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A C MOORE ARTS & CRAFTS INC  
Form 10-Q  
November 14, 2003

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2003

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: 000-23157

A.C. MOORE ARTS & CRAFTS, INC.

-----  
(Exact name of registrant as specified in charter)

Pennsylvania

22-3527763

-----  
(State or other jurisdiction of  
incorporation or organization)

-----  
(I.R.S. Employer  
Identification No.)

500 University Court, Blackwood, NJ 08012

-----  
(Address of principal executive offices)  
(Zip Code)

(856) 228-6700

-----  
(Registrant's telephone number, including area code)

N/A

-----  
(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 the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

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| Class                               | Outstanding at November 12, 2003 |
|-------------------------------------|----------------------------------|
| -----<br>Common Stock, no par value | -----<br>19,346,891              |

A.C. MOORE ARTS & CRAFTS, INC.

TABLE OF CONTENTS

PART I: FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited)

Consolidated Balance Sheets as of September 30, 2003 and December 31, 2002.....

Consolidated Statements of Income for the three and nine month periods  
ended September 30, 2003 and 2002.....

Consolidated Statements of Cash Flows for the nine month periods  
ended September 30, 2003 and 2002.....

Notes to Consolidated Financial Statements.....

Item 2. Management's Discussion and Analysis of Financial Condition  
and Results of Operations.....

Item 3. Quantitative and Qualitative Disclosures About Market Risk.....

Item 4. Controls and Procedures.....

PART II: OTHER INFORMATION

Item 1. Legal Proceedings.....

Item 2. Changes in Securities and Use of Proceeds.....

Item 3. Defaults Upon Senior Securities.....

Item 4. Submission of Matters to a Vote of Security Holders.....

Item 5. Other Information.....

Item 6. Exhibits and Reports on Form 8-K.....

SIGNATURES.....

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## PART I. FINANCIAL INFORMATION

### ITEM 1. FINANCIAL STATEMENTS

#### A. C. MOORE ARTS & CRAFTS, INC. CONSOLIDATED BALANCE SHEETS (dollars in thousands)

|   | September 30,<br>2003<br>----- |
|---|--------------------------------|
| ASSETS  | (unaudited)                    |
| Current assets:   |                                |
| Cash and cash equivalents   | \$ 24,989                      |
| Inventories   | 125,084                        |
| Prepaid expenses and other current assets   | 5,654                          |
|   | -----                          |
|   | 155,727                        |
| Marketable securities   | 14,161                         |
| Property and equipment, net   | 36,524                         |
| Other assets  | 1,873                          |
|   | -----                          |
|   | \$208,285                      |
|   | =====                          |
| LIABILITIES AND SHAREHOLDERS' EQUITY  |                                |
| Current liabilities:  |                                |
| Current portion of capital leases   | \$ 815                         |
| Trade accounts payable  | 34,042                         |
| Accrued payroll and payroll taxes   | 3,794                          |
| Accrued expenses  | 7,522                          |
| Income taxes payable  | --                             |
|   | -----                          |
|   | 46,173                         |
|   | -----                          |
| Long-term liabilities:  |                                |
| Capitalized equipment leases, less current portion  | --                             |
| Deferred tax liability  | 6,019                          |
| Other long-term liabilities   | 4,496                          |
|   | -----                          |
|   | 10,515                         |
|   | -----                          |
|   | 56,688                         |
|   | -----                          |
| SHAREHOLDERS' EQUITY  |                                |
| Preferred stock, no par value, 10,000,000 shares<br>authorized, none issued   |                                |
| Common stock, no par value, 40,000,000 shares<br>authorized, 19,319,195 shares outstanding at September 30, 2003<br>and 18,806,047 outstanding at December 31, 2002 | 104,487                        |
| Retained earnings   | 47,110                         |
|   | -----                          |
|   | 151,597                        |
|   | -----                          |
|   | \$208,285                      |

