

Notes to the Consolidated Financial Statements

May 5, 2007 (in millions except share capital)

Note 1 Summary of Significant Accounting Policies

BASIS OF CONSOLIDATION

Empire Company Limited (the "Company") is a diversified Canadian company whose key businesses include food retailing, real estate and corporate investment activities. These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"), and include the accounts of the Company, all subsidiary companies, including 72.1% owned Sobeys Inc. ("Sobeys"), and certain enterprises considered variable interest entities ("VIEs") where control is achieved on a basis other than through ownership of a majority of voting rights. Investments in which the Company has significant influence are accounted for by the equity method. Investments in significant joint ventures are consolidated on a proportionate basis.

The Company's fiscal year ends on the first Saturday in May. As a result of this, the fiscal year is usually 52 weeks but results in a duration of 53 weeks every five to six years.

CHANGES IN ACCOUNTING POLICIES

ADOPTED DURING FISCAL 2007

Vendor consideration

During the first quarter of fiscal 2007, the Company implemented, on a retroactive basis, the Canadian Institute of Chartered Accountants ("CICA") Emerging Issues Committee ("EIC") Abstract 156, "Accounting by a Vendor for Consideration Given to a Customer (including a Reseller of the Vendor's Products)". This abstract requires a vendor to generally record cash consideration given to a customer as a reduction to the selling price of the vendor's products or services and reflect it as a reduction of revenue when recognized in the statement of earnings.

Prior to the implementation of EIC-156, the Company recorded certain sales incentives paid to independent franchisees, associates and independent accounts in cost of sales, selling and administrative expenses on the statement of earnings. Accordingly, the implementation of EIC-156 on a retroactive basis resulted in a reduction in both revenue and cost of sales, selling and administrative expenses during fiscal 2007 of \$141.2 (2006 – \$135.2). As reclassifications, these changes did not impact net earnings or earnings per share.

ADOPTED DURING FISCAL 2006

Vendor allowances

During the first quarter of fiscal 2006, the Company adopted the amendment to EIC-144 issued in January 2005. The amendment requires disclosure of the amount of any vendor allowances that have been recognized in income but for which the full requirements for entitlement have not yet been met (see Note 25).

FUTURE CHANGES IN ACCOUNTING POLICIES

Financial instruments

In January 2005, the CICA issued Section 3855 of the Handbook, "Financial Instruments – Recognition and Measurement", which describes the standards for recognizing and measuring financial assets, financial liabilities and derivatives. This Section requires that all financial assets be measured at fair value, with some exceptions for loans and investments that are classified as held-to-maturity, and that all financial liabilities be measured at fair value if they are derivatives or classified as held for trading purposes. Other financial liabilities are measured at their amortized cost, and all derivative financial instruments are measured at fair value, even when they are part of a hedging relationship.

The CICA has also reissued Handbook Section 3860 as Section 3861, "Financial Instruments – Disclosure and Presentation", which establishes standards for presentation of financial instruments and non-financial derivatives, and identifies the information that should be disclosed about them.

These changes are applicable to the Company for the first quarter of fiscal 2008. The effect of adopting this Section is not expected to be significant as investments, at a cost of \$188.2, have been sold in the first quarter of fiscal 2008 (see Note 27).

Hedges

In January 2005, the CICA issued Section 3865 of the Handbook, "Hedges", which describes how and when hedge accounting can be used.

Hedging is an activity used to change an exposure to one or more risks by creating an offset between changes in the fair value of a hedged item and a hedging item, changes in the cash flows attributable to a hedged item and a hedging item, or changes resulting from a risk exposure related to a hedged item and a hedging item.

Under hedge accounting, all gains, losses, revenues and expenses from the derivative and the item it hedges are recorded in the statement of earnings or the other comprehensive income statement in the same period.

These changes are applicable to the Company for the first quarter of fiscal 2008. The effect of adopting this section is not expected to be significant.

Comprehensive income

In January 2005, the CICA issued Handbook Section 1530, "Comprehensive Income". The section describes how to report and disclose comprehensive income and its components.

The main components of other comprehensive income include unrealized gains and losses on available-for-sale investments, and gains and losses on cash flow hedges.

These changes are applicable to the Company for the first quarter of fiscal 2008. The effect of adopting these sections is not expected to be significant.

Inventories

In March 2007, the CICA issued Handbook Section 3031, "Inventories", which has replaced existing Section 3030 with the same title. The new Section establishes that inventories should be measured at the lower of cost and net realizable value, with guidance on the determination of cost. The new standard is effective for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2008 and is therefore applicable for the Company's first quarter of fiscal 2009. The Company is currently evaluating the impact of this new standard.

Accounting changes

In July 2006, the CICA issued Handbook Section 1506, "Accounting Changes", which describes the criteria for changing accounting policies, along with the accounting and disclosure for changes in accounting policies, changes in accounting estimates and corrections of errors. These changes came into effect as of January 1, 2007 and are applicable for the first quarter of fiscal 2008.

CASH AND CASH EQUIVALENTS

Cash and cash equivalents are defined as cash, treasury bills and guaranteed investments with a maturity less than 90 days at date of acquisition.

INVENTORIES

Warehouse inventories are valued at the lower of cost and net realizable value with cost being determined on a first-in, first-out ("FIFO") or a moving average cost basis. Retail inventories are valued at the lower of cost and net realizable value. Cost is determined using FIFO or the retail method. The retail method uses the anticipated selling price less normal profit margins, substantially on an average cost basis. Real estate inventory of residential properties is carried at the lower of cost and net realizable value.

PORTFOLIO INVESTMENTS

Portfolio investments are accounted for under the cost method. Investment income is recognized on an accrual basis. Portfolio investments are written down when the inherent loss is determined to be other than temporary. Gains and losses on sale of investments are recorded in earnings as realized.

PROPERTY AND EQUIPMENT

Property and equipment is recorded at net book value, being original cost less accumulated depreciation and any writedowns for impairment.

Depreciation on real estate buildings is calculated using the straight-line method with reference to each property's book value, its estimated useful life (not exceeding 40 years) and its residual value. Deferred leasing costs are amortized over the terms of the related leases.

Depreciation of other property and equipment is recorded on a straight-line basis over the estimated useful lives of the assets as follows:

Equipment	3 – 20 years
Buildings	10 – 40 years
Leasehold improvements	Lesser of lease term and 7 – 10 years

Property and equipment is reviewed for impairment when events or circumstances indicate that the carrying value exceeds the sum of the undiscounted future cash flows expected from use and eventual disposal. Property and equipment is reviewed for impairment annually. The carrying value of the property and equipment is also reviewed whenever events or changes in circumstances indicate that the carrying value of property and equipment may not be recoverable. If property and equipment is determined to be impaired, the impairment loss is measured at the excess of the carrying value over fair value.

Assets to be disposed are classified as held for sale and are no longer depreciated. Assets held for sale are recognized at the lower of book value and fair value less cost of disposal.

The Company follows the full cost method of accounting for its exploration and development of petroleum and natural gas reserves. Costs initially capitalized are depleted and depreciated using the unit-of-production method based on production volumes, before royalties, in relation to the Company's share of estimated proved petroleum and natural gas reserves.

CAPITALIZATION OF COSTS

(a) Construction projects

Certain subsidiary companies and joint ventures capitalize interest during the construction period until the project opening date. The amount of interest capitalized to construction in progress in the current year was \$1.5 (2006 – \$0.5).

(b) Commercial properties

Certain subsidiaries and joint ventures capitalize the direct carrying and operating costs applicable to the unleased areas of each new project for a reasonable period from the project opening date until a certain level of occupancy is reached. No amounts were capitalized in fiscal 2006 or 2007.

