

KROGER CO
Form 10-Q/A
September 26, 2005

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q/A
Amendment No. 1

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

For the quarterly period ended August 13, 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)

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)

(Zip Code)

(513) 762-4000

(Registrant's telephone number, including area code)

Unchanged

(Former name, former address and former fiscal year, if changed since last report)

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

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

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

There were 724,866,659 shares of Common Stock (\$1 par value) outstanding as of September 16, 2005.

EXPLANATORY NOTE:

This Amendment No. 1 to Form 10-Q is filed solely to correct a typographical error in a heading on the Consolidated Statements of Operations in Part I, Item 1. The text in the third column has been corrected from August 13, 2004 to August 13, 2005.

PART I - FINANCIAL INFORMATION**Item 1. Financial Statements.****THE KROGER CO.****CONSOLIDATED STATEMENTS OF OPERATIONS**

(in millions, except per share amounts)

(unaudited)

	Second Quarter Ended		Two Quarters Ended	
	August 13, 2005	August 14, 2004	August 13, 2005	August 14, 2004
Sales	\$ 13,865	\$ 12,980	\$ 31,813	\$ 29,885
Merchandise costs, including advertising, warehousing, and transportation, excluding items shown separately below	10,464	9,721	23,907	22,244
Operating, general and administrative	2,528	2,434	5,824	5,642
Rent	145	154	348	366
Depreciation and amortization	294	290	682	662
	<u>434</u>	<u>381</u>	<u>1,052</u>	<u>971</u>
Operating Profit	434	381	1,052	971
Interest expense	121	152	280	325
	<u>313</u>	<u>229</u>	<u>772</u>	<u>646</u>
Earnings before income tax expense	313	229	772	646
Income tax expense	117	87	282	241
	<u>196</u>	<u>142</u>	<u>490</u>	<u>405</u>
Net earnings	\$ 196	\$ 142	\$ 490	\$ 405
	<u>0.27</u>	<u>0.19</u>	<u>0.68</u>	<u>0.55</u>
Net earnings per basic common share	\$ 0.27	\$ 0.19	\$ 0.68	\$ 0.55
	<u>722</u>	<u>737</u>	<u>725</u>	<u>739</u>
Average number of common shares used in basic calculation	722	737	725	739
	<u>0.27</u>	<u>0.19</u>	<u>0.67</u>	<u>0.54</u>
Net earnings per diluted common share	\$ 0.27	\$ 0.19	\$ 0.67	\$ 0.54
	<u>730</u>	<u>744</u>	<u>731</u>	<u>747</u>
Average number of common shares used in diluted calculation	730	744	731	747

The accompanying notes are an integral part of the Consolidated Financial Statements.

THE KROGER CO.

CONSOLIDATED BALANCE SHEETS

(in millions, except per share amounts)

(unaudited)

	August 13, 2005	January 29, 2005
	<u> </u>	<u> </u>
ASSETS		
Current assets		
Cash In stores	\$ 129	\$ 144
Cash Temporary cash investments	250	
	<u> </u>	<u> </u>
Total Cash	379	144
Deposits in-transit	510	506
Receivables	641	661
Receivables - Taxes		167
FIFO Inventory	4,642	4,729
LIFO Credit	(392)	(373)
Prefunded employee benefits		300
Prepaid and other current assets	264	272
	<u> </u>	<u> </u>
Total current assets	6,044	6,406
Property, plant and equipment, net	11,435	11,497
Goodwill	2,192	2,191
Other assets and investments	417	397
	<u> </u>	<u> </u>
Total Assets	\$ 20,088	\$ 20,491
LIABILITIES		
Current liabilities		
Current portion of long-term debt, at face value, including obligations under capital leases and financing obligations	\$ 295	\$ 71
Accounts payable	3,421	3,598
Accrued salaries and wages	649	659
Deferred income taxes	267	267
Other current liabilities	1,875	1,721
	<u> </u>	<u> </u>
Total current liabilities	6,507	6,316
Long-term debt including obligations under capital leases and financing obligations:		
Long-term debt, at face value, including obligations under capital leases and financing obligations	6,879	7,830
Adjustment to reflect fair value interest rate hedges (Note 11)	47	70
	<u> </u>	<u> </u>
Long-term debt including obligations under capital leases and financing obligations	6,926	7,900
Deferred income taxes	911	939
Other long-term liabilities	1,849	1,796
	<u> </u>	<u> </u>
Total Liabilities	16,193	16,951
Commitments and Contingencies (Note 10)		

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SHAREOWNERS EQUITY

Preferred stock, \$100 par, 5 shares authorized and unissued		
Common stock, \$1 par, 1,000 shares authorized: 924 shares issued in 2005 and 918 shares issued in 2004	924	918
Additional paid-in capital	2,482	2,432
Accumulated other comprehensive loss	(200)	(202)
Accumulated earnings	4,026	3,541
Common stock in treasury, at cost, 201 shares in 2005 and 190 shares in 2004	(3,337)	(3,149)
	<u>3,895</u>	<u>3,540</u>
Total Shareowners Equity		
	<u>\$ 20,088</u>	<u>\$ 20,491</u>

The accompanying notes are an integral part of the Consolidated Financial Statements.