=====

See accompanying notes to financial statements

3

## A. C. MOORE ARTS &amp; CRAFTS, INC.

CONSOLIDATED STATEMENTS OF INCOME  
(dollars in thousands, except per share data)  
(unaudited)

|   | Three months ended<br>September 30, |            | Ni    |
|---|-------------------------------------|------------|-------|
|   | 2003                                | 2002       |       |
| Net sales   | \$ 98,600                           | \$ 89,726  | \$ 28 |
| Cost of sales (including buying and distribution costs)             | 61,987                              | 56,423     | 17    |
| Gross Margin  | 36,613                              | 33,303     | 10    |
| Selling, general and administrative expenses                        | 33,842                              | 31,180     | 9     |
| Pre-opening expenses  | 821                                 | 850        |       |
| Income from operations  | 1,950                               | 1,273      |       |
| Net interest (income)   | (92)                                | (150)      |       |
| Income before income taxes  | 2,042                               | 1,423      |       |
| Income tax expense  | 780                                 | 566        |       |
| Net income  | \$ 1,262                            | \$ 857     | \$    |
| Basic net income per share  | \$ 0.07                             | \$ 0.05    | \$    |
| Weighted average shares outstanding                                 | 19,247,590                          | 18,741,640 | 19,04 |
| Diluted net income per share  | \$ 0.06                             | \$ 0.04    | \$    |
| Weighted average shares outstanding plus impact of<br>stock options | 19,980,409                          | 19,807,463 | 19,65 |

See accompanying notes to financial statements

4

## A.C. MOORE ARTS &amp; CRAFTS, INC

CONSOLIDATED STATEMENTS OF CASH FLOWS  
(dollars in thousands)  
(unaudited)

Nine Mon

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|   | September<br>2003<br>----- |
|---|----------------------------|
| Cash flows from operating activities:   |                            |
| Net income  | \$ 2,733                   |
| Adjustments to reconcile net income to net cash (used in) operating activities: |                            |
| Depreciation and amortization   | 5,014                      |
| Provision for deferred income taxes   | 869                        |
| Changes in assets and liabilities:  |                            |
| Inventories   | (22,587)                   |
| Prepaid expenses and other current assets                                       | (2,925)                    |
| Accounts payable, accrued payroll, payroll taxes<br>and accrued expenses        | 7,042                      |
| Income taxes payable  | (1,041)                    |
| Other long-term liabilities   | 522                        |
| Other   | (22)                       |
|   | -----                      |
| Net cash (used in) operating activities   | (10,395)<br>-----          |
| Cash flows from investing activities:   |                            |
| Capital expenditures  | (13,541)                   |
| Investment in marketable securities   | (14,161)                   |
|   | -----                      |
| Cash flows (used in) investing activities                                       | (27,702)<br>-----          |
| Cash flows from financing activities:   |                            |
| Proceeds from sale of shares  | --                         |
| Proceeds from line of credit  | --                         |
| Repayment of line of credit   | --                         |
| Exercise of stock options   | 2,533                      |
| Repayment of capital leases   | (1,031)                    |
|   | -----                      |
| Net cash provided by financing activities                                       | 1,502<br>-----             |
| Net increase (decrease) in cash   | (36,595)                   |
| Cash and cash equivalents at beginning of period                                | 61,584<br>-----            |
| Cash and cash equivalents at end of period                                      | \$ 24,989<br>=====         |

See accompanying notes to financial statements

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(UNAUDITED)

(1) Basis of Presentation

The consolidated financial statements included herein include the accounts of A.C. Moore Arts & Crafts, Inc. and its wholly owned subsidiaries (collectively the "Company"). The Company is a chain of 78 retail stores selling arts and

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crafts merchandise. The stores are located throughout the eastern United States.

These financial statements have been prepared by management without audit and should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2002. Due to the seasonality of the Company's business, the results for the interim periods are not necessarily indicative of the results for the year. The accompanying consolidated financial statements reflect, in the opinion of management, all adjustments necessary for a fair presentation of the interim financial statements. In the opinion of management, all such adjustments are of a normal and recurring nature.

