

# Accounting policies

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the group and company financial statements except as noted below.

## Basis of accounting

The financial statements have been prepared in accordance with applicable accounting standards and under the historical cost convention, modified to include the revaluation of certain land and buildings. However, compliance with SSAP19 'Accounting for investment properties' requires a departure from the requirements of the Companies Act 1985 relating to the depreciation of investment properties as described in note 11 to the financial statements.

A separate profit and loss account for the company has not been presented as permitted by section 230 (4) of the Companies Act 1985.

During the year, new requirements on revenue recognition, in the form of an Application Note to FRS5 'Reporting the Substance of Transactions', were issued and became effective for this year's Report and Accounts. The effects of implementing this Application Note are shown in note 1(iv).

## Consolidation

The group financial statements combine the results of the company and all its subsidiaries and joint ventures, to the extent of group ownership and after eliminating intra-group transactions.

Unless otherwise stated, the acquisition method of accounting has been adopted. Under this method, the results of subsidiary undertakings acquired or disposed of in the year are included in the consolidated profit and loss account from the date of acquisition or up to the date of disposal.

Joint ventures are those undertakings, not recognised as subsidiaries, in which the group has a participating interest and are jointly controlled. The group's share of the results of joint ventures, which are accounted for under the gross equity method, are included in the profit and loss account and its share of their net assets is included in investments in the group balance sheet.

In the company balance sheet, investments in subsidiaries and joint ventures are stated at cost (being the par value of shares issued where merger relief applies) less impairments.

During the comparative year Boots Group PLC was introduced as the new holding company of the Boots Group by way of a Scheme of Arrangement under section 425 of the Companies Act 1985. This was accounted for as a capital reorganisation and merger accounting principles have been applied, as if the company had always been the holding company of the group.

## Foreign currencies

The results and cash flows of overseas subsidiaries and the results of joint ventures are translated into sterling on an average exchange rate basis, weighted by the actual results of each month. Assets and liabilities including currency swaps are translated into sterling at the rates of exchange ruling at the balance sheet date.

Exchange differences arising from the translation of the results and net assets of overseas subsidiaries, less offsetting exchange differences on foreign currency borrowings and currency swaps hedging those assets (net of any related tax effects), are dealt with through reserves.

Where foreign currency hedges are taken out for committed future foreign currency purchases, the fair value of those hedges are not included in the profit and loss account and balance sheet. All other exchange differences are dealt with in the profit and loss account.

The cost of the company investment in shares in overseas subsidiaries is stated at the rate of exchange in force at the date each investment was made, except where hedge accounting applies in which case the year end rate is used.

## Goodwill and intangible assets

Goodwill on acquisitions comprises the excess of the fair value of the consideration plus any associated costs for investments in subsidiary undertakings and joint ventures over the fair value of net assets acquired. Fair values are attributed to the identifiable assets and liabilities that existed at the date of acquisition, reflecting their condition at that date. Adjustments are also made to bring the accounting policies of acquired businesses into alignment with those of the group. The costs of integrating and reorganising acquired businesses are charged to the post-acquisition profit and loss account.

Goodwill arising on acquisitions prior to 1st April 1998 has been set off against reserves. On disposal of such businesses, any goodwill previously set off against reserves is charged in the calculation of the profit or loss on disposal. For subsequent acquisitions goodwill is recognised within fixed assets in the year in which it arises and amortised on a straight line basis over its useful economic life, not exceeding 20 years.

The cost of intangible assets acquired (which are capitalised only if separately identifiable) is not amortised except where the end of the useful economic lives of the acquired intangible asset can be reasonably foreseen. Similar assets created within the business are not capitalised and expenditure is charged against profits in the year in which it is incurred. The carrying value of intangible assets (including in particular those being amortised over periods greater than 20 years) is reviewed annually and any impairment in value charged to the profit and loss account.

## Tangible fixed assets and depreciation

Depreciation of tangible fixed assets is provided to write off the cost or valuation, less residual value, by equal instalments over their expected useful economic lives as follows:

- Freehold land, investment properties, assets in the course of construction – not depreciated
- Freehold and long leasehold buildings, depreciated to their estimated residual values over their useful economic lives of not more than 50 years
- Short leasehold properties – remaining period of lease when less than 50 years
- Computer equipment including software – 3 to 8 years
- Motor cars – 4 or 5 years
- Other motor vehicles – 3 to 10 years
- Fixtures and plant – 3 to 20 years

Any impairment in the value of fixed assets is recognised immediately.

The group adopted the transitional provisions of FRS15 'Tangible Fixed Assets' to retain the book value of land and buildings many of which were last revalued in 1993 and has not adopted a policy of annual revaluations for the future.

Investment properties are revalued annually and included in the balance sheet at their open market value (adjusted to exclude the benefit of formal lease arrangements with group companies).

