

ASBURY AUTOMOTIVE GROUP INC  
Form 10-Q  
May 09, 2007

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

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**FORM 10-Q**

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

For the quarterly period ended March 31, 2007

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: 001-31262

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**ASBURY AUTOMOTIVE GROUP, INC.**

(Exact name of Registrant as specified in its charter)

**Delaware**

(State or other jurisdiction of incorporation or organization)

**01-0609375**

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

**622 Third Avenue, 37th Floor  
New York, New York**

(Address of principal executive offices)

**10017**

(Zip Code)

**(212) 885-2500**

(Registrant's telephone number, including area code)

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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 a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act:

Large Accelerated Filer

Accelerated Filer

Non-Accelerated Filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

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Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: The number of shares of common stock outstanding as of May 4, 2007, was 32,414,542 (net of 2,836,706 treasury shares).

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ASBURY AUTOMOTIVE GROUP, INC.  
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**PART I. FINANCIAL INFORMATION**

**Item 1. Condensed Consolidated Financial Statements**

**ASBURY AUTOMOTIVE GROUP, INC.**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
**(In thousands, except share and per share data)**  
**(Unaudited)**

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|                                                                                                                                                                 | March 31,<br>2007 | December 31,<br>2006 |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------|----------------------|
| <b>ASSETS</b>                                                                                                                                                   |                   |                      |
| <b>CURRENT ASSETS:</b>                                                                                                                                          |                   |                      |
| Cash and cash equivalents                                                                                                                                       | \$ 94,497         | \$ 129,170           |
| Contracts-in-transit                                                                                                                                            | 115,720           | 126,012              |
| Accounts receivable (net of allowance of \$476 and \$648, respectively)                                                                                         | 141,312           | 167,562              |
| Inventories                                                                                                                                                     | 780,491           | 775,313              |
| Deferred income taxes                                                                                                                                           | 13,961            | 13,961               |
| Prepaid and other current assets                                                                                                                                | 69,328            | 55,099               |
| Assets held for sale                                                                                                                                            | 22,359            | 25,947               |
| Total current assets                                                                                                                                            | 1,237,668         | 1,293,064            |
| PROPERTY AND EQUIPMENT, net                                                                                                                                     | 204,782           | 202,584              |
| GOODWILL                                                                                                                                                        | 447,021           | 447,996              |
| OTHER LONG-TERM ASSETS                                                                                                                                          | 88,741            | 87,193               |
| Total assets                                                                                                                                                    | \$ 1,978,212      | \$ 2,030,837         |
| <b>LIABILITIES AND SHAREHOLDERS EQUITY</b>                                                                                                                      |                   |                      |
| <b>CURRENT LIABILITIES:</b>                                                                                                                                     |                   |                      |
| Floor plan notes payable manufacturer affiliated                                                                                                                | \$ 225,676        | \$ 319,896           |
| Floor plan notes payable non-manufacturer affiliated                                                                                                            | 445,762           | 380,881              |
| Current maturities of long-term debt                                                                                                                            | 24,841            | 23,144               |
| Accounts payable                                                                                                                                                | 67,149            | 63,951               |
| Accrued liabilities                                                                                                                                             | 86,499            | 89,296               |
| Liabilities associated with assets held for sale                                                                                                                |                   | 3,887                |
| Total current liabilities                                                                                                                                       | 849,927           | 881,055              |
| LONG-TERM DEBT                                                                                                                                                  | 477,880           | 454,010              |
| DEFERRED INCOME TAXES                                                                                                                                           | 45,702            | 53,991               |
| OTHER LONG-TERM LIABILITIES                                                                                                                                     | 35,345            | 29,948               |
| COMMITMENTS AND CONTINGENCIES (Note 11)                                                                                                                         |                   |                      |
| <b>SHAREHOLDERS EQUITY:</b>                                                                                                                                     |                   |                      |
| Preferred stock, \$.01 par value per share, 10,000,000 shares authorized                                                                                        |                   |                      |
| Common stock, \$.01 par value per share, 90,000,000 shares authorized, 35,181,154 and 35,071,401 shares issued, including shares held in treasury, respectively | 352               | 351                  |
| Additional paid-in capital                                                                                                                                      | 431,648           | 431,725              |
| Retained earnings                                                                                                                                               | 190,118           | 196,393              |
| Treasury stock, at cost; 2,836,706 and 1,536,706 shares held, respectively                                                                                      | (50,634)          | (14,559)             |
| Accumulated other comprehensive loss                                                                                                                            | (2,126)           | (2,077)              |
| Total shareholders equity                                                                                                                                       | 569,358           | 611,833              |
| Total liabilities and shareholders equity                                                                                                                       | \$ 1,978,212      | \$ 2,030,837         |

See Notes to Condensed Consolidated Financial Statements.

**ASBURY AUTOMOTIVE GROUP, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF INCOME**  
(In thousands, except per share data)  
(Unaudited)