### (2) Common Stock and Earnings per Share

On June 25, 2002, the Company's Board of Directors declared a two-for-one stock split to shareholders of record as of the close of business on July 15, 2002 payable on July 31, 2002. All references to the number of shares of common stock, per share prices and earnings per share amounts in the consolidated financial statements and accompanying notes included in this Quarterly Report on Form 10-Q have been adjusted to reflect the split on a retroactive basis.

### (3) Management Estimates

The preparation of these consolidated financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of expenses during the reported period and related disclosures. Significant estimates made as of and for the three and nine month periods ended September 30, 2003 and 2002 include provisions for shrinkage, capitalized buying, warehousing and distribution costs related to inventory, and markdowns of merchandise inventories. Actual results could differ materially from those estimates.

### (4) Marketable Securities

Marketable securities represent investments in municipal bonds with maturities of twelve months or longer from time of purchase. They are classified as held-to-maturity and recorded at amortized cost.

6

### (5) Recent Accounting Pronouncements

In November 2002, the Emerging Issues Task Force reached consensus on Issue 02-16, Accounting by a Customer (including a Reseller) for Cash Consideration Received from a Vendor. EITF Issue 02-16 addresses the accounting for cash consideration received by a customer from a vendor (e.g., slotting fees, cooperative advertising payments, buydowns) and rebates or refunds from a vendor that is payable only if the customer completes a specified cumulative level of purchases or remains a customer for a specified time period. The EITF is effective for agreements modified or entered into after January 1, 2003.

The Company has historically treated cooperative advertising allowances as a reduction of advertising expense. Under EITF 02-16, cooperative advertising allowances should be treated as a reduction of inventory cost unless they represent a reimbursement of specific, incremental and identifiable costs incurred by the customer to sell the vendor's product. The Company does not expect this issue to have a material impact on the 2003 financial statements since substantially all of the cooperative advertising allowance agreements for 2003 were entered into prior to January 1, 2003.

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The Company has assessed the historic volume of cooperative advertising reimbursements that have been received in order to determine which of these reimbursements would meet the specific, identifiable and incremental criteria outlined under this issue and accordingly, qualify as a direct offset to advertising expense. Based on the Company's analysis of the impact on net income, and the administrative cost to identify and track reimbursements between those qualifying for expense offset and those requiring inventory cost reduction, beginning in 2004 the Company has elected to treat all cooperative advertising funds received from vendors as a reduction in the cost of inventory and recognize them as a reduction to cost of goods sold when the inventory is sold. We estimate that the prospective change in the timing of income recognition will reduce 2004 EPS by approximately \$0.12 per share.

The adoption of this accounting principle does not change the ultimate cash to be received under these agreements, only the timing of when it is reflected in net income. This change will have a positive effect on our cash flow.

7

In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure an amendment of FASB Statement No. 123". SFAS 148 amends SFAS 123 to provide alternative methods of transition for an entity that voluntarily changes to the fair value based method of accounting for stock-based employee compensation. It also amends the disclosure provisions of SFAS 123 to require prominent disclosure about the effects on reported net income of an entity's accounting policy decisions with respect to stock-based employee compensation. It also amends APB Opinion No. 28, "Interim Financial Reporting", to require disclosure about those effects in interim financial information. The Company adopted the disclosure requirements of SFAS 148 for the fiscal year ended December 31, 2002.

The Company accounts for its employee stock options using the intrinsic value method prescribed in Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" (APB 25). Compensation cost for stock options is measured as the excess of the quoted market price of the Company's stock at the date of grant over the amount an employee must pay to acquire the stock.

