3,329	3,827
Issuance of common stock:								
Stock options and warrants exercised	4	4	35					39
Restricted stock issued	1	1	9					10
Treasury stock activity:								
Treasury stock purchases, at cost				19	(301)			(301)
Stock options and restricted stock exchanged				1	(5)			(5)
Tax benefits from exercise of stock options and warrants			21					21
Other comprehensive gain, net of income tax of \$(49)						82		82
Net earnings							312	312
Balances at January 31, 2004	913	913	2,382	170	(2,827)	(124)	3,641	3,985
Issuance of common stock:								
Stock options and warrants exercised	4	4	25					29
Restricted stock issued	1	1	9					10
Treasury stock activity:								
Treasury stock purchases, at cost				18	(294)			(294)
Stock options and restricted stock exchanged				2	(28)			(28)
Tax benefits from exercise of stock options and warrants			16					16
Other comprehensive loss net of income tax of \$47						(78)		(78)
Net loss							(100)	(100)
Balances at January 29, 2005	918	\$ 918	\$ 2,432	190	\$(3,149)	\$ (202)	\$ 3,541	\$ 3,540

Comprehensive income:

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Net earnings (loss)	\$ (100)	\$ 312	\$ 1,202
Reclassification adjustment for losses included in net earnings (loss), net of income tax of \$(14) in 2003 and \$(11) in 2002		23	18
Unrealized gain (loss) on hedging activities, net of income tax of \$1 in 2004, \$(2) in 2003 and \$6 in 2002	(1)	3	(11)
Additional minimum pension liability adjustment, net of income tax of \$46 in 2004, \$(33) in 2003 and \$107 in 2002	(77)	56	(180)
Comprehensive income (loss)	<u>\$ (178)</u>	<u>\$ 394</u>	<u>\$ 1,029</u>

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

All amounts are in millions except per share amounts.

Certain prior-year amounts have been reclassified to conform to current year presentation.

1. ACCOUNTING POLICIES

The following is a summary of the significant accounting policies followed in preparing these financial statements.

Description of Business, Basis of Presentation and Principles of Consolidation

The Kroger Co. (the Company) was founded in 1883 and incorporated in 1902. As of January 29, 2005, the Company was one of the largest retailers in the United States based on annual sales. The Company also manufactures and processes food for sale by its supermarkets. The Company employs approximately 289,000 full and part-time employees. The accompanying financial statements include the consolidated accounts of the Company and its subsidiaries. Significant intercompany transactions and balances have been eliminated.

Fiscal Year

The Company's fiscal year ends on the Saturday nearest January 31. The last three fiscal years consist of the 52-week period ended January 29, 2005, the 52-week period ended January 31, 2004, and the 52-week period ended February 1, 2003.

Pervasiveness of Estimates

The preparation of financial statements in conformity with Generally Accepted Accounting Principles (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities. Disclosure of contingent assets and liabilities as of the date of the consolidated financial statements and the reported amounts of consolidated revenues and expenses during the reporting period also is required. Actual results could differ from those estimates.

Inventories

Inventories are stated at the lower of cost (principally on a last-in, first-out (LIFO) basis) or market. In total, approximately 97% of inventories for 2004 and approximately 97% of inventories for 2003 were valued using the LIFO method. Cost for the balance of the inventories was determined using the first-in, first-out (FIFO) method. Replacement cost was higher than the carrying amount by \$373 at January 29, 2005 and

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\$324 at January 31, 2004. The Company follows the Link-Chain, Dollar-Value LIFO method for purposes of calculating its LIFO charge or credit.

The item-cost method of accounting to determine inventory cost before the LIFO adjustment is followed for substantially all non-perishable store inventories at the Company's supermarket divisions. This method involves counting each item in inventory, assigning costs to each of these items based on the actual purchase costs (net of vendor allowances) of each item and recording the actual cost of items sold. The item-cost method of accounting allows for more accurate reporting of periodic inventory balances and enables management to more precisely manage inventory when compared to the retail method of accounting.

The Company evaluates inventory shortages throughout the year based on actual physical counts in its facilities. Allowances for inventory shortages are recorded based on the results of these counts to provide for estimated shortages as of the financial statement date.

Property, Plant and Equipment

Generally, property, plant and equipment are recorded at cost. Depreciation expense, which includes the amortization of assets recorded under capital leases, is computed principally using the straight-line method over the estimated useful lives of individual assets. Leasehold improvements are depreciated over the shorter of the remaining life of the applicable lease or the useful life of the asset. Buildings and land improvements are depreciated based on lives varying from 10 to 40 years. Some store equipment acquired as a result of the Fred Meyer merger was assigned a 15-year life. The life of this equipment was not changed. All new purchases of store equipment are assigned lives varying from three to nine years. Manufacturing plant and distribution center equipment is depreciated over lives varying from three to 15 years. Leasehold improvements are amortized over the lives of the leases to which they relate, which vary from four to 25 years. Depreciation expense was \$1,256 in 2004, \$1,209 in 2003 and \$1,087 in 2002.

Interest costs on significant projects constructed for the Company's own use are capitalized as part of the costs of the newly constructed facilities. Upon retirement or disposal of assets, the cost and related accumulated depreciation are removed from the balance sheet and any gain or loss is reflected in net earnings.

Deferred Rent

The Company recognizes rent holidays, including the time period during which the Company has access to the property for construction of buildings or improvements, as well as construction allowances and escalating rent provisions on a straight-line basis over the term of the lease. The deferred amount is included in Other Current Liabilities and Other Long-Term Liabilities on the Company's Consolidated Balance Sheets.

Goodwill

The Company adopted Statement of Financial Accounting Standards (SFAS) No. 142 on February 3, 2002. Accordingly, goodwill was reviewed for impairment during the first and fourth quarters of 2002, and also during the fourth quarters of 2003 and 2004. Results of these impairment reviews are summarized in Note 5.

The Company reviews goodwill for impairment during the fourth quarter of each year, and also upon the occurrence of trigger events. The reviews are performed at the operating division level. Potential impairment is indicated when the carrying value of a division, including goodwill, exceeds its fair value. Generally, fair value represents a multiple of earnings, or discounted projected future cash flows. Projected future cash flows are based on management's knowledge of the current operating environment and expectations for the future. If potential for impairment exists, the fair value of a division is subsequently measured against the fair value of its underlying assets and liabilities, excluding goodwill, to estimate an implied fair value of the division's goodwill. Impairment loss is recognized for any excess of the carrying value of the division's goodwill over the implied fair value.

Intangible Assets

In addition to goodwill, the Company has recorded intangible assets totaling \$20 and \$29 for liquor licenses and pharmacy prescription file purchases, respectively at January 29, 2005. Balances at January 31, 2004 were \$20 for liquor licenses and \$21 for pharmacy prescription files. Owned liquor licenses are not amortized, while liquor licenses that must be renewed are amortized over their useful life. Pharmacy prescription file purchases are amortized over seven years. These assets are tested annually for impairment.

Impairment of Long-Lived Assets

In accordance with SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, the Company monitors the carrying value of long-lived assets for potential impairment each quarter based on whether certain trigger events have occurred. These events include current period losses combined with a history of losses or a projection of continuing losses or a significant decrease in the market value of an asset. When a trigger event occurs, an impairment calculation is performed, comparing projected undiscounted future cash flows, utilizing current cash flow information and expected growth rates related to specific stores, to the carrying value for those stores. If impairment is identified for long-lived assets to be held and used, discounted future cash flows are compared to the asset's current carrying value. Impairment is recorded when the carrying value exceeds the discounted cash flows. With respect to owned property and equipment held for disposal, the value of the

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property and equipment is adjusted to reflect recoverable values based on previous efforts to dispose of similar assets and current economic conditions. Impairment is recognized for the excess of the carrying value over the estimated fair market value, reduced by estimated direct costs of disposal.

The Company performs impairment reviews at both the division and corporate levels. Generally, for reviews performed by local divisional management, costs to reduce the carrying value of long-lived assets are reflected in the Consolidated Statements of Earnings as Operating, general and administrative expense. Cost to reduce the carrying value of long-lived assets that result from corporate level strategic plans are separately identified in the Consolidated Statements of Earnings as Asset impairment charges.

Refer to Note 3 for a description of the asset impairment charge recorded during 2003.

Store Closing Costs

All closed store liabilities related to exit or disposal activities initiated after December 31, 2002, are accounted for in accordance with SFAS No. 146, Accounting for Costs Associated with Exit or Disposal Activities. The Company provides for closed store liabilities relating to the present value of the estimated remaining noncancellable lease payments after the closing date, net of estimated subtenant income. The Company estimates the net lease liabilities using a discount rate to calculate the present value of the remaining net rent payments on closed stores. The closed store lease liabilities usually are paid over the lease terms associated with the closed stores, which generally have remaining terms ranging from one to 20 years. Adjustments to closed store liabilities primarily

relate to changes in subtenant income and actual exit costs differing from original estimates. Adjustments are made for changes in estimates in the period in which the change becomes known. Store closing liabilities are reviewed quarterly to ensure that any accrued amount that is not a sufficient estimate of future costs, or that no longer is needed for its originally intended purpose, is adjusted to income in the proper period.

Owned stores held for disposal are reduced to their estimated net realizable value. Costs to reduce the carrying values of property, equipment and leasehold improvements are accounted for in accordance with our policy on impairment of long-lived assets. Inventory write-downs, if any, in connection with store closings, are classified in Merchandise costs. Costs to transfer inventory and equipment from closed stores are expensed as incurred.

The following table summarizes accrual activity for future lease obligations of stores closed that were closed in the normal course of business, not part of a coordinated closing.

	Future Lease Obligations
Balance at February 3, 2002	\$ 66
Additions	(14)
Payments	(16)
Adjustments	
Balance at February 2, 2003	36
Additions	10
Payments	(9)
Adjustments	(2)
Balance at February 1, 2004	35
Additions	28
Payments	(10)
Adjustments	12
Balance at February 31, 2005	\$ 65

Interest Rate Risk Management

The Company uses derivative instruments primarily to manage its exposure to changes in interest rates. The Company's current program relative to interest rate protection and the methods by which the Company accounts for its derivative instruments are described in Note 9.

Commodity Price Protection

The Company enters into purchase commitments for various resources, including raw materials utilized in its manufacturing facilities and energy to be used in its stores, manufacturing facilities and administrative offices. The Company enters into commitments expecting to take delivery of and to utilize those resources in the conduct of the normal course of business. The Company's current program relative to commodity price protection and the methods by which the Company accounts for its purchase commitments are described in Note 9.

Benefit Plans

The determination of the obligation and expense for company-sponsored pension plans and other post-retirement benefits is dependent on the selection of assumptions used by actuaries and the Company in calculating those amounts. Those assumptions are described in Note 18 and include, among others, the discount rate, the expected long-term rate of return on plan assets and the rates of increase in compensation and health care costs. In accordance with generally accepted accounting principles, actual results that differ from the assumptions are accumulated and amortized over future periods and, therefore, generally affect the recognized expense and recorded obligation in future periods. While the Company believes that the assumptions are appropriate, significant differences in actual experience or significant changes in assumptions may materially affect the pension and other post-retirement obligations and future expense.

The Company also participates in various multi-employer plans for substantially all union employees. Pension expense for these plans is recognized as contributions are funded. Refer to Note 18 for additional information regarding the Company's benefit plans.

Stock Option Plans

The Company applies Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations in accounting for its stock option plans. The Company grants options for common stock at an option price equal to the fair market value of the stock at the date of the grant. Accordingly, the Company does not record stock-based compensation expense for these options. The Company also makes restricted stock awards. Compensation expense included in net earnings for restricted stock awards totaled approximately \$8, \$8 and \$6 after-tax, in 2004, 2003 and 2002, respectively. The Company's stock option plans are more fully described in Note 13.