(c) Development properties and land held for future development

A subsidiary company capitalizes interest, real estate taxes and other expenses to the extent that they relate to properties for immediate development. To the extent that the resulting carrying value exceeds its fair market value, the excess is charged against income. The carrying costs on the balance of properties held for future development are capitalized as incurred. An amount of \$0.7 (2006 – \$0.2) was capitalized during the year.

LEASES

Leases meeting certain criteria are accounted for as capital leases. The imputed interest is charged against income. If the lease contains a term that allows ownership to pass to the Company or there is a bargain purchase option the capitalized value is depreciated over the estimated useful life of the related asset. Otherwise the capitalized value is depreciated on a straight-line basis over the lesser of the lease term and its estimated useful life. Capital lease obligations are reduced by rental payments net of imputed interest. All other leases are accounted for as operating leases.

Lease allowances and incentives received are recorded as a deferred credit and amortized as a reduction of lease expense over the terms of the lease. Real estate lease expense is amortized straight-line over the entire term of the lease including free rent periods related to store fixturing. A store fixturing period varies by store but is generally considered to be one month prior to the store opening.

GOODWILL

Goodwill represents the excess of the purchase price of the business acquired over the fair value of the underlying net tangible and intangible assets acquired at the date of acquisition. Goodwill is not amortized but rather is subject to an annual impairment review or more frequently if circumstances exist that might indicate the value is impaired. Should the carrying value exceed the fair value, the carrying value will be written down to the fair value.

INTANGIBLES

Intangibles arise on the purchase of a new business, existing franchises and the acquisition of pharmacy prescription files. Amortization on limited life intangibles is recorded on a straight-line basis over 10-15 years. Intangible assets with indefinite useful lives are not amortized but rather are subject to an annual impairment review or more frequently if circumstances exist that might indicate their value is impaired. Should the carrying value exceed the fair value of intangible assets (e.g. trademarks), the carrying value will be written down to the fair value.

DEFERRED COSTS

Deferred costs consist of deferred store marketing, deferred financing and deferred purchase agreements and are included in other assets.

Deferred costs are amortized on a straight-line basis as follows:

- Deferred store marketing – up to 7 years
- Deferred financing – over the term of the debt
- Deferred purchase agreements – over the term of the purchase agreement

ASSETS HELD FOR SALE

Certain land and buildings have been listed for sale and reclassified as "Assets held for sale" in accordance with CICA Handbook Section 3475, "Disposal of Long-lived Assets and Discontinued Operations". These assets are expected to be sold within a twelve month period, are no longer productive assets and there is no longer an intent to develop for future use. Assets held for sale are valued at the lower of book value and fair value less cost of disposal.

STORE OPENING EXPENSES

Opening expenses of new stores and store conversions are written off on a straight-line basis during the first year of operation.

FUTURE INCOME TAXES

The Company accounts for income taxes under the liability method. The difference between the tax basis of assets and liabilities and their carrying value on the balance sheet is used

to calculate future tax assets and liabilities. The future tax assets and liabilities have been measured using substantively enacted tax rates that will be in effect when the differences are expected to reverse.

DEFERRED REVENUE

Deferred revenue consists of long-term supplier purchase agreements, rental revenue arising from the sale of subsidiaries and gains on sale leaseback transactions. Deferred revenue is being taken into income on a straight-line basis over the term of the related agreements.

FOREIGN CURRENCY TRANSLATION

Assets and liabilities of self-sustaining foreign investments are translated at exchange rates in effect at the balance sheet date. The revenues and expenses are translated at average exchange rates for the year. Cumulative gains and losses on translation are shown as a separate component of shareholders' equity.

Other assets and liabilities are translated at the exchange rate in effect at the balance sheet date. These exchange gains or losses are recognized in operating income. Revenues and expenses denominated in foreign currencies are translated into Canadian dollars at the average exchange rate for the period.

REVENUE RECOGNITION

Food sales are recognized at the point-of-sale. Sales include revenues from customers through corporate stores operated by the Company and consolidated VIEs, and revenue from sales to non-VIE franchised stores, affiliated stores and independent accounts. Revenue received from non-VIE franchised stores, affiliated stores and independent accounts is mainly derived from the sale of product. The Company also collects franchise fees under two types of arrangements. Franchise fees contractually due based on the dollar value of product shipped are recorded as revenue when the product is shipped. Franchise fees contractually due based on the franchisee's retail sales are recorded as revenue weekly upon invoicing based on the franchisee's retail sales. Real Estate revenue is recognized in accordance with the lease agreements with tenants on a straight-line basis.

FINANCIAL INSTRUMENTS

The Company uses various derivative financial instruments to hedge its exposure to foreign exchange and interest rate risks. If documentation and effectiveness requirements are met, gains and losses on these instruments are deferred and recognized in earnings in the same period the related hedged risk is realized (settlement accounting). If effectiveness requirements are not met, gains and losses on these instruments are recognized in earnings as the fair value of the instrument changes. Amounts received or paid, including any gains and losses on instruments used to hedge these risks are recognized over the term of the hedged item. The derivatives are not recorded on the balance sheet.

PENSION BENEFIT PLANS AND OTHER BENEFIT PLANS

The cost of the Company's pension benefits for defined contribution plans are expensed at the time active employees are compensated. The cost of defined benefit pension plans and other benefit plans is accrued based on actuarial valuations, which are determined using the projected benefit method pro-rated on service and management's best estimate of the expected long-term rate of return on plan assets, salary escalation, retirement ages and expected growth rate of health care costs.

Current market values are used to value benefit plan assets. The obligation related to employee future benefits is measured using current market interest rates, assuming a portfolio of Corporate AA bonds with terms to maturity that, on average, match the terms of the obligation.

The impact of changes in plan amendments is amortized on a straight-line basis over the expected average remaining service life ("EARSL") of active members. For pension benefit plans, the actuarial gains and losses and the impact of changes in the actuarial basis in excess of 10% of the greater of the projected benefit obligation and the market value of assets are amortized on a straight-line basis over the EARSL of the active members. For the Company's Supplemental Executive Retirement Plan, the impact of changes in the plan provisions are amortized over five years. For other benefit plans, actuarial gains and losses are recognized immediately.

USE OF ESTIMATES

The preparation of consolidated financial statements in conformity with Canadian generally accepted accounting principles, requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Certain of these estimates require subjective or complex judgements by management that may be uncertain. Some of these items include the valuation of inventories, goodwill, employee future benefits and income taxes. Changes to these estimates could materially impact the financial statements. These estimates are based on management's best knowledge of current events and actions that the Company may undertake in the future. Actual results could differ materially from these estimates.

EARNINGS PER SHARE

Earnings per share is calculated by dividing the earnings available to common shareholders by the weighted average number of common shares outstanding during the year. Diluted earnings per share is calculated using the treasury stock method.