THE KROGER CO.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in millions and unaudited)

	Two Quarters Ended	
	August 13, 2005	August 14, 2004
Cash Flows From Operating Activities:		
Net earnings	\$ 490	\$ 405
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	682	662
LIFO charge	19	19
Deferred income taxes	(28)	102
Other	30	(3)
Changes in operating assets and liabilities net of effects from acquisitions of businesses:		
Inventories	88	78
Receivables	20	82
Deposits in-transit	(3)	82
Prepaid expenses	300	286
Accounts payable	(135)	62
Accrued expenses	59	(87)
Accrued income taxes	303	143
Contribution to company-sponsored pension plans	(107)	(14)
Long-term liabilities	74	(13)
Net cash provided by operating activities	1,792	1,804
Cash Flows From Investing Activities:		
Capital expenditures, excluding acquisitions	(672)	(848)
Proceeds from sale of assets	42	46
Payments for acquisitions, net of cash acquired		(25)
Other	(16)	10
Net cash used by investing activities	(646)	(817)
Cash Flows From Financing Activities:		
Proceeds from issuance of long-term debt	6	
Payments on long-term debt	(43)	(800)
Borrowings (payments) on bank revolver	(694)	4
Financing charges incurred		(4)
Increase (decrease) in book overdrafts	(44)	(69)
Proceeds from issuance of capital stock	55	19
Treasury stock purchases	(191)	(169)
Net cash used by financing activities	(911)	(1,019)
Net decrease in cash and temporary cash investments	235	(32)
Cash and temporary cash investments:		
Beginning of year	144	159

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End of quarter	\$ 379	\$ 127
Supplemental disclosure of cash flow information:		
Cash paid during the year for interest	\$ 298	\$ 377
Cash paid (refunded) during the year for income taxes	\$ 5	\$ (7)
Non-cash changes related to purchase acquisitions:		
Fair value of assets acquired	\$	\$ 18
Goodwill recorded	\$	\$ 7
Liabilities assumed	\$	\$ 1

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

Basis of Presentation and Principles of Consolidation

The accompanying financial statements include the consolidated accounts of The Kroger Co. and its subsidiaries. The January 29, 2005 balance sheet was derived from audited financial statements and, due to its summary nature, does not include all disclosures required by generally accepted accounting principles (GAAP). Significant intercompany transactions and balances have been eliminated. References to the Company in these Consolidated Financial Statements mean the consolidated company.

In the opinion of management, the accompanying unaudited Consolidated Financial Statements include all normal, recurring adjustments that are necessary for a fair presentation of results of operations for such periods but should not be considered as indicative of results for a full year. The financial statements have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been omitted, pursuant to SEC regulations. Accordingly, the accompanying consolidated financial statements should be read in conjunction with the fiscal 2004 Annual Report on Form 10-K of The Kroger Co. filed with the SEC on April 15, 2005, as amended.

The unaudited information included in the Consolidated Financial Statements for the second quarter and two quarters ended August 13, 2005 and August 14, 2004 include the results of operations of the Company for the 12-week and 28-week periods then ended.

Vendor Allowances

The Company recognizes all vendor allowances as a reduction in merchandise costs when the related product is sold. In most cases, vendor allowances are applied to the related product by item, and therefore reduce the carrying value of inventory by item. When it is not practicable to allocate vendor allowances to the product by item, vendor allowances are recognized as a reduction in merchandise costs based on inventory turns and recognized as the product is sold.

Store Closing and Other Expense Allowances

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All closed store liabilities related to exit or disposal activities initiated after December 31, 2002, are accounted for in accordance with Statement on Financial Accounting Standards (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 lease buyouts. 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 the Company's 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 in the normal course of business.