Had compensation cost for the Company's stock-based compensation plan been determined based on the fair value at the grant date for awards under those plans, consistent with the requirements of SFAS No. 123, "Accounting for Stock-Based Compensation," net income and earnings per share would have been reduced to the following pro-forma amounts:

|                              |                        | Three Months Ended<br>September 30, |            | Nin      |
|------------------------------|------------------------|-------------------------------------|------------|----------|
|                              |                        | 2003                                | 2002       | 2003     |
| Net income.....              | As reported            | \$1,262,000                         | \$ 857,000 | \$2,733, |
|                              | Compensation cost, net | 305,000                             | 188,000    | 860,     |
|                              | Pro forma              | 957,000                             | 669,000    | 1,873,   |
| Basic earnings per share.... | As reported            | \$ .07                              | \$ .05     | \$       |
|                              | Pro forma              | .05                                 | .04        |          |

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|                              |             |    |     |    |     |    |
|------------------------------|-------------|----|-----|----|-----|----|
| Diluted earnings per share.. | As reported | \$ | .06 | \$ | .04 | \$ |
|                              | Pro forma   |    | .05 |    | .03 |    |

The pro forma results may not be representative of the effects on reported operations for future years. The fair value of the options was calculated using a Black-Scholes options pricing model with the following weighted-average assumptions: risk-free interest rate of 3.2% for 2003, 4.1% for 2002, 5.1% for 2001, 6.3% for 2000 and; no dividend yield; and a weighted average expected life of the options of 4.5 years for 2003 and seven years for 2002, 2001, and 2000. In accordance with the provisions of SFAS No. 123 the expected stock price volatility was 56.0% for 2003, 45.2% for 2002, 48.4% for 2001, and 46.6% for 2000.

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

The following discussion and analysis contains certain forward-looking statements. These forward-looking statements do not constitute historical facts and involve risks and uncertainties. Actual results could differ materially from those referred to in the forward-looking statements due to a number of factors, including, but not limited to, the following: the impact of the adoption of EITF Issue 02-16, customer demand, the effect of economic conditions, the impact of adverse weather conditions, the impact of competitors' locations or pricing, the availability of acceptable real estate locations for new stores, difficulties with respect to new information system technologies, supply constraints or difficulties, the effectiveness of advertising strategies and the impact of the threat of terrorist attacks and war. For additional information concerning factors that could cause actual results to differ materially from the information contained herein, reference is made to the information under the heading "Cautionary Statement Relating to Forward Looking Statements" in our Annual Report on Form 10-K as filed with the Securities and Exchange Commission.

8

Due to the importance of our peak selling season, which includes Fall/Halloween, Thanksgiving and Christmas, the fourth quarter has historically contributed, and we expect it will continue to contribute, disproportionately to our profitability for the entire year. As a result, our quarterly results of operations may fluctuate. In addition, results of a period shorter than a full year may not be indicative of results expected for the entire year.

Our quarterly results of operations also may fluctuate based upon such factors as the length of holiday seasons, the date on which holidays fall, the number and timing of new store openings, the amount of store pre-opening expenses, the amount of net sales contributed by new and existing stores, the mix of products sold, the amount of sales returns, the timing and level of markdowns and other competitive factors.

Results of Operations

The following table sets forth, for the periods indicated, selected statement of operations data expressed as a percentage of net sales and the number of stores open at the end of each such period:

Three months ended  
September 30,

Ni



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|   | 2003   | 2002   | 2001   |
|---|--------|--------|--------|
|   | -----  | -----  | -----  |
| Net sales.....                                    | 100.0% | 100.0% | 100.0% |
| Cost of sales.....                                | 62.9%  | 62.9%  | 63.0%  |
|   | -----  | -----  | -----  |
| Gross margin.....                                 | 37.1%  | 37.1%  | 36.9%  |
| Selling, general and administrative expenses..... | 34.3%  | 34.8%  | 34.8%  |
| Store pre-opening expenses.....                   | 0.8%   | 0.9%   | 0.8%   |
|   | -----  | -----  | -----  |
| Income from operation.....                        | 2.0%   | 1.4%   | 1.4%   |
| Net interest (income) expense.....                | (0.1)% | (0.2)% | (0.1)% |
|   | -----  | -----  | -----  |
| Income before income taxes.....                   | 2.1%   | 1.6%   | 1.6%   |
| Income tax expense.....                           | 0.8%   | 0.6%   | 0.6%   |
|   | -----  | -----  | -----  |
| Net income.....                                   | 1.3%   | 1.0%   | 1.0%   |
|   | =====  | =====  | =====  |
| <br>  |        |        |        |
| Number of stores open at end of period.....       | 78     | 70     | 68     |

