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SEARS ROEBUCK ACCEPTANCE CORP

Form 10-Q

August 11, 2004

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 JULY 3, 2004

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 July 31, 2004 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 26 WEEKS ENDED JULY 3, 2004

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PART I. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

SEARS ROEBUCK ACCEPTANCE CORP.
CONDENSED STATEMENTS OF FINANCIAL POSITION

	(unaudited)		
(millions, except share data)	July 3, 2004	June 28, 2003	Jan. 3, 2004
	-----	-----	-----
Assets			
Cash and cash equivalents	\$ 352	\$ 2,449	\$ 1,286
Notes of Sears	7,029	16,252	7,743
Other assets	24	167	28
	-----	-----	-----
Total assets	\$ 7,405	\$ 18,868	\$ 9,057
	=====	=====	=====
Liabilities			
Commercial paper (net of unamortized discount of \$1, \$4 and \$1)	\$ 734	\$ 3,208	\$ 774
Medium-term notes (net of unamortized discount of \$2, \$4 and \$3)	1,142	4,242	2,701
Discrete underwritten debt (net of unamortized discount of \$8, \$56 and \$8)	1,838	7,794	1,838
Accrued interest and other liabilities	54	191	128
	-----	-----	-----
Total liabilities	3,768	15,435	5,441
	-----	-----	-----
Commitments and contingent liabilities			
Shareholder's Equity			
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)	-
Retained earnings	2,452	2,251	2,431
	-----	-----	-----
Total shareholder's equity	3,637	3,433	3,616
	-----	-----	-----
Total liabilities and shareholder's equity	\$ 7,405	\$ 18,868	\$ 9,057
	=====	=====	=====

See notes to condensed financial statements.

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SEARS ROEBUCK ACCEPTANCE CORP.

CONDENSED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME
(unaudited)

(millions, except ratios)	13 Weeks Ended		26 Weeks Ended	
	July 3, 2004	June 28, 2003	July 3, 2004	June 28, 2003
	-----	-----	-----	-----
Revenues				
Earnings on notes of Sears	\$ 69	\$ 248	\$ 147	\$ 499
Earnings on cash equivalents	3	9	6	16
	-----	-----	-----	-----
Total revenues	72	257	153	515
	-----	-----	-----	-----
Expenses				
Interest expense and amortization of debt discount/premium	55	204	119	410
Loss on early retirement of debt	1	-	1	-
Operating expenses	1	1	1	1
	-----	-----	-----	-----
Total expenses	57	205	121	411
	-----	-----	-----	-----
Income before income taxes	15	52	32	104
Income taxes	5	18	11	36
	-----	-----	-----	-----
Net income	\$ 10	\$ 34	\$ 21	\$ 68
	=====	=====	=====	=====
Total comprehensive income	\$ 10	\$ 34	\$ 21	\$ 68
	=====	=====	=====	=====
Ratios of earnings to fixed charges	1.27	1.25	1.27	1.25

See notes to condensed financial statements.

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SEARS ROEBUCK ACCEPTANCE CORP.

CONDENSED STATEMENTS OF CASH FLOWS
(unaudited)

(millions)	26 Weeks Ended	
	July 3, 2004	June 28, 2003
	-----	-----
Cash flows from operating activities:		
Net income	\$ 21	\$ 68
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		

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Depreciation, amortization and other noncash items	5	11
Increase in other assets	(1)	(15)
(Decrease)increase in other liabilities	(74)	31
Loss on early retirement of debt	1	-
	-----	-----
Net cash (used in) provided by operating activities	(48)	95
	-----	-----
Cash flows from investing activities:		
Decrease (increase) in notes of Sears	714	(900)
	-----	-----
Net cash provided by (used in) investing activities	714	(900)
	-----	-----
Cash flows from financing activities:		
(Decrease)increase in commercial paper, primarily 90 days or less	(40)	339
Proceeds from issuance of long-term debt	29	3,060
Payments for redemption of long-term debt	(1,589)	(1,687)
Issue costs paid to issue debt	-	(21)
	-----	-----
Net cash (used in)provided by financing activities	(1,600)	1,691
	-----	-----
Net (decrease) increase in cash and cash equivalents	(934)	886
Cash and cash equivalents at beginning of period	1,286	1,563
	-----	-----
Cash and cash equivalents at end of period	\$ 352	\$ 2,449
	=====	=====

See notes to condensed financial statements.

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SEARS ROEBUCK ACCEPTANCE CORP.
 NOTES TO CONDENSED FINANCIAL STATEMENTS
 (unaudited)

1. Significant Accounting Policies

The unaudited interim financial statements of Sears Roebuck Acceptance Corp. (the "Company" or "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 53 weeks ended January 3, 2004, and these financial statements should be read in conjunction

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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 investment portfolio, which consists of cash and cash equivalents, fluctuated from a low of \$351 million to a high of \$1,261 million in the second quarter of 2004. On May 17, 2004, SRAC, through a syndicate of banks, obtained an unsecured, three-year revolving credit facility in the amount of \$2.0 billion. The new facility replaced a 364-day facility, which expired in May 2004. No borrowings were outstanding under this committed credit facility at the end of the second quarter of 2004. Sears has guaranteed any borrowings under this facility. The facility and related Sears guarantee require SRAC and Sears to maintain certain fixed charge ratios and a specified level of tangible net worth for Sears' domestic segment. SRAC and Sears were in compliance with these covenants at July 3, 2004.