|                                                    | <b>For the Three Months<br/>Ended March 31,</b> |                  |
|----------------------------------------------------|-------------------------------------------------|------------------|
|                                                    | <b>2007</b>                                     | <b>2006</b>      |
| <b>REVENUES:</b>                                   |                                                 |                  |
| New vehicle                                        | \$ 824,451                                      | \$ 809,657       |
| Used vehicle                                       | 378,147                                         | 352,415          |
| Parts, service and collision repair                | 174,288                                         | 168,529          |
| Finance and insurance, net                         | 38,684                                          | 35,150           |
| Total revenues                                     | 1,415,570                                       | 1,365,751        |
| <b>COST OF SALES:</b>                              |                                                 |                  |
| New vehicle                                        | 764,914                                         | 752,607          |
| Used vehicle                                       | 341,978                                         | 319,982          |
| Parts, service and collision repair                | 84,615                                          | 84,243           |
| Total cost of sales                                | 1,191,507                                       | 1,156,832        |
| <b>GROSS PROFIT</b>                                | <b>224,063</b>                                  | <b>208,919</b>   |
| <b>OPERATING EXPENSES:</b>                         |                                                 |                  |
| Selling, general and administrative                | 176,386                                         | 163,291          |
| Depreciation and amortization                      | 5,328                                           | 4,955            |
| Income from operations                             | 42,349                                          | 40,673           |
| <b>OTHER INCOME (EXPENSE):</b>                     |                                                 |                  |
| Floor plan interest expense                        | (11,216 )                                       | (8,937 )         |
| Other interest expense                             | (11,786 )                                       | (10,903 )        |
| Interest income                                    | 1,965                                           | 727              |
| Loss on extinguishment of long-term debt           | (17,737 )                                       |                  |
| Other income, net                                  | 292                                             | 344              |
| Total other expense, net                           | (38,482 )                                       | (18,769 )        |
| Income before income taxes                         | 3,867                                           | 21,904           |
| <b>INCOME TAX EXPENSE</b>                          | <b>1,458</b>                                    | <b>8,214</b>     |
| <b>INCOME FROM CONTINUING OPERATIONS</b>           | <b>2,409</b>                                    | <b>13,690</b>    |
| <b>DISCONTINUED OPERATIONS, net of tax</b>         | <b>(1,976 )</b>                                 | <b>(1,137 )</b>  |
| <b>NET INCOME</b>                                  | <b>\$ 433</b>                                   | <b>\$ 12,553</b> |
| <b>EARNINGS PER COMMON SHARE:</b>                  |                                                 |                  |
| Basic                                              |                                                 |                  |
| Continuing operations                              | \$ 0.07                                         | \$ 0.42          |
| Discontinued operations                            | (0.06 )                                         | (0.04 )          |
| Net income                                         | \$ 0.01                                         | \$ 0.38          |
| Diluted                                            |                                                 |                  |
| Continuing operations                              | \$ 0.07                                         | \$ 0.41          |
| Discontinued operations                            | (0.06 )                                         | (0.04 )          |
| Net income                                         | \$ 0.01                                         | \$ 0.37          |
| <b>WEIGHTED AVERAGE COMMON SHARES OUTSTANDING:</b> |                                                 |                  |
| Basic                                              | 33,333                                          | 32,922           |
| Diluted                                            | 34,161                                          | 33,584           |

See Notes to Condensed Consolidated Financial Statements.



**ASBURY AUTOMOTIVE GROUP, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(In thousands)**  
**(Unaudited)**



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|                                                                                             | For the Three Months<br>Ended March 31, |            |
|---------------------------------------------------------------------------------------------|-----------------------------------------|------------|
|                                                                                             | 2007                                    | 2006       |
| <b>CASH FLOW FROM OPERATING ACTIVITIES:</b>                                                 |                                         |            |
| Net income                                                                                  | \$ 433                                  | \$ 12,553  |
| Adjustments to reconcile net income to net cash (used in) provided by operating activities- |                                         |            |
| Depreciation and amortization                                                               | 5,328                                   | 4,955      |
| Depreciation and amortization from discontinued operations                                  | 27                                      | 84         |
| Stock-based compensation                                                                    | 1,895                                   | 1,369      |
| Amortization of deferred financing fees                                                     | 627                                     | 573        |
| Change in allowance for doubtful accounts                                                   | (172 )                                  | (216 )     |
| Loss (gain) on sale of discontinued operations, net                                         | 2,001                                   | (53 )      |
| Loss on extinguishment of long-term debt                                                    | 17,737                                  |            |
| Deferred income taxes                                                                       | (903 )                                  |            |
| Other adjustments                                                                           | 3,284                                   | 1,361      |
| Changes in operating assets and liabilities, net of acquisitions and divestitures-          |                                         |            |
| Contracts-in-transit                                                                        | 10,292                                  | 23,292     |
| Accounts receivable                                                                         | 20,786                                  | 9,839      |
| Proceeds from the sale of accounts receivable                                               | 5,636                                   | 4,649      |
| Inventories                                                                                 | 609                                     | (63,645 )  |
| Prepaid and other current assets                                                            | (17,397 )                               | (7,468 )   |
| Floor plan notes payable manufacturer affiliated                                            | (94,219 )                               | 98,695 )   |
| Accounts payable and accrued liabilities                                                    | 498                                     | (15,058 )  |
| Excess tax benefits from share-based payment arrangements                                   | (891 )                                  | (381 )     |
| Other long-term assets and liabilities                                                      | 69                                      | 3,137      |
| Net cash (used in) provided by operating activities                                         | (44,360 )                               | 73,686     |
| <b>CASH FLOW FROM INVESTING ACTIVITIES:</b>                                                 |                                         |            |
| Capital expenditures internally financed                                                    | (10,230 )                               | (5,534 )   |
| Capital expenditures externally financed                                                    | (2,687 )                                | (6,410 )   |
| Proceeds from the sale of assets                                                            | 8,389                                   | 9,275      |
| Other investing activities                                                                  | (1,827 )                                | (529 )     |
| Net cash used in investing activities                                                       | (6,355 )                                | (3,198 )   |
| <b>CASH FLOW FROM FINANCING ACTIVITIES:</b>                                                 |                                         |            |
| Floor plan borrowings non-manufacturer affiliated                                           | 663,002                                 | 677,249    |
| Floor plan repayments non-manufacturer affiliated                                           | (602,008 )                              | (747,686 ) |
| Proceeds from borrowings                                                                    | 265,000                                 | 902        |
| Repayments of debt                                                                          | (253,919 )                              | (1,554 )   |
| Debt issuance costs                                                                         | (7,250 )                                |            |
| Purchase of convertible note hedge                                                          | (19,309 )                               |            |
| Sale of warrants                                                                            | 8,924                                   |            |
| Purchase of treasury stock                                                                  | (36,075 )                               |            |
| Payment of dividends                                                                        | (6,708 )                                |            |
| Proceeds from the sale of assets associated with sale-leaseback agreements                  | 3,181                                   |            |
| Proceeds from the exercise of stock options, net                                            | 313                                     | 2,900      |
| Excess tax benefits from share-based payment arrangements                                   | 891                                     | 381        |
| Net cash provided by (used in) financing activities                                         | 16,042                                  | (67,808 )  |
| Net (decrease) increase in cash and cash equivalents                                        | (34,673 )                               | 2,680      |
| CASH AND CASH EQUIVALENTS, beginning of period                                              | 129,170                                 | 57,194     |
| CASH AND CASH EQUIVALENTS, end of period                                                    | \$ 94,497                               | \$ 59,874  |

See Note 10 for supplemental cash flow information.