	Future Lease Obligations	
	2005	2004
Balance at beginning of year	\$ 65	\$ 35
Additions	8	21
Payments	(5)	(5)
Adjustments	(3)	
Balance at end of Second Quarter	\$ 65	\$ 51

In addition, the Company also maintains a \$56 liability for facility closure costs for locations closed in California prior to the Fred Meyer merger, a \$14 liability relating to a charitable contribution required as a result of the Fred Meyer merger and a \$11 liability for store closing costs related to two distinct, formalized plans that coordinated the closing of several locations over relatively short periods of time in 2000 and 2001.

2. STOCK OPTION PLANS

The Company applies Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations to account 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 \$1 and \$2, after-tax, for the second quarter of 2005 and 2004, respectively. Restricted stock expense totaled \$3 and \$5, after-tax, for the first two quarters of 2005 and 2004, respectively. The Company's stock option plans are more fully described in the Company's fiscal 2004 Annual Report on Form 10-K.

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

	Second Quarter		Year-To-Date	
	2005	2004	2005	2004
Net earnings, as reported	\$ 196	\$ 142	\$ 490	\$ 405
Add: Stock-based compensation expense included in net earnings, net of income tax benefits	1	2	3	5
Subtract: Total stock-based compensation expense determined under fair value method for all awards, net of income tax benefits	(10)	(8)	(18)	(21)
Pro forma net earnings	\$ 187	\$ 136	\$ 475	\$ 389
Net earnings per basic common share, as reported	\$ 0.27	\$ 0.19	\$ 0.68	\$ 0.55

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Pro forma earnings per basic common share	\$ 0.26	\$ 0.18	\$ 0.66	\$ 0.53
Net earnings per diluted common share, as reported	\$ 0.27	\$ 0.19	\$ 0.67	\$ 0.54
Pro forma earnings per diluted common share	\$ 0.26	\$ 0.18	\$ 0.65	\$ 0.52

To calculate pro forma stock-based compensation, the Company estimated the fair value of each option grant, on the date of the grant, using the Black-Scholes option pricing model with the following weighted average assumptions used for grants in 2005 and 2004.

	<u>2005</u>	<u>2004</u>
Weighted average expected volatility (based on historical volatility)	30.83%	30.13%
Weighted average risk-free interest rate	4.11%	3.99%
Expected term (based on historical results)	8.7 years	8.7 years

The weighted average fair value of options granted during 2005 and 2004 was \$7.64 per share granted and \$7.91 per share granted, respectively. The Company uses a risk-free interest rate based upon the yield of a treasury note maturing at a date that approximates the option's expected term.

3. DEBT OBLIGATIONS

Long-term debt consists of:

	August 13, 2005	January 29, 2005
	<u>2005</u>	<u>2005</u>
Credit Facility and Commercial Paper borrowings	\$	\$ 694
4.95% to 8.92% Senior Notes and Debentures due through 2031	6,391	6,391
5.00% to 10.23% mortgages due in varying amounts through 2017	210	218
Other	185	202
	<u>6,786</u>	<u>7,505</u>
Total debt, excluding capital leases and financing obligations	6,786	7,505
Less current portion	(270)	(46)
	<u>6,516</u>	<u>7,459</u>
Total long-term debt, excluding capital leases and financing obligations	\$ 6,516	\$ 7,459

4. COMPREHENSIVE INCOME

Comprehensive income is as follows:

	Second Quarter Ended		Year-To-Date	
	August 13, 2005	August 14, 2004	August 13, 2005	August 14, 2004
	<u>2005</u>	<u>2004</u>	<u>2005</u>	<u>2004</u>
Net earnings	\$ 196	\$ 142	\$ 490	\$ 405
Unrealized gain (loss) on hedging activities, net of tax ⁽¹⁾	1		2	
	<u>197</u>	<u>142</u>	<u>492</u>	<u>405</u>
Comprehensive income	\$ 197	\$ 142	\$ 492	\$ 405

⁽¹⁾ Amount is net of tax of \$1 for the second quarter of 2005 and \$1 for the first two quarters of 2005.

During 2005, other comprehensive income consisted of reclassifications of previously deferred losses on cash flow hedges into net earnings as well as market value adjustments to reflect cash flow hedges at fair value as of the respective balance sheet dates.

5. BENEFIT PLANS

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The following table provides the components of net periodic benefit costs for the Company-sponsored pension plans and other post-retirement benefits for the second quarter of 2005 and 2004.