Three Months Ended September 30, 2003 Compared to Three Months Ended September 30, 2002

Net Sales. Net sales increased \$8.9 million, or 9.9%, to \$98.6 million in the three months ended September 30, 2003 from \$89.7 million in the comparable 2002 period. This increase is comprised of (i) net sales of \$5.2 million from seven new stores opened in 2003, (ii) net sales of \$2.1 million from stores opened in 2002 not included in the comparable store base, and (iii) a comparable store sales increase of \$1.6 million, or 2%. Stores are added to the comparable store base at the beginning of the fourteenth full month of operation.

9

Gross Margin. Gross margin is net sales minus the cost of merchandise and certain distribution and purchasing costs. The gross margin was 37.1% of net sales in both the three month periods ended September 30, 2003 and September 30, 2002.

Selling, General, and Administrative Expenses. Selling, general and administrative expenses include (a) direct store level expenses, including rent and related operating costs, payroll, advertising, depreciation and other direct costs, and (b) corporate level costs not directly associated with or allocable to cost of sales including executive salaries, accounting and finance, corporate information systems, office facilities and other corporate expenses. Selling, general and administrative expenses increased \$2.7 million, or 8.5%, in the three months ended September 30, 2003 to \$33.8 million from \$31.2 million in the three months ended September 30, 2002. The increase is principally accountable from stores opened in 2003 which were not open during 2002 and the stores opened in 2002 not in the comparable store base. As a percentage of sales, selling, general and administrative costs decreased to 34.3% of net sales in the three months ended September 30, 2003 from 34.8% of net sales in the three months ended September 30, 2002. This decrease is primarily due to leveraging store and central costs from the increase in sales in our comparable store base.

Store Pre-Opening Expenses. We expense store pre-opening expenses as

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incurred. Pre-opening expenses for the four new stores which opened in the third quarter of 2003 and the store which we relocated in August, amounted to \$821,000. In the third quarter of 2002, we incurred store pre-opening expenses of \$850,000 related to the six stores opened in that quarter.

Net Interest (Income). In the third quarter of 2003, we had net interest income of \$92,000 compared with net interest income of \$150,000 in 2002. The change is due to lower interest rates earned on proceeds from the proceeds of our sale of shares in March 2002.

Income Taxes. Our effective income tax rate was 38.2% for the third quarter ended September 30, 2003 and 39.8% for the third quarter ended September 30, 2002. The decrease in the effective tax rate is principally the result of tax free interest income in 2003.

Nine Months Ended September 30, 2003 Compared to Nine Months Ended September 30, 2002

Net Sales. Net sales increased \$25.8 million, or 10.0%, to \$284.2 million in the nine months ended September 30, 2003 from \$258.4 million in the comparable 2002 period. This increase is comprised of (i) net sales of \$7.5 million from seven new stores opened in 2003, (ii) net sales of \$15.3 million from stores opened in 2002 not included in the comparable store base, and (iii) a comparable store sales increase of \$3.0 million, or 1%. Sales were significantly impacted by severe weather conditions throughout our trading area in the first quarter.

Gross Margin. The gross margin decreased to 36.9% of net sales in the nine months ended September 30, 2003 from 37.0% in the nine months ended September 30, 2002. The decrease occurred during the first quarter due to more aggressive promotions in response to the difficult sales environment and to a change in sales mix resulting from the weather and a later Easter.