Note 2 Sale of Wajax Income Fund

On June 6, 2005, the shareholders of Wajax Limited, an equity accounted investment, approved a Plan of Arrangement to convert into Wajax Income Fund ("Wajax"). The Company owned approximately 45% of the outstanding shares of Wajax Limited (on a fully diluted basis). The Plan of Arrangement was completed on June 15, 2005 with the Company receiving one unit of Wajax for each Wajax Limited share held. Through a secondary offering on June 21, 2005, the Company sold a total of 2.5 million Wajax units for net proceeds of approximately \$44.0. On June 29, 2005, the underwriter exercised their over-allotment option to purchase 375,000 Wajax units at \$19.25 per

unit, resulting in additional net proceeds of \$6.8. This reduced the Company's ownership percentage to approximately 27.6%. Details of the sale are as follows:

Net proceeds	\$	50.8
Book value		21.1
		29.7
Equity share of income fund conversion-related items		4.1
Capital gain before income taxes		25.6
Income taxes		2.1
Net capital gain	\$	23.5

Note 3 Sale of Property to Crombie REIT

On March 23, 2006, the Company's real estate segment sold 44 commercial properties to Crombie Real Estate Investment Trust ("Crombie REIT"). Included in the proceeds is an interest in Crombie REIT giving the Company effective ownership of 48.3%. The Company's investment in Crombie REIT is accounted using the equity method. Details of the sale are as follows:

Proceeds		
Cash	\$	267.7
Investment in Crombie REIT		200.8
		468.5
Book value of assets sold and liabilities assumed		
Property and equipment		593.2
Net working capital		(1.0)
Employee future benefits obligation		(2.2)
Future income taxes		(44.7)
Long-term debt		(312.9)
		232.4
Early extinguishment of long-term debt		25.4
Share of issue costs		9.4
Other costs		17.1
		284.3
Capital gain before deferral and income taxes		184.2
Deferral of capital gain related to retained interest		(88.2)
Capital gain before income taxes		96.0
Income taxes		19.8
Net capital gain	\$	76.2

Note 4 Earnings Per Share

Earnings per share amounts are calculated on the weighted average number of shares outstanding after providing for preferred share dividends accrued to the balance sheet date. Diluted earnings per share is calculated on the assumption that all the outstanding stock options were exercised and share purchase loans were repaid at the beginning of the year.

Earnings applicable to common shares is comprised of the following:

	2007	2006
Operating earnings	\$ 204.4	\$ 202.0
Capital gains and other items, net of tax of \$1.4 (2006 – \$14.4)	5.7	94.8
Net earnings	210.1	296.8
Preferred share dividends	(0.4)	(0.3)
Earnings applicable to common shares	\$ 209.7	\$ 296.5

Earnings per share is comprised of the following:

	2007	2006
Operating earnings	\$ 3.11	\$ 3.08
Capital gains and other items	0.09	1.45
Basic earnings per share	\$ 3.20	\$ 4.53
Operating earnings	\$ 3.10	\$ 3.07
Capital gains and other items	0.09	1.44
Diluted earnings per share	\$ 3.19	\$ 4.51

Note 5 Investments, at Equity

	May 5, 2007	May 6, 2006
Wajax Income Fund (27.6% interest)	\$ 32.2	\$ 33.1
Crombie REIT (48.1% interest)	109.3	112.8
U.S. residential real estate partnerships	1.3	11.6
	\$ 142.8	\$ 157.5

The Company's carrying value of its investment in Wajax Income Fund is as follows:

	May 5, 2007	May 6, 2006
Balance, beginning of year	\$ 33.1	\$ 55.1
Equity earnings	20.6	16.3
Distributions received	(21.5)	(13.1)
Book value of equity interest sold	-	(25.2)
Balance, end of year	\$ 32.2	\$ 33.1

The Company's carrying value of its investment in Crombie REIT is as follows:

	May 5, 2007	May 6, 2006
Balance, beginning of year	\$ 112.8	\$ -
Interest received in Crombie REIT	-	200.8
Less deferral of gain due to retained interest		(88.2)
Equity earnings	11.6	0.2
Distributions received	(15.1)	-
Balance, end of year	\$ 109.3	\$ 112.8

Note 6 Property and Equipment

	Cost	Accumulated Depreciation	May 5, 2007 Net Book Value
Food segment			
Land	\$ 152.8	\$ -	\$ 152.8
Land held for future development	129.0	-	129.0
Buildings	782.5	161.7	620.8
Equipment	1,819.5	1,170.1	649.4
Leasehold improvements	397.9	243.9	154.0
Assets under capital leases	83.1	34.5	48.6
	3,364.8	1,610.2	1,754.6
Real estate and other segments			
Land	78.8	-	78.8
Land held for future development	26.8	-	26.8
Buildings	399.1	102.2	296.9
Equipment	72.7	32.6	40.1
Leasehold improvements	52.4	12.1	40.3
Petroleum and natural gas costs	78.7	13.3	65.4
	708.5	160.2	548.3
Total	\$ 4,073.3	\$ 1,770.4	\$ 2,302.9

	Cost	Accumulated Depreciation	May 6, 2006 Net Book Value
Food segment			
Land	\$ 138.6	\$ -	\$ 138.6
Land held for future development	89.5	-	89.5
Buildings	681.1	135.7	545.4
Equipment	1,707.4	1,062.7	644.7
Leasehold improvements	361.0	218.2	142.8
Assets under capital leases	78.9	27.7	51.2
	3,056.5	1,444.3	1,612.2
Real estate and other segments			
Land	79.6	-	79.6
Land held for future development	23.6	-	23.6
Buildings*	385.9	94.1	291.8
Equipment	69.4	26.9	42.5
Leasehold improvements	51.6	8.3	43.3
Petroleum and natural gas costs	54.0	3.4	50.6
	664.1	132.7	531.4
Total	\$ 3,720.6	\$ 1,577.0	\$ 2,143.6

* During the year ended May 6, 2006, based on revised estimates of holding periods, it was determined that the carrying value of five commercial properties was impaired. Accordingly, the Company recorded an impairment charge of \$27.4 to reduce their carrying value to estimated fair value using external appraisals.

Note 7 Other Assets

	May 5, 2007	May 6, 2006
Loans and mortgages receivable	\$ 65.1	\$ 68.4
Deferred costs	144.3	101.4
Accrued benefit asset (Note 21)	42.7	36.2
Restricted cash	5.7	14.7
Other	48.6	25.4
Intangibles (less accumulated amortization of \$11.7; 2006 - \$7.6)	38.2	27.2
	\$ 344.6	\$ 273.3

LOANS RECEIVABLE

Loans receivable represent long-term financing to certain retail associates. These loans are primarily secured by inventory, fixtures and equipment, bear various interest rates and have repayment terms up to ten years. The carrying amount of the loans receivable approximates fair value based on the variable interest rates charged on the loans and the operating relationship of the associates with the Company.

The loans and mortgages receivable are net of current portions of \$14.5 (2006 - \$15.9).

Note 8 Bank Indebtedness

As security for certain bank loans the Company has provided an assignment of certain marketable securities and, in certain divisions and subsidiaries, general assignments of receivables and leases, first floating charge debentures on assets and the assignment of proceeds of fire insurance policies.

Under the terms of a credit agreement entered into between the Company and a banking syndicate, a revolving term credit facility of \$300.0 was established. During the third quarter of fiscal 2006, the expiry date of the revolving unsecured credit facility was extended from June 22, 2006 to December 20, 2010. All indebtedness and obligations under the agreement shall be payable in full on December 20, 2010. Interest payable on this facility fluctuates with changes in the prime interest rate.

