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SEARS ROEBUCK ACCEPTANCE CORP

Form 10-Q

November 05, 2003

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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q

X QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF  
THE SECURITIES EXCHANGE ACT OF 1934  
FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 27, 2003

OR

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

Commission file number 1-4040

SEARS ROEBUCK ACCEPTANCE CORP.  
(Exact name of registrant as specified in its charter)

Delaware 51-0080535  
(State of Incorporation) (I.R.S. Employer Identification No.)

3711 Kennett Pike, Greenville, Delaware 19807  
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: 302/434-3100

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, and has been subject to such filing requirements for the past 90 days.  
Yes  No

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

As of October 25, 2003 the Registrant had 350,000 shares of capital stock outstanding, all of which were held by Sears, Roebuck and Co.

Registrant meets the conditions set forth in General Instructions H(1)(a) and (b) of Form 10-Q and is therefore filing this Form with a reduced disclosure format.

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SEARS ROEBUCK ACCEPTANCE CORP.

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13 WEEKS AND 39 WEEKS ENDED SEPTEMBER 27, 2003

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PART I. FINANCIAL INFORMATION  
ITEM 1. FINANCIAL STATEMENTS

SEARS ROEBUCK ACCEPTANCE CORP.

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STATEMENTS OF FINANCIAL POSITION

	(unaudited)		
(millions, except share data)	Sept.27, 2003	Sept.28, 2002	Dec. 28, 2002
<b>Assets</b>			
Cash and cash equivalents	\$ 1,126	\$ 377	\$ 1,563
Notes of Sears	17,227	17,883	15,352
Other assets	149	142	139
	-----	-----	-----
Total assets	\$ 18,502	\$ 18,402	\$ 17,054
	=====	=====	=====
<b>Liabilities</b>			
Commercial paper (net of unamortized discount of \$3, \$6 and \$5)	\$ 3,312	\$ 4,008	\$ 2,869
Medium-term notes (net of unamortized discount of \$3, \$5 and \$5)	4,248	2,336	2,118
Discrete underwritten debt (net of unamortized discount of \$55, \$59 and \$58)	7,295	8,541	8,542
Accrued interest and other liabilities	179	184	160
	-----	-----	-----
Total liabilities	15,034	15,069	13,689
	-----	-----	-----
<b>Commitments and contingent liabilities</b>			
<b>Shareholder's Equity</b>			
Common share, par value \$100 per share; 500,000 shares authorized; 350,000 shares issued and outstanding	35	35	35
Capital in excess of par value	1,150	1,150	1,150
Accumulated other comprehensive loss	(3)	(3)	(3)
Retained income	2,286	2,151	2,183
	-----	-----	-----
Total shareholder's equity	3,468	3,333	3,365
	-----	-----	-----
Total liabilities and shareholder's equity	\$ 18,502	\$ 18,402	\$ 17,054
	=====	=====	=====

See notes to financial statements.

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SEARS ROEBUCK ACCEPTANCE CORP.

STATEMENTS OF INCOME AND COMPREHENSIVE INCOME  
(unaudited)

(millions, except ratios)	13 Weeks Ended		39 Weeks Ended	
	Sept.27, 2003	Sept.28, 2002	Sept.27, 2003	Sept.28, 2002

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Revenues	-----	-----	-----	-----
Earnings on notes of Sears	\$ 257	\$ 255	\$ 756	\$ 729
Earnings on cash equivalents	5	2	21	10
	-----	-----	-----	-----
Total revenues	262	257	777	739
	-----	-----	-----	-----
Expenses				
Interest expense and amortization of debt discount/premium	201	205	611	588
Loss on debt extinguishment	7	-	7	-
Operating expenses	-	-	1	1
	-----	-----	-----	-----
Total expenses	208	205	619	589
	-----	-----	-----	-----
Income before income taxes	54	52	158	150
Income taxes	19	18	55	52
	-----	-----	-----	-----
Net income	\$ 35	\$ 34	\$ 103	\$ 98
	-----	-----	-----	-----
Total other comprehensive income(loss)				
Losses on cash flow hedge, net of tax	-	-	-	(3)
	-----	-----	-----	-----
Total comprehensive income	\$ 35	\$ 34	\$ 103	\$ 95
	=====	=====	=====	=====
Ratios of earnings to fixed charges	1.26	1.25	1.26	1.26

See notes to financial statements.