See Notes to Condensed Consolidated Financial Statements.



**ASBURY AUTOMOTIVE GROUP, INC.**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(Unaudited)**

## 1. DESCRIPTION OF BUSINESS

Asbury Automotive Group, Inc. is a national automotive retailer, operating 112 franchises (85 dealership locations) in 21 metropolitan markets within 10 states as of March 31, 2007. We offer an extensive range of automotive products and services, including new and used vehicles, vehicle maintenance, replacement parts, collision repair services, and financing, insurance and service contracts. We offer 33 domestic and foreign brands of new vehicles, including four heavy truck brands. We also operate 23 collision repair centers that serve our markets.

Our retail network is currently organized into four regions and includes nine dealership groups, each marketed under different local brands: (i) Florida (comprising our Coggin dealerships, operating primarily in Jacksonville and Orlando, and our Courtesy dealerships operating in Tampa), (ii) West (comprising our McDavid dealerships operating throughout Texas and our California dealerships operating in Los Angeles, Sacramento and Fresno), (iii) Mid-Atlantic (comprising our Crown dealerships operating in North Carolina, South Carolina and Southern Virginia) and (iv) South (comprising our Nalley dealerships operating in Atlanta, Georgia, and our North Point dealerships operating in Little Rock, Arkansas). Our Plaza dealerships operating in St. Louis, Missouri and our Gray Daniels dealerships operating in Jackson, Mississippi remain standalone operations.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### *Basis of Presentation*

The accompanying unaudited interim condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ( GAAP ), and reflect the condensed consolidated accounts of Asbury Automotive Group, Inc. and our wholly owned subsidiaries. All intercompany transactions have been eliminated in consolidation.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts of assets and liabilities and disclosures of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the periods presented. Accordingly, actual results could differ from these estimates. Estimates and assumptions are reviewed quarterly and the effects of revisions are reflected in the condensed consolidated financial statements in the period they are determined to be necessary. Refer to Critical Accounting Estimates in Item 2 Management's Discussion and Analysis of Financial Condition and Results of Operations for more information on our critical estimates.

In the opinion of management, all adjustments (consisting only of normal, recurring adjustments) considered necessary for a fair presentation of the unaudited interim condensed consolidated financial statements as of March 31, 2007, and for the three months ended March 31, 2007 and 2006 have been included. The results of operations for the three months ended March 31, 2007 are not necessarily indicative of the results that may be expected for the full year. Our interim unaudited condensed consolidated financial statements should be read together with our consolidated financial statements and the notes thereto contained in our Annual Report on Form 10-K/A for the year ended December 31, 2006.

**In accordance with Statement of Financial Accounting Standards ( SFAS ) No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, certain amounts reflected in the accompanying Condensed Consolidated Balance Sheets as of March 31, 2007 and December 31, 2006, have been classified as Assets Held for Sale and Liabilities Associated with Assets Held for Sale. In addition, the accompanying Condensed Consolidated Statement of Income for the three months ended March 31, 2006, has been reclassified to reflect the status of our discontinued operations as of March 31, 2007.**

*Revenue Recognition*

Revenue from the sale of new and used vehicles is recognized upon delivery, passage of title, signing of the sales contract and approval of financing. Revenue from the sale of parts, service and collision repair is recognized upon delivery of parts to the customer or at the time vehicle service or repair work is completed. Manufacturer incentives and rebates, including manufacturer holdbacks, floor plan interest assistance and certain advertising assistance, are recognized as a component of new vehicle cost of sales when earned, generally at the time the related vehicles are sold.

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We receive commissions from third party lending and insurance institutions for arranging customer financing and for the sale of vehicle service contracts, credit life insurance and disability insurance to customers (collectively F&I ). We may be charged back ( chargebacks ) for F&I commissions in the event a contract is terminated. F&I commissions are recorded at the time the vehicles are sold and a reserve for future chargebacks is established based on historical operating results and the termination provisions of the applicable contracts. F&I commissions, net of estimated chargebacks, are included in Finance and insurance, net in the accompanying Consolidated Statements of Income.

### *Goodwill and Other Intangible Assets*

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Goodwill represents the excess cost of the businesses acquired over the fair market value of the identifiable net assets. We have determined that based on how we operate our business, allocate resources, and regularly review our financial data and operating results that we qualify as a single reporting unit for purposes of testing goodwill for impairment. We evaluate our operations and financial results in the aggregate by dealership. The dealership general managers are responsible for customer facing activities, including inventory management and advertising and personnel decisions; and have the flexibility to respond to local market conditions. The corporate management team, with input from the regional management teams, is responsible for infrastructure and general strategy decisions.

The fair market value of our manufacturer franchise rights is determined at the acquisition date through discounting the projected cash flows specific to each franchise. We have determined that manufacturer franchise rights have an indefinite life as there are no legal, contractual, economic or other factors that limit their useful lives and they are expected to generate cash flows indefinitely due to the historically long lives of the manufacturers' brand names. Due to the fact that manufacturer franchise rights are specific to the location in which we acquire a dealership, we have determined that the dealership is the reporting unit for purposes of testing for impairment.

In accordance with SFAS No. 142, Goodwill and Other Intangible Assets, we do not amortize goodwill and other intangible assets that are deemed to have indefinite lives. We review goodwill and indefinite lived manufacturer franchise rights for impairment annually on October 1st of each year, or more often if events or circumstances indicate that impairment may have occurred. We are subject to financial statement risk to the extent that intangible assets become impaired due to decreases in the related fair market value of our underlying businesses.

### *Derivative Instruments and Hedging Activities*

We utilize derivative financial instruments to manage our capital structure. The types of risks hedged are those relating to the variability of cash flows and changes in the fair value of our financial instruments caused by movements in interest rates. We document our risk management strategy and assess hedge effectiveness at the inception and during the term of each hedge. Derivatives are reported at fair value on the accompanying Consolidated Balance Sheets.