Sears has issued guarantees in support of SRAC's outstanding public debt in order to maintain SRAC's exemption from being deemed an "investment company" under the Investment Company Act of 1940, as amended. These guarantees are continuous, have no recourse provisions and require Sears to repay all SRAC's outstanding debt including interest and principal and any borrowings under the credit facility, in the event SRAC defaults on its payment obligations.

3. Legal Proceedings

On June 17, 2003, an action was filed in the Northern District of Illinois against Sears and certain of its officers, purportedly on behalf of a class of all persons who, between June 21, 2002 and October 17, 2002, purchased the 7% notes that SRAC issued on June 21, 2002.

An amended complaint has been filed, naming as additional defendants certain former Sears officers, SRAC and certain of its officers and several investment banking firms who acted as underwriters for SRAC's March 18, May 21 and June 21, 2002 notes offerings. The amended complaint alleges that the defendants made misrepresentations or omissions concerning Sears' credit business from October 24, 2001 to October 17, 2002 and in the registration statements and prospectuses relating to the offerings. The amended complaint alleges that these misrepresentations and omissions violated Sections 10(b) and 20(a) of the Securities Exchange Act and Rule 10b-5 promulgated thereunder, and Sections 11, 12 and 15 of the Securities Act of 1933 and purports to be brought on behalf of a class of all persons who purchased any security of SRAC between October 24, 2001 and October 17, 2002, inclusive. Motions to dismiss the amended complaint are pending.

The consequences of this matter are not presently determinable but, in the opinion of management of SRAC after consulting with legal counsel and

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taking into account applicable third party insurance coverage, the ultimate liability is not expected to have a material adverse effect on annual results of operations, financial position, liquidity or capital resources of SRAC. No amounts have been accrued for this matter in the financial statements.

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4. 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

	2004			2003		
	Volume	Avg. Coupon	Avg. Orig. Term	Volume	Avg. Coupon	Avg. Orig. Term
13 Weeks Ended:						
Medium-term notes	\$ 29	1.78%	5.0	\$1,280	3.57%	2.4
26 Weeks Ended:						
Medium-term notes	\$ 29	1.78%	5.0	\$2,810	4.64%	3.0
Discrete debt	\$ -	-%	-	\$ 250	7.40%	40.0

GROSS OUTSTANDING

	7/3/04			6/28/03		
	Balance	Avg. Coupon	Avg. Remain. Term	Balance	Avg. Coupon	Avg. Remain. Term
Medium-term notes	\$1,144	5.28%	2.7	\$4,246	2.65%	2.6
Discrete debt	\$1,846	6.80%	11.4	\$7,850	6.82%	14.9

MATURITIES

Year	Medium-term notes	Discrete debt	Total
2004	\$ 173	\$ -	\$ 173
2005	185	112	297
2006	265	190	455
2007	67	269	336
2008	317	-	317
Thereafter	137	1,275	1,412
Total	\$1,144	\$1,846	\$ 2,990

Maturity schedule assumes debt that is callable within one year of this Quarterly report will be retired.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

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

We have reviewed the accompanying condensed statements of financial position of Sears Roebuck Acceptance Corp. (a wholly-owned subsidiary of Sears, Roebuck and Co.) as of July 3, 2004 and June 28, 2003, and the related condensed statements of income and comprehensive income for the 13 week and 26 week periods then ended and condensed cash flows for the 26 week period then ended. These condensed interim financial statements are the responsibility of the Sears Roebuck Acceptance Corp.'s management.

We conducted our reviews in accordance with standards of the Public Company Accounting Oversight Board(United States).

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 standards of the Public Company Accounting Oversight Board (United States), 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 condensed 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 standards of the Public Company Accounting Oversight Board(United States), the statement of financial position of Sears Roebuck Acceptance Corp. as of January 3, 2004, 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 March 9, 2004, we expressed an unqualified opinion on those financial statements.

In our opinion, the information set forth in the accompanying

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condensed statement of financial position as of January 3, 2004 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
August 9, 2004

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SEARS ROEBUCK ACCEPTANCE CORP.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS

Overview

Sears Roebuck Acceptance Corp.'s ("SRAC") investment in the Notes of Sears, Roebuck and Co. ("Sears") decreased in the second quarter and first half of 2004 as Sears continued to utilize the cash proceeds from the sale of its Credit and Financial Products business to pay down its debt. SRAC retired a portion of its debt with the funds received from Sears as payment on the Notes, resulting in reduced levels of both assets and debt during the quarter. Lower average asset and debt levels coupled with a reduction in average interest rates drove both earnings and interest expense down in the second quarter and first half of 2004. SRAC expects the Sears Note and debt levels to decline further as proceeds are passed to SRAC for debt retirement, resulting in reduced earnings and expenses.