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SEARS ROEBUCK ACCEPTANCE CORP.

STATEMENTS OF CASH FLOWS

(unaudited)

(millions)	39 Weeks Ended	
	Sept.27, 2003	Sept.28, 2002
	-----	-----
Cash flows from operating activities:		
Net income	\$ 103	\$ 98
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, amortization and other noncash items	16	10
Loss on debt extinguishment	7	-
Increase in other assets	(8)	(2)
Increase(decrease)in other liabilities	19	(8)
	-----	-----
Net cash provided by operating activities	138	98

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Cash flows from investing activities:	-----	-----
Increase in notes of Sears	(1,875)	(1,869)
	-----	-----
Net cash used in		
investing activities	(1,875)	(1,869)
	-----	-----
Cash flows from financing activities:		
Increase in commercial paper,		
primarily 90 days or less	443	783
Proceeds from issuance of long-term debt	3,195	1,832
Payments for redemption of long-term debt	(2,316)	(1,042)
Issue costs paid to issue debt	(21)	(24)
	-----	-----
Net cash provided by		
financing activities	1,301	1,549
	-----	-----
Net decrease in cash and		
cash equivalents	(437)	(222)
Cash and cash equivalents at beginning		
of period	1,563	599
	-----	-----
Cash and cash equivalents at end of period	\$ 1,126	\$ 377
	=====	=====

See notes to financial statements.

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SEARS ROEBUCK ACCEPTANCE CORP.

NOTES TO FINANCIAL STATEMENTS  
(unaudited)

1. Significant Accounting Policies

The unaudited interim financial statements of Sears Roebuck Acceptance Corp. ("SRAC"), a wholly-owned subsidiary of Sears, Roebuck and Co. ("Sears"), reflect all adjustments (consisting only of normal recurring accruals) which are, in the opinion of management, necessary for a fair statement of the results for the interim periods presented.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted. The significant accounting policies used in the presentation of these financial statements are consistent with the summary of significant accounting policies set forth in SRAC's Annual Report on Form 10-K for the 52 weeks ended December 28, 2002, and these financial statements should be read in conjunction with the financial statements and notes found therein. The results of operations for the interim periods should not be considered indicative of the results to be expected for the full year.

2. Back-up Liquidity

SRAC continued to provide support for 100% of its outstanding commercial paper through its investment portfolio and committed credit facilities. SRAC's

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investment portfolio, which consists of cash and cash equivalents, fluctuated from a low of \$1.1 billion to a high of \$2.4 billion in the third quarter of 2003. On September 27, 2003, SRAC's committed credit facilities consisted of a \$3.5 billion unsecured 364-day revolving credit facility expiring February 23, 2004 which includes an option to extend the repayment of borrowings, if any, through February 2005. Effective November 3, 2003, SRAC amended the facility extending the termination date to May 2004 for consenting lenders and modifying the option to extend the repayment of any borrowings to November 2004. The amendment also provides for the commitment amount under this facility to be reduced to \$2.5 billion 30 days following the sale of Sears' Credit and Financial Products business.

As of September 27, 2003, there have been no outstanding borrowings related to this credit facility.

### 3. Legal Proceedings

On June 16, 2003, a lawsuit was filed in the United States District Court for the Northern District of Illinois against Sears, certain of its officers, and SRAC, alleging that certain public announcements and SEC filings by Sears and SRAC concerning Sears credit card business violated Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, Rule 10b-5 promulgated thereunder, and Section 11 of the Securities Act of 1933, and seeking damages. An amended complaint was filed on October 16, 2003, naming additional individuals and certain investment banks as defendants. The plaintiffs purport to represent a class of noteholders who purchased certain notes issued by SRAC between October 24, 2001 and October 17, 2002, whether by prospectus or otherwise. SRAC believes that these claims lack merit and is defending against them vigorously.

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The consequences of this matter are not presently determinable but, in the opinion of management of SRAC after consulting with legal counsel and taking into account insurance, the ultimate liability is not expected to have a material effect on annual results of operations, financial position, liquidity or capital resources of SRAC.

### 4. Subsequent Events

On October 17, 2003, SRAC commenced cash tender offers to purchase any and all of its unsecured public term debt securities maturing after 2003, which includes 174 series of securities with an aggregate principal amount of approximately \$10.7 billion. The offers are expected to expire on November 14, 2003, unless previously terminated or extended. If all of the \$10.7 billion of debt is retired through the cash tender offers, the Company expects to realize a \$695 million after-tax loss on the extinguishment of that debt in the fourth quarter of 2003. This loss will consist of the expected premium paid to retire the debt and the writeoff of unamortized debt issuance costs.