Selling, General, and Administrative Expenses. Selling, general and administrative expenses increased \$9.0 million, or 10.0%, in the nine months ended September 30, 2003 to \$99.3 million from \$90.3 million in the nine months ended September 30, 2002. The increase is principally accountable from stores opened in 2003 which were not open during 2002 and the stores opened in 2002 not in the comparable store base. As a percentage of sales, selling, general and administrative costs was 34.9% of net sales in both the nine month periods ended September 30, 2003 and September 30, 2002.

10

Store Pre-Opening Expenses. Pre-opening expenses for the seven new stores opened in the first nine months of 2003 and the stores we relocated amounted to \$1.6 million. In the first nine months of 2002, we opened 10 stores and incurred store pre-opening expenses of \$1.9 million.

Net Interest (Income). In the first nine months of 2003, we had net interest income of \$319,000 compared with net interest income of \$326,000 in 2002. The change is due to interest earned over the full nine months from the proceeds of our sale of shares in March 2002, offset by lower interest rates in 2003 compared with 2002.

Income Taxes. Our effective income tax rate was 38.2% for the nine months ended September 20, 2003 and 39.8% for the nine months ended September 30, 2002. The decrease in the effective tax rate is principally the result of tax free interest income in 2003.

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### Liquidity and Capital Resources

Our cash is used primarily for working capital to support inventory requirements and capital expenditures, pre-opening expenses and beginning inventory for new stores. In recent years, we have financed our operations and new store openings primarily with cash from operations, the net proceeds we received from our initial public offering in 1997 and with borrowing under bank financing agreements. In March 2002 we completed a secondary offering in which we sold 3,500,000 new post-split shares, with net cash proceeds of \$52,130,000.

At September 30, 2003 and December 31, 2002 our working capital was \$109.6 million and \$123.8 million, respectively. Cash used in operations was \$10.4 million for the nine months ended September 30, 2003 as a result of an increase in inventory of \$22.6 million to support the new stores and the increase of accounts payable and accrued expenses of \$7.0 million.

Net cash used in investing activities during the nine months ended September 30, 2003 was \$27.7 million. This included \$14.2 million for investments in marketable securities with a maturity of over one year and \$13.5 million for capital expenditures. In 2003, we expect to spend approximately \$31.0 million on capital expenditures, which includes approximately \$22.0 million for land, building, equipment and systems for our new distribution center, \$6.5 million for new store openings, and the remainder for remodeling existing stores, upgrading systems in existing stores, warehouse equipment, and corporate systems development. The total cost of the new distribution center is estimated to be between \$40.0 and \$42.0 million. We expect to finance \$30.0 million of this project through long-term debt.

In the year ended December 31, 2002, net cash provided by financing activities was principally the \$52.1 million proceeds from our sale of shares in March 2002.

We currently have a \$25.0 million line of credit agreement with Wachovia Bank, which expires on January 1, 2005. Borrowing under this line will bear interest at LIBOR plus 95 basis points. At September 30, 2003 there were no borrowings outstanding under this agreement.

On October 28, 2003 we signed two mortgage loans with Wachovia Bank relating to the new corporate offices and distribution center. The mortgages total \$30.0 million and are secured by land, building, and equipment. Borrowings under the mortgages are repayable at between seven and 15 years and will bear interest rates that will vary between LIBOR plus 85 basis points and LIBOR plus 135 basis points, depending on the debt service coverage ratio and the length of the mortgage payment. We have the option of fixing the interest rate at any time.

11

We believe the cash generated from operations during the year, funds received through the financing of the new distribution center and available borrowings under the credit agreement will be sufficient to finance our working capital and capital expenditure requirements for at least the next 12 months.