The following table illustrates the effect on net earnings, net earnings per basic common share and net earnings per diluted common share if compensation cost for all options had been determined based on the fair market value recognition provision of SFAS No. 123:

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Net earnings (loss), as reported	\$ (100)	\$ 312	\$ 1,202
Add: Stock-based compensation expense included in net earnings, net of income tax benefits	8	8	6
Subtract: Total stock-based compensation expense determined under fair value method for all awards, net of income tax benefits ⁽¹⁾	(48)	(48)	(47)
Pro forma net earnings (loss)	\$ (140)	\$ 272	\$ 1,161
Earnings (loss) per basic common share, as reported	\$ (0.14)	\$ 0.42	\$ 1.54
Pro forma earnings (loss) per basic common share	\$ (0.19)	\$ 0.36	\$ 1.49
Earnings (loss) per diluted common share, as reported	\$ (0.14)	\$ 0.41	\$ 1.52
Pro forma earnings (loss) per diluted common share	\$ (0.19)	\$ 0.36	\$ 1.47

⁽¹⁾ Refer to Note 13 for a summary of the assumptions used for options issued in each year at an option price equal to the fair market value of the stock at the date of the grant.

Deferred Income Taxes

Deferred income taxes are recorded to reflect the tax consequences of differences between the tax basis of assets and liabilities and their financial reporting basis. Refer to Note 6 for the types of differences that give rise to significant portions of deferred income tax assets and liabilities. Deferred income taxes are classified as a net current or noncurrent asset or liability based on the classification of the related asset or liability for financial reporting purposes. A deferred tax asset or liability that is not related to an asset or liability for financial reporting is classified according to the expected reversal date.

Tax Contingencies

Various taxing authorities periodically audit the Company's income tax returns. These audits include questions regarding the Company's tax filing positions, including the timing and amount of deductions and the allocation of income to various tax jurisdictions. In evaluating the exposures connected with these various tax filing positions, including state and local taxes, the Company records allowances for probable exposures. A number of years may elapse before a particular matter, for which an allowance has been established, is audited and fully resolved. As of January 29, 2005, tax years 1999 to 2002 were undergoing examination by the Internal Revenue Service.

The establishment of the Company's tax contingency allowances relies on the judgment of management to estimate the exposures associated with the Company's various filing positions. Although management believes those estimates and judgments are reasonable, actual results could differ, resulting in gains or losses that may be material to the Consolidated Statements of Operations.

To the extent the Company prevails in matters for which allowances have been established, or are required to pay amounts in excess of these allowances, the Company's effective tax rate in any given financial statement period could be materially affected. An unfavorable tax settlement could require use of cash and result in an increase in the Company's effective tax rate in the year of resolution. A favorable tax settlement would

be recognized as a reduction in the Company's effective tax rate in the year of resolution.

Self-Insurance Costs

The Company primarily is self-insured for costs related to workers' compensation and general liability claims. Liabilities are actuarially determined and are recognized based on claims filed and an estimate of claims incurred but not reported. The liabilities for workers' compensation claims are accounted for on a present value basis. The Company has purchased stop-loss coverage to limit its exposure to any significant exposure on a per claim basis. The Company is insured for covered costs in excess of these per claim limits.

The assumptions underlying the ultimate costs of existing claim losses are subject to a high degree of unpredictability, which can affect the liability recorded for such claims. For example, variability in inflation rates of health care costs inherent in these claims can impact amounts realized. Similarly, changes in legal trends and interpretations, as well as a change in the nature and method of how claims are settled can impact ultimate costs. Although the Company's estimates of liabilities incurred do not anticipate significant changes in historical trends for these variables, any changes could have a considerable impact on future claim costs and currently recorded liabilities.

Revenue Recognition

Revenues from the sale of products are recognized at the point of sale of the Company's products. Discounts provided to customers by the Company at the time of sale are recognized as a reduction in sales as the products are sold. Discounts provided by vendors, usually in the form of paper coupons, are not recognized as a reduction in sales provided the coupons are redeemable at any retailer that accepts coupons. The Company does not recognize a sale when it sells gift cards and gift certificates. Rather, a sale is recognized when the gift card or gift certificate is redeemed to purchase the Company's products.

Merchandise Costs

In addition to the product costs, net of discounts and allowances; advertising costs (see separate discussion below); inbound freight charges; warehousing costs, including receiving and inspection costs; transportation costs; and manufacturing production and operational costs are included in the Merchandise costs line item of the Consolidated Statements of Earnings. Warehousing, transportation and manufacturing management salaries are also included in the Merchandise costs line item; however, purchasing management salaries and administration costs are included in the Operating, general, and administrative line item along with most of the Company's other managerial and administrative costs. Rent expense and depreciation expense are shown separately in the Consolidated Statements of Operations.

Warehousing and transportation costs include distribution center direct wages, repairs and maintenance, utilities, inbound freight and, where applicable, third party warehouse management fees, as well as transportation direct wages and repairs and maintenance. These costs are recognized in the periods the related expenses are incurred.

The Company believes the classification of costs included in merchandise costs could vary widely throughout the industry. The Company's approach is to include in the Merchandise costs line item the direct, net costs of acquiring products and making them available to customers in its stores. The Company believes this approach most accurately presents the actual costs of products sold.

The Company recognizes all vendor allowances as a reduction in merchandise costs when the related product is sold. When possible, vendor allowances are applied to the related product by item and therefore reduce the carrying value of inventory by item. When the items are sold, the vendor allowance is recognized. When it is not possible, due to systems constraints, to allocate vendor allowances to the product by item, vendor allowances are recognized as a reduction in merchandise costs based on inventory turns and therefore recognized as the product is sold. In fiscal 2004, the Company recognized approximately \$3,100 of vendor allowances as a reduction in merchandise costs. More than 80% of all vendor allowances were recognized in the item cost with the remainder being based on inventory turns.

Prior to the adoption of Emerging Issues Task Force (EITF) Issue No. 02-16, Accounting By A Customer (Including A Reseller) For Certain Consideration Received From A Vendor, promotional and contract allowances were recognized when the promotion ran and slotting allowances were recognized when the product was first stocked. For all contracts entered into or modified after January 1, 2003, the Company has recognized prospectively, and will continue to recognize, vendor allowances when the related merchandise is sold. Net earnings in 2002 were

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not affected by the adoption of Issue No. 02-16. Adoption of the Issue resulted in a \$28 pre-tax charge that was included in merchandise costs in 2002. This expense was offset by a corresponding \$28 pre-tax LIFO credit that also was included in merchandise costs in 2002.

Advertising Costs

The Company's advertising costs are recognized in the periods the related expenses are incurred and are included in the Merchandise costs line item of the Consolidated Statements of Operations. The Company's pre-tax advertising costs totaled \$528 in 2004, \$527 in 2003 and \$510 in 2002. The Company does not record vendor allowances for co-operative advertising as a reduction of advertising expense.

Consolidated Statements of Cash Flows

For purposes of the Consolidated Statements of Cash Flows, the Company considers all highly liquid debt instruments purchased with an original maturity of three months or less to be temporary cash investments. Book overdrafts, which are included in accounts payable, represent disbursements that are funded as the item is presented for payment. Book overdrafts totaled \$562, \$587 and \$480 as of January 29, 2005, January 31, 2004, and February 1, 2003, respectively, and are reflected as a financing activity in the Consolidated Statements of Cash Flows.

Segments

The Company operates retail food and drug stores, multi-department stores, jewelry stores, and convenience stores throughout the United States. The Company's retail operations, which represent approximately 99% of consolidated sales, are its only reportable segment. All of the Company's operations are domestic.

2. MERGER-RELATED COSTS

There were no merger-related costs incurred in 2004 or 2003. Pre-tax, merger-related costs totaled \$1 in 2002. All of the costs in 2002 resulted from the issuance of restricted stock and the related market value adjustments. Restrictions on these stock awards lapsed in 2002 based on the achievement of synergy goals established in connection with the Fred Meyer merger. All synergy-based awards were earned provided that recipients were still employed on the stated restriction lapsing date.

The following table shows the changes in accruals related to business combinations:

	Facility Closure Costs	Incentive Awards and Contributions
	<u> </u>	<u> </u>
Balance at February 2, 2002	\$ 94	\$ 30
Additions		1
Payments	(20)	(11)
	<u> </u>	<u> </u>
Balance at February 1, 2003	74	20
Adjustment of charitable contribution allowance		(5)
Payments	(10)	
	<u> </u>	<u> </u>
Balance at January 31, 2004	64	15
Payments	(7)	(1)
	<u> </u>	<u> </u>
Balance at January 29, 2005	<u>\$ 57</u>	<u>\$ 14</u>

The \$57 liability for facility closure costs primarily represents the present value of lease obligations remaining through 2019 for locations closed in California prior to the Fred Meyer merger. The \$14 liability relates to a charitable contribution required as a result of the Fred Meyer merger. The Company is required to make this contribution by May 2006.

3. ASSET IMPAIRMENT CHARGES AND RELATED ITEMS

During 2003, the Company authorized closure of several stores throughout the country based on results for 2002 and 2003, as well as updated projections for 2004 and beyond. This event triggered an impairment review of stores slated for closure as well as several other under-performing locations in the fourth quarter 2003. The review resulted in a pre-tax charge totaling \$120. These charges are more fully described below. No corporate-level asset impairment charges were recorded in 2004 or 2002.

Assets to be Disposed of

The impairment charges for assets to be disposed of related primarily to the carrying values of land, buildings, equipment and leasehold improvements for stores that have closed or have been approved for closure. The impairment charges were determined by estimating the fair values of the locations, less costs of disposal. Fair values were based on third party offers to purchase the assets, or market value for comparable properties, if available. As a result, pre-tax impairment charges related to assets to be disposed of were recognized, reducing the carrying value of fixed assets by \$54 in 2003.

Assets to be Held and Used

The impairment charges for assets to be held and used related primarily to the carrying values of land, buildings, equipment and leasehold improvements for stores that will continue to be operated by the Company. Updated projections, based on revised operating plans, were used, on a gross basis, to determine whether the assets were impaired. Then, discounted cash flows were used to estimate the fair value of the assets for purposes of measuring the impairment charge. As a result, impairment charges related to assets to be held and used were recognized, reducing the carrying value of fixed assets by \$66 in 2003.

Related Items: Lease Liabilities Coordinated Store Closing Plans

In 2000 and 2001, the Company recorded expense related to the present value of lease liabilities for stores identified for closure. Due to operational changes, performance improved at five stores subsequent to the recording of the future lease liabilities. As a result of this improved performance, in the first quarter of 2003 the Company modified its original plans and determined that these five locations will remain open. Additionally, closing and exit costs at other locations previously recorded were less costly than anticipated. In total, in the first quarter of 2003, the Company recorded pre-tax income of \$10 to adjust these liabilities to reflect the outstanding lease commitments through 2020 at the locations remaining under the plans. The following table summarizes the changes in the balances of the liabilities:

Balances at February 2, 2002 ⁽¹⁾	\$ 64
Payments	(4)
	<hr/>
Balances at February 1, 2003	60
Lease liabilities reversed	(10)
Payments, including \$12 related to the synthetic lease buyout	(18)
	<hr/>
Balances at January 31, 2004	32
Payments	19
	<hr/>
Balances at January 29, 2005	\$ 13
	<hr/>

⁽¹⁾ The beginning balance represents the balance of impairment charges recorded in prior years.

The \$13 liability for store closing liabilities relates to the present value of lease obligations remaining through 2020. Sales at store remaining under the plan totaled \$18, \$17 and \$17 in 2004, 2003 and 2002, respectively.

4. RESTRUCTURING CHARGES

On December 11, 2001, the Company outlined the Strategic Growth Plan (the Plan) to support additional investment in its core business to increase sales and market share. The Plan had three key elements: reduction of operating, general and administrative expenses, increased coordination of merchandising and procurement activities, and targeted retail price reductions. During 2001, the Company recorded a pre-tax restructuring charge of \$37 primarily for severance agreements associated with the Plan. Restructuring charges related to the Plan totaled \$15, pre-tax, in 2002. The majority of the 2002 expenses related to severance agreements, distribution center consolidation and conversion costs. No restructuring charges related to the plan were incurred in 2004 and 2003.

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The following table summarizes the changes in the balances of the liabilities associated with the Plan:

	Severance & Other Costs
	<u> </u>
Balance at February 2, 2002	\$ 37
Additions	15
Payments	(44)
	<u> </u>
Balance at February 1, 2003	\$ 8
Additions	
Payments	(3)
	<u> </u>
Balance at January 31, 2004	\$ 5
Additions	
Payments	(1)
	<u> </u>
Balance at January 29, 2005	<u>\$ 4</u>

All severance agreements associated with these liabilities have been paid. The remaining \$4 of liabilities represent long-term obligations, including lease commitments through 2009 related to the consolidation of the Company's Nashville division office.