SRAC syndicated a new \$2.0 billion unsecured, three-year facility in the second quarter of 2004.

Results of Operations

SRAC revenues decreased \$185 million and \$362 million in the second quarter and first half of 2004, respectively, versus the comparable 2003 periods. SRAC's revenues are derived primarily from the earnings on its investment in the notes of Sears and invested cash. The decreases in revenue resulted primarily from

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\$10.6 billion and \$10.0 billion decreases in average earning asset levels and 191 and 194 basis point reductions in average rates on these assets in the second quarter and first half of 2004, respectively, versus the 2003 periods.

SRAC's interest and related expenses, including loss on early retirement of debt, decreased 73% to \$56 million from \$204 million and 71% to \$120 million from \$410 million for the second quarter and first half of 2004, respectively, as compared to the comparable 2003 periods. Interest and related expenses decreased during the second quarter and first half of 2004 primarily as a result of significantly lower debt levels accompanied by lower average interest rates. SRAC's average total debt levels decreased 74% to \$3.9 billion and 70% to \$4.4 billion in the second quarter and first six months of 2004, respectively, compared with \$14.8 billion and \$14.6 billion for the same periods in 2003. Debt levels in 2004 declined from the comparable 2003 periods as a result of the November 2003 cash tender offer in which SRAC retired \$6.2 billion of its outstanding term debt, coupled with a reduction in its short term borrowing program and term debt retirement of approximately \$0.6 billion and \$1.6 billion during the 13- and 26- week periods ended July 3, 2004. SRAC expects to retire an additional \$173 million of term debt by year-end 2004. SRAC's cost of funds on all debt averaged 5.24% in the second quarter and 5.10% in the first six months of 2004 compared to 5.36% and 5.43% for the same periods in 2003.

The ratings on SRAC's debt as of July 3, 2004, appear in the table below:

	Moody's Investors Service	Fitch Ratings	Standard & Poor's Ratings Services
Unsecured term debt	Baal	BBB	BBB
Unsecured commercial paper	P-2	F2	A-2

During the second quarter, Fitch Ratings lowered its rating of SRAC's unsecured term debt from BBB+, with a negative outlook, to BBB, with a stable outlook. SRAC's short-term rating of F2 was affirmed. In July 2004, Standard & Poor's revised the outlook for SRAC's debt ratings from stable to negative.

During the second quarter of 2004, SRAC syndicated a new \$2.0 billion unsecured, three-year credit facility. This facility provides support for SRAC's direct-issue commercial paper program and is available for other general purposes. Sears has guaranteed any borrowings under this facility. No borrowings were outstanding under this committed credit facility at the end of the second quarter of 2004. The facility and related Sears guarantee contain certain financial covenants for both SRAC and

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Sears' domestic segment. As of July 3, 2004, SRAC and Sears were in compliance with these covenants.

SRAC's net income of \$10 million and \$21 million for the second quarter and first half of 2004, respectively, decreased from the comparable 2003 period amounts of \$34 million and \$68 million.

SRAC's ratio of earnings to fixed charges for both the second quarter and first half of 2004 was 1.27, compared to 1.25 for the comparable 2003 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 Rule 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, as of 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 July 3, 2004 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II. OTHER INFORMATION

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:

Registrant filed a Current Report on Form 8-K dated May 17, 2004 [Items 5 and 7].

SEARS ROEBUCK ACCEPTANCE CORP.

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

George F. Slook
Vice President, Finance
and Assistant Secretary
(authorized officer of
Registrant)

August 10, 2004

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- 3(a) Certificate of Incorporation of the Registrant, as in effect at November 13, 1987 [Incorporated by reference to Exhibit 28(c) to 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 Registrant's Quarterly Report on Form 10-Q for the Quarter ended October 2, 1999*].
- 4 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.
- 10(a) Three-Year Credit Agreement dated as of May 17, 2004 among Sears Roebuck Acceptance Corp., the banks, financial institutions and other institutional lenders (the "Lenders") listed on the signature pages thereof, Barclays Bank PLC, as syndication agent, Bank of America, N.A., Bank One, NA and Wachovia Bank National Association, as documentation agents, Citigroup Global Markets Inc. and Barclays Capital, the Investment Banking Division of Barclays Bank PLC, as joint lead arrangers and joint bookrunners, and Citibank, N.A., as administrative agent for the Lenders [Incorporated by reference to Exhibit 10(a) to Registrant's Current Report on Form 8-K dated May 17, 2004*].
- 10(b) Guarantee, dated as of May 17, 2004, by Sears, Roebuck and Co. in favor of the Benefitted Parties [Incorporated by reference to Exhibit 10(b) to Registrant's Current Report on Form 8-K dated May 17, 2004*]
- 12 Calculation of ratio of earnings to fixed charges.**
- 15 Acknowledgement of awareness from Deloitte & Touche LLP, dated August 9, 2004, 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**

* SEC File No. 1-4040.

** Filed herewith