The changes in fair value of the effective portion of cash flow hedges are reported as a component of accumulated other comprehensive income (loss). Amounts in accumulated other comprehensive income (loss) are reclassified to interest expense to the extent the hedge becomes ineffective. The change in fair value of fair value hedges are recorded as a component of interest expense. Changes in the fair value of the associated hedged exposures are also recorded as a component of interest expense.

Measurements of hedge effectiveness are based on comparisons between the gains or losses of the actual interest rate swaps and the gains or losses of hypothetical interest rate swaps, which are designed to reflect the critical terms of the defined hedged exposures. Ineffective portions of these interest rate swaps are reported as a component of interest expense in the accompanying Consolidated Statements of Income. We recognized minor ineffectiveness during the three months ended March 31, 2007, and no ineffectiveness during the three months ended March 31, 2006.

### *Statements of Cash Flows*

Borrowings and repayments of floor plan notes payable to a party unaffiliated with the manufacturer of a particular new vehicle, and all floor plan notes payable relating to pre-owned vehicles, are classified as financing activities on the accompanying Condensed Consolidated Statements of Cash Flows with borrowings reflected separately from repayments. The net change in floor plan notes payable to a party affiliated with the manufacturer of a particular new vehicle is classified as an operating activity on the Condensed Consolidated Statements of Cash Flows.

In November 2006, General Motors sold 51% of their financing subsidiary, General Motors Acceptance Corporation ( GMAC ), to an investment consortium led by Cerberus FIM Investors, LLC. Prior to this transaction, the net change in

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floor plan notes payable to GMAC was classified as an operating activity on the accompanying Consolidated Statements of Cash Flows as borrowings and repayments of floor plan notes payable at our General Motors dealerships were with a manufacturer affiliated lender. Floor plan notes payable related to vehicles financed prior to this change in control will continue to be classified as Floorplan notes payable manufacturer affiliated on the accompanying Consolidated Balance Sheets, with subsequent repayments classified as an operating activity, since these GMAC borrowings occurred while General Motors had control of GMAC. Following the sale of GMAC, General Motors no longer has a majority ownership of or controls GMAC, and therefore, beginning in December 2006, floor plan notes payable related to vehicles financed after this change in control are classified as Floorplan notes payable non-manufacturer affiliated on the accompanying Consolidated Balance Sheets, with the related borrowings and repayments presented separately as financing activities on the accompanying Consolidated Statements of Cash Flows.

Loaner vehicle activity accounts for a significant portion of Prepaid and Other Current Assets on the accompanying Consolidated Statements of Cash Flows. We acquire loaner vehicles through borrowings with manufacturer affiliated lenders, therefore we classify the acquisition of loaner vehicles and the related borrowings as an operating activity in Prepaid and Other Current Assets in the accompanying Consolidated Statements of Cash Flows. When loaner vehicles are taken out of loaner status they are transferred to used vehicle inventory, which is reflected as a non-cash transfer in the accompanying Consolidated Statements of Cash Flows. The cash outflow to repay loaner vehicle loans are reflected in Prepaid and Other Current Assets and the cash inflow upon the sale of a loaner vehicle is reflected in Inventory on the accompanying Consolidated Statements of Cash Flows. Therefore, the net impact of loaner vehicle activity on the accompanying Consolidated Statements of Cash Flows is a cash outflow in Prepaid and Other Current Assets and a cash inflow in Inventory.

Construction reimbursements from third parties in connection with sale-leaseback agreements for the construction of new dealership facilities or leasehold improvements to our dealership facilities are included in investing activities in the accompanying Condensed Consolidated Statements of Cash Flows.

Proceeds from the sale of dealership facilities and the related real estate previously owned and subsequently leased back in connection with sale-leaseback agreements are reflected as financing activities in the accompanying Consolidated Statements of Cash Flows.

Externally financed capital expenditures include all expenditures that we have financed during the reporting period or intend to finance in future reporting periods through sale-leaseback transactions or mortgage financing. Internally financed capital expenditures include all capital expenditures which were paid using available cash and for which we do not intend to seek external financing.

Tax benefits related to share-based awards that are fully vested prior to the adoption of SFAS No. 123R are included as cash inflows from financing activities and cash outflows from operating activities on the accompanying Condensed Consolidated Statements of Cash Flows. Excess tax benefits related to share-based awards that are partially vested upon or granted after the adoption of SFAS No. 123R are included as cash inflows from financing activities and cash outflows from operating activities within the accompanying Condensed Consolidated Statements of Cash Flows.

Net proceeds from share-based payment arrangements include payments from employees upon the exercise of stock options, net of payments of employee income taxes in connection with net share settlements of share-based awards. Net share settlements of share-based awards result in (i) the issuance of shares of our common stock with a value equal to the employee's intrinsic value and (ii) the payment of the income tax on behalf of the employee in lieu of issuing additional shares of common stock.

### *Recent Accounting Pronouncements*



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In June 2006, the FASB issued FASB Interpretation ( FIN ) No. 48 Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109 . FIN 48 establishes a single model to address accounting for uncertain tax positions. FIN 48 clarifies the accounting for income taxes by prescribing a minimum recognition threshold a tax position is required to meet before being recognized as well as providing guidance on derecognition, measurement classification, interest and penalties and disclosure.

We adopted the provisions of FIN 48 effective January 1, 2007 and recognized no material adjustment in our liability for unrecognized tax benefits. As of January 1, 2007, we had \$3.6 million of total unrecognized tax benefits. Of that amount \$2.4 million, net of the federal effect, if recognized would favorably impact our effective rate in future periods. We do not expect these amounts to change materially in the next twelve months.

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In connection with the adoption of FIN 48, we analyzed our filing positions in all of the federal and state jurisdictions where we are required to file tax returns, as well as all open years in these jurisdictions. We have uncertain tax positions in certain of the states in which we do business; however, none of the states individually constitute a major tax jurisdiction, as defined. Years subject to audit range as far back as 2003. The Internal Revenue Service commenced examinations of our consolidated federal returns for the years 2004 and 2005 in the first quarter of 2007, and certain of our subsidiary returns for 2003, 2004 and 2005 in the fourth quarter 2006. In addition, we have various state audits for years 2003, 2004 and 2005, being performed as of March 31, 2007. To date, no material adjustments have been proposed and we do not anticipate that these examinations will result in a material change to our financial position or results of operations.