5. GOODWILL, NET

As described in Note 1, the Company adopted SFAS No. 142 on February 3, 2002. The transitional impairment review required by SFAS No. 142 resulted in a \$26 pre-tax non-cash loss to write off the jewelry store division goodwill based on its implied fair value. Impairment primarily resulted from the recent operating performance of the division and review of the division's projected future cash flows on a discounted basis, rather than on an undiscounted basis, as was the standard under SFAS No. 121, prior to adoption of SFAS No. 142. This loss was recorded as a cumulative effect of an accounting change, net of a \$10 tax benefit, in the first quarter of 2002.

The annual evaluation of goodwill performed during the fourth quarter of 2003 resulted in a \$444 non-cash impairment charge related to the goodwill at the Company's Smith's division. In 2003, the Company's Smith's division experienced a substantial decline in operating performance when compared to prior year performance and budgeted 2003 result. Additionally, the Company forecasted a further decline in the future operating performance of the division reflecting the necessary investments in capital and targeted retail price reductions in order to maintain and grow market share and provide acceptable long-term return on capital. The impairment charge, which was non-deductible for income tax purposes, adjusted the carrying value of the division's goodwill to its implied fair value.

The annual evaluation of goodwill performed during the fourth quarter of 2004 resulted in a \$900 pre-tax, non-cash impairment charge related to goodwill at the Company's Ralphs and Food 4 Less divisions. The divisions' operating performance suffered due to the intense competitive environment during the 2003 southern California labor dispute and recovery period after the labor dispute. The decreased operating performance was the result of the investments in personnel, training, capital and price reductions necessary to help regain Ralphs' business lost during the labor dispute and to maintain business gained by Food 4 Less that were not subject to the labor dispute. As a result of this decline and the decline in future expected operating performance, the divisions' carrying value of goodwill exceeded its implied fair value resulting in the impairment charge. Most of the impairment charge was non-deductible for income tax purposes. After the impairment charge, the Company maintains \$1,458 of goodwill for the Ralphs and Food 4 Less divisions.

The following table summarizes the changes in the Company's net goodwill balance through January 29, 2005.

Balance at February 2, 2002	\$ 3,594
Cumulative effect of an accounting change	(26)
Goodwill recorded	9
Reclassifications	(2)
	<hr/>
Balance at February 1, 2003	\$ 3,575
Goodwill impairment charge	(444)
Goodwill recorded	9
Purchase accounting adjustments	(6)
	<hr/>
Balance at January 31, 2004	\$ 3,134
Goodwill impairment charge	(900)
Goodwill recorded	6
Purchase accounting adjustments	(49)
	<hr/>
Balance at January 29, 2005	<u>\$ 2,191</u>

6. PROPERTY, PLANT AND EQUIPMENT, NET

Property, plant and equipment, net consists of:

	<u>2004</u>	<u>2003</u>
Land	\$ 1,580	\$ 1,519
Buildings and land improvements	4,975	4,435
Equipment	7,797	7,745
Leasehold improvements	3,804	3,555
Construction-in-progress	541	636
Leased property under capital leases	506	535
	<u>19,203</u>	<u>18,425</u>
Accumulated depreciation and amortization	(7,706)	(7,247)
	<u>11,497</u>	<u>11,178</u>
Total	\$ 11,497	\$ 11,178

Accumulated depreciation for leased property under capital leases was \$252 at January 29, 2005 and \$246 at January 31, 2004.

Approximately \$982 and \$1,180, original cost, of Property, Plant and Equipment collateralized certain mortgages at January 29, 2005 and January 31, 2004, respectively.

7. TAXES BASED ON INCOME

The provision for taxes based on income consists of:

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Federal			
Current	\$ 96	\$ 177	\$ 293
Deferred	258	238	360
	<u>354</u>	<u>415</u>	<u>653</u>
State and local	36	39	79
	<u>390</u>	<u>454</u>	<u>732</u>
Tax benefit from cumulative effect of an accounting change			(10)
	<u>\$ 390</u>	<u>\$ 454</u>	<u>\$ 722</u>

A reconciliation of the statutory federal rate and the effective rate follows:

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	<u>2004</u>	<u>2003</u>	<u>2002</u>
Statutory rate	35.0%	35.0%	35.0%
State income taxes, net of federal tax benefit	2.6%	3.3%	2.6%
Non-deductible goodwill	99.8%	20.3%	0.0%
Other changes, net	(2.9)%	0.7%	(0.1)%
	<u>134.5%</u>	<u>59.3%</u>	<u>37.5%</u>

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The tax effects of significant temporary differences that comprise tax balances were as follows:

	2004	2003
	<u> </u>	<u> </u>
Current deferred tax assets:		
Net operating loss carryforwards	\$ 19	\$ 19
	<u> </u>	<u> </u>
Total current deferred tax assets	19	19
Current deferred tax liabilities:		
Compensation related costs	(19)	(4)
Insurance related costs	(136)	(13)
Inventory related costs	(100)	(127)
Other	(31)	(13)
	<u> </u>	<u> </u>
Total current deferred tax liabilities	(286)	(157)
	<u> </u>	<u> </u>
Current deferred taxes	\$ (267)	\$ (138)
	<u> </u>	<u> </u>
Long-term deferred tax assets:		
Compensation related costs	\$ 383	\$ 264
Insurance related costs	15	15
Lease accounting	45	46
Closed store reserves	115	91
Net operating loss carryforwards	79	98
Other	129	96
	<u> </u>	<u> </u>
	766	610
Valuation allowance		(150)
	<u> </u>	<u> </u>
Long-term deferred tax assets, net	766	460
Long-term deferred tax liabilities:		
Depreciation	(1,502)	(1,243)
Deferred income	(203)	(191)
	<u> </u>	<u> </u>
Total long-term deferred tax liabilities	(1,705)	(1,434)
	<u> </u>	<u> </u>
Long-term deferred taxes	\$ (939)	\$ (974)
	<u> </u>	<u> </u>

At January 29, 2005, the Company had net operating loss carryforwards for federal income tax purposes of \$256 that expire from 2010 through 2018. In addition, the Company had net operating loss carryforwards for state income tax purposes of \$467 that expire from 2009 through 2023. The utilization of certain of the Company's net operating loss carryforwards may be limited in a given year.

The Company's valuation allowance pertained to a Ralphs Grocery Co., pre-acquisition federal tax controversy. It was determined that it is more likely than not that the associated tax benefits will be utilized by the Company. As a result, the valuation allowance was removed and goodwill was reduced. Separately, an allowance was established with regard to the pre-acquisition controversy with an offsetting increase to goodwill.

At January 29, 2005, the Company had state Alternative Minimum Tax Credit carryforwards of \$4. In addition, the Company had other state credits of \$18, which expire from 2005 through 2014. The utilization of certain of the Company's credits may be limited in a given year.

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The amounts of cash paid for income taxes in 2004, 2003 and 2002 were reduced by approximately \$106, \$130 and \$106, respectively, as a result of federal bonus depreciation. This provision expired in December 2004 and the Company expects the related cash benefit will begin to reverse in 2005.

8. DEBT OBLIGATIONS

Long-term debt consists of:

	<u>2004</u>	<u>2003</u>
Credit Facilities	\$ 694	\$ 391
4.95% to 8.92% Senior Notes and Debentures due through 2031	6,391	6,842
5.00% to 10.23% mortgages due in varying amounts through 2017	218	481
Other	202	159
	<u> </u>	<u> </u>
Total debt	7,505	7,873
Less current portion	(46)	(225)
	<u> </u>	<u> </u>
Total long-term debt	\$ 7,459	\$ 7,648
	<u> </u>	<u> </u>

As of January 29, 2005, the Company had a \$1,800 Five-Year Credit Agreement maturing in 2009, and a \$700 Five-Year Credit Agreement maturing in 2007, unless earlier terminated by the Company. Borrowings under these credit agreements bear interest at the option of the Company at a rate equal to either (i) the highest, from time to time of (A) the base rate of Citibank, N.A., (B) ½% over a moving average of secondary market morning offering rates for three-month certificates of deposit adjusted for reserve requirements, and (C) ½% over the federal funds rate or (ii) an adjusted Eurodollar rate based upon the London Interbank Offered Rate (Eurodollar Rate) plus an Applicable Margin. In addition, the Company pays a Facility Fee in connection with these credit agreements. Both the Applicable Margin and the Facility Fee vary based upon the Company's achievement of a financial ratio or credit rating. At January 29, 2005, the Applicable Margin was .375% and the Facility Fee was .125% for both facilities. The credit agreements contain covenants, which, among other things, require the maintenance of certain financial ratios, including fixed charge coverage and leverage ratios. The Company may prepay the credit agreements in whole or in parts, at any time, without a prepayment penalty. The weighted average interest rate on the amounts outstanding under the credit facilities was 2.49% and 1.13% at January 29, 2005 and January 31, 2004, respectively.

At January 29, 2005, the Company had borrowed \$694 under the A2/P2/F2 rated commercial paper program. These borrowings are backed by the Company's credit facilities and reduce the amount available under the credit facilities.

At January 29, 2005, the Company also maintained a \$75 money market line. In addition to credit agreement borrowings, borrowings under the money market line and some outstanding letters of credit reduce funds available under the Company's credit agreements. At January 29, 2005, these letters of credit totaled \$312. The Company had no borrowings under the money market line at January 29, 2005. The Company's credit agreement borrowings have been classified as long-term borrowings because the Company expects that these borrowings will be refinanced using the same type of securities. The Company has the ability to refinance these borrowings on a long-term basis, and has presented the amounts accordingly.

At January 29, 2005, the Company also had a \$100 pharmacy receivable securitization facility that provided capacity incremental to the \$2,500 described above. Funds received under this \$100 facility do not reduce funds available under the Credit Facilities. Collection rights to some of the Company's pharmacy accounts receivable balances are sold to initiate the drawing of funds under the facility. As of January 29, 2005, the Company had no borrowings under this \$100 facility.

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Most of the Company's outstanding public debt is subject to early redemption at varying times and premiums, at the option of the Company. In addition, subject to certain conditions, some of the Company's publicly issued debt will be subject to redemption, in whole or in part, at the option of the holder upon the occurrence of a redemption event, upon not less than five days' notice prior to the date of redemption, at a redemption price equal to the default amount, plus a specified premium. Redemption Event is defined in the indentures as the occurrence of (i) any person or group, together with any affiliate thereof, beneficially owning 50% or more of the voting power of the Company or (ii) any one person or group, or affiliate thereof, succeeding in having a majority of its nominees elected to the Company's Board of Directors, in each case, without the consent of a majority of the continuing directors of the Company.

The aggregate annual maturities and scheduled payments of long-term debt, as of year-end 2004, for the years subsequent to 2004 are:

2005	\$ 46
2006	\$ 554
2007	\$ 525
2008	\$ 998
2009	\$ 1,094
Thereafter	\$ 4,288
	<hr/>
Total debt	\$ 7,505

9. FINANCIAL INSTRUMENTS

Interest Rate Risk Management

The Company historically has used derivatives to manage its exposure to changes in interest rates. The interest differential to be paid or received is accrued as interest expense. SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities, as amended, defines derivatives, requires that derivatives be carried at fair value on the balance sheet and provides for hedge accounting when certain conditions are met. In accordance with this standard, the Company's derivative financial instruments are recognized on the balance sheet at fair value. Changes in the fair value of derivative instruments designated as cash flow hedges, to the extent the hedges are highly effective, are recorded in other comprehensive income, net of tax effects. Ineffective portions of cash flow hedges, if any, are recognized in current period earnings. Other comprehensive income or loss is reclassified into current period earnings when the hedged transaction affects earnings. Changes in the fair value of derivative instruments designated as fair value hedges, along with corresponding changes in the fair values of the hedged assets or liabilities, are recorded in current period earnings.

The Company assesses, both at the inception of the hedge and on an ongoing basis, whether derivatives used as hedging instruments are highly effective in offsetting the changes in the fair value or cash flow of the hedged items. If it is determined that a derivative is not highly effective as a hedge or ceases to be highly effective, the Company discontinues hedge accounting prospectively.