Note 9 Long-term Debt

	May 5, 2007			May 6, 2006
	Food Segment	Real Estate and other Segments	Total	Total
First mortgage loans, average interest rate 9.3%, due 2008-2026	\$ 25.2	\$ 130.4	\$ 155.6	\$ 167.2
Medium Term Notes, interest Rate 5.8%, due October 6, 2036	125.0	–	125.0	–
Medium Term Notes, interest rate 6.1%, due October 29, 2035	175.0	–	175.0	175.0
Medium Term Notes, interest rate 7.2%, due February 26, 2018	100.0	–	100.0	100.0
Debentures, average interest rate 10.4%, due 2008-2016	58.1	30.7	88.8	95.7
Notes payable and other debt primarily at interest rates fluctuating with the prime rate	79.7	101.3	181.0	215.6
Capital lease obligations, net of imputed interest	49.7	–	49.7	49.2
	612.7	262.4	875.1	802.7
Less amount due within one year	30.0	52.5	82.5	95.4
	\$ 582.7	\$ 209.9	\$ 792.6	\$ 707.3

Long-term debt is secured by land and buildings, specific charges on certain assets and additional security as described in Note 8. Capital lease obligations are secured by the related capital lease asset.

On October 21, 2005, the Company filed a short form base shelf prospectus providing for the issuance of up to \$500.0 of unsecured Medium Term Notes. On October 28, 2005, the

Company issued new Medium Term Notes of \$175.0, maturing on October 29, 2035. On November 1, 2005, Medium Term Notes of \$175.0 were repaid according to the terms of the agreement. On October 6, 2006, the Company issued new Medium Term Notes of \$125.0, maturing on October 6, 2036.

During the year, the Company increased its capital lease obligation by \$5.6 (2006 – \$29.0) with a similar increase in assets under capital lease.

Debt retirement payments and capital lease obligations in each of the next five fiscal years are:

	Long Term Debt	Capital Leases
2008	\$ 72.3	\$ 10.2
2009	\$ 74.2	\$ 7.7
2010	\$ 33.8	\$ 7.2
2011	\$ 38.8	\$ 6.5
2012	\$ 27.1	\$ 5.6
Thereafter	\$ 579.2	\$ 12.5

OPERATING LEASES

The net aggregate, annual, minimum rent payable under operating leases for fiscal 2008 is approximately \$178.1 (\$249.1 gross less expected sub-lease income of \$71.0).

The commitments over the next five fiscal years are:

	Net Lease Obligation	Gross lease Obligation
2008	\$ 178.1	\$ 249.1
2009	\$ 164.7	\$ 230.6
2010	\$ 157.0	\$ 219.0
2011	\$ 151.1	\$ 207.2
2012	\$ 144.0	\$ 195.8
Thereafter	\$ 1,073.5	\$ 1,392.1

Note 10 Other Liabilities

	May 5, 2007	May 6, 2006
Deferred revenue	\$ 6.5	\$ 3.3
Deferred hedge gain	2.5	10.2
Above market leases from acquisitions	4.4	5.0
Asset retirement obligations	0.6	0.4
	\$ 14.0	\$ 18.9

Note 11 Capital Stock

	No. of Shares
AUTHORIZED	
Preferred shares, par value of \$25 each, issuable in series. Series 2 cumulative, redeemable, rate of 75% of prime.	2,814,100
2002 Preferred Shares, par value of \$25 each, issuable in series.	992,000,000
Non-Voting Class A shares, without par value.	259,107,435
Class B common shares, without par value, voting.	40,800,000

	May 5, 2007		May 6, 2006	
	No. of Shares		No. of Shares	
ISSUED AND OUTSTANDING:				
Preferred shares, Series 2	300,000	\$ 7.5	331,900	\$ 8.3
Non-Voting Class A	31,174,037	184.5	31,175,047	183.7
Class B common	34,560,763	7.7	34,560,763	7.7
		199.7		199.7
Loans receivable from officers and employees under share purchase plan		(3.6)		(4.6)
		\$ 196.1		\$ 195.1

During the year, under a normal course issuer bid which expires on July 27, 2007, the Company purchased for cancellation 46,047 (2006 – 20,254) Non-Voting Class A shares. The purchase price was \$1.9 of which \$1.6 of the purchase price (representing the premium on common shares purchased for cancellation) was charged to retained earnings.

During the year, the Company purchased for cancellation 31,900 Series 2 preferred shares for \$0.8.

During the year, 27,674 options were exercised for \$0.2. Options allowed holders to purchase Non-Voting Class A shares at \$6.555 per share. There are no longer any options outstanding.

During the year, 18,373 (2006 – 20,254) Non-Voting Class A shares were issued under the Company's share purchase plan to certain officers and employees for \$0.8 (2006 – \$0.8), which was based on the average trading price of the Non-Voting Class A shares on the Toronto Stock Exchange for the five previous trading days.

Loans receivable from officers and employees of \$3.6 (2006 – \$4.6) under the Company's share purchase plan are classified as a reduction of Shareholders' Equity. Loan repayments will result in a corresponding increase in Share Capital. The loans are non-interest bearing and non-recourse, secured by 125,265 (2006 – 229,484) Non-Voting Class A shares. Market value of the shares at May 5, 2007 was \$5.3 (May 6, 2006 – \$9.9).

Under certain circumstances, where an offer (as defined in the share conditions) is made to purchase Class B common shares, the holders of the Non-Voting Class A shares shall be entitled to receive a follow-up offer at the highest price per share paid, pursuant to such offer to purchase Class B common shares.

During the year, Nil (2006 – 24,462) Class B common shares were exchanged for Nil (2006 – 24,462) Non-Voting Class A shares.

Note 12 Investment Income

	2007	2006
Dividend and interest income	\$ 9.7	\$ 8.3
Share of earnings of companies accounted using the equity method	31.8	23.5
	\$ 41.5	\$ 31.8

Note 13 Capital Gains and Other Items

	2007	2006
Gain on sale of investments	\$ 6.2	\$ 11.6
Other items	0.9	3.4
Gain on sale of Wajax Income Fund (Note 2)	–	25.6
Gain on sale of property to Crombie REIT (Note 3)	–	96.2
Reduction of book value of real estate assets (Note 6)	–	(27.4)
	\$ 7.1	\$ 109.4

Note 14 Income Taxes

Income tax expense varies from the amount that would be computed by applying the combined federal and provincial statutory tax rate as a result of the following:

	2007	2006
Income tax expense according to combined statutory rate of 32.5% (2006 – 34.8%)	\$ 123.0	\$ 141.8
Increase (decrease) in income taxes resulting from		
Rate changes effect on timing differences	(2.0)	(1.6)
Non-taxable dividends and equity earnings	(2.2)	(3.5)
Large corporation tax	–	2.0
	118.8	138.7
Capital gains and other items	1.4	14.4
	\$ 120.2	\$ 153.1

May 5, 2007 income tax expense attributable to net earnings consists of:

	Current	Future	Total
Operations	\$ 104.9	\$ 13.9	\$ 118.8
Capital gains and other items	(0.1)	1.5	1.4
	\$ 104.8	\$ 15.4	\$ 120.2

May 6, 2006 income tax expense attributable to net earnings consists of:

	Current	Future	Total
Operations	\$ 127.7	\$ 11.0	\$ 138.7
Capital gains and other items	14.1	0.3	14.4
	\$ 141.8	\$ 11.3	\$ 153.1

The tax effect of temporary differences that give rise to significant portions of future income taxes are presented below:

	May 5, 2007	May 6, 2006
Property and equipment	\$ 71.3	\$ 64.1
Investments	38.9	59.0
Employee future benefits obligation	(34.9)	(34.8)
Restructuring provisions	(11.6)	(5.0)
Pension contributions	18.6	17.4
Deferred costs	41.0	28.4
Deferred credits	54.8	54.6
Goodwill and intangibles	10.2	8.6
Other	(14.3)	(14.4)
	\$ 174.0	\$ 177.9
Future income taxes – current liabilities	\$ 40.4	\$ 46.1
Future income taxes – non-current liabilities	133.6	131.8
	\$ 174.0	\$ 177.9