We recognize interest and penalties related to income tax matters in income tax expense. As of March 31, 2007, we had approximately \$0.7 million of accrued interest related to uncertain tax positions and no accrual for penalties. We do not expect the amount of accrued interest to change materially in the next twelve months.

### 3. INVENTORIES

Inventories consist of the following:

| (In thousands)        | As of<br>March 31,<br>2007 | December 31,<br>2006 |
|-----------------------|----------------------------|----------------------|
| New vehicles          | \$ 606,054                 | \$ 616,275           |
| Used vehicles         | 130,767                    | 115,927              |
| Parts and accessories | 43,670                     | 43,111               |
| Total inventories     | \$ 780,491                 | \$ 775,313           |

The lower of cost or market reserves reduced total inventory cost by \$4.9 million and \$4.8 million as of March 31, 2007 and December 31, 2006, respectively. In addition to the inventories shown above, we have \$4.8 million of inventory as of December 31, 2006, classified as Assets Held for Sale on the accompanying Condensed Consolidated Balance Sheets as it is associated with franchises held for sale. There was no inventory classified as Assets Held for Sale as of March 31, 2007.

### 4. GOODWILL AND MANUFACTURER FRANCHISE RIGHTS

During the three months ended March 31, 2007, we sold two franchises (two dealership locations) resulting in the removal of approximately \$1.0 million of Goodwill and approximately \$2.3 million of manufacturer franchise rights from our Condensed Consolidated Balance Sheets. Manufacturer franchise rights totaled \$37.2 million and \$39.5 million as of March 31, 2007 and December 31, 2006, respectively, and are included in Other Long-term Assets on the accompanying Condensed Consolidated Balance Sheets.

### 5. ASSETS AND LIABILITIES HELD FOR SALE

Assets and liabilities classified as held for sale include (i) assets and liabilities associated with discontinued operations held for sale at each balance sheet date, and (ii) costs of completed construction projects and related reimbursements during the construction period associated with pending sale-leaseback transactions.

As of December 31, 2006, assets and liabilities associated with discontinued operations included two franchises (two dealership locations) in Arkansas. During the three months ended March 31, 2007, we sold the two franchises (two dealership locations) that had been held for sale as of December 31, 2006. There were no assets or liabilities associated with discontinued operations as of March 31, 2007.

Assets associated with pending sale-leaseback transactions as of March 31, 2007, and December 31, 2006, include three and two completed construction projects, respectively, totaling \$11.3 million and \$9.7 million, respectively. As of March 31, 2007, we had not received any reimbursements associated with these sale-leaseback transactions. We expect to expect to receive final reimbursement during 2007.

Assets held for sale include real estate not currently used in our operations totaling \$11.1 million as of March 31, 2007 and December 31, 2006.



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A summary of assets and liabilities held for sale is as follows:

| (In thousands)              | As of<br>March 31,<br>2007 | December 31,<br>2006 |
|-----------------------------|----------------------------|----------------------|
| <b>Assets:</b>              |                            |                      |
| Inventories                 | \$                         | \$ 4,808             |
| Property and equipment, net | 22,359                     | 21,139               |
| Total assets                | 22,359                     | 25,947               |
| <b>Liabilities:</b>         |                            |                      |
| Floor plan notes payable    |                            | 3,887                |
| Total liabilities           |                            | 3,887                |
| Net assets held for sale    | \$ 22,359                  | \$ 22,060            |

Included in Prepaid and Other Current Assets on the accompanying Condensed Consolidated Balance Sheets are costs associated with construction projects, which we intend to sell through sale-leaseback transactions but have not been completed, and therefore are not available for sale. In connection with these construction projects, we have entered into sale-leaseback agreements whereby an unaffiliated third party purchased the land and is reimbursing us for the cost of construction of dealership facilities being constructed on the land. We capitalize the cost of the construction during the construction period and record a corresponding liability equal to the amount of the reimbursed funds. Upon completion of the construction and receipt of the final reimbursement, we remove the cost of construction and the related liability from our Condensed Consolidated Balance Sheets. The book value of assets associated with construction projects that have not been completed as of March 31, 2007 and December 31, 2006, totaled \$4.7 million and \$4.4 million, respectively. As of March 31, 2007 and December 31, 2006, there were no liabilities associated with these construction projects.

## 6. LONG-TERM DEBT

Long-term debt consists of the following:

| (In thousands)                                                                                                                                                     | As of<br>March 31,<br>2007 | December 31,<br>2006 |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------|----------------------|
| 9% Senior Subordinated Notes due 2012                                                                                                                              | \$ 11,908                  | \$ 250,000           |
| 8% Senior Subordinated Notes due 2014 (\$179.4 million and \$182.4 million face value, respectively, net of hedging activity of \$7,455 and \$7,848, respectively) | 171,975                    | 174,582              |
| 7.625% Senior Subordinated Notes due 2017                                                                                                                          | 150,000                    |                      |
| 3% Senior Subordinated Convertible Notes Due 2012                                                                                                                  | 115,000                    |                      |
| Mortgage notes payable                                                                                                                                             | 26,587                     | 26,837               |
| Notes payable collateralized by loaner vehicles                                                                                                                    | 23,000                     | 21,279               |
| Capital lease obligations                                                                                                                                          | 3,426                      | 3,552                |
| Other notes payable                                                                                                                                                | 825                        | 904                  |
|                                                                                                                                                                    | 502,721                    | 477,154              |
| Less current portion                                                                                                                                               | (24,841 )                  | (23,144 )            |
| Long-term debt                                                                                                                                                     | \$ 477,880                 | \$ 454,010           |

### Long-term Debt Refinancing

During the three months ended March 31, 2007, we initiated a refinancing of our long-term debt which included (i) a cash tender offer for all of our \$250.0 million 9% Senior Subordinated Notes due 2012 ( 9% Notes ), (ii) the issuance of \$115.0 million of 3% Senior Subordinated Convertible Notes due 2012 ( 3% Notes ), which have an initial conversion price of \$33.99 and (iii) the issuance of \$150.0 million of 7.625% Senior Subordinated Notes due 2017. As of March 31, 2007, we had completed the issuance of our 3% Notes and 7.625% Notes and repurchased \$238.1 million of our 9% Notes through our tender offer. We plan to call the remaining \$11.9 million of our 9% Notes on the first call date of June 15, 2007. Upon completion of our long-term debt refinancing, we expect our annual interest expense will decrease by approximately \$7.9 million.