Profits and losses arising from the disposal of properties which have previously been revalued are calculated by reference to their carrying value.

Interest is capitalised on tangible fixed assets in the course of construction or development. The capitalisation rate applied depends on whether the construction is financed by a specific borrowing (based on actual interest rate) or whether it is financed by general borrowings (based on the weighted average rate on all non-specific borrowings).

#### **Fixed Asset Investment in Own Shares**

Own shares, which have been purchased for the benefit of employees under various incentive schemes, are held as fixed asset investments in the balance sheet. These shares are held in three employee ownership trusts:

- The shares held by the qualifying employee share ownership trust (QUEST) holds shares for the all employee SAYE scheme. They are initially capitalised at the purchase price with the discount given to employees being written off on acquisition.
- Shares owned by the ESOP Trust form part of the Boots Long Term Bonus Scheme for executive directors and senior employees. These shares are capitalised at cost on acquisition and are amortised over the relevant qualifying and service periods of the bonus scheme.
- Shares owned by the all employee share ownership plan (AESOP) are conditionally gifted to all employees employed at a qualifying date and then held in trust for a qualifying service period of not less than three years. These shares are capitalised at cost and subsequently amortised over the relevant qualifying period.

Impairment tests are performed on the carrying value of the shares to reflect any permanent diminution in value.

#### **Cash and liquid resources**

Cash, for the purpose of the cash flow statement, comprises cash in hand and deposits repayable on demand, less overdrafts payable on demand.

Liquid resources are current asset investments which are disposable without curtailing or disrupting the business and are either readily convertible into known amounts of cash at or close to their carrying values or traded in an active market. Liquid resources comprise term deposits of less than one year (other than cash).

#### **Derivative financial instruments**

The derivative financial instruments used by the group to manage its interest rate and currency risks are interest rate swaps and forward rate contracts. Interest receipts and payments arising on interest rate swaps are recognised within net interest payable over the period of the contract. Termination payments made or received are amortised over the life of the underlying exposure in cases where the exposure continues to exist, and taken to the profit and loss account immediately where the underlying exposure ceases to exist. Gains and losses arising on forward currency contracts entered into to hedge trading transactions are recognised in the profit and loss account in the same period as the underlying exposure. Forward contracts hedging cash and borrowings are valued at closing rates of exchange at each period end, with gains and losses offset against the related cash and borrowings. The interest differential on these instruments is recognised against net interest payable.

#### **Turnover**

Turnover comprises sales to external customers (excluding VAT and other sales taxes) and rental income. Consideration received from customers is only recorded as turnover when the group has completed full performance in respect of that consideration.

#### **Stocks**

Stocks are valued at the lower of cost and net realisable value. Cost comprises purchase cost of goods, direct labour and those overheads related to manufacture and distribution based on normal activity levels.

#### **Research and development**

Expenditure on research and development, other than on buildings and plant, is charged against profit in the year in which it is incurred.

#### **Pensions**

The company and its UK subsidiaries operate pension schemes under which contributions by employees and by the companies are held in trust funds separated from the companies' finances. Actuarial valuations of the schemes are conducted at three year intervals and include a review of contributions.

The cost of providing pensions is spread over the employees' working lives with the companies. The cost charged to the profit and loss account in any year may not always equal the employer contributions to the pension schemes.

**Leases**

The rental costs of properties and other assets held under operating leases are charged to the profit and loss account on a straight line basis. Benefits received as an incentive to sign a lease, whatever form they may take, are credited to the profit and loss account on a straight line basis over the lease term or, if shorter than the full lease term, over the period to the review date on which the rent is first expected to be adjusted to the prevailing market rate.

The cost of assets held under finance leases (being leases which give rights to the group approximating to ownership) is included under tangible fixed assets and depreciation is provided in accordance with the policy for the class of asset concerned. The corresponding obligations under these leases are shown as creditors. The finance charge element of rentals is charged to the profit and loss account to produce, or approximate to, a constant periodic rate of charge on the remaining balance of the outstanding obligations.

**Deferred taxation**

Deferred tax is provided in respect of all timing differences that have originated, but not reversed, by the balance sheet date except as required by FRS19 'Deferred Tax' as detailed below. Deferred tax is measured on a non-discounted basis at the tax rates that are expected to apply in the periods in which timing differences reverse, based on tax rates and laws substantively enacted at the balance sheet date.

No provision is made for taxation liabilities which would arise on the distribution of profits retained by overseas subsidiaries and joint ventures as there is no commitment to remit these profits. It is not anticipated that any significant taxation will become payable on the revaluation surplus or sale of properties, as taxation on gains on properties used for the purpose of the group's trade is expected to be deferred indefinitely or eliminated by capital losses.