Note 15 Supplementary Cash Flow Information

	2007	2006
a) Items not affecting cash		
Depreciation and amortization	\$ 243.9	\$ 225.8
Future income taxes	15.4	10.1
Amortization of deferred items	44.4	35.8
Equity in earnings of other companies, net of dividends received	–	(4.1)
Minority interest	46.0	55.8
Stock-based compensation	1.4	1.0
Long-term lease obligation	16.1	8.5
Employee future benefits obligation	4.8	4.2
Rationalization costs (Note 24)	15.5	–
Gain on sale of Wajax Income Fund, net of tax of \$2.1	–	(23.5)
Gain on sale of property to Crombie REIT, net of tax of \$19.8	–	(76.2)
Reduction of book value of real estate assets, net of tax of \$(10.4)	–	17.0
	\$ 387.5	\$ 254.4
b) Other information		
Net interest paid	\$ 58.9	\$ 83.1
Net income taxes paid	\$ 168.2	\$ 102.1

Note 16 Joint Ventures

The financial statements include the Company's proportionate share of the accounts of incorporated and unincorporated joint ventures. A summary of these amounts is as follows:

	May 5, 2007	May 6, 2006
Assets	\$ 136.3	\$ 101.0
Liabilities	\$ 72.7	\$ 60.0
Equity and advances	63.6	41.0
	\$ 136.3	\$ 101.0

	2007	2006
Revenues	\$ 111.8	\$ 98.2
Expenses	41.7	43.4
Income before income taxes	\$ 70.1	\$ 54.8
Cash provided (used)		
Operating activities	\$ 68.7	\$ 62.3
Investing activities	(34.2)	4.7
Financing activities	3.3	3.9
	\$ 37.8	\$ 70.9

Note 17 Segmented Information

	2007	2006
Revenue		Restated (Note 1)
Food	\$ 13,032.0	\$ 12,718.1
Real estate		
Commercial	38.4	137.8
Inter-segment	34.3	54.0
Residential	146.1	84.9
	218.8	276.7
Investment and other operations	150.2	122.8
	13,401.0	13,117.6
Elimination	(34.3)	(54.0)
	\$ 13,366.7	\$ 13,063.6

	2007	2006
Operating income		
Food	\$ 300.2	\$ 331.6
Real estate		
Commercial	46.8	87.0
Residential	71.2	51.3
Investment and other operations	31.6	31.3
Corporate expenses	(9.5)	(9.8)
	\$ 440.3	\$ 491.4

	May 5, 2007	May 6, 2006
Identifiable assets		
Food	\$ 3,409.0	\$ 3,119.5
Goodwill	746.5	691.7
	4,155.5	3,811.2
Real estate	609.4	634.7
Investment and other operations (including goodwill of \$40.1; 2006 – \$40.1)	460.0	605.6
	\$ 5,224.9	\$ 5,051.5

	2007	2006
Depreciation and amortization		
Food	\$ 215.3	\$ 196.6
Real estate	6.8	16.9
Investment and other operations	21.8	12.3
	\$ 243.9	\$ 225.8

	2007	2006
Capital expenditure		
Food	\$ 482.8	\$ 421.3
Real estate	16.2	67.9
Investment and other operations	46.2	57.2
	\$ 545.2	\$ 546.4

The Company operates principally in two business segments: food and real estate. The food segment consists of distribution of food products in Canada. The real estate segment consists of development and ownership of both commercial and residential properties. Commercial real estate is mainly shopping centres and office buildings in Central and Eastern Canada. Residential real estate is the development of housing lots for resale. Inter-segment transactions are at market values.

Note 18 Financial Instruments

CREDIT RISK

There is no significant concentration of credit risk. The credit risk exposure is considered normal for the business.

FAIR VALUE OF FINANCIAL INSTRUMENTS

The book value of cash and cash equivalents, receivables, income taxes receivable, loans and mortgages, bank indebtedness, and accounts payable and accrued liabilities approximate fair values at May 5, 2007. The fair value of investments is \$717.1 (May 6, 2006 – \$824.2).

The total fair value of long-term debt is estimated to be \$907.5 (May 6, 2006 – \$866.4). The fair value of variable rate long-term debt is assumed to approximate its carrying amount.

The fair value of other long-term debt has been estimated by discounting future cash flows at a current rate offered for debt of similar maturities and credit quality.

INTEREST RATE RISK

The majority of the Company's debt is at fixed rates. Accordingly, there is limited exposure for interest rate risk.

The Company has fixed the interest rate on \$20 of its long term debt at 4.28% by utilizing interest rate exchange agreements of which \$10 expires in December, 2011 and \$10 expires in January, 2012. The fair value of these contracts at year-end was nil.

FOREIGN CURRENCY RISK

Investments include \$44.5 Canadian that is denominated in U.S. funds. Bank indebtedness includes \$4.5 Canadian that is denominated in U.S. funds and it acts as a partial hedge to the foreign exchange fluctuations inherent in the residual value of certain equipment.

At May 5, 2007, there are outstanding forward exchange contracts to sell a notional amount of \$31.0, maturing over the next 12 months at a weighted average rate of U.S. 87.90 cents per Canadian dollar. The fair value of the outstanding forward exchange contracts, based on settlement requirements at May 5, 2007, is a positive value of U.S. \$0.9 due to the strengthening of the Canadian dollar since the dates on which the contracts were entered.

The Company also uses forward contracts to fix the exchange rate on some of its expected requirements for Euros and U.S. dollars. Amounts received or paid related to instruments used to hedge foreign exchange, including any gains and losses, are recognized in the cost of purchases. The fair value of these contracts at year end was \$0.9.

Note 19 Contingent Liabilities

At May 5, 2007 the Company was contingently liable for letters of credit issued in the aggregate amount of \$48.5 (May 6, 2006 – \$47.6).

Sobeys has guaranteed certain bank loans contracted by franchise affiliates. As at May 5, 2007 these loans amounted to approximately \$2.9 (May 6, 2006 – \$1.3).

Sobeys has guaranteed certain equipment leases of its franchise affiliates. Under the terms of the guarantee should a franchise affiliate be unable to fulfill their lease obligation, Sobeys would be required to fund the difference of the lease commitments up to a maximum of \$100.0 on a cumulative basis. Sobeys approves each of the contracts. The aggregate, annual, minimum rent payable under the guaranteed operating equipment leases for fiscal 2008 is approximately \$29.4. The guaranteed lease commitments over the next five fiscal years are:

	Guaranteed lease commitments	
2008	\$	29.4
2009	\$	25.5
2010	\$	21.7
2011	\$	17.0
2012	\$	6.4
Thereafter	\$	–

Upon entering into the lease of its Mississauga distribution centre in March 2000, Sobeys guaranteed to the landlord the performance, by SERCA Foodservice, of all its obligation under the lease. The remaining term of the lease is 13 years with an aggregate obligation of \$40.4 (2006 – \$43.3). At the time of the sale of assets of SERCA Foodservice to Sysco Corp., the lease of the Mississauga distribution centre was assigned to and assumed by the purchaser, and Sysco Corp. agreed to indemnify and hold Sobeys harmless from any liability it may incur pursuant to its guarantee.