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During the three months ended March 31, 2007, we recognized a \$17.7 million loss on the extinguishment of \$238.1 million of our 9% Notes and \$3.0 million of our 8% Notes. Included in the \$17.7 million loss are (i) a \$12.4 million premium on the repurchase of the 9% Notes and 8% Notes, (ii) \$5.2 million of costs associated with a pro-rata write-off of

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unamortized debt issuance costs associated with the 9% Notes and 8% Notes, and (iii) \$0.1 million of costs associated with a pro-rata write-off of the unamortized value of our terminated fair value swap associated with the 8% Notes.

In connection with the sale of our 3% Notes, we entered into convertible note hedge transactions with respect to our common stock, with Goldman, Sachs & Co. and Deutsche Bank AG, London Branch (collectively, the counterparties). The convertible note hedge transactions will cover, subject to customary anti-dilution adjustments, approximately 3.4 million shares of common stock at a strike price of \$33.99 per share of common stock, which corresponds to the initial conversion price of the 3% Notes.

We also entered into separate warrant transactions whereby we sold to the counterparties warrants to acquire, subject to customary anti-dilution adjustments, approximately 3.4 million shares of our common stock at a strike price of \$45.09 per share. On exercise of the warrants, we have the option to deliver cash or common stock equal to the difference between the then market price and strike price.

The convertible note hedge and warrant transactions are separate contracts and are not part of the terms of the 3% Notes and will not affect the holders' rights under the 3% Notes. Holders of the 3% Notes will not have any rights with respect to the convertible note hedge and warrant transactions. The convertible hedge and warrant transactions will generally have the effect of increasing the conversion price of the 3% Notes to \$45.09, which is a 62.50% premium over the market price of our common stock at the time of pricing. The convertible note hedge transactions are expected to offset the potential dilution upon conversion of the 3% Notes in the event that the market value per share of our common stock at the time of exercise is greater than the strike price of the convertible note hedge transactions.

The warrant transactions and the underlying shares of common stock issuable upon exercise of the warrants have not been registered under the Securities Act or the securities laws of any other jurisdiction and may not be offered or sold in the United States absent registration or an applicable exemption from registration requirements.

### *3% Senior Subordinated Convertible Notes due 2012*

On March 16, 2007, we issued \$115.0 million in aggregate principal amount of our 3% Notes, receiving net proceeds of \$111.4 million. The sale of the notes was exempt from registration pursuant to Rule 144A under the Securities Act of 1933. During the second quarter of 2007, we expect to file a shelf registration statement with the Securities and Exchange Commission covering the resale of the notes and the underlying common stock. The costs related to the issuance of these notes were capitalized and are being amortized to other interest expense over the term of the notes. We pay interest on these notes on March 15 and September 15 of each year until their maturity on September 15, 2012. If and when these notes are converted, we will pay cash for the principal amount of each note and, if applicable, shares of our common stock based on a daily conversion value calculated on a proportionate basis for each volume weighted average price (VWAP) trading day (as defined in the notes) and the relevant 30 VWAP trading day observation period. The initial conversion rate for the notes will be 29.4172 shares of common stock per \$1,000 principal amount of notes, which is equivalent to an initial conversion price of \$33.99 per share. The conversion rate will be subject to adjustment in some events but will not be adjusted for accrued interest.

Our 3% Notes are guaranteed by all our wholly-owned current subsidiaries and all of our future domestic subsidiaries that have outstanding, incur or guarantee any other indebtedness. The terms of our 3% Notes, in certain circumstances, restrict our ability to, among other things, sell all or substantially all of our assets.

### *7.625% Senior Subordinated Notes due 2017*

On March 26, 2007, we issued \$150.0 million of our 7.625% Notes, receiving net proceeds of \$146.3 million. The sale of the notes was exempt from registration pursuant to Rule 144A and Regulation S under the Securities Act of 1933, as amended. During the second quarter of 2007, we expect to file a registration statement with the Securities and Exchange Commission in connection with an exchange offer to exchange the notes for new notes with substantially identical terms that are registered under the Securities Act of 1933 and, therefore, will generally be freely transferable. The costs related to the issuance of these notes were capitalized and are being amortized to other interest expense over the term of the notes. We pay interest on these notes on March 15 and September 15 of each year until their maturity on March 15, 2017. At any time during the term of the 7.625% Notes we may, at our option, choose to redeem all or a portion of these notes at a price equal to 100% of their principal amount plus the applicable premium set forth in the 7.625% Notes indenture. On or before March 15, 2010, we may, at our option, use the net proceeds of one or more equity offerings to redeem up to 35% of the aggregate principal amount of these notes at a redemption price equal to 107.625% of their principal amount plus accrued and unpaid interest thereon.



Our 7.625% Notes are guaranteed by all of our wholly-owned current subsidiaries and all of our future domestic subsidiaries that have outstanding, incur or guarantee any other indebtedness. The terms of our 7.625% Notes, in certain circumstances, restrict our ability to, among other things, incur additional indebtedness, pay dividends, repurchase our common stock and merge or sell all or substantially all our assets.

## 7. DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITY

In November 2006, we entered into an interest rate swap agreement with a notional principal amount of \$150.0 million as a hedge against the changes in interest rates of our variable rate floor plan notes payable for a period of two years beginning in November 2006. The swap agreement was designated and qualifies as a cash flow hedge of future changes in interest rates of our variable rate floor plan notes payable and is not expected to contain any ineffectiveness. As of March 31, 2007, the swap agreement had a fair value of \$0.4 million, which was included in Other Long-Term Liabilities on the accompanying Condensed Consolidated Balance Sheet.