	Second Quarter			
	Pension Benefits		Other Benefits	
	2005	2004	2005	2004
Components of net periodic benefit cost:				
Service cost	\$ 28	\$ 25	\$ 3	\$ 2
Interest cost	28	26	5	5
Expected return on plan assets	(30)	(28)		
Amortization of:				
Transition asset				
Prior service cost	1	5	(2)	(1)
Actuarial (gain) loss	6	2	1	
Net periodic benefit cost	\$ 33	\$ 30	\$ 7	\$ 6

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The following table provides the components of net periodic benefit costs for the Company-sponsored pension plans and other post-retirement benefits for the first two quarters of 2005 and 2004:

	Year-To-Date			
	Pension Benefits		Other Benefits	
	2005	2004	2005	2004
Components of net periodic benefit cost:				
Service cost	\$ 66	\$ 59	\$ 6	\$ 5
Interest cost	65	61	11	12
Expected return on plan assets	(69)	(66)		
Amortization of:				
Transition asset				
Prior service cost	3	3	(4)	(3)
Actuarial (gain) loss	14	5	1	
Net periodic benefit cost	\$ 79	\$ 62	\$ 14	\$ 14

In addition to the \$107 contributed to the Company-sponsored pension plans in the first two quarters of 2005, the Company is required to make cash contributions totaling \$36 during the balance of fiscal 2005. The Company may elect to make additional contributions during 2005 in order to maintain its desired funding status, as described in Note 12, Subsequent Events.

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 Company recognizes expense in connection with these plans as contributions are funded, in accordance with GAAP.

6. INCOME TAXES

The effective income tax rate was 36.5% for the first two quarters of 2005 and 37.3% for the first two quarters of 2004. In addition to the effect of state taxes, the effective income tax rate differed from the federal statutory rate due to a reduction of previously recorded tax contingency allowances resulting from a revision of the required allowances based on resolutions with tax authorities during the quarters.

7. EARNINGS PER COMMON SHARE

Earnings per basic common share equals net earnings divided by the weighted average number of common shares outstanding. Earnings per diluted common share equals net earnings divided by the weighted average number of common shares outstanding, after giving effect to dilutive stock options, restricted stock and warrants.

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

	Second Quarter Ended			Second Quarter Ended		
	August 13, 2005			August 14, 2004		
	Earnings (Numerator)	Shares (Denominator)	Per Share Amount	Earnings (Numerator)	Shares (Denominator)	Per Share Amount
Earnings per basic common share	\$ 196	722	\$ 0.27	\$ 142	737	\$ 0.19
Dilutive effect of stock options and warrants		8			7	
Earnings per diluted common share	\$ 196	730	\$ 0.27	\$ 142	744	\$ 0.19
	Two Quarters Ended			Two Quarters Ended		
	August 13, 2005			August 14, 2004		
	Earnings (Numerator)	Shares (Denominator)	Per Share Amount	Earnings (Numerator)	Shares (Denominator)	Per Share Amount
Earnings per basic common share	\$ 490	725	\$ 0.68	\$ 405	739	\$ 0.55
Dilutive effect of stock options and warrants		6			8	
Earnings per diluted common share	\$ 490	731	\$ 0.67	\$ 405	747	\$ 0.54

The Company had options outstanding for approximately 24 shares and 33 shares during the second quarters of 2005 and 2004, respectively, that were excluded from the computations of earnings per diluted common share because their inclusion would have had an anti-dilutive effect on earnings per share. For the first two quarters of 2005 and 2004, the Company had options outstanding for approximately 26 and 30 shares, respectively, that were excluded from the computations of diluted earnings per share because their inclusion would have had an anti-dilutive effect on earnings per share.

8. RECENTLY ISSUED ACCOUNTING STANDARDS

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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.

Prior to the adoption of SFAS No. 123R, the Company is accounting for share-based compensation expense under the recognition and measurement provisions of APB No. 25, *Accounting for Stock Issued to Employees* and is following the accepted practice of recognizing share-based compensation expense over the explicit vesting period. SFAS No. 123R will require the immediate recognition at the grant date of the full share-based compensation expense for grants to retirement eligible employees, as the explicit vesting period is non-substantive. The estimated effect of applying the explicit vesting period approach versus the non-substantive approach is not material to any period presented. The Company expects to adopt SFAS No. 123R in the first quarter of fiscal 2006 and expects the adoption to reduce net earnings by \$0.04-\$0.06 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.

In May 2005, the FASB issued SFAS No. 154, Accounting Changes and Error Corrections, a replacement of APB Opinion No. 20 and FASB Statement No. 3. SFAS No. 154 requires retrospective application to prior periods financial statements for changes in accounting principle, unless it is impracticable to determine either the period-specific effects or the cumulative effect of the change. SFAS No. 154 also requires that retrospective application of a change in accounting principle be limited to the direct effects of the change. Indirect effects of a change in accounting principle should be recognized in the period of the accounting change. SFAS No. 154 further requires a change in depreciation, amortization or depletion method for long-lived, non-financial assets to be accounted for as a change in accounting estimate effected by a change in accounting principle. SFAS No. 154 will become effective for the Company's fiscal year beginning January 29, 2006.