### Recent Accounting Pronouncements

In November 2002, the Emerging Issues Task Force reached consensus on Issue 02-16, Accounting by a Customer (including a Reseller) for Cash

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Consideration Received from a Vendor. EITF Issue 02-16 addresses the accounting for cash consideration received by a customer from a vendor (e.g., slotting fees, cooperative advertising payments, buydowns) and rebates or refunds from a vendor that is payable only if the customer completes a specified cumulative level of purchases or remains a customer for a specified time period. The EITF is effective for agreements modified or entered into after January 1, 2003. See Note 5 to the Consolidated Financial Statements for further description of the estimated impact of the adoption of EITF 02-16.

In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure an amendment of FASB Statement No. 123". SFAS 148 amends SFAS 123 to provide alternative methods of transition for an entity that voluntarily changes to the fair value based method of accounting for stock-based employee compensation. It also amends the disclosure provisions of SFAS 123 to require prominent disclosure about the effects on reported net income of an entity's accounting policy decisions with respect to stock-based employee compensation. It also amends APB Opinion No. 28, "Interim Financial Reporting", to require disclosure about those effects in interim financial information. The Company adopted the disclosure requirements of SFAS 148 for the fiscal year ended December 31, 2002 and the subsequent interim periods.

### General

On June 25, 2002, our Board of Directors approved a two-for-one stock split to shareholders of record as of the close of business on July 15, 2002. The shares were distributed on July 31, 2002.

12

### Critical Accounting Policies

Our significant accounting policies are described in Note 1 to the Consolidated Financial Statements presented in our Annual Report on Form 10-K for the year ended December 31, 2002. Management believes that the following accounting policies affect the more significant estimates used in preparing the consolidated financial statements.

#### Inventory Valuation

We value our inventories at stores at the lower of cost or market as determined using the retail inventory method. Because we do not have perpetual inventory records for inventory in our stores, we perform complete physical inventories in each of our stores at the end of each year. The actual physical count of merchandise is made principally by third party inventory counting service firms. We believe our process results in reasonable estimates of our retail inventory on hand at year end.

Inventory valuation methods also require certain management estimates and judgments. These include estimates of net realizable value on product designated for clearance or on slow moving merchandise. The accuracy of our estimates can be affected by many factors, some of which are outside of our control, including changes in economic conditions and consumer buying trends. Historically, we have not experienced significant differences in our estimates of recovery compared with actual results. We believe our process results in reasonable estimates of our inventory each quarter.

#### Co-Operative Advertising Allowances

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The costs incurred for advertising are expensed the first time the advertising takes place, and are offset by re-imburements received under cooperative advertising programs with certain vendors. Co-op advertising funds are only recognized when we have performed our contractual obligation under a co-op advertising agreement.

Under the guidance set forth in Emerging Issues Task Force (EITF) 02-16 "Accounting by a Customer (Including a Reseller) for Certain Consideration Received From a Vendor," cooperative advertising allowances should be treated as a reduction of inventory cost unless they represent a reimbursement of specific, incremental and identifiable costs incurred by the customer to sell the vendor's product. Under the transition rules set forth in EITF 02-16, this treatment is required for all agreements entered into or modified after January 1, 2003.

We have historically treated cooperative advertising allowances as a reduction of advertising expense. Under EITF 02-16, cooperative advertising allowances should be treated as a reduction of inventory cost unless they represent a reimbursement of specific, incremental, identifiable costs incurred by the customer to sell the vendor's product. We do not expect this issue to have a material impact on our 2003 financial statements since substantially all of the cooperative advertising allowance agreements for 2003 were entered into prior to January 1, 2003.

We have assessed the historic volume of cooperative advertising reimbursements that have been received in order to determine which of these reimbursements would meet the specific, identifiable and incremental criteria outlined under this issue and accordingly, qualify as a direct offset to advertising expense. Based on our analysis of the impact on net income, and the administrative cost to identify and track reimbursements between those qualifying for expense offset and those requiring inventory cost reduction, beginning in 2004 we have elected to treat all cooperative advertising funds received from vendors as a reduction in the cost of inventory and recognize them as a reduction to cost of goods sold when the inventory is sold. We estimate that the prospective change in the timing of income recognition will reduce 2004 EPS by approximately \$0.12 per share.