Three of our interest rate swap agreements terminated in March 2006, which resulted in a cash payment of \$13.7 million, which equaled the fair market value of the swap agreements. Included in Accumulated Other Comprehensive Loss on our Condensed Consolidated Balance Sheet as of March 31, 2007, was \$3.1 million (\$2.0 million, net of tax) of unrecognized amortization related to our two terminated cash flow swaps, which are being amortized through March 2014 as a component of Floor Plan Interest Expense on the accompanying Condensed Consolidated Statements of Income. Amortization of these terminated cash flow swaps will total \$0.9 million for the year ended December 31, 2007. In addition, included as a reduction to our 8% Notes as of March 31, 2007, was \$7.5 million of unrecognized amortization related to our terminated fair value swap, which is being amortized through March 2014 as a component of Other Interest Expense on the accompanying Condensed Consolidated Statements of Income. Amortization of this terminated fair value swap will total \$1.1 million for the year ended December 31, 2007.

We have an interest rate swap with a current notional principal amount of \$14.0 million. The swap was designed to provide a hedge against changes in interest rates of our variable rate mortgage notes payable through maturity in June 2011. This interest rate swap qualifies for cash flow hedge accounting treatment and will contain minor ineffectiveness. Under the terms of the swap agreement, we make payments based on a fixed rate of 6.08% and receive a variable rate cash flows based on one-month LIBOR. As of March 31, 2007 and December 31, 2006, the swap agreement had a fair value of \$0.3 million, which was included in Other Long-Term Assets on the accompanying Condensed Consolidated Balance Sheets.

## 8. COMPREHENSIVE INCOME

The following table provides a reconciliation of net income to comprehensive income:

| (In thousands)                                               | For the Three Months<br>Ended March 31, |           |
|--------------------------------------------------------------|-----------------------------------------|-----------|
|                                                              | 2007                                    | 2006      |
| Net income                                                   | \$ 433                                  | \$ 12,553 |
| Other comprehensive income:                                  |                                         |           |
| Change in fair value of cash flow swaps                      | (351 )                                  | 2,019     |
| Amortization of expired cash flow swaps                      | 224                                     | 80        |
| Income tax benefit (expense) associated with cash flow swaps | 78                                      | (787 )    |
| Comprehensive income                                         | \$ 384                                  | \$ 13,865 |

## 9. DISCONTINUED OPERATIONS



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During the three months ended March 31, 2007, we sold two franchises (two dealership locations). There were no franchises pending disposition as of March 31, 2007. The accompanying Condensed Consolidated Statements of Income for the three months ended March 31, 2006, have been reclassified to reflect the status of our discontinued operations as of March 31, 2007.

The following table provides further information regarding our discontinued operations as of March 31, 2007, and includes the results of businesses sold prior to March 31, 2007:

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| (Dollars in thousands)                                     | For the Three Months<br>Ended March 31, |             |
|------------------------------------------------------------|-----------------------------------------|-------------|
|                                                            | 2007                                    | 2006        |
| <b>Franchises:</b>                                         |                                         |             |
| Mid-line Domestic                                          |                                         | 6           |
| Mid-line Import                                            |                                         | 2           |
| Value                                                      | 2                                       | 3           |
| Luxury                                                     |                                         | 1           |
| <b>Total</b>                                               | <b>2</b>                                | <b>12</b>   |
| <b>Ancillary Businesses</b>                                |                                         |             |
|                                                            |                                         | 1           |
| Revenues                                                   | \$ 1,396                                | \$ 51,439   |
| Cost of sales                                              | 1,478                                   | 43,269      |
| Gross profit                                               | (82 )                                   | 8,170       |
| Operating expenses                                         | 964                                     | 9,435       |
| Loss from operations                                       | (1,046 )                                | (1,265 )    |
| Other expense, net                                         | (20 )                                   | (607 )      |
| Gain (loss) on disposition of discontinued operations, net | (2,001 )                                | 53          |
| Loss before income taxes                                   | (3,067 )                                | (1,819 )    |
| Income tax benefit                                         | 1,091                                   | 682         |
| Discontinued operations, net of tax                        | \$ (1,976 )                             | \$ (1,137 ) |

## 10. SUPPLEMENTAL CASH FLOW INFORMATION

During the three months ended March 31, 2007 and 2006, we made interest payments, net of amounts capitalized, totaling \$26.6 million and \$18.3 million, respectively. During the three months ended March 31, 2006, we received \$0.5 million of proceeds associated with our interest rate swap agreement that was entered into in December 2003 in connection with the issuance of our 8% Senior Subordinated Notes due 2014.

During the three months ended March 31, 2007 and 2006, we made income tax payments totaling \$5.2 million and \$5.5 million, respectively.

## 11. COMMITMENTS AND CONTINGENCIES

A significant portion of our vehicle business involves the sale of vehicles, parts or vehicles composed of parts that are manufactured outside the United States of America. As a result, our operations are subject to customary risks of importing merchandise, including fluctuations in the relative values of currencies, import duties, exchange controls, trade restrictions, work stoppages and general political and socio-economic conditions in foreign countries. The United States of America or the countries from which our products are imported may, from time to time, impose new quotas, duties, tariffs or other restrictions, or adjust presently prevailing quotas, duties or tariffs, which may affect our operations and our ability to purchase imported vehicles and/or parts at reasonable prices.

Manufacturers may direct us to implement costly capital improvements to dealerships as a condition upon entering into franchise agreements with them. Manufacturers also typically require that their franchises meet specific standards of appearance. These factors, either alone or in combination, could cause us to divert our financial resources to capital projects from uses that management believes may be of higher long-term value, such as acquisitions.

Substantially all of our facilities are subject to federal, state and local provisions regarding the discharge of materials into the environment. Compliance with these provisions has not had, nor do we expect such compliance to have, any material effect upon our capital expenditures, net earnings, financial condition, liquidity or competitive position. We believe that our current practices and procedures for the control and disposition of such materials comply with applicable federal, state and local requirements.



From time to time, we and our dealerships are named in claims involving the manufacture and sale or lease of motor vehicles, including but not limited to the charging of administrative fees, the operation of dealerships, contractual disputes and other matters arising in the ordinary course of our business. With respect to certain of these claims, the sellers of our acquired dealerships have indemnified us. We do not expect that any potential liability from these claims will materially affect our financial condition, liquidity, results of operations or financial statement disclosures.