The Company's current program relative to interest rate protection contemplates both fixing the rates on variable rate debt and hedging the exposure to changes in the fair value of fixed-rate debt attributable to changes in interest rates. To do this, the Company uses the following guidelines: (i) used average daily bank balance to determine annual debt amounts subject to interest rate exposure, (ii) limit the annual amount subject to interest rate reset and the amount of floating rate debt to a combined total of \$2.5 billion or less, (iii) include no leverage products, and (iv) hedge without regard to profit motive or sensitivity to current mark-to-market status.

Annually, the Company reviews with the Financial Policy Committee of the Board of Directors compliance with the guidelines. These guidelines may change as the Company's needs dictate.

The table below summarizes the outstanding interest rate swaps designated as hedges as of January 29, 2005, and January 31, 2004. The variable component of each interest rate swap outstanding at January 29, 2005, was based on LIBOR as of January 29, 2005. The variable component of each interest rate swap outstanding at January 31, 2004, was based on LIBOR as of January 31, 2004.

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	2004		2003	
	Pay Floating	Pay Fixed	Pay Floating	Pay Fixed
Notional amount	\$ 1,375	\$	\$ 1,825	\$ 300
Duration in years	4.29		2.63	0.04
Average variable rate	6.29%		5.67%	1.12%
Average fixed rate	6.98%		7.45%	3.22%

Commodity Price Protection

The Company enters into purchase commitments for various resources, including raw materials utilized in its manufacturing facilities and energy to be used in its stores, manufacturing facilities and administrative offices. The Company enters into commitments expecting to take delivery of and to utilize those resources in the conduct of normal business. Those commitments for which the Company expects to utilize or take delivery in a reasonable amount of time in the normal course of business qualify as normal purchases and normal sales. Any commitments for which the Company does not expect to take delivery, and, as a result will require net settlement, are marked to fair value on a quarterly basis.

Some of the product the Company purchases is shipped in corrugated cardboard packaging. The corrugated cardboard is sold when it is economical to do so. In the fourth quarter of 2004, the Company entered into six derivative instruments to protect it from declining corrugated cardboard prices. The derivatives, accounted for as cash flow hedges, contain a three-year term. None of the contracts, either individually or in the aggregate, hedge more than 50% of the Company's expected corrugated cardboard sales. As of January 29, 2005, a liability totaling \$2 had been recorded for the instruments. Corresponding charges were recorded as Other Comprehensive Loss, net of income tax effects.

10. FAIR VALUE OF FINANCIAL INSTRUMENTS

The following methods and assumptions were used to estimate the fair value of each class of financial instrument for which it was practicable to estimate that value:

Cash and Temporary Cash Investments, Store Deposits In-Transit, Receivables, Prepaid and Other Current Assets, Accounts Payable, Accrued Salaries and Wages and Other Current Liabilities

The carrying amounts of these items approximated fair value.

Long-term Investments

The fair values of these investments were estimated based on quoted market prices for those or similar investments.

Long-term Debt

The fair value of the Company's long-term debt, including the current portion thereof and excluding borrowings under the credit facilities, was estimated based on the quoted market price for the same or similar issues. If quoted market prices were not available, the fair value was based upon the net present value of the future cash flows using the forward interest rate yield curve in effect at the respective year-ends. The carrying values of long-term debt outstanding under the Company's credit facilities approximated fair value.

Interest Rate Protection Agreements

The fair value of these agreements was based on the net present value of the future cash flows using the forward interest rate yield curve in effect at the respective year-ends.

The estimated fair values of the Company's financial instruments are as follows:

	2004		2003	
	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
Cash and temporary cash investments	\$ 144	\$ 144	\$ 159	\$ 159
Store deposits in-transit	\$ 506	\$ 506	\$ 579	\$ 579
Long-term investments for which it is				
Practicable	\$ 89	\$ 89	\$ 70	\$ 70
Not Practicable	\$ 15	\$	\$ 15	\$
Debt for which it is ⁽¹⁾				
Practicable	\$ (7,505)	\$ (8,304)	\$ (7,873)	\$ (8,919)
Not Practicable	\$	\$	\$	\$
Interest Rate Protection Agreements				
Receive fixed swaps ⁽²⁾	\$ (11)	\$ (11)	\$ 6	\$ 6
Corrugated Cardboard Price Protection Agreements ⁽³⁾	\$ (2)	\$ (2)	\$	\$

⁽¹⁾ Excludes capital lease obligations

⁽²⁾ As of January 29, 2005, the Company maintained 10 interest rate swap agreements, with notional amounts totaling approximately \$1,375, to manage its exposure to changes in the fair value of its fixed rate debt resulting from interest rate movements by effectively converting a portion of the Company's debt from fixed to variable rates. These agreements mature at varying times between July 2006 and January 2015. Variable rates for these agreements are based on U.S. dollar London Interbank Offered Rate (LIBOR). The differential between fixed and variable rates to be paid or received is accrued as interest rates change in accordance with the agreements and is recognized over the life of the agreements as an adjustment to interest expense. All interest rate swap agreements are being accounted for as fair value hedges. As of January 29, 2005, liabilities totaling \$11 were recorded to reflect the fair value of these agreements, offset by decreases in the fair value of the underlying debt.

⁽³⁾ See Note 9 for a description of the corrugated cardboard price protection agreements.

11. LEASES AND LEASE-FINANCED TRANSACTIONS

The Company operates primarily in leased facilities. Lease terms generally range from 10 to 20 years with options to renew for varying terms. Terms of certain leases include escalation clauses, percentage rent based on sales or payment of executory costs such as property taxes, utilities or insurance and maintenance. Rent expense for leases with escalation clauses, capital improvement funding or other lease concessions is accounted for on a straight-line basis beginning with the earlier of the lease commencement date or the date the Company takes possession. Portions of certain properties are subleased to others for periods generally ranging from one to 20 years.

Rent expense (under operating leases) consists of:

	2004	2003	2002
Minimum rentals	\$ 772	\$ 744	\$ 743
Contingent payments	9	9	10

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Sublease income	(101)	(96)	(93)
	<u> </u>	<u> </u>	<u> </u>
	\$ 680	\$ 657	\$ 660
	<u> </u>	<u> </u>	<u> </u>

Minimum annual rentals and payments under capital leases and lease-financed transactions for the five years subsequent to 2004 and in the aggregate are:

	Capital Leases	Operating Leases	Lease- Financed Transaction
2005	\$ 62	\$ 794	\$ 5
2006	59	756	5
2007	55	682	5
2008	53	649	5
2009	51	603	5
Thereafter	372	4,391	60
	<u>652</u>	<u>\$ 7,875</u>	<u>\$ 85</u>
Less estimated executory costs included in capital leases	(4)		
Net minimum lease payments under capital leases	648		
Less amount representing interest	(296)		
Present value of net minimum lease payments under capital leases	<u>\$ 352</u>		

Total future minimum rentals under noncancellable subleases at January 29, 2005, were \$401.

12. EARNINGS PER COMMON SHARE

Basic earnings per common share equals net earnings divided by the weighted average number of common shares outstanding. Diluted earnings per common share equals net earnings divided by the weighted average number of common shares outstanding after giving effect to dilutive stock options and warrants.

The following table provides a reconciliation of earnings before the cumulative effect of an accounting change and shares used in calculating basic earnings per share to those used in calculating diluted earnings per share.

	For the year ended January 29, 2005			For the year ended January 31, 2004			For the year ended February 1, 2003		
	Earnings (Numer- ator)	Shares (Denomi- nator)	Per Share Amount	Earnings (Numer- ator)	Shares (Denomi- nator)	Per Share Amount	Earnings (Numer- ator)	Shares (Denomi- nator)	Per Share Amount
Basic EPS	\$ (100)	736	\$ (0.14)	\$ 312	747	\$ 0.42	\$ 1,218	779	\$ 1.56
Dilutive effect of stock option awards and warrants					7			12	
Diluted EPS	\$ (100)	736	\$ (0.14)	\$ 312	754	\$ 0.41	\$ 1,218	791	\$ 1.54



For the years ended January 29, 2005, January 31, 2004 and February 1, 2003, there were options outstanding for approximately 61.5, 33.7 and 25.0 shares of common stock, respectively, that were excluded from the computation of diluted EPS. These shares were excluded because their inclusion would have had an anti-dilutive effect on EPS.

13. STOCK OPTION PLANS

The Company applies Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations in accounting for its stock option plans. All awards become immediately exercisable upon certain changes of control of the Company.

The Company grants options for common stock to employees under various plans, as well as to its non-employee directors, at an option price equal to the fair market value of the stock at the date of grant. In addition to cash payments, the plans generally provide for the exercise of options by exchanging issued shares of stock of the Company. At January 29, 2005, approximately 8.0 shares of common stock were available for future options under these plans. Options generally will expire 10 years from the date of grant. Options vest in one year to five years from the date of grant or, for certain options, the earlier of the Company's stock reaching certain pre-determined market prices or nine years and six months from the date of grant.

In addition to the stock options described above, the Company also awards restricted stock to employees under various plans. The restrictions on these awards generally lapse in one year to five years from the date of the awards and expense is recognized over the lapsing cycle. The Company generally records expense for restricted stock awards in an amount equal to the fair market value of the underlying stock on the date of award. For approximately 1.0 shares of restricted stock that vested in 2002 based on the achievement of synergy goals established in connection with the Fred Meyer merger, the Company recorded expense in an amount equal to the fair market value of the underlying stock on the date the synergy goals were achieved. The Company issued approximately 0.2, 0.7 and 1.1 shares of restricted stock in 2004, 2003 and 2002, respectively. As of January 29, 2005, approximately 0.1 shares of common stock were available for future restricted stock awards. Compensation expense included in net earnings for restricted stock awards totaled approximately \$8, \$8 and \$6, after-tax, in 2004, 2003 and 2002, respectively.

Changes in options outstanding under the stock option plans, excluding restricted stock awards, were:

	<u>Shares subject to option</u>	<u>Weighted average exercise price</u>
Outstanding, year-end 2001	59.7	\$ 15.48
Granted	14.5	\$ 18.53
Exercised	(6.8)	\$ 6.27
Canceled or Expired	(1.2)	\$ 22.31
	<u>66.2</u>	<u>\$ 16.97</u>
Outstanding, year-end 2002	66.2	\$ 16.97
Granted	0.3	\$ 16.34
Exercised	(4.9)	\$ 7.59
Canceled or Expired	(1.5)	\$ 21.19
	<u>60.1</u>	<u>\$ 17.62</u>
Outstanding, year-end 2003	60.1	\$ 17.62
Granted	6.7	\$ 17.28
Exercised	(4.2)	\$ 7.29
Canceled or Expired	(1.1)	\$ 20.99
	<u>61.5</u>	<u>\$ 18.20</u>
Outstanding, year-end 2004	61.5	\$ 18.20

A summary of options outstanding and exercisable at January 29, 2005 follows:

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Range of Exercise Prices	Number Outstanding	Weighted- Average Remaining Contractual Life	Weighted- Average Exercise Price	Options Exercisable	Weighted- Average Exercise Price
		(In years)			
\$ 3.57 - \$10.37	\$ 9.7	1.00	\$ 8.78	9.7	\$ 8.78
\$10.38 - \$14.92	\$ 12.6	5.66	\$ 14.34	9.0	\$ 14.11
\$14.93 - \$16.59	\$ 6.2	5.15	\$ 16.55	4.8	\$ 16.56
\$16.60 - \$22.81	\$ 13.5	6.26	\$ 19.31	5.9	\$ 21.05
\$22.82 - \$31.91	\$ 19.5	5.74	\$ 25.14	14.1	\$ 25.45
	\$ 61.5	5.03	\$ 18.20	43.5	\$ 17.81

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If compensation cost for the Company's stock option plans had been determined based upon the fair value at the grant date for awards under these plans consistent with the methodology prescribed under SFAS No. 123, Accounting for Stock-Based Compensation, the Company's net earnings and diluted earnings per common share would have been reduced to the pro forma amounts below:

	2004		2003		2002	
	Actual	Pro Forma	Actual	Pro Forma	Actual	Pro Forma
Net earnings (loss)	\$ (100)	\$ (140)	\$ 312	\$ 272	\$ 1,202	\$ 1,161
Earnings (loss) per diluted common share	\$ (0.14)	\$ (0.19)	\$ 0.41	\$ 0.36	\$ 1.52	\$ 1.47

The fair value of each option grant was estimated on the date of grant using the Black-Scholes option-pricing model, based on historical assumptions shown in the table below. These amounts reflected in this pro forma disclosure are not indicative of future amounts. The following table reflects the assumptions used for grants awarded in each year to option holders:

	2004	2003	2002
Weighted average expected volatility (based on historical volatility)	30.13%	30.23%	29.72%
Weighted average risk-free interest rate	3.99%	3.33%	4.40%
Expected term (based on historical results)	8.7 years	8.5 years	8.4 years

The weighted average fair value of options granted during 2004, 2003 and 2002 was \$7.91, \$7.09 and \$8.49, respectively. The Company utilizes a risk-free interest rate based upon the yield of a treasury note maturing at a date that approximates the option's vest date.