On November 3, 2003, Sears completed the sale of its domestic Credit and Financial Products business to Citicorp. The sale generated total proceeds of \$32 billion, consisting of the assumption of \$10 billion

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of securitized debt by Citicorp and cash proceeds received by Sears of \$22 billion. Proceeds from Sears' sale of the Credit and Financial Products business are intended to be earmarked primarily to retire debt that supported the domestic credit card receivables, return cash to Sears shareholders; and for general corporate purposes. Sears may use acquired funds from the sale of its Credit business to redeem a portion of its Sears Note to fund the repayment of SRAC's tendered debt.

As a result of Sears' sale of its Credit and Financial Products business, on November 3, 2003, Sears executed guarantees pursuant to which it has agreed to guarantee (1) SRAC's debt securities issued or to be issued under the indenture dated as of May 15, 1995 between SRAC and JPMorgan Chase Bank, as trustee, and the indenture dated as of October 1, 2002 between SRAC and BNY Midwest Trust Company, as trustee; and (2) SRAC's commercial paper notes issued or to be issued under its commercial paper program.

### 5. Medium-term Notes and Discrete Underwritten Debt

Medium-term notes and discrete underwritten debt are issued with either a floating rate indexed to LIBOR or a fixed rate.

(dollars in millions; term in years)

#### ISSUANCE

	2003			2002		
	Volume	Avg. Coupon	Avg. Orig. Term	Volume	Avg. Coupon	Avg. Orig. Term
13 Weeks Ended:						
Medium-term notes	\$ 135	1.89%	5.0	\$ -	-%	-
Discrete debt	\$ -	-%	-	\$ -	-%	-
39 Weeks Ended:						
Medium-term notes	\$2,945	4.51%	3.1	\$ 15	4.50%	2.6
Discrete debt	\$ 250	7.40%	40.0	\$1,850	7.03%	24.9

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#### GROSS OUTSTANDING

	9/27/03			9/28/02		
	Balance	Avg. Coupon	Avg. Remain. Term	Balance	Avg. Coupon	Avg. Remain. Term
Medium-term notes	\$4,251	4.80%	2.8	\$2,341	5.88%	1.3

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Discrete debt            \$7,350    6.81%    13.3    \$8,600    6.97%    13.2

### MATURITIES

Year	Medium-term notes	Discrete debt	Total
2003	\$ 429	\$ 250*	\$ 679
2004	1,702	-	1,702
2005	204	250	454
2006	507	550	1,057
2007	104	-	104
Thereafter	1,305	6,300	7,605
<b>Total</b>	<b>\$4,251</b>	<b>\$7,350</b>	<b>\$11,601</b>

\*On September 23, 2003, SRAC announced that it elected to call for redemption the entire \$250 million outstanding principal amount of its 6.95% notes due March 23, 2038. The redemption date was October 23, 2003.

On September 1, 2003, SRAC redeemed the entire \$250 million outstanding principal amount of its 7% notes due March 1, 2038, which resulted in a loss on debt extinguishment of \$7 million. On October 23, 2003, SRAC also redeemed the entire \$250 million outstanding principal amount of its 6.95% notes due October 23, 2038, which resulted in a loss on debt extinguishment of \$7 million.

On October 17, 2003, SRAC commenced cash tender offers to purchase any and all of its unsecured public term debt securities maturing after 2003, which includes 174 series of securities with an aggregate principal amount of approximately \$10.7 billion. The offers are expected to expire on November 14, 2003, unless previously terminated or extended. (see Note 4)

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### INDEPENDENT ACCOUNTANTS' REPORT

To the Board of Directors and Shareholder of  
Sears Roebuck Acceptance Corp.:

We have reviewed the accompanying statements of financial position of Sears Roebuck Acceptance Corp. (a wholly-owned subsidiary of Sears, Roebuck and Co.) as of September 27, 2003 and



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September 28, 2002, and the related statements of income and comprehensive income for the 13 week and 39 week periods then ended and cash flows for the 39 week periods then ended. These interim financial statements are the responsibility of Sears Roebuck Acceptance Corp.'s management.