On June 21, 2005 Sobeys received a notice of reassessment from Canada Revenue Agency ("CRA") for fiscal years 1999 and 2000 related to the Goods and Services Tax ("GST"). CRA asserts that Sobeys was obliged to collect GST on sales of tobacco products to Status Indians. The total tax, interest and penalties in the reassessment was \$13.6. Sobeys has reviewed this matter, has received legal advice and believes it

was not required to collect GST. During the second quarter of fiscal 2006, Sobeys filed a Notice of Objection with CRA. Accordingly the company has not recorded in its statement of earnings any of the tax, interest or penalties in the notice of reassessment. Sobeys has deposited with CRA funds to cover the total tax, interest and penalties in the reassessment and has recorded this amount as a long-term receivable from CRA pending resolution of the matter.

In the third quarter of fiscal 2007, Sobeys was named as a defendant in a lawsuit brought by beneficiaries of a multi-employer pension plan. The lawsuit alleges mismanagement of certain pension plan investments by the trustees of the pension plan and seeks, among other remedies, payment of \$1,000.0 in damages from the trustees and the contributing employers, of which Sobeys is one of approximately 440. Sobeys played no role in the management of the pension plan and intends to contest the lawsuit. Accordingly, the Company has not recorded in its statement of earnings any amount related to this lawsuit.

The Company and certain subsidiaries are presently under audit by CRA and certain provincial taxing authorities for fiscal years 2001 through 2006. The principal matters under audit are:

- The tax treatment of gains realized on the sale of shares in Hannaford Bros. Co. ("Hannaford") in fiscal 2001;
- The tax treatment of gains realized on the sale of shares in Delhaize America Inc. in fiscal years 2001 and 2002; and
- The taxation of income from certain of the Company's real estate investments for fiscal years 2003 to 2006.

Reassessments have been received in respect of the sale of shares of Hannaford. In the event that the tax authorities are successful in respect of the Hannaford transaction, which the Company believes is unlikely, the maximum potential exposure in excess of provisions taken is approximately \$30.0.

The Company has appealed the reassessments in respect of the sale of Hannaford shares. The Company expects that it will be substantially successful on its appeals of each of these reassessments. The Company also believes that the ultimate resolution of these matters will not, in any event, have a material impact on earnings because it has made adequate provisions for each of these matters. Should the ultimate outcome materially differ from the provisions established, the effective tax rate and earnings of the Company could be materially affected, negatively or positively, in the period in which the matters are resolved.

The Company entered into an agreement with Crombie REIT to fund certain property redevelopments and originally issued and recorded a note payable to Crombie REIT in the amount of \$39.6 related thereto. The Company has agreed to pay for all additional costs and expenses required for the redevelopment of those properties. In the event that the redevelopment costs are less than \$39.6, the savings will be paid to the Company.

The Company has agreed to indemnify its directors and officers and particular employees in accordance with the Company's policies. The Company maintains insurance policies that may provide coverage against certain claims.

There are various claims and litigation, which the Company is involved with, arising out of the ordinary course of business operations. The Company's management does not consider the exposure to such litigation to be material, although this cannot be predicted with certainty.

Note 20 Related Party Transactions

The Company rents premises from Crombie REIT. In addition, Crombie REIT provides administrative and management services to the Company. The rental payments are at fair value and the charges incurred for administrative and management services are on a cost recovery basis. The Company has non-interest bearing notes payable to Crombie REIT in the amount of \$33.1.

On October 2, 2006, the Company sold two commercial properties to Crombie REIT for cash proceeds of \$32.4, which was fair market value. Since the sale was to an equity accounted investment, no gain was recorded on the sale.

Note 21 Employee Future Benefits

The company has a number of defined benefit and defined contribution plans providing pension and other retirement benefits to most of its employees.

The Company uses December 31 as an actuarial valuation date and April 30 as a measurement date for accounting purposes for its defined benefit pension plans.

DEFINED CONTRIBUTION PENSION PLANS

The contributions required by the employee and the employer are specified. The employee's pension depends on what level of retirement income (for example, annuity purchase) that can be achieved with the combined total of employee and employer contributions and investment income over the period of plan membership, and the annuity purchase rates at the time of the employee's retirement.

	Most recent valuation date	Next required valuation date
Retirement Pension Plan	December 31, 2004	December 31, 2007
Senior Management Pension Plan	December 31, 2004	December 31, 2007

DEFINED BENEFIT PENSION PLANS

The ultimate retirement benefit is defined by a formula that provides a unit of benefit for each year of service. Employee contributions, if required, pay for part of the cost of the benefit, but the employer contributions fund the balance. The employer contributions are not specified or defined within the plan text; they are based on the result of actuarial valuations which determine the level of funding required to meet the total obligation as estimated at the time of the valuation.

DEFINED CONTRIBUTION PLANS

The total expense and cash contributions for the Company's defined contribution plans are as follows:

2007	\$	14.5
2006	\$	14.2

DEFINED BENEFIT PLANS

Information about the Company's defined benefits plans, in aggregate, is as follows:

	Pension Benefit Plans 2007	Pension Benefit Plans 2006	Other Benefit Plans 2007	Other Benefit Plans 2006
ACCRUED BENEFIT OBLIGATION				
Balance, beginning of year	\$ 269.3	\$ 267.0	\$ 114.1	\$ 108.7
Current service cost, net of employee contributions	2.3	2.4	2.5	2.9
Interest cost	14.9	14.5	5.9	6.1
Employee contributions	0.3	0.4	–	–
Divestitures	–	(0.8)	–	(2.2)
Benefits paid	(18.6)	(20.0)	(3.8)	(3.7)
Actuarial losses (gains)	20.5	5.8	(2.1)	2.3
Balance, end of year	\$ 288.7	\$ 269.3	\$ 116.6	\$ 114.1
PLAN ASSETS				
Market value, beginning of year	\$ 267.2	\$ 244.4	\$ –	\$ –
Actual return on plan assets	27.9	33.0	–	–
Employer contributions	6.5	9.3	3.8	3.7
Employee contributions	0.3	0.4	–	–
Benefits paid	(18.6)	(19.9)	(3.8)	(3.7)
Market value, end of year	\$ 283.3	\$ 267.2	\$ –	\$ –
FUNDED STATUS				
Deficit	\$ (5.4)	\$ (2.1)	\$ (116.6)	\$ (114.1)
Unamortized past service cost	0.5	0.7	1.0	1.1
Unamortized actuarial losses	47.6	37.6	13.5	15.7
Accrued benefit asset (liability)	\$ 42.7	\$ 36.2	\$ (102.1)	\$ (97.3)
EXPENSE				
Current service cost	\$ 2.3	\$ 2.5	\$ 2.5	\$ 2.9
Interest cost	14.9	14.5	5.9	6.1
Actual return on plan assets	(27.9)	(33.0)	–	–
Actuarial losses (gains)	20.4	5.8	(2.1)	2.3
Expense (income) before adjustments	9.7	(10.2)	6.3	11.3
Expected vs actual return on plan assets	9.4	16.0	–	–
Recognized vs actual past service costs	0.2	0.2	0.1	0.1
Recognized vs actual actuarial (gains) losses	(19.3)	(3.9)	2.2	(3.5)
Net expenses	\$ –	\$ 2.1	\$ 8.6	\$ 7.9
CLASSIFICATION OF ACCRUED BENEFIT ASSET (LIABILITY)				
Other assets	\$ 68.4	\$ 60.8	\$ –	\$ –
Other liabilities	(25.7)	(24.6)	(102.1)	(97.3)
Accrued benefit asset (liability)	\$ 42.7	\$ 36.2	\$ (102.1)	\$ (97.3)

Included in the above accrued benefit obligation at year-end are the following amounts in respect of plans that are not funded:

	Pension Benefit Plans 2007	Pension Benefit Plans 2006	Other Benefit Plans 2007	Other Benefit Plans 2006
Accrued benefit obligation	\$ 20.9	\$ 19.9	\$ 102.1	\$ 97.3

The significant actuarial assumptions adopted in measuring the Company's accrued benefit obligations are as follows (weighted-average assumptions as of May 5, 2007):

	Pension Benefit Plans 2007	Pension Benefit Plans 2006	Other Benefit Plans 2007	Other Benefit Plans 2006
Discount rate	5.00%	5.50%	5.25%	5.50%
Expected long-term rate of return on plan assets	7.00%	7.00%		
Rate of compensation increase	4.00%	4.00%		

For measurement purposes, a 10% fiscal 2007 annual rate of increase in the per capita cost of covered health care benefits was assumed. The cumulative rate expectation to 2016 is 5%. The expected average remaining service period of the active employees covered by the pension benefit plans ranges from 11 to 13 years with a weighted average of 11 years at year end. The expected average remaining service period of the active employees covered by the other benefit plans range from 12 to 16 years with a weighted average of 16 years at year end.