Grants in 2004 returned to normal levels after grants in 2003 were unusually low and, conversely, grants in 2002 were unusually high, due primarily to a general grant of approximately 3.8 stock options to management and support employees, and approximately 3.9 options to executives including senior officers and division presidents, that was approved by the Compensation Committee of the Board of Directors on December 12, 2002 (fiscal 2002). This grant replaced a planned grant in May 2003 and was accelerated to secure the continued alignment of employee interests with those of the shareholders as strategic plans are implemented. The Committee also made awards of restricted stock to senior officers and division presidents in recognition of their vital role in a challenging operating environment. The restrictions on these shares will lapse after three years, assuming the recipients' continued employment with the Company during that period.

In addition to the stock options described above, at January 29, 2005, there were 4.2 warrants outstanding. The warrants, exercisable at \$11.91, were originally issued pursuant to a Warrant Agreement dated May 23, 1996. Approximately 0.5 warrants expire in May 2005 and the remaining 3.7 warrants expire in May 2006.

14. COMMITMENTS AND CONTINGENCIES

The Company continuously evaluates contingencies based upon the best available evidence.

The Company believes that allowances for loss have been provided to the extent necessary and that its assessment of contingencies is reasonable. To the extent that resolution of contingencies results in amounts that vary from the Company's estimates, future earnings will be

charged or credited.

The principal contingencies are described below:

Insurance The Company's workers' compensation risks are self-insured in certain states. In addition, other workers' compensation risks and certain levels of insured general liability risks are based on retrospective premium plans, deductible plans, and self-insured retention plans. The liability for workers' compensation risks is accounted for on a present value basis. Actual claim settlements and expenses incident thereto may differ from the provisions for loss. Property risks have been underwritten by a subsidiary and are reinsured with unrelated insurance companies. Operating divisions and subsidiaries have paid premiums, and the insurance subsidiary has provided loss allowances, based upon actuarially determined estimates.

Litigation The United States Attorney's Office for the Central District of California is investigating the hiring practices of Ralphs Grocery Company (Ralphs), a wholly-owned subsidiary of The Kroger Co., during the labor dispute from October 2003

through February 2004. Among matters under investigation is the extent to which some locked-out employees were allowed to work under false identities or false Social Security numbers, despite Company policy forbidding such conduct. A grand jury has convened to consider whether such acts violated federal criminal statutes. The Company is cooperating with the investigation. Although the Company expects some adverse action to be taken, management is not able to estimate the dollar amount of penalties or liability Ralphs may incur. In addition, these alleged practices are the subject of claims that Ralphs' conduct of the lockout was unlawful, and that Ralphs is liable under the National Labor Relations Act (NLRA). The Los Angeles Regional Office of the National Labor Relations Board (NLRB) has notified the charging parties that all charges alleging that Ralphs' lockout violated the NLRA have been dismissed. That decision is being appealed to the General Counsel of the NLRB.

On February 2, 2004, the Attorney General for the State of California filed an action in Los Angeles federal court (California, ex rel Lockyer v. Safeway, Inc. dba Vons, a Safeway Company; Albertson's, Inc. and Ralphs Grocery Company, a division of The Kroger Co., United States District Court Central District of California, Case No. CV04-0687) alleging that certain provisions of the Mutual Strike Assistance Agreement (the Agreement) between the Company, Albertson's, Inc. and Safeway Inc. (collectively, the Retailers) which contained a provision designed to prevent the union from placing disproportionate pressure on one or more of the Retailers by picketing such Retailer(s) but not the other Retailer(s) during the labor dispute in southern California violated Section 1 of the Sherman Act. The lawsuit seeks declarative and injunctive relief. Under the Agreement, the Company paid approximately \$147 million to the other Retailers. The lawsuit raises claims that could question the validity of those payments as well as claims that the Retailers unlawfully restrained competition. The Company continues to believe it has strong defenses against this lawsuit and is vigorously defending it. Although this lawsuit is subject to uncertainties inherent to the litigation process, based on the information presently available to the Company, management does not expect that the ultimate resolution of this action will have a material effect, favorable or adverse, on the Company's financial condition, results of operation or cash flows.

On November 24, 2004, the Company was notified by the office of the United States Attorney for the District of Colorado that the Drug Enforcement Agency (DEA) had referred a matter to it for investigation regarding alleged violations of the Controlled Substances Act by the Company's King Soopers division. The government alleges that ineffective controls and procedures, as well as improper record keeping, permitted controlled substances to be diverted from pharmacies operated by King Soopers. As a result of these allegations, the Company has retained a consultant to assist it in reviewing its policies and procedures, record keeping and training in its pharmacies, and is taking corrective action, as warranted. The Company is cooperating with the Assistant U.S. Attorney and the DEA, and expects to resolve this matter in the near future. The Company does not expect that the ultimate resolution of this investigation will have a material effect on the Company's financial condition, results of operations or cash flows.

On March 30, 2005, the United States District Court for the Northern District of Illinois rendered a decision in an action (Central States, Southeast and Southwest Areas Pension Fund et al. v. The Kroger Co.) alleging that the Company has failed to make contributions to a multi-employer pension fund in connection with certain employees the Company had viewed as exempt from the contribution requirement. The Court's decision was adverse to the Company's position, resulting in an order that would require payments of approximately \$13 million. The Company has not yet decided whether to appeal. A related decision, also adverse to the Company, has been appealed to the United States Court of Appeals for the Seventh Circuit and is awaiting decision. The ultimate resolution is not expected to have a material effect on the results of operations as the Company believes it has recorded adequate allowances related to these contingencies.

Various claims and lawsuits arising in the normal course of business, including suits charging violations of certain antitrust and civil rights laws, are pending against the Company. Some of these suits purport or have been determined to be class actions and/or seek substantial damages. Any damages that may be awarded in antitrust cases will be automatically trebled. Although it is not possible at this time to evaluate the merits of all of these claims and lawsuits, nor their likelihood of success, the Company is of the belief that any resulting liability will not have a material adverse effect on the Company's financial position.

The Company continually evaluates its exposure to loss contingencies arising from pending or threatened litigation and believes it has made adequate provisions therefor. Nonetheless, assessing and predicting the outcomes of these matters involves substantial uncertainties. It remains possible that despite management's current belief, material differences in actual outcomes or changes in management's evaluation or predications could arise that could have a material adverse impact on the Company's financial condition or results of operation.

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Guarantees The Company periodically enters into real estate joint ventures in connection with the development of certain properties. The Company usually sells its interests in such partnerships upon completion of the projects. As of January 29, 2005, the Company was a partner with 50% ownership in four real estate joint ventures for which it has guaranteed approximately \$12 of debt incurred by the ventures. Based on the covenants underlying this indebtedness as of January 29, 2005, it is unlikely that the Company will be responsible for repayment of these obligations.

Assignments The Company is contingently liable for leases that have been assigned to various third parties in connection with facility closings and dispositions. The Company could be required to satisfy the obligations under the leases if any of the assignees are unable to fulfill their lease obligations. Due to the wide distribution of the Company's assignments among third parties, and various other remedies available, the Company believes the likelihood that it will be required to assume a material amount of these obligations is remote.

15. SUBSEQUENT EVENTS

On March 16, 2005, Standard & Poor's Ratings Services placed its ratings for the Company, as well as Safeway Inc. and Albertson's, Inc., on CreditWatch with negative implications. Standard & Poor's indicated that it expects any downgrade, if warranted by their review, to be limited to one level, with ratings not expected to fall below investment grade.

16. WARRANT DIVIDEND PLAN

On February 28, 1986, the Company adopted a warrant dividend plan providing for stock purchase rights to owners of the Company's common stock. The plan was amended and restated as of April 4, 1997, and further amended on October 18, 1998. Each share of common stock currently has attached one-fourth of a right. Each right, when exercisable, entitles the holder to purchase from the Company one ten-thousandth of a share of Series A Preferred Shares, par value \$100 per share, at \$87.50 per one ten-thousandth of a share. The rights will become exercisable, and separately tradable, 10 business days following a tender offer or exchange offer resulting in a person or group having beneficial ownership of 10% or more of the Company's common stock. In the event the rights become exercisable and thereafter the Company is acquired in a merger or other business combination, each right will entitle the holder to purchase common stock of the surviving corporation, for the exercise price, having a market value of twice the exercise price of the right. Under certain other circumstances, including certain acquisitions of the Company in a merger or other business combination transaction, or if 50% or more of the Company's assets or earnings power are sold under certain circumstances, each right will entitle the holder to receive upon payment of the exercise price, shares of common stock of the acquiring company with a market value of two times the exercise price. At the Company's option, the rights, prior to becoming exercisable, are redeemable in their entirety at a price of \$0.01 per right. The rights are subject to adjustment and expire March 19, 2006.

17. STOCK

Preferred Stock

The Company has authorized 5 shares of voting cumulative preferred stock; 2 were available for issuance at January 29, 2005. Fifty thousand shares have been designated as Series A Preferred Shares and are reserved for issuance under the Company's warrant dividend plan. The stock has a par value of \$100 and is issuable in series.

Common Stock

The Company has authorized 1,000 shares of common stock, \$1 par value per share. On May 20, 1999, the shareholders authorized an amendment to the Amended Articles of Incorporation to increase the authorized shares of common stock from 1,000 to 2,000 when the Board of Directors determines it to be in the best interest of the Company.

Common Stock Repurchase Program

In December 1999, the Company began a program to repurchase common stock to reduce dilution resulting from its employee stock option plans. This program is solely funded by proceeds from stock option exercises, including the tax benefit. The Company reacquired approximately \$28, \$24 and \$65 under the stock option program in fiscal 2004, 2003 and 2002, respectively. Effective December 10, 2002, the Board authorized an additional stock repurchase program totaling \$500. The Company made open market purchases of \$277 and \$63 under this plan in fiscal 2003 and 2002, respectively. During fiscal 2004, the Company made open market purchases totaling \$144 to complete the program. In September 2004, the Board authorized a new \$500 stock repurchase program to replace the December 2002 program. As of January 29, 2005, the Company had made open market purchases totaling \$147 under the September 2004 program. Purchases of stock under the Board approved repurchase programs are made when the expected return exceeds our cost of capital.

18. BENEFIT PLANS

The Company administers non-contributory defined benefit retirement plans for substantially all non-union employees and some union-represented employees as determined by the terms and conditions of collective bargaining agreements. Funding for the pension plans is based on a review of the specific requirements and on evaluation of the assets and liabilities of each plan.

In addition to providing pension benefits, the Company provides certain health care benefits for retired employees. The majority of the Company's employees may become eligible for these benefits if they reach normal retirement age while employed by the Company. Funding of retiree health care benefits occurs as claims or premiums are paid.

Information with respect to change in benefit obligation, change in plan assets, net amounts recognized at end of fiscal years, weighted average assumptions and components of net periodic benefit cost follow:

	Pension Benefits		Other Benefits	
	2004	2003	2004	2003
Change in benefit obligation:				
Benefit obligation at beginning of fiscal year	\$ 1,844	\$ 1,674	\$ 363	\$ 352
Service cost	107	100	10	8
Interest cost	115	107	21	21
Plan participants' contributions			9	8
Amendments		13	(24)	(41)
Actuarial loss	161	35	19	44
Benefits paid	(95)	(85)	(32)	(29)
Benefit obligation at end of fiscal year	\$ 2,132	\$ 1,844	\$ 366	\$ 363
Change in plan assets:				
Fair value of plan assets at beginning of fiscal year	\$ 1,379	\$ 1,089	\$	\$
Actual return on plan assets	135	271		
Employer contribution	39	104	23	21
Plan participants' contributions			9	8
Benefits paid	(95)	(85)	(32)	(29)
Fair value of plan assets at end of fiscal year	\$ 1,458	\$ 1,379	\$	\$

Pension plan assets include \$112 and \$134 of common stock of The Kroger Co. at January 29, 2005 and January 31, 2004, respectively. The plan owned 6.6 and 7.3 shares of The Kroger Co. common stock at January 29, 2005 and January 31, 2004, respectively.