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. The adoption of FIN 47 is not expected to have a material effect on the Company's Consolidated Financial Statements.

In June 2005, the Emerging Issues Task Force (EITF) reached a consensus on EITF Issue No. 05-6, Determining the Amortization Period for Leasehold Improvements Purchased After Lease Inception or Acquired in a Business Combination. EITF No. 05-6 requires that leasehold improvements acquired in a business combination be amortized over the shorter of the useful life of the assets or a term that includes required lease periods and renewals deemed to be reasonably assured at the date of acquisition. EITF No. 05-6 further requires that leasehold improvements that are placed into service significantly after and not contemplated at or near the beginning of the lease term shall be amortized over the shorter of the useful life of the assets or a term that includes the required lease periods and renewals deemed to be reasonably assured at the date of acquisition. EITF No. 05-6 became effective for the Company's fiscal quarter beginning August 14, 2005. The adoption of EITF No. 05-6 is not expected to have a material effect on the Company's Consolidated Financial Statements.

9. GUARANTOR SUBSIDIARIES

The Company's outstanding public debt (the Guaranteed Notes) is jointly and severally, fully and unconditionally guaranteed by The Kroger Co. and certain of its subsidiaries (the Guarantor Subsidiaries). At August 13, 2005, a total of approximately \$6.3 billion of Guaranteed Notes were outstanding. The Guarantor Subsidiaries and non-guarantor subsidiaries are direct or indirect 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 represented less than 3% on an individual and aggregate basis of consolidated assets, pre-tax earnings, cash flow and equity. Therefore, the non-guarantor subsidiaries' information is not separately presented in the tables below.

There are no current restrictions on the ability of the Guarantor Subsidiaries to make payments under the guarantees referred to above. The obligations of each guarantor under its guarantee are limited to the maximum amount permitted under Bankruptcy Law, the Uniform Fraudulent Conveyance Act, the Uniform Fraudulent Transfer Act, or any similar Federal or state law (e.g. laws requiring adequate capital to pay dividends) respecting fraudulent conveyance or fraudulent transfer.

The following tables present summarized financial information as of August 13, 2005, and January 29, 2005, and for the second quarters ended, and the two quarters ended, August 13, 2005 and August 14, 2004:

Condensed Consolidating

Balance Sheets

As of August 13, 2005

	The Kroger Co.	Guarantor Subsidiaries	Eliminations	Consolidated
Current assets				
Cash, including temporary cash investments	\$ 23	\$ 356	\$	\$ 379
Deposits in-transit	66	444		510
Accounts receivable	503	640	(502)	641
Net inventories	421	3,829		4,250
Prepaid and other current assets	69	195		264
	<u>1,082</u>	<u>5,464</u>	<u>(502)</u>	<u>6,044</u>
Total current assets	1,082	5,464	(502)	6,044
Property, plant and equipment, net	1,298	10,137		11,435
Goodwill	56	2,136		2,192
Other assets and investments	548	(131)		417
Investment in and advances to subsidiaries	10,445		(10,445)	
	<u>13,429</u>	<u>17,606</u>	<u>(10,947)</u>	<u>20,088</u>
Total assets	\$ 13,429	\$ 17,606	\$ (10,947)	\$ 20,088
Current liabilities				
Current portion of long-term debt including obligations under capital leases and financing obligations	\$ 295	\$	\$	\$ 295
Accounts payable	203	3,720	(502)	3,421
Other current liabilities	242	2,549		2,791
	<u>740</u>	<u>6,269</u>	<u>(502)</u>	<u>6,507</u>
Total current liabilities	740	6,269	(502)	6,507
Long-term debt including obligations under capital leases and financing obligations				
Face value long-term debt including obligations under capital leases and financing obligations	6,849	30		6,879
Adjustment to reflect fair value interest rate hedges	47			47
	<u>6,896</u>	<u>30</u>		<u>6,926</u>
Long-term debt including obligations under capital leases and financing obligations	6,896	30		6,926
Other long-term liabilities	1,898	862		2,760
	<u>9,534</u>	<u>7,161</u>	<u>(502)</u>	<u>16,193</u>
Total liabilities	9,534	7,161	(502)	16,193
Shareowners' Equity	3,895	10,445	(10,445)	3,895
	<u>13,429</u>	<u>17,606</u>	<u>(10,947)</u>	<u>20,088</u>
Total liabilities and shareowners' equity	\$ 13,429	\$ 17,606	\$ (10,947)	\$ 20,088