The table below outlines the sensitivity of the fiscal 2007 key economic assumptions used in measuring the accrued benefit plan obligations and related expenses of the Company's pension and other benefit plans. The sensitivity of each key assumption has been calculated independently. Changes to more than one assumption simultaneously may amplify or reduce impact on the accrued benefit obligations or benefit plan expenses.

	Pension Plans		Other Benefit Plans	
	Benefit Obligations	Benefit Cost ⁽¹⁾	Benefit Obligations	Benefit Cost ⁽¹⁾
Expected long term rate of return on plan assets		7.00%		
Impact of: 1% increase		\$ (2.8)		
1% decrease		\$ 2.8		
Discount rate	5.00%	5.00%	5.25%	5.25%
Impact of: 1% increase	\$ (32.6)	\$ 0.4	\$ (17.2)	\$ (0.6)
1% decrease	\$ 36.7	\$ (0.8)	\$ 20.7	\$ 0.7
Growth rate of health costs ⁽²⁾			10.00%	10.00%
Impact of: 1% increase			\$ 17.4	\$ 1.8
1% decrease			\$ (13.6)	\$ (1.3)

(1) Reflects the impact on the current service cost, the interest cost and the expected return on assets.

(2) Gradually decreasing to 5.0% in 2016 and remaining at that level thereafter.

The asset mix of the defined benefit pension plans as at year end is as follows:

	2007	2006
Cash and short-term investments	2.43%	3.32%
Bonds, debenture, fixed income pooled funds and real estate funds	18.20%	17.92%
Equities and pooled equities fund	78.55%	77.91%
Accrued interest and dividends	0.22%	0.20%
Foreign currency hedges	0.60%	0.65%
Total investments	100.00%	100.00%

Within these securities are investments in Empire Company Limited. The market value of these shares at year end are as follows:

	2007	% of plan assets	2006	% of plan assets
	\$ 92.2	9.3%	\$ 93.4	10.2%

Note 22 Business Acquisitions

SOBEYS

During fiscal 2007, the Company increased its ownership interest in Sobeys from 70.3% to 72.1% by way of purchase of shares on the open market. The acquisition was accounted using the purchase method with operating results being included in the consolidated financial statements from the date of each share acquisition. The cash consideration paid was \$48.6, goodwill increased by \$13.0 and minority interest decreased by \$35.6.

During fiscal 2006, the Company increased its ownership interest in Sobeys from 68.4% to 70.3% by way of purchase of shares on the open market. The acquisition was accounted using the purchase method with operating results being included in the consolidated financial statements from the date of each share acquisition. The cash consideration paid was \$49.5, goodwill increased by \$13.2 and minority interest decreased by \$36.3.

OTHER ACQUISITIONS

During fiscal 2007, Sobeys acquired franchisee stores and prescription files as part of its normal course of operations for total cash consideration of \$16.7. The acquisitions were accounted using the purchase method with net identifiable assets recorded at \$15.8 (including intangible assets of \$8.2) and goodwill recorded at \$0.9.

On August 27, 2006, Sobeys acquired substantially all of the food distribution assets of Achille de la Chevrotière Ltée and its associated companies ("ADL") for an amount of \$79.2. The assets acquired include 25 owned or franchised retail store operations, other wholesale supply agreements and distribution facilities in Rouyn-Noranda, Québec. Sixteen of the franchised retail store operations are considered VIEs under the Company's policy (see Note 27). They have been included in the consolidated results of the Company. The acquisition was accounted using the purchase method with the results of ADL being consolidated since the acquisition date. During the third quarter, management carried out a detailed analysis and changes were made to the preliminary allocation of the excess consideration paid over net assets acquired as disclosed in the second quarter. The measurement and allocation of intangible assets was also

completed and amended from \$21.5 to \$6.8. As a result goodwill was adjusted from \$21.7 to \$41.3 to reflect the finalized valuation of ADL. The final purchase price allocation, which has incorporated management's assessment of fair value, is as follows:

.....		
Consideration		
Cash	\$	75.8
Acquisition costs		3.4
.....		
Total consideration paid		79.2
.....		
Net assets acquired		
Current assets		28.0
Long term assets		27.7
Current liabilities assumed		(20.0)
Long term liabilities assumed		(4.6)
.....		
Total net assets acquired		31.1
.....		
Excess consideration paid over		
net assets acquired	\$	48.1
.....		
Allocation of excess consideration paid		
over net assets acquired		
Intangible assets	\$	6.8
Goodwill		41.3
.....		
	\$	48.1
.....		

During fiscal 2006, Sobeys acquired franchisee stores and prescription files as part of its normal course of operations for total cash consideration of \$5.3. The acquisitions were accounted using the purchase method with net identifiable assets recorded at \$5.0 (including intangible assets of \$1.2) and goodwill recorded at \$0.3.

On September 30, 2005, ETL Canada Holdings Limited (a subsidiary of the Company) acquired 27 theatres with 202 screens located in Ontario and Western Canada from Cineplex Galaxy LP. On October 21, 2005 ETL Canada Holdings Limited further acquired one theatre with four screens in Western Canada from Motion Picture Distribution LP. The total cash consideration of the acquisitions was \$87.8. The acquisitions were accounted using the purchase method with net identifiable assets recorded at \$51.5 (including intangible assets of \$6.0) and goodwill recorded at \$36.3.

Note 23 Stock-based Compensation

DEFERRED SHARE UNITS

Members of the Board of Directors may elect to receive all or any portion of their fees in Deferred Share Units ("DSUs") in lieu of cash. The number of DSUs received is determined by the market value of the Company's Non-Voting Class A shares on each director's fee payment date. Additional DSUs are received as dividend equivalents. DSUs cannot be redeemed for cash until the holder is no longer a director of the Company. The redemption value of a DSU equals the market value of an Empire Company Limited Non-Voting Class A share at the time of the redemption. On an ongoing basis, the Company values the DSU obligation at the current market value of a corresponding number of Non-Voting Class A shares and records any increase in the DSU obligation as an operating expense. At May 5, 2007, there were 66,435 (May 6, 2006 – 60,470) DSUs outstanding. During the year, the stock-based compensation expense was \$0.6 (2006 – \$1.0).

SHARE PURCHASE LOANS

The Company has a Share Purchase Loan plan for employees of the Company whereby loans are granted to purchase Non-Voting Class A Shares. These loans have been treated as stock-based compensation in accordance with EIC Abstract 132.