We conducted our reviews in accordance with standards established by the American Institute of Certified Public Accountants. A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with auditing standards generally accepted in the United States of America, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to such interim financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

We have previously audited, in accordance with auditing standards generally accepted in the United States of America, the statement of financial position of Sears Roebuck Acceptance Corp. as of December 28, 2002 and the related statements of income and comprehensive income, shareholder's equity and cash flows for the year then ended (not presented herein); and in our report dated February 14, 2003, except for Note 5, as to which the date is February 24, 2003, we expressed an unqualified opinion on those financial statements. In our opinion, the information set forth in the accompanying statement of financial position as of December 28, 2002 is fairly stated, in all material respects, in relation to the statement of financial position from which it has been derived.

/s/ Deloitte & Touche LLP  
-----  
Deloitte & Touche LLP  
Philadelphia, Pennsylvania  
November 4, 2003

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SEARS ROEBUCK ACCEPTANCE CORP.

### ITEM 2. ANALYSIS OF RESULTS OF OPERATIONS

During the third quarter of 2003, SRAC revenues increased to \$262 million from \$257 million in the comparable 2002 period. For the 39 week period ended September 27, 2003, SRAC's revenues increased to \$777 million from \$739 million for the comparable 2002 period. The increase in revenues resulted from increases in average earning asset levels of \$300 million and \$800 million in the 13 and 39 week periods of 2003 versus the 2002 periods.

SRAC's interest and related expenses, including losses associated with the early extinguishment of debt, increased 1% to \$208 million from

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\$205 million and 5% to \$618 million from \$588 million for the 13 and 39 week periods of 2003, respectively, as compared to the comparable 2002 periods. Interest and related expenses increased during the 13 and 39 week period of 2003 due to a loss on the early extinguishment of debt related to the writeoff of unamortized issue expense of \$7 million and increases in average long-term debt levels. The loss on debt extinguishment related to a \$250 million 7% note due March 1, 2038 and redeemed September 1, 2003. SRAC's average long-term debt increased to \$11.9 billion and \$11.6 billion in the 13 and 39 weeks of 2003, compared with \$11.0 billion and \$10.4 billion for the same periods in 2002. Increases in interest and related expenses attributed to long-term debt levels were partially offset by reductions in average short-term debt levels and overall cost of funds. SRAC's short-term borrowings averaged \$3.4 billion in the third quarter and \$3.2 billion in the 39 week period of 2003, compared to \$4.1 billion and \$3.8 billion for the respective 2002 periods. SRAC's cost of short-term funds averaged 1.35% in the third quarter and 1.57% in the first nine months of 2003 compared to 2.13% and 2.27% for the same periods in 2002. SRAC's cost of long-term funds averaged 6.14% and 6.36% in the 13 and 39 weeks of 2003 compared to 6.53% and 6.54% for the comparable 2002 periods.

SRAC's net income of \$35 million and \$103 million for the 13 and 39 weeks of 2003, respectively, increased from the comparable 2002 period amounts of \$34 million and \$98 million.

SRAC's ratio of earnings to fixed charges for both the 13 and 39 weeks of 2003 was 1.26, compared to 1.25 and 1.26 for the comparable 2002 periods.

### Item 4. CONTROLS AND PROCEDURES

The Company's management, including Keith E. Trost, President (principal executive officer) and George F. Slook, Vice President, Finance (principal financial officer), have evaluated the effectiveness of the Company's "disclosure controls and procedures," as such term is defined in Rules 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended, (the "Exchange Act"). Based upon their evaluation, the principal executive officer and principal financial officer concluded that, at the end of the period covered by this report, the Company's disclosure controls and procedures were effective for the purpose of ensuring that the information required to be disclosed in the reports that the Company files or submits under the Exchange Act with the Securities and Exchange Commission (the "SEC") (1) is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and (2) is accumulated and communicated to the Company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. In addition, based on that evaluation, no change in the Company's internal control over financial reporting occurred during the quarter ended September 27, 2003 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

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SEARS ROEBUCK ACCEPTANCE CORP.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

On June 16, 2003, a lawsuit was filed in the United States District Court for the Northern District of Illinois against Sears, Roebuck and Co. ("Sears"), certain of its officers, and SRAC, alleging that certain public announcements and SEC filings by Sears and SRAC concerning Sears credit card business violated Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, Rule 10b-5 promulgated thereunder, and Section 11 of the Securities Act of 1933, and seeking damages. An amended complaint was filed on October 16, 2003, naming additional individuals and certain investment banks as defendants. The plaintiffs purport to represent a class of noteholders who purchased certain notes issued by SRAC between October 24, 2001 and October 17, 2002, whether by prospectus or otherwise. SRAC believes that these claims lack merit and is defending against them vigorously.