Condensed Consolidating

Balance Sheets

As of January 29, 2005

	The Kroger Co.	Guarantor Subsidiaries	Eliminations	Consolidated
Current assets				
Cash, including temporary cash investments	\$ 32	\$ 112	\$	\$ 144
Deposits in-transit	20	486		506
Accounts receivable	583	747	(502)	828
Net inventories	415	3,941		4,356
Prepaid and other current assets	275	297		572
	<u>1,325</u>	<u>5,583</u>	<u>(502)</u>	<u>6,406</u>
Total current assets	1,325	5,583	(502)	6,406
Property, plant and equipment, net	1,277	10,220		11,497
Goodwill	20	2,171		2,191
Other assets and investments	642	(245)		397
Investment in and advances to subsidiaries	10,518		(10,518)	
	<u>13,782</u>	<u>17,729</u>	<u>(11,020)</u>	<u>20,491</u>
Total assets	\$ 13,782	\$ 17,729	\$ (11,020)	\$ 20,491
Current liabilities				
Current portion of long-term debt including obligations under capital leases and financing obligations	\$ 71	\$	\$	\$ 71
Accounts payable	188	3,912	(502)	3,598
Other current liabilities	319	2,328		2,647
	<u>578</u>	<u>6,240</u>	<u>(502)</u>	<u>6,316</u>
Total current liabilities	578	6,240	(502)	6,316
Long-term debt including obligations under capital leases and financing obligations				
Face value long-term debt including obligations under capital leases and financing obligations	7,797	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 and financing obligations	7,867	33		7,900
Other long-term liabilities	1,797	938		2,735
	<u>10,242</u>	<u>7,211</u>	<u>(502)</u>	<u>16,951</u>
Total liabilities	10,242	7,211	(502)	16,951
Shareowners' Equity	3,540	10,518	(10,518)	3,540
	<u>13,782</u>	<u>17,729</u>	<u>(11,020)</u>	<u>20,491</u>
Total liabilities and shareowners' equity	\$ 13,782	\$ 17,729	\$ (11,020)	\$ 20,491

Condensed Consolidating

Statements of Operations

For the Quarter Ended August 13, 2005

	The Kroger Co.	Guarantor Subsidiaries	Eliminations	Consolidated
Sales	\$ 1,959	\$ 12,123	\$ (217)	\$ 13,865
Merchandise costs, including warehousing and transportation	1,511	9,168	(215)	10,464
Operating, general and administrative	393	2,135		2,528
Rent	33	114	(2)	145
Depreciation and amortization	17	277		294
Operating profit	5	429		434
Interest expense	118	3		121
Equity in earnings of subsidiaries	279		(279)	
Earnings (loss) before income tax expense	166	426	(279)	313
Income tax expense (benefit)	(30)	147		117
Net earnings	\$ 196	\$ 279	\$ (279)	\$ 196

Condensed Consolidating

Statements of Operations

For the Quarter Ended August 14, 2004

	The Kroger Co.	Guarantor Subsidiaries	Eliminations	Consolidated
Sales	\$ 2,172	\$ 11,045	\$ (237)	\$ 12,980
Merchandise costs, including warehousing and transportation	1,824	8,122	(225)	9,721
Operating, general and administrative	320	2,114		2,434
Rent	42	124	(12)	154
Depreciation and amortization	19	271		290
Operating profit (loss)	(33)	414		381
Interest expense	155	(3)		152
Equity in earnings of subsidiaries	260		(260)	
Earnings (loss) before income tax expense	72	417	(260)	229
Income tax expense (benefit)	(70)	157		87
Net earnings	\$ 142	\$ 260	\$ (260)	\$ 142

Condensed Consolidating

Statements of Operations

For the Two Quarters Ended August 13, 2005

	The Kroger Co.	Guarantor Subsidiaries	Eliminations	Consolidated
Sales	\$ 4,489	\$ 27,828	\$ (504)	\$ 31,813
Merchandise costs, including warehousing and transportation	3,632	20,775	(500)	23,907
Operating, general and administrative	862	4,962		5,824
Rent	89	263	(4)	348
Depreciation and amortization	42	640		682
Operating profit (loss)	(136)	1,188		1,052
Interest expense	274	6		280
Equity in earnings of subsidiaries	768		(768)	
Earnings (loss) before income tax expense	358	1,182	(768)	772
Income tax expense (benefit)	(132)	414		282
Net earnings	\$ 490	\$ 768	\$ (768)	\$ 490