The compensation cost relating to the fiscal 2007 Share Purchase Loans was determined to be \$0.2 (2006 – \$0.2) with amortization of the cost over 7 years. The total increase in contributed surplus in relation to the Share Purchase Loan compensation cost for fiscal 2007 is \$0.1 (2006 – \$0.2). The contributed surplus balance was reduced by \$0.1 in relation to shares issued under the Share Purchase Loan that have been treated as stock-based compensation that became fully vested with the employee during fiscal 2007. Shares become vested when the employees' outstanding loan balance is reduced. The compensation cost was calculated using the Black-Scholes model with the following assumptions:

	2007	2006
Expected life	7 years	7 years
Risk-free interest rate	4.40%	4.25%
Expected volatility	19.7%	21.8%
Dividend yield	1.4%	1.5%

Note 24 Business Rationalization Costs

During the third quarter of fiscal 2007, Sobeys completed a rationalization of administrative functions in Atlantic Canada. Sobeys also began to incur costs associated with the development of a new grocery distribution centre in Vaughan, Ontario. These costs primarily relate to severance in both the Atlantic and Ontario regions along with fixed asset and inventory write-offs. In the fourth quarter of fiscal 2007, Sobeys also recorded rationalization costs related to its Québec distribution

network. Sobeys expects to incur additional administrative rationalization costs in the first half of fiscal 2008 enabled by its continuing business process and system initiative. The dollar value of these additional costs will be quantified and disclosed in the first quarter of fiscal 2008. The costs associated with the organizational change are recorded as incurred as cost of sales, selling and administrative expenses in the statement of earnings, as follows:

	Beginning Liability	Incurred	Paid Written off	Ending Liability	Anticipated	Total
Severance						
Atlantic	\$ -	\$ 4.7	\$ 1.5	\$ 3.2	\$ -	\$ 4.7
Ontario	-	5.3	0.7	4.6	-	5.3
Québec	-	4.3	-	4.3	-	4.3
Other costs	-	1.1	1.1	-	-	1.1
	-	15.4	3.3	12.1	-	15.4
Asset write-offs	-	3.4	3.4	-	-	3.4
	\$ -	\$ 18.8	\$ 6.7	\$ 12.1	\$ -	\$ 18.8

Note 25 Vendor Allowances

The Company receives allowances from certain vendors whose products are purchased for resale. Included in these vendor programs are allowances for volume purchases, exclusivity allowances, listing fees and other allowances. The Company recognizes these allowances as a reduction of cost of sales, selling and administrative expenses and related inventories in accordance with EIC-144. Certain allowances from vendors are

contingent on the Company achieving minimum purchase levels. These allowances are recognized when it is probable that the minimum purchase level will be met, and the amount of allowance can be estimated. As of the year ended May 5, 2007, the Company has recognized \$2.4 (2006 – \$3.5) of allowances in income where it is probable that the minimum purchase level will be met and the amount of allowance can be estimated.

Note 26 Variable Interest Entities

Variable interest entities are defined under Accounting Guideline (“AcG”)-15, “Consolidation of Variable Interest Entities”, as entities that do not have sufficient equity at risk to finance their activities without additional subordinated financial support, or where the equity holders lack the overall characteristics of a controlling financial interest. The guideline requires that the VIE be consolidated with the financial results of the entity deemed to be the primary beneficiary of the VIE’s expected losses and its expected residual returns.

The Company implemented AcG-15 on May 7, 2005 retroactively without restatement of prior periods. Entities that have been identified as meeting the characteristics of a VIE were consolidated in the Company’s results effective for the fourth quarter of fiscal 2005.

The Company has identified the following entities as VIEs:

FRANCHISE AFFILIATES

The Company has identified 271 (May 6, 2006 – 300) franchise affiliate stores whose franchise agreements result in the Company being deemed the primary beneficiary of the entity according to AcG-15. The results for these entities were consolidated with the results of the Company.

WAREHOUSE AND DISTRIBUTION AGREEMENT

The Company has an agreement with an independent entity to provide warehouse and distribution services for one of its distribution centres. The terms of the agreement with this entity require the Company to consolidate its results with those of the Company pursuant to AcG-15.

The Company has consolidated the results of these franchise affiliates and the entity providing warehouse and distribution services effective at the fourth quarter of fiscal 2005.

In the prior year, a charge of \$3.6 (net of minority interest of \$1.9) to retained earnings was required to reflect additional minority interest in the VIEs.

Note 27 Subsequent Events

(a) On April 26, 2007, the Company and Sobeys jointly announced that they had entered into an arrangement agreement ("the Arrangement") pursuant to which the Company would acquire all of the outstanding common shares of Sobeys that it did not then own at a price of \$58.00 per share. The transaction valued the Sobeys shares not then owned by the Company at approximately \$1.06 billion.

The Arrangement required various approvals to comply with applicable corporate and securities laws: The Sobeys shareholders approved the Arrangement at a special shareholders' meeting held on June 9, 2007 by the requisite majority; the Supreme Court of Nova Scotia gave its sanction to the Arrangement on June 13, 2007; the Arrangement became effective upon registration of the final Court order with the Nova Scotia Registry of Joint Stock Companies at the close of business on June 15, 2007, at which time the Company acquired all the outstanding shares of Sobeys that it did not previously own. Subsequently, the Sobeys common shares ceased trading on the Toronto Stock Exchange, and were de-listed at the close of business on June 18, 2007.

The acquisition was financed by funds of \$278.0, received primarily from sale of certain portfolio investments, and by advances of \$784.0 under new credit facilities (the "Credit Facilities"). The Credit Facilities consist of a \$950.0 unsecured revolving credit maturing on June 8, 2010 (subject to annual extensions at the request of the Company) and a \$50.0 unsecured non-revolving credit maturing June 30, 2007. The Credit Facilities are subject to certain financial covenants. Interest on the debt varies based on the designation of the loan (bankers' acceptances ("BA") rate loans, Canadian prime rate loans, U.S. base rate loans or LIBOR loans), fluctuations in the underlying rates, and in the case of the BA rate loans or LIBOR loans, the margin applicable to the financial covenants.

On June 18, 2007, the Company entered into two delayed fixed rate interest swaps. The first swap in an amount of \$200.0 is for a period of three years at a fixed interest rate of 5.00%. The second swap in an amount of \$200.0 is for a period of five years at a fixed interest rate of 5.05%. Both swaps became effective on July 23, 2007.

On June 27, 2007, pursuant to the terms of the Credit Facilities, Empire and Sobeys filed notice with the lenders requesting the establishment of a new \$300.0 million five-year credit facility in favour of Sobeys at the same interest rate as the Credit Facilities. On July 23, 2007, Sobeys drew down \$300.0 million from the new credit facility, the proceeds of which were used to pay a dividend to Empire. Empire used the proceeds from the dividend to reduce its indebtedness under the Credit Facilities and the Credit Facilities were reduced accordingly. On that date, Empire transferred the second swap to Sobeys.

(b) On July 16, 2007, the Company announced that Sobeys and Thrifty Foods ("Thrifty") have entered into an agreement that will see Sobeys purchase the British Columbia-based grocery retailer. The transaction is based on an enterprise value of \$260.0 and is subject to adjustments for, among other items, assumed liabilities and working capital at closing. Thrifty's business includes 20 full-service supermarkets, a main distribution centre and a wholesale division on Vancouver Island and the lower mainland of British Columbia. The deal is expected to close during the Company's second quarter following receipt of regulatory approval and completion of due diligence. The transaction is expected to be financed with cash and available banking facilities.

Note 28 Comparative Figures

Comparative figures have been reclassified, where necessary, to reflect the current year's presentation and to record the effects of retroactive application of certain new accounting standards.