	Pension Benefits		Other Benefits	
	2004	2003	2004	2003

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Net liability recognized at end of fiscal year:				
Funded status at end of year	\$ (674)	\$ (465)	\$ (366)	\$ (363)
Unrecognized actuarial (gain) loss	498	361	45	34
Unrecognized prior service cost	22	28	(60)	(50)
Unrecognized net transition (asset) obligation		(1)	1	1
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Net liability recognized at end of fiscal year	\$ (154)	\$ (77)	\$ (380)	\$ (378)
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Prepaid benefit cost	\$	\$ 2	\$	\$
Accrued benefit liability	(376)	(79)	(380)	(378)
Additional minimum liability	(123)	(227)		
Intangible asset	24	29		
Accumulated other comprehensive loss	321	198		
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Net liability recognized at end of fiscal year	\$ (154)	\$ (77)	\$ (380)	\$ (378)
	<u> </u>	<u> </u>	<u> </u>	<u> </u>

	Pension Benefits		Other Benefits	
	2004	2003	2004	2003
Weighted average assumptions				
Discount rate Benefit obligation	5.75%	6.25%	5.75%	6.25%
Discount rate Net periodic benefit cost	6.25%	6.75%	6.25%	6.75%
Expected return on plan assets	8.50%	8.50%		
Rate of compensation increase	3.50%	3.50%		

To determine the expected return on pension plan assets, the Company contemplates current and forecasted plan asset allocations as well as historical and forecasted returns on various asset categories. The average annual return on pension plan assets was 10.9% for the ten calendar years ended December 31, 2004, net of all fees and expenses. The Company reduced the pension return assumption to 8.5% for 2004 and 2003 from 9.5% in 2002. The Company believes the reduction in the pension return assumption was appropriate because future returns are not expected to achieve the same level of performance as the historical average annual return. For measurement purposes, a 9% initial annual rate of increase, and a 5% ultimate annual rate of increase, in the per capita cost of other benefits, were assumed for pre-retirement age personnel in 2004. In 2003, a 10% initial annual rate of increase, and a 5% ultimate annual rate of increase were assumed.

	Pension Benefits			Other Benefits		
	2004	2003	2002	2004	2003	2002
Components of net periodic benefit cost:						
Service cost	\$ 107	\$ 100	\$ 78	\$ 10	\$ 8	\$ 13
Interest cost	115	107	108	21	21	24
Expected return on plan assets	(121)	(122)	(134)			
Amortization of:						
Transition asset	(1)	(1)	(1)			
Prior service cost	5	5	3	(5)	(5)	(2)
Actuarial (gain) loss	12	3	2			(2)
Net periodic benefit cost	\$ 117	\$ 92	\$ 56	\$ 26	\$ 24	\$ 33

The following table provides the projected benefit obligation (PBO), accumulated benefit obligation (ABO) and the fair value of plan assets for all company-sponsored pension plans. As of year-end 2005, the PBO, ABO and fair value of plan assets related to the nonqualified, excess retirement benefit plan (Nonqualified Plan) were \$86, \$80 and \$0, respectively. The Nonqualified Plan is not funded because of unfavorable tax treatment that would be received if it were funded.

	2004	2003
PBO at end of fiscal year	\$ 2,132	\$ 1,844
ABO at end of fiscal year	\$ 1,957	\$ 1,683
Fair value of plan assets at end of year	\$ 1,458	\$ 1,379

The following table provides information about the target and actual pension plan asset allocations. Allocation percentages are shown as of December 31 for each respective year. The pension plan measurement date is the December 31st nearest the fiscal year-end.

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	Target allocations	Actual allocations	
	2004	2004	2003
Pension plan asset allocation, as of December 31:			
Domestic equity securities	40.0%	39.5%	40.7%
International equity securities	22.0	25.1	24.1
Investment grade debt securities	19.0	18.6	21.3
High yield debt securities	8.0	8.2	8.6
Private equity	5.0	3.8	3.5
Hedge funds	3.0	2.3	0.0
Real estate	3.0	0.5	0.4
Other	0.0	2.0	1.4
Total	100.0%	100.0%	100.0 %

Investment objectives, policies and strategies are set by the Pension Investment Committee (the Committee) appointed by the CEO. The primary objectives include holding, protecting and investing the assets and distributing benefits to participants and beneficiaries of the pension plans. Investment objectives have been established based on a comprehensive review of the capital markets and each underlying plan's current and projected financial requirements. The time horizon of the investment objectives is long-term in nature and plan assets are managed on a going-concern basis.

Investment objectives and guidelines specifically applicable to each manager of assets are established and reviewed annually. Derivative instruments may be used for specified purposes. Any use of derivative instruments for a purpose or in a manner not specifically authorized is prohibited, unless approved in advance by the Committee. Common stock of The Kroger Co. is included in plan assets subject to statutory limitations restricting additional purchases when the fair value of the stock equals or exceeds 10% of plan assets.

The current target allocations shown represent 2005 targets that were established in 2004. To maintain actual asset allocations consistent with target allocations, assets are reallocated or rebalanced on a regular basis. Cash flow from employer contributions and participant benefit payments is used to fund underweight asset classes and divest overweight asset classes, as appropriate. The Company expects that cash flow will be sufficient to meet most rebalancing needs. The Company made cash contributions of \$35 in 2004 and \$100 in 2003. The Company is required to make cash contributions totaling \$142 during fiscal 2005, and may make additional contributions throughout fiscal 2005. The Company expects any additional contributions made during 2005 will reduce its minimum required contributions in future years.

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. A one-percentage-point change in the assumed health care cost trend rates would have the following effects:

	<u>1% Point Increase</u>	<u>1% Point Decrease</u>
Effect on total of service and interest cost components	\$ 4	\$ (4)
Effect on postretirement benefit obligation	\$ 44	\$ (38)

The Company also contributes to various multi-employer pension plans based on obligations arising from most of its collective bargaining agreements. These plans provide retirement benefits to participants based on their service to contributing employers. The benefits are paid from assets held in trust for that purpose. Trustees are appointed in equal number by employers and unions. The trustees typically are responsible for determining the level of benefits to be provided to participants as well as for such matters as the investment of the assets and the administration of the plans.

The Company recognizes expense in connection with these plans as contributions are funded, in accordance with GAAP. The Company made contributions to these plans, and recognized expense, of \$180 in 2004, \$169 in 2003, and \$153 in 2002. The Company estimates it would have contributed an additional \$2 million in 2004 and \$13 million in 2003, but its obligation to contribute was suspended during the labor disputes.

Based on the most recent information available to it, the Company believes that the present value of actuarial accrued liabilities in most or all of these multi-employer plans substantially exceeds the value of the assets held in trust to pay benefits. Although underfunding can result in the imposition of excise taxes on contributing employers, increased contributions can reduce underfunding so that excise taxes are not triggered. Moreover, if the Company were to exit certain markets or otherwise cease making contributions to these funds, the Company could trigger a substantial withdrawal liability. Any adjustment for withdrawal liability will be recorded when it is probable that a liability exists and can be reasonably estimated, in accordance with GAAP.

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The Company also administers certain defined contribution plans for eligible union and non-union employees. The cost of these plans for 2004, 2003 and 2002 was \$12, \$14 and \$20, respectively.

19. RECENTLY ISSUED ACCOUNTING STANDARDS

In May 2004, the FASB issued Staff Position (FSP) No. 106-2, Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003. FSP No. 106-2 supersedes FSP No. 106-1, Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003, and provides guidance on the accounting, disclosure and transition related to the Prescription Drug Act. FSP No. 106-2 became effective for the third quarter of 2004. The adoption of FSP No. 106-2 had no material effect on the Company's Consolidated Financial Statements. Detailed regulations in this area continue to evolve that could have an effect on the Company going forward, which effect the Company does not expect to be material.

In December 2004, the FASB issued FSP No. 109-1, Application of FASB Statement No. 109, Accounting for Income Taxes, to the Tax Deduction on Qualified Production Activities Provided by the American Jobs Creation Act of 2004, which provides accounting and disclosure guidance on the Acts qualified production activities deduction. The Company is currently evaluating the impact of this guidance on its effective tax rate for 2005 and subsequent periods.

In December 2004, the FASB issued SFAS No. 123 (Revised 2004), Share-Based Payment (SFAS No. 123R), which replaces SFAS No. 123, supersedes APB No. 25 and related interpretations and amends SFAS No. 95, Statement of Cash Flows. The provisions of SFAS No. 123R are similar to those of SFAS No. 123; however, SFAS No. 123R requires all share-based payments to employees, including grants of employee stock options, to be recognized in the financial statements as compensation cost based on their fair value on the date of grant. Fair value of share-based awards will be determined using option pricing models (e.g. Black-Scholes or binomial models) and assumptions that appropriately reflect the specific circumstances of the awards. Compensation cost will be recognized over the vesting period based on the fair value of awards that actually vest. The Company expects to adopt SFAS No. 123R in the first quarter of 2006 and that the adoption to reduce net earnings by \$0.04-\$0.05 per diluted share during fiscal 2006.

In November 2004, the FASB issued SFAS No. 151, Inventory Costs, an amendment of ARB No. 43, Chapter 4 which clarifies that inventory costs that are abnormal are required to be charged to expense as incurred as opposed to being capitalized into inventory as a product cost. SFAS No. 151 provides examples of abnormal costs to include costs of idle facilities, excess freight and handling costs and spoilage. SFAS No. 151 will become effective for the Company's fiscal year beginning January 29, 2006. The adoption of SFAS No. 151 is not expected to have a material effect on the Company's Consolidated Financial Statements.

FASB Interpretation No. 47 (FIN 47) Accounting for Conditional Asset Retirement Obligations was issued by the FASB in March 2005. FIN 47 provides guidance relating to the identification of and financial reporting for legal obligations to perform an asset retirement activity. The Interpretation requires recognition of a liability for the fair value of a conditional asset retirement obligation when incurred if the liability's fair value can be reasonably estimated. FIN 47 is effective no later than the end of fiscal years ending after December 15, 2005. We do not expect adoption of FIN 47 to have a material effect on our Consolidated Financial Statements.

SFAS No. 145, Rescission of FASB Statement No. 4, 44, and 64, Amendment of FASB Statement No. 13 and Technical Corrections, was issued by the FASB in April of 2002. SFAS No. 145 became effective for Kroger on February 2, 2003. This Statement eliminates the requirement that gains and losses due to the extinguishment of debt be aggregated and, if material, classified as an extraordinary item, net of the related income tax effect. Adoption of SFAS No. 145 required us to reclassify the debt extinguishments recorded as extraordinary items in 2002 as interest expense in the respective periods. These debt extinguishments were recorded during the first two quarters of 2002 and totaled \$19 million of pre-tax expense. Pre-tax expense totaling \$18 related to premiums paid in connection with the repurchase of \$100 of long-term bonds, and the write-off of the related deferred financing costs, was recorded in 2003. The 2004 expenses of \$3 pre-tax, related to a premium paid in connection with the redemption of the Company's \$750 7.375% bonds due March 2005, net of the effect of reduced interest expense for the balance of the year.

20. GUARANTOR SUBSIDIARIES

The Company's outstanding public debt (the Guaranteed Notes) is jointly and severally, fully and unconditionally guaranteed by The Kroger Co. and some of its subsidiaries (the Guarantor Subsidiaries). At January 29, 2005, a total of approximately \$6.3 billion of Guaranteed Notes were outstanding. The Guarantor Subsidiaries and non-guarantor subsidiaries are wholly-owned subsidiaries of The Kroger Co. Separate financial statements of The Kroger Co. and each of the Guarantor Subsidiaries are not presented because the guarantees are full and unconditional and the Guarantor Subsidiaries are jointly and severally liable. The Company believes that separate financial statements and other disclosures concerning the Guarantor Subsidiaries would not be material to investors.