Condensed Consolidating

Statements of Operations

For the Two Quarters Ended August 14, 2004

	The Kroger Co.	Guarantor Subsidiaries	Eliminations	Consolidated
Sales	\$ 4,393	\$ 26,003	\$ (511)	\$ 29,885
Merchandise costs, including warehousing and transportation	3,554	19,173	(483)	22,244
Operating, general and administrative	804	4,838		5,642
Rent	96	298	(28)	366
Depreciation and amortization	59	603		662
Operating profit (loss)	(120)	1,091		971
Interest expense	311	14		325
Equity in earnings of subsidiaries	672		(672)	
Earnings (loss) before income tax expense	241	1,077	(672)	646
Income tax expense (benefit)	(164)	405		241
Net earnings	\$ 405	\$ 672	\$ (672)	\$ 405

Condensed Consolidating

Statements of Cash Flows

For the Quarter Ended August 13, 2005

	The Kroger Co.	Guarantor Subsidiaries	Consolidated
	<u> </u>	<u> </u>	<u> </u>
Net cash provided by operating activities	\$ 839	\$ 953	\$ 1,792
Cash flows from investing activities:			
Capital expenditures, excluding acquisitions	(65)	(607)	(672)
Other	10	16	26
	<u> </u>	<u> </u>	<u> </u>
Net cash used by investing activities	(55)	(591)	(646)
Cash flows from financing activities:			
Proceeds from issuance of long-term debt	6		6
Payments on long-term debt	(40)	(3)	(43)
Payments on bank revolver	(694)		(694)
Proceeds from issuance of capital stock	55		55
Treasury stock purchases	(191)		(191)
Other	(2)	(42)	(44)
Net change in advances to subsidiaries	73	(73)	
	<u> </u>	<u> </u>	<u> </u>
Net cash used by financing activities	(793)	(118)	(911)
Net increase (decrease) in cash	(9)	244	235
Cash:			
Beginning of year	32	112	144
	<u> </u>	<u> </u>	<u> </u>
End of quarter	\$ 23	\$ 356	\$ 379
	<u> </u>	<u> </u>	<u> </u>

Condensed Consolidating

Statements of Cash Flows

For the Quarter Ended August 14, 2004

	The Kroger Co.	Guarantor Subsidiaries	Consolidated
	<u> </u>	<u> </u>	<u> </u>
Net cash provided by operating activities	\$ 283	\$ 1,521	\$ 1,804
Cash flows from investing activities:			
Capital expenditures, excluding acquisitions	(78)	(770)	(848)
Other		31	31
	<u> </u>	<u> </u>	<u> </u>
Net cash used by investing activities	(78)	(739)	(817)
	<u> </u>	<u> </u>	<u> </u>

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Cash flows from financing activities:			
Payments on long-term debt	(717)	(83)	(800)
Borrowings on bank revolver	4		4
Proceeds from issuance of capital stock	19		19
Treasury stock purchases	(169)		(169)
Other	(32)	(41)	(73)
Net change in advances to subsidiaries	687	(687)	
	<u> </u>	<u> </u>	<u> </u>
Net cash used by financing activities	(208)	(811)	(1,019)
	<u> </u>	<u> </u>	<u> </u>
Net decrease in cash	(3)	(29)	(32)
Cash:			
Beginning of year	26	133	159
	<u> </u>	<u> </u>	<u> </u>
End of quarter	\$ 23	\$ 104	\$ 127
	<u> </u>	<u> </u>	<u> </u>

10. COMMITMENTS AND CONTINGENCIES

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

Management believes that allowances for loss have been provided to the extent necessary and that its assessment of contingencies is reasonable. Allowances for loss are included in other current liabilities and other long-term liabilities. To the extent that resolution of contingencies results in amounts that vary from management'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. The liability for general liability risks is not present-valued. Actual claim settlements and expenses incident thereto may differ from the provisions for loss.

Litigation On September 8, 2005, the Los Angeles City Attorney's office filed a misdemeanor complaint against a subsidiary of the Company, Ralphs Grocery Company (People v. Ralphs Grocery Company, Superior Court of California, County of Los Angeles, Case No. 5CR02616) regarding alleged violations of the California Water Code. Ralphs operates a system at one store location to treat groundwater within an underground basement because of the presence of naturally occurring petroleum associated with the nearby La Brea tar pits, which system is subject to a discharge permit issued by the California Regional Water Quality Control Board (Board). The misdemeanor complaint alleges that Ralphs violated California Water Code Section 13387(a)(2) in connection with its obligations under the permit. Ralphs Grocery Company has been advised that the Los Angeles City Attorney's office also intends to file a civil complaint against Ralphs in the Superior Court of California, City of Los Angeles, under California Business and Professions Code Section 17200, alleging other violations of the same discharge permit. The Company does not expect that the ultimate resolution of these matters by either settlement or litigation 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. A related decision, also adverse to the Company, was appealed to the United States Court of Appeals for the Seventh Circuit. On July 26, 2005, the Company resolved both of these actions through execution of a settlement agreement.