The consequences of this matter are not presently determinable but, in the opinion of management of SRAC after consulting with legal counsel and taking into account insurance, the ultimate liability is not expected to have a material effect on annual results of operations, financial position, liquidity or capital resources of SRAC.

Item 6. Exhibits and Reports on Form 8-K

(a) The exhibits listed in the "Exhibit Index" are filed as part of this report.

(b) Reports on Form 8-K:

There were no current reports on Form 8-K filed by SRAC during the quarter for which this report is filed.

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SIGNATURE

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.

SEARS ROEBUCK ACCEPTANCE CORP.  
(Registrant)

By: /s/ George F. Slook  
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George F. Slook  
Vice President, Finance  
and Assistant Secretary  
(principal financial  
officer and authorized  
officer of Registrant)

November 5, 2003

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EXHIBIT INDEX

- 3(a) Certificate of Incorporation of the Registrant, as in effect at November 13, 1987 [Incorporated by reference to Exhibit 28(c) to the Registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 1987\*].
- 3(b) By-laws of the Registrant, as in effect at October 20, 1999 [Incorporated by reference to Exhibit 3(b) to the Registrant's Quarterly Report on Form 10-Q for the Quarter ended October 2, 1999\*].
- 4(a) The Registrant hereby agrees to furnish the Commission, upon request, with each instrument defining the rights of holders of long-term debt of the Registrant with respect to which the total amount of securities authorized does not exceed 10% of the total assets of the Registrant.

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- 4(b) Fixed Charge Coverage and Ownership Agreement dated as of September 24, 2002 between Sears Roebuck Acceptance Corp. and Sears, Roebuck and Co. [Incorporated by reference to Exhibit 4(f) of Registration Statement No. 333-92082].
- 4(c) Indenture dated as of October 1, 2002 between the Registrant and BNY Midwest Trust Company.[Incorporated by reference to Exhibit 4(b) to Registrant's Quarterly Report on Form 10-Q for the quarter ended September 28, 2002\*].
- 4(d) Form of Fixed-Rate InterNotes [Incorporated by reference to Exhibit 4 to the Registrant's Current Report on Form 8-K dated April 23, 2003\*].
- 4(e) Supplemental Indenture dated as of November 3, 2003 among the Registrant, Sears Roebuck and Co. and BNY Midwest Trust Company.\*\*
- 4(f) Supplemental Indenture dated as of November 3, 2003 among the Registrant, Sears Roebuck and Co. and JPMorgan Chase Bank (successor to The Chase Manhattan Bank, N.A.).\*\*
- 4(g) Guarantee executed by Sears, Roebuck and Co. under the Indenture, dated as of May 15, 1995, between Registrant and JPMorgan Chase Bank (successor to The Chase Manhattan Bank, N.A.), as supplemented by the First Supplemental Indenture, dated as of November 3, 2003\*\*
- 4(h) Guarantee executed by Sears, Roebuck and Co. under the Indenture, dated as of October 1, 2002, between Registrant and BNY Midwest Trust Company, as supplemented by the First Supplemental Indenture, dated as of November 3, 2003\*\*
- 10 Acknowledgement and Extension Agreement, dated as of August 19, 2003, among Sears, Roebuck and Co. ("Sears"), Registrant, and Certain Lenders that are parties to the 364-Day Credit Agreement dated as of February 24, 2003 [Incorporated by reference to Exhibit 10(c) to Sears'Quarterly Report on Form 10-Q for the quarter ended September 27, 2003 (SEC File No 1-416)].
- 12 Calculation of ratio of earnings to fixed charges.\*\*
- 15 Acknowledgement of awareness from Deloitte & Touche LLP, dated November 4, 2003, concerning unaudited financial information.\*\*
- 31(a) Certification of Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002\*\*
- 31(b) Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002\*\*
- 32 Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted by Section 906 of the Sarbanes-Oxley Act of 2002\*\*

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\* SEC File No. 1-4040.

\*\* Filed herewith.