The non-guaranteeing subsidiaries represent less than 3% on an individual and aggregate basis of consolidated assets, pretax earnings, cash flow, and equity for all periods presented, except for consolidated pre-tax earnings in 2004 and 2003. Therefore, the non-guarantor subsidiaries information is not separately presented in the balance sheets and the statements of cash flows, but rather is included in the column labeled Guarantor Subsidiaries, for those periods. The non-guaranteeing subsidiaries represented approximately 10% of 2004 consolidated pre-tax earnings and 4% of 2003 consolidated pre-tax earnings. Therefore, the non-guarantor subsidiaries information is separately presented in the Condensed Consolidated Statements of Earnings for 2004 and 2003.

There are no current restrictions on the ability of the Guarantor Subsidiaries to make payments under the guarantees referred to above, except, however, the obligations of each guarantor under its guarantee are limited to the maximum amount as will result in obligations of such guarantor under its guarantee not constituting a fraudulent conveyance or fraudulent transfer for purposes of Bankruptcy Law, the Uniform Fraudulent Conveyance Act, the Uniform Fraudulent Transfer Act, or any similar Federal or state law (e.g., adequate capital to pay dividends under corporate laws).

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The following tables present summarized financial information as of January 29, 2005 and January 31, 2004 and for the three years ended January 29, 2005.

Condensed Consolidating

Balance Sheets

As of January 29, 2005

	<u>The Kroger Co.</u>	<u>Guarantor Subsidiaries</u>	<u>Eliminations</u>	<u>Consolidated</u>
Current assets				
Cash	\$ 32	\$ 112	\$	\$ 144
Store deposits in-transit	20	486		506
Receivables	81	747		828
Net inventories	415	3,941		4,356
Prepaid and other current assets	275	297		572
	<u>823</u>	<u>5,583</u>		<u>6,406</u>
Total current assets	823	5,583		6,406
Property, plant and equipment, net	1,277	10,220		11,497
Goodwill, net	20	2,171		2,191
Other assets	642	(245)		397
Investment in and advances to subsidiaries	10,518		(10,518)	
	<u>13,280</u>	<u>17,729</u>	<u>(10,518)</u>	<u>20,491</u>
Total Assets	\$ 13,280	\$ 17,729	\$ (10,518)	\$ 20,491
Current liabilities				
Current portion of long-term debt including obligations under capital leases	\$ 71	\$	\$	\$ 71
Accounts payable	(314)	4,092		3,778
Other current liabilities	319	2,148		2,467
	<u>76</u>	<u>6,240</u>		<u>6,316</u>
Total current liabilities	76	6,240		6,316
Long-term debt including obligations under capital leases				
Face value long-term debt including obligations under capital leases	7,797	33		7,830
Adjustment to reflect fair value interest rate hedges	70			70
	<u>7,867</u>	<u>33</u>		<u>7,900</u>
Long-term debt including obligations under capital leases	7,867	33		7,900
Fair value interest rate hedges	11			11
Other long-term liabilities	1,786	938		2,724
	<u>9,740</u>	<u>7,211</u>		<u>16,951</u>
Total Liabilities	9,740	7,211		16,951
Shareowners Equity	3,540	10,518	(10,518)	3,540
	<u>13,280</u>	<u>17,729</u>	<u>(10,518)</u>	<u>20,491</u>
Total Liabilities and Shareowners equity	\$ 13,280	\$ 17,729	\$ (10,518)	\$ 20,491

Condensed Consolidating

Balance Sheets

As of January 31, 2004

	The Kroger Co.	Guarantor Subsidiaries	Eliminations	Consolidated
Current assets				
Cash	\$ 26	\$ 133	\$	\$ 159
Store deposits in-transit	64	515		579
Receivables	106	634		740
Net inventories	414	3,755		4,169
Prepaid and other current assets	271	280		551
	<u>881</u>	<u>5,317</u>		<u>6,198</u>
Total current assets	881	5,317		6,198
Property, plant and equipment, net	1,129	10,049		11,178
Goodwill, net	21	3,113		3,134
Fair value interest rate hedges	6			6
Other assets	576	(329)		247
Investment in and advances to subsidiaries	11,982		(11,982)	
	<u>14,595</u>	<u>18,150</u>	<u>(11,982)</u>	<u>20,763</u>
Total Assets	\$ 14,595	\$ 18,150	\$ (11,982)	\$ 20,763
Current liabilities				
Current portion of long-term debt including obligations under capital leases	\$ 242	\$ 6	\$	\$ 248
Accounts payable	215	3,422		3,637
Other current liabilities	689	1,591		2,280
	<u>1,146</u>	<u>5,019</u>		<u>6,165</u>
Total current liabilities	1,146	5,019		6,165
Long-term debt including obligations under capital leases				
Face value long-term debt including obligations under capital leases	7,699	313		8,012
Adjustment to reflect fair value interest rate hedges	104			104
	<u>7,803</u>	<u>313</u>		<u>8,116</u>
Long-term debt including obligations under capital leases	7,803	313		8,116
Other long-term liabilities	1,661	836		2,497
	<u>10,610</u>	<u>6,168</u>		<u>16,778</u>
Total Liabilities	10,610	6,168		16,778
Shareowners Equity	3,985	11,982	(11,982)	3,985
	<u>14,595</u>	<u>18,150</u>	<u>(11,982)</u>	<u>20,763</u>
Total Liabilities and Shareowners equity	\$ 14,595	\$ 18,150	\$ (11,982)	\$ 20,763

Condensed Consolidating**Statements of Operations****For the Year ended January 29, 2005**

	<u>The Kroger Co.</u>	<u>Guarantor Subsidiaries</u>	<u>Non-Guarantor Subsidiaries</u>	<u>Eliminations</u>	<u>Consolidated</u>
Sales	\$ 8,003	\$ 49,432	\$ 41	\$ (1,042)	\$ 56,434
Merchandise costs, including warehousing and transportation	6,420	36,721		(1,001)	42,140
Operating, general and administrative	1,126	9,494	(9)		10,611
Rent	194	527		(41)	680
Depreciation and amortization	110	1,142	4		1,256
Goodwill impairment charge		900			900
	<u>153</u>	<u>648</u>	<u>46</u>		<u>847</u>
Interest expense	529	6	22		557
Equity in earnings of subsidiaries	434			(434)	
	<u>58</u>	<u>642</u>	<u>24</u>	<u>(434)</u>	<u>290</u>
Earnings (loss) before tax expense	58	642	24	(434)	290
Tax expense (benefit)	158	231	1		390
	<u>(100)</u>	<u>411</u>	<u>23</u>	<u>(434)</u>	<u>(100)</u>
Net earnings (loss)	\$ (100)	\$ 411	\$ 23	\$ (434)	\$ (100)

Condensed Consolidating**Statements of Operations****For the Year ended January 31, 2004**

	<u>The Kroger Co.</u>	<u>Guarantor Subsidiaries</u>	<u>Non-Guarantor Subsidiaries</u>	<u>Eliminations</u>	<u>Consolidated</u>
Sales	\$ 6,935	\$ 47,752	\$ 45	\$ (941)	\$ 53,791
Merchandise costs, including warehousing and transportation	5,583	34,943		(889)	39,637
Operating, general and administrative	1,305	9,060	(11)		10,354
Rent	168	541		(52)	657
Depreciation and amortization	91	1,114	4		1,209
Goodwill impairment charge		444			444
Asset impairment charge		120			120
	<u>(212)</u>	<u>1,530</u>	<u>52</u>		<u>1,370</u>
Operating profit (loss)	(212)	1,530	52		1,370
Interest expense	568	15	21		604
Equity in earnings of subsidiaries	966			(966)	
	<u>186</u>	<u>1,515</u>	<u>31</u>	<u>(966)</u>	<u>766</u>
Earnings (loss) before tax expense	186	1,515	31	(966)	766
Tax expense (benefit)	(126)	571	9		454

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Net earnings (loss)	<u>\$ 312</u>	<u>\$ 944</u>	<u>\$ 22</u>	<u>\$ (966)</u>	<u>\$ 312</u>
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Condensed Consolidating

Statements of Operations

For the Year ended February 1, 2003

	The Kroger Co.	Guarantor Subsidiaries	Eliminations	Consolidated
Sales	\$ 6,545	\$ 46,100	\$ (885)	\$ 51,760
Merchandise costs, including warehousing and transportation	5,254	33,389	(833)	37,810
Operating, general and administrative	1,230	8,388		9,618
Rent	168	544	(52)	660
Depreciation and amortization	86	1,001		1,087
Merger-related costs, restructuring charges and related items	10	6		16
Operating profit (loss)	(203)	2,772		2,569
Interest expense	583	36		619
Equity in earnings of subsidiaries	1,710		(1,710)	
Earnings (loss) before tax expense	924	2,736	(1,710)	1,950
Tax expense (benefit)	(294)	1,026		732
Earnings (loss) before cumulative effect of an Accounting change	1,218	1,710	(1,710)	1,218
Cumulative effect of an accounting change	(16)			(16)
Net earnings (loss)	\$ 1,202	\$ 1,710	\$ (1,710)	\$ 1,202

Condensed Consolidating

Statements of Cash Flows

For the Year ended January 29, 2005

	<u>The Kroger Co.</u>	<u>Guarantor Subsidiaries</u>	<u>Consolidated</u>
Net cash provided by operating activities	\$ (890)	\$ 3,220	\$ 2,330
Cash flows from investing activities:			
Capital expenditures	(161)	(1,454)	(1,615)
Other	22	(15)	7
Net cash used by investing activities	(139)	(1,469)	(1,608)
Cash flows from financing activities:			
Proceeds from issuance of long-term debt	616		616
Reductions in long-term debt	(724)	(286)	(1,010)
Proceeds from issuance of capital stock	25		25
Capital stock reacquired	(319)		(319)
Other	(27)	(22)	(49)
Net change in advances to subsidiaries	1,464	(1,464)	
Net cash provided (used) by financing activities	1,035	(1,772)	(737)
Net (decrease) increase in cash and temporary cash investments	6	(21)	(15)
Cash and temporary investments:			
Beginning of year	26	133	159
End of year	\$ 32	\$ 112	\$ 144

Condensed Consolidating

Statements of Cash Flows

For the Year ended January 31, 2004

	The Kroger Co.	Guarantor Subsidiaries	Consolidated
Net cash provided by operating activities	\$ 385	\$ 1,830	\$ 2,215
Cash flows from investing activities:			
Capital expenditures	(176)	(1,824)	(2,000)
Other	(59)	33	(26)
Net cash used by investing activities	(235)	(1,791)	(2,026)
Cash flows from financing activities:			
Proceeds from issuance of long-term debt	247	100	347
Reductions in long-term debt	(347)	(140)	(487)
Proceeds from issuance of capital stock	39		39
Proceeds from interest rate swap terminations	114		114
Capital stock reacquired	(301)		(301)
Other	(23)	110	87
Net change in advances to subsidiaries	104	(104)	
Net cash provided (used) by financing activities	(167)	(34)	(201)
Net (decrease) increase in cash and temporary cash investments	(17)	5	(12)
Cash and temporary investments:			
Beginning of year	43	128	171
End of year	\$ 26	\$ 133	\$ 159

Condensed Consolidating

Statements of Cash Flows

For the Year ended February 1, 2003

	The Kroger Co.	Guarantor Subsidiaries	Consolidated
	<u> </u>	<u> </u>	<u> </u>
Net cash provided by operating activities	\$ 2,171	\$ 1,012	\$ 3,183
	<u> </u>	<u> </u>	<u> </u>
Cash flows from investing activities:			
Capital expenditures	(173)	(1,718)	(1,891)
Other	51	(67)	(16)
	<u> </u>	<u> </u>	<u> </u>
Net cash used by investing activities	(122)	(1,785)	(1,907)
	<u> </u>	<u> </u>	<u> </u>
Cash flows from financing activities:			
Proceeds from issuance of long-term debt	1,353		1,353
Reductions in long-term debt	(1,702)	(55)	(1,757)
Proceeds from issuance of capital stock	41		41
Capital stock reacquired	(785)		(785)
Other	(25)	(93)	(118)
Net change in advances to subsidiaries	(913)	913	
	<u> </u>	<u> </u>	<u> </u>
Net cash provided (used) by financing activities	(2,031)	765	(1,266)
	<u> </u>	<u> </u>	<u> </u>
Net (decrease) increase in cash and temporary cash investments	18	(8)	10
Cash and temporary investments:			
Beginning of year	25	136	161
	<u> </u>	<u> </u>	<u> </u>
End of year	\$ 43	\$ 128	\$ 171
	<u> </u>	<u> </u>	<u> </u>