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 purport or have been determined to be class actions and/or seek substantial damages. Any damages that may be awarded in an antitrust case will be automatically trebled. Although it is not possible at this time to evaluate the merits of all 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 therefore. 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 predictions

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could arise that could have a material adverse effect on the Company's financial condition or results of operation.

Guarantees The Company periodically enters into real estate joint ventures in connection with the development of certain properties. The Company usually sells its interest in such partnerships upon completion of the projects. As of August 13, 2005, the Company was a partner with 50% ownership in two real estate joint ventures for which it has guaranteed approximately \$7 of debt incurred by the ventures. Based on the covenants underlying this indebtedness as of August 13, 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 obligations under 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 satisfy a material amount of these obligations is remote.

Benefit Plans The Company administers certain 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 an 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. Funding for the retiree health care benefits occurs as claims or premiums are paid.

The determination of the obligation and expense for the Company's pension and other post-retirement benefits is dependent on the Company's selection of assumptions used by actuaries in calculating those amounts. Those assumptions are described in the Company's fiscal 2004 Annual Report on Form 10-K 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. 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 such 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.

In addition to the \$107 contributed to Company-sponsored pension plans in the first two quarters of 2005, the Company is required to make cash contributions totaling \$36 during the balance of fiscal 2005. The Company may elect to make additional contributions during 2005 in order to maintain its desired funding levels, as described in Note 12, Subsequent Events. Among other things, investment performance of plan assets, the interest rates required to be used to calculate pension obligations and future changes in legislation will determine the amounts of any additional contributions.

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.

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. Because the Company is only one of a number of employers contributing to these plans, it is difficult to ascertain what the Company's share of the underfunding would be, although we anticipate the Company's contributions to these plans will increase each year. 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 determined, in accordance with GAAP.

11. FAIR VALUE INTEREST RATE HEDGES

In 2003, the Company reconfigured a portion of its interest derivative portfolio by terminating six interest rate swap agreements that were accounted for as fair value hedges. Approximately \$114 of proceeds received as a result of these terminations were recorded as adjustments to the carrying values of the underlying debt and are being amortized over the remaining lives of the debt. As of August 13, 2005, the unamortized balances totaled approximately \$71.

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At the end of the second quarter of 2005, the Company maintained 10 interest rate swap agreements that are being accounted for as fair value hedges. As of August 13, 2005, liabilities totaling \$25 have been recorded to reflect the fair value of these new agreements, offset by reductions in the fair value of the underlying debt.

12. SUBSEQUENT EVENTS

On September 14, 2005, the Company made a cash contribution totaling \$140 to its Company-sponsored pension plans, of which \$36 was required. The Company expects the additional \$104 contribution will reduce its minimum required contributions in future years.

PART II OTHER INFORMATION

Item 6. Exhibits.

EXHIBIT 3.1 - Amended Articles of Incorporation of the Company are hereby incorporated by reference to Exhibit 3.1 of the Company's Quarterly Report on Form 10-Q for the quarter ended October 3, 1998. The Company's Regulations are incorporated by reference to Exhibit 4.2 of the Company's Registration Statement on Form S-3 as filed with the Securities and Exchange Commission on January 28, 1993, and bearing Registration No. 33-57552.

EXHIBIT 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.

*EXHIBIT 10.1 Material Contracts 2005 Deferred Compensation Plan for Independent Directors

*EXHIBIT 10.2 2005 Executive Deferred Compensation Plan

EXHIBIT 31.1 Rule 13a 14(a) / 15d 14(a) Certifications Chief Executive Officer

EXHIBIT 31.2 Rule 13a 14(a) / 15d 14(a) Certifications Chief Financial Officer

EXHIBIT 32.1 Section 1350 Certifications

*EXHIBIT 99.1 Additional Exhibits - Statement of Computation of Ratio of Earnings to Fixed Charges.

* Previously filed.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

THE KROGER CO.

Dated: September 26, 2005

By: /s/ David B. Dillon

David B. Dillon
Chairman of the Board and Chief Executive Officer

Dated: September 26, 2005

By: /s/ J. Michael Schlotman

J. Michael Schlotman
Senior Vice President and Chief Financial Officer

Exhibit Index

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