13

The adoption of this accounting principle does not change the ultimate cash to be received under these agreements, only the timing of when it is reflected in net income. This change will have a positive effect on our cash flow.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Not Applicable.

### ITEM 4. CONTROLS AND PROCEDURES

As required by Rule 13a-15(b), A.C. Moore management, including its chief executive officer and chief financial officer, conducted an evaluation as of the end of the period covered by this report, of the effectiveness of A.C. Moore's disclosure controls and procedures as defined in Exchange Act Rule 13a-15(e). Based on that evaluation, A.C. Moore's chief executive officer and chief financial officer concluded that A.C. Moore's disclosure controls and procedures were effective in reaching a reasonable level of assurance that management is timely alerted to material information relating to A.C. Moore during the period when A.C. Moore's periodic reports are being prepared. As required by Rule 13a-15(d), A.C. Moore management, including its chief executive officer and chief financial officer, also conducted an evaluation of A.C.

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Moore's internal control over financial reporting to determine whether any changes occurred during the quarter covered by this report that have materially affected, or are reasonably likely to materially affect, A.C. Moore's internal control over financial reporting. Based on that evaluation, there has been no such change during the quarter covered by this report.

14

### PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Not Applicable.

ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not Applicable.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

Not Applicable

ITEM 5. OTHER INFORMATION

None

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits.

10.1 Loan Agreement dated as of October 28, 2003, by and between Wachovia Bank, National Association and A.C. Moore Arts & Crafts, Inc., A.C. Moore Incorporated, Moorestown Finance, Inc., Blackwood Assets, Inc. and A.C. Moore Urban Renewal, LLC. A.C. Moore will furnish to the Securities and Exchange Commission a copy of any omitted exhibits or schedules upon request.

10.2 Construction Loan Agreement dated as of October 28, 2003, by and between Wachovia Bank, National Association and A.C. Moore Arts & Crafts, Inc., A.C. Moore Incorporated, Moorestown Finance, Inc., Blackwood Assets, Inc. and A.C. Moore Urban Renewal, LLC. A.C. Moore will furnish to the Securities and Exchange Commission a copy of any omitted exhibits or schedules upon request.

10.3 Mortgage, Assignment of Rents and Security Agreement and Financing Statement dated as of October 28, 2003, by and between A.C. Moore Urban Renewal, LLC and Wachovia Bank, National Association. A.C. Moore will furnish to the Securities and Exchange Commission a copy of any omitted exhibits upon request.

31.1 Certification of Chief Executive Officer pursuant to Rules 13a-14(a) and 15d-14(a) promulgated under the Securities Exchange Act of 1934, as amended ("Exchange Act").

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31.2 Certification of Chief Financial Officer pursuant to Rules 13a-14(a) and 15d-14(a) promulgated under the Exchange Act.

15

32 Certification of the Company's Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(b) Reports on Form 8-K filed or furnished in the quarter ended September 30, 2003:

8-K, Item 9, furnished on July 3, 2003 regarding a Company press release concerning earnings and other information

8-K, Item 9, furnished on July 16, 2003 regarding a Company press release concerning earnings and other information

8-K, Item 5, filed on July 28, 2003 regarding the plan of Mr. Richard Drake under Rule 10b5-1 under the Exchange Act

16

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.

A.C. MOORE ARTS & CRAFTS, INC.

Date: November 14, 2003

By: /s/ John E. Parker

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John E. Parker  
Chief Executive Officer  
(duly authorized officer  
and principal executive  
officer)

Date: November 14, 2003

By: /s/ Leslie H. Gordon

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Leslie H. Gordon  
Executive Vice President  
and Chief Financial Officer  
(duly authorized officer  
and principal financial

officer)

17

Exhibit Index

| Exhibit No.<br>----- | Description<br>-----  |
|----------------------|---|
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18