

26. VARIABLE INTEREST ENTITIES (“VIEs”)

Pursuant to AcG 15, Loblaw consolidates all VIEs for which it is the primary beneficiary. AcG 15 defines a VIE as an entity that either does not have sufficient equity at risk to finance its activities without subordinated financial support or where the holders of the equity at risk lack the characteristics of a controlling financial interest. AcG 15 requires the primary beneficiary to consolidate VIEs and considers an entity to be the primary beneficiary of a VIE if it holds variable interests that expose it to a majority of the VIE’s expected losses or that entitle it to receive a majority of the VIE’s expected residual returns or both. Loblaw has identified the following significant VIEs:

Independent Franchisees

Loblaw enters into various forms of franchise agreements that generally require the independent franchisee to purchase inventory from Loblaw and pay certain fees in exchange for services provided by Loblaw and for the right to use certain trademarks and licenses owned by Loblaw. Independent franchisees generally lease the land and building from Loblaw, and when eligible, may obtain financing through a structure involving independent trusts to facilitate the purchase of the majority of their inventory and fixed assets, consisting mainly of fixtures and equipment. These trusts are administered by a major Canadian chartered bank. Under the terms of certain franchise agreements, Loblaw may also lease equipment to independent franchisees. Independent franchisees may also obtain financing through operating lines of credit with traditional financial institutions or through issuing preferred shares or notes payable to Loblaw. Loblaw monitors the financial condition of its independent franchisees and provides for estimated losses or write-downs on its accounts and notes receivable or investments when appropriate.

As at year end 2007, 137 (2006 – 123) of Loblaw’s independent franchise stores met the criteria for a VIE and were consolidated pursuant to AcG 15.

Warehouse and Distribution Agreement

Loblaw has warehouse and distribution agreements with third-party entities to provide to Loblaw distribution and warehousing services from dedicated facilities. Loblaw has no equity interest in these third-party entities; however, the terms of the agreement with the third-party entities are such that Loblaw has determined that the third-party entities meet the criteria for a VIE that requires consolidation by Loblaw. The impact of the consolidation of the warehouse and distribution entities was not material.

Accordingly, the Company has included the results of these independent franchisees and these third-party entities that provide distribution and warehousing services in its consolidated financial statements. The consolidation of these VIEs by the Company does not result in any change to its tax, legal or credit risks, nor does it result in the Company assuming any obligations of these third parties.

Independent Trust

Loblaw has also identified that it holds a variable interest, by way of a standby letter of credit, in an independent trust which is used to securitize credit card receivables for PC Bank. In these securitizations, PC Bank sells a portion of its credit card receivables to the independent trust in exchange for cash. Although this independent trust has been identified as a VIE, it was determined that Loblaw is not the primary beneficiary and therefore this VIE is not subject to consolidation by the Company. The Company’s maximum exposure to loss as a result of its involvement with this independent trust is disclosed in notes 12 and 25.

During 2006, PC Bank restructured its credit card securitization program. Eagle Credit Card Trust (“Eagle”), a previously established independent trust, issued \$500 of five year senior notes and subordinated notes due in 2011 at a weighted average rate of 4.5% to finance the purchase of credit card receivables previously securitized by PC Bank through an independent trust. The subordinated notes provide credit support to those notes which are more senior. PC Bank will continue to service the credit card receivables on behalf of Eagle, but will not receive any fee for its servicing obligations and has a retained interest in the securitized receivables represented by the right to future cash flows after obligations to investors have been met. In accordance with Canadian GAAP, the financial statements of Eagle are not consolidated with those of the Company. The restructuring of the portfolio yielded a nominal net loss.