21. QUARTERLY DATA (UNAUDITED)

	Quarter				Total Year (52 Weeks)
	First (16 Weeks)	Second (12 Weeks)	Third (12 Weeks)	Fourth (12 Weeks)	
2004					
Sales	\$ 16,905	\$ 12,980	\$ 12,854	\$ 13,695	\$ 56,434
Net earnings (loss)	\$ 263	\$ 142	\$ 143	\$ (648)	\$ (100)
Net earnings (loss) per basic common share	\$ 0.35	\$ 0.19	\$ 0.19	\$ (0.89)	\$ (0.14)
Average number of shares used in basic calculation	741	737	736	730	736
Net earnings (loss) per diluted common share	\$ 0.35	\$ 0.19	\$ 0.19	\$ (0.89)	\$ (0.14)
Average number of shares used in diluted calculation	749	744	742	730	736
	First (16 Weeks)	Second (12 Weeks)	Third (12 Weeks)	Fourth (12 Weeks)	Total Year (52 Weeks)
2003					
Sales	\$ 16,266	\$ 12,351	\$ 12,141	\$ 13,033	\$ 53,791
Net earnings (loss)	\$ 352	\$ 190	\$ 110	\$ (340)	\$ 312
Net earnings (loss) per basic common share	\$ 0.47	\$ 0.25	\$ 0.15	\$ (0.45)	\$ 0.42
Average number of shares used in basic calculation	754	747	743	743	747
Net earnings (loss) per diluted common share	\$ 0.46	\$ 0.25	\$ 0.15	\$ (0.45)	\$ 0.41
Average number of shares used in diluted calculation	761	756	754	743	754

PART IV

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES

(a)1. Financial Statements:

Report of Independent Auditors

Consolidated Balance Sheets as of January 29, 2005 and January 31, 2004

Consolidated Statements of Operations for the years ended January 29, 2005, January 31, 2004 and February 1, 2003

Consolidated Statements of Cash Flows for the years ended January 29, 2005, January 31, 2004 and February 1, 2003

Consolidated Statement of Changes in Shareowners Equity

Notes to Consolidated Financial Statements

(a)2. Financial Statement Schedules:

There are no Financial Statement Schedules included with this filing for the reason that they are not applicable or are not required or the information is included in the financial statements or notes thereto.

(a)3. Exhibits

- 3.1 Amended Articles of Incorporation of The Kroger Co. are incorporated by reference to Exhibit 3.1 of The Kroger Co. s Quarterly Report on Form 10-Q for the quarter ended October 3, 1998. The Kroger Co. s Regulations are incorporated by reference to Exhibit 4.2 of The Kroger Co. s Registration Statement on Form S-3 (Registration No. 33-57552) filed with the SEC on January 28, 1993.
- 4.1 Instruments defining the rights of holders of long-term debt of the Company and its subsidiaries are not filed as Exhibits because the amount of debt under each instrument is less than 10% of the consolidated assets of the Company. The Company undertakes to file these instruments with the Commission upon request.
- 10.1 Material Contracts Executive Employment Agreement dated as of November 30, 2001, between the Company and David B. Dillon. Incorporated by reference to Exhibit 10.2 to the Company s Form 10-K for fiscal year ended February 2, 2002.
- 10.2 Non-Employee Directors Deferred Compensation Plan. Incorporated by reference to Appendix J to Exhibit 99.1 of Fred Meyer, Inc. s Current Report on Form 8-K dated September 9, 1997, SEC File No. 1-133339.
- *10.3 The Kroger Co. Deferred Compensation Plan for Independent Directors.
- *10.4 The Kroger Co. Executive Deferred Compensation Plan.
- 10.5 Form of Amended and Restated Rights Agreement dated as of April 4, 1997. Incorporated by reference to Exhibit 1 of The Kroger Co. s Form 8-A/A filed with the SEC on April 4, 1997.
- 10.6 Amendment No. 1 to Amended and Restated Rights Agreement dated as of October 18, 1998. Incorporated by reference to Exhibit 2 of The Kroger Co. s Form 8-A/A filed with the SEC on October 27, 1998.
- 10.7 2005 Bonus Plan for Executive Officers. Incorporated by reference to Exhibit 99.1 of The Kroger Co. s Current Report on Form 8-K filed with the SEC on March 17, 2005.
- 10.8 The Kroger Co. 1997 Long-Term Incentive Plan. Incorporated by reference to Exhibit 4.2 of The Kroger Co. s Form S-8 filed with the SEC on May 15, 1997.
- 10.9 The Kroger Co. 1999 Long-Term Incentive Plan. Incorporated by reference to Exhibit 4.2 of The Kroger Co. s Form S-8 filed with the SEC on May 20, 1999.
- 10.10

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The Kroger Co. 2002 Long-Term Incentive Plan. Incorporated by reference to Exhibit 4.2 of The Kroger Co. s Form S-8 filed with the SEC on June 27, 2002.

- *10.11 Form of Restricted Stock Grant Agreement under Long-Term Incentive Plans.
- *10.12 Form of Non-Qualified Stock Option Grant Agreement under Long-Term Incentive Plans.

- 10.13 Five Year Credit Agreement dated as of May 20, 2004. Incorporated by reference to Exhibit 99.1 of The Kroger Co. s Current Report on Form 8-K filed with the SEC on May 24, 2004.
- 10.14 Five Year Credit Agreement dated as of May 22, 2002. Incorporated by reference to Exhibit 99.2 of The Kroger Co. s Current Report on Form 8-K filed with the SEC on May 24, 2002.
- *10.15 4(2) Commercial Paper Program Dealer Agreement between The Kroger Co., as Issuer and Banc of America Securities, LLC, as Dealer dated as of December 3, 2003, as amended on July 23, 2004.
- *10.16 4(2) Commercial Paper Program Dealer Agreement between The Kroger Co., as Issuer and Citigroup Global Markets Inc., as Dealer dated as of December 3, 2003, as amended on June 9, 2004.
- 10.17 Disclosure of compensation of non-employee directors. Incorporated by reference to Item 2.02 of The Kroger Co. s Form 8-K dated December 10, 2004.
- *12.1 Statement of Computation of Ratio of Earnings to Fixed Charges.
- *21.1 Subsidiaries of the Registrant.
- *23.1 Consent of Independent Accountants.
- *24.1 Powers of Attorney.
- *31.1 Rule 13a-14(a)/15d-14(a) Certification.
- *31.2 Rule 13a-14(a)/15d-14(a) Certification.
- 31.3 Rule 13a-14(a)/15d-14(a) Certification.
- 31.4 Rule 13a-14(a)/15d-14(a) Certification.
- *32.1 Section 1350 Certifications.
- 32.2 Section 1350 Certifications.

* Previously filed.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Company has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Dated: April 18, 2005

THE KROGER CO.
By (*David B. Dillon)
David B. Dillon
Chief Executive Officer
(principal executive officer)

Dated: April 18, 2005

By (*J. Michael Schlotman)
J. Michael Schlotman
Chief Financial Officer
(principal financial officer)

Dated: April 18, 2005

By (*M. Elizabeth Van Oflen)
M. Elizabeth Van Oflen
Vice President & Controller
(principal accounting officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Company and in the capacities indicated on the 18th of April 2005.

(*Reuben V. Anderson) Reuben V. Anderson	Director
Robert D. Beyer	Director
(*John L. Clendenin) John L. Clendenin	Director
(*David B. Dillon) David B. Dillon	Chairman and Chief Executive Officer
(*David B. Lewis)	Director

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David B. Lewis

(*John T. LaMacchia)
John T. LaMacchia

Director

(*Edward M. Liddy)
Edward M. Liddy

Director

(*Don W. McGeorge)
Don W. McGeorge

President, Chief Operating Officer, and Director

(*W. Rodney McMullen)
W. Rodney McMullen

Vice Chairman and Director

(*Clyde R. Moore)
Clyde R. Moore

Director

(*Katherine D. Ortega)
Katherine D. Ortega

Director

(*Steven R. Rogel)
Steven R. Rogel

Director

(*Bobby S. Shackouls)
Bobby S. Shackouls

Director

(*Susan M. Phillips)
Susan M. Phillips

Director

By: (*Bruce M. Gack)
Bruce M. Gack
Attorney-in-fact

EXHIBIT INDEX

Exhibit No.

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- 4.1 Instruments defining the rights of holders of long-term debt of the Company and its subsidiaries are not filed as Exhibits because the amount of debt under each instrument is less than 10% of the consolidated assets of the Company. The Company undertakes to file these instruments with the Commission upon request.
- 10.1 Material Contracts Executive Employment Agreement dated as of November 30, 2001, between the Company and David B. Dillon. Incorporated by reference to Exhibit 10.2 to the Company s Form 10-K for fiscal year ended February 2, 2002.
- 10.2 Non-Employee Directors Deferred Compensation Plan. Incorporated by reference to Appendix J to Exhibit 99.1 of Fred Meyer, Inc. s Current Report on Form 8-K dated September 9, 1997, SEC File No. 1-133339.
- *10.3 The Kroger Co. Deferred Compensation Plan for Independent Directors.
- *10.4 The Kroger Co. Executive Deferred Compensation Plan.
- 10.5 Form of Amended and Restated Rights Agreement dated as of April 4, 1997. Incorporated by reference to Exhibit 1 of The Kroger Co. s Form 8-A/A filed with the SEC on April 4, 1997.
- 10.6 Amendment No. 1 to Amended and Restated Rights Agreement dated as of October 18, 1998. Incorporated by reference to Exhibit 2 of The Kroger Co. s Form 8-A/A filed with the SEC on October 27, 1998.
- 10.7 2005 Bonus Plan for Executive Officers. Incorporated by reference to Exhibit 99.1 of The Kroger Co. s Current Report on Form 8-K filed with the SEC on March 17, 2005.
- 10.8 The Kroger Co. 1997 Long-Term Incentive Plan. Incorporated by reference to Exhibit 4.2 of The Kroger Co. s Form S-8 filed with the SEC on May 15, 1997.
- 10.9 The Kroger Co. 1999 Long-Term Incentive Plan. Incorporated by reference to Exhibit 4.2 of The Kroger Co. s Form S-8 filed with the SEC on May 20, 1999.
- 10.10 The Kroger Co. 2002 Long-Term Incentive Plan. Incorporated by reference to Exhibit 4.2 of The Kroger Co. s Form S-8 filed with the SEC on June 27, 2002.
- *10.11 Form of Restricted Stock Grant Agreement under Long-Term Incentive Plans.
- *10.12 Form of Non-Qualified Stock Option Grant Agreement under Long-Term Incentive Plans.
- 10.13 Five Year Credit Agreement dated as of May 20, 2004. Incorporated by reference to Exhibit 99.1 of The Kroger Co. s Current Report on Form 8-K filed with the SEC on May 24, 2004.
- 10.14 Five Year Credit Agreement dated as of May 22, 2002. Incorporated by reference to Exhibit 99.2 of The Kroger Co. s Current Report on Form 8-K filed with the SEC on May 24, 2002.
- *10.15 4(2) Commercial Paper Program Dealer Agreement between The Kroger Co., as Issuer and Banc of America Securities, LLC, as Dealer dated as of December 3, 2003, as amended on July 23, 2004.
- *10.16 4(2) Commercial Paper Program Dealer Agreement between The Kroger Co., as Issuer and Citigroup Global Markets Inc., as Dealer dated as of December 3, 2003, as amended on June 9, 2004.
- 10.17 Disclosure of compensation of non-employee directors. Incorporated by reference to Item 2.02 of The Kroger Co. s Form 8-K dated December 10, 2004.

- *12.1 Statement of Computation of Ratio of Earnings to Fixed Charges.
 - *21.1 Subsidiaries of the Registrant.
 - *23.1 Consent of Independent Accountants.
 - *24.1 Powers of Attorney.
 - *31.1 Rule 13a-14(a)/15d-14(a) Certification.
 - *31.2 Rule 13a-14(a)/15d-14(a) Certification.
 - 31.3 Rule 13a-14(a)/15d-14(a) Certification.
 - 31.4 Rule 13a-14(a)/15d-14(a) Certification.
 - *32.1 Section 1350 Certifications.
 - 32.2 Section 1350 Certifications.
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* Previously filed.