Our dealerships hold dealer agreements with a number of vehicle manufacturers. In accordance with the individual dealer agreements, each dealership is subject to certain rights and restrictions typical of the industry. The ability of the manufacturers to influence the operations of the dealerships or the loss of a dealer agreement could have a negative impact on our operating results.

## 12. STOCK-BASED COMPENSATION

A summary of options outstanding and exercisable under the Plans as of March 31, 2007, and changes during the three months then ended is presented below:

|                                         | Stock Options | Weighted Average Exercise Price | Weighted Average Remaining Contractual Term | Aggregate Intrinsic Value* |
|-----------------------------------------|---------------|---------------------------------|---------------------------------------------|----------------------------|
| Options outstanding - December 31, 2006 | 1,528,179     | \$ 14.57                        |                                             |                            |
| Granted                                 |               | \$                              |                                             |                            |
| Exercised                               | (239,427)     | \$ 16.34                        |                                             |                            |
| Expired / Forfeited                     | (11,669)      | \$ 14.01                        |                                             |                            |
| Options outstanding - March 31, 2007    | 1,277,083     | \$ 14.26                        | 6.3                                         | \$ 17,866,391              |
| Options exercisable - March 31, 2007    | 1,037,949     | \$ 14.23                        | 6.1                                         | \$ 14,552,045              |

\* Based on the closing price of our common stock on March 30, 2007, which was \$28.25 per share.

Net cash received from option exercises for the three months ended March 31, 2007 was \$0.3 million. The actual intrinsic value of options exercised during the three months ended March 31, 2007 was \$2.6 million. The actual tax benefit realized for the tax deductions from option exercises totaled \$1.0 million for the three months ended March 31, 2007.

A summary of performance share units and restricted share units as of March 31, 2007, and changes during the three months ended is presented below:

|                                                      | Shares   | Weighted Average Grant Date Fair Value |
|------------------------------------------------------|----------|----------------------------------------|
| Performance Share Units - December 31, 2006          | 468,125  | \$ 20.15                               |
| Granted                                              | 199,000  | \$ 26.98                               |
| Performance estimate                                 |          | \$                                     |
| Vested                                               |          | \$                                     |
| Forfeited (including 2,188 of performance estimates) | (10,938) | \$ 20.09                               |
| Performance Share Units - March 31, 2007*            | 656,187  | \$ 22.22                               |

\* Includes an estimate of 91,437 out of a maximum of 292,600 issuable upon attaining certain performance metrics

|                                            | Shares  | Weighted Average Grant Date Fair Value |
|--------------------------------------------|---------|----------------------------------------|
| Restricted Share Units - December 31, 2006 | 29,728  | \$ 21.65                               |
| Granted                                    | 21,409  | \$ 26.98                               |
| Vested                                     |         | \$                                     |
| Forfeited                                  | (2,500) | \$ 22.98                               |
| Restricted Share Units - March 31, 2007    | 48,637  | \$ 23.93                               |

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Each performance share unit provides an opportunity for the employee to receive a number of shares of our common stock based on our performance during a three year period as measured against objective performance goals as determined by the compensation committee of our board of directors. The actual number of shares earned may range from 0% to 180% of the target number of shares depending upon achievement of the performance goals.

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**13. CONDENSED CONSOLIDATING FINANCIAL INFORMATION**

Our Committed Credit Facility is guaranteed by all of our current subsidiaries, other than our current Toyota and Lexus dealership subsidiaries, and all of our future domestic restricted subsidiaries, other than our future Toyota and Lexus dealership facilities. The following tables set forth, on a condensed consolidating basis, our balance sheets, statements of income and statements of cash flows, of our guarantor and non-guarantor subsidiaries for all financial statement periods presented in our interim condensed consolidated financial statements.

**Condensed Consolidating Balance Sheet**  
**As of March 31, 2007**  
(In thousands)

|                                                      | Parent<br>Company | Guarantor<br>Subsidiaries | Non-<br>guarantor<br>Subsidiaries | Eliminations  | Condensed<br>Consolidated |
|------------------------------------------------------|-------------------|---------------------------|-----------------------------------|---------------|---------------------------|
| <b>ASSETS</b>                                        |                   |                           |                                   |               |                           |
| Current assets:                                      |                   |                           |                                   |               |                           |
| Cash and cash equivalents                            | \$                | \$ 94,497                 | \$                                | \$            | \$ 94,497                 |
| Inventories                                          |                   | 724,200                   | 56,291                            |               | 780,491                   |
| Other current assets                                 |                   | 291,556                   | 48,765                            |               | 340,321                   |
| Assets held for sale                                 |                   | 22,359                    |                                   |               | 22,359                    |
| Total current assets                                 |                   | 1,132,612                 | 105,056                           |               | 1,237,668                 |
| Property and equipment, net                          |                   | 198,292                   | 6,490                             |               | 204,782                   |
| Goodwill                                             |                   | 393,819                   | 53,202                            |               | 447,021                   |
| Other long-term assets                               |                   | 88,467                    | 274                               |               | 88,741                    |
| Investment in subsidiaries                           | 569,358           | 93,667                    |                                   | (663,025 )    |                           |
| Total assets                                         | \$ 569,358        | \$ 1,906,857              | \$ 165,022                        | \$ (663,025 ) | \$ 1,978,212              |
| <b>LIABILITIES AND SHAREHOLDERS EQUITY</b>           |                   |                           |                                   |               |                           |
| Current liabilities:                                 |                   |                           |                                   |               |                           |
| Floor plan notes payable manufacturer affiliated     | \$                | \$ 225,676                | \$                                | \$            | \$ 225,676                |
| Floor plan notes payable non-manufacturer affiliated |                   | 399,960                   | 45,802                            |               | 445,762                   |
| Other current liabilities                            |                   | 152,976                   | 25,513                            |               | 178,489                   |
| Total current liabilities                            |                   | 778,612                   | 71,315                            |               | 849,927                   |
| Long-term debt                                       |                   | 477,841                   | 39                                |               | 477,880                   |
| Other long-term liabilities                          |                   | 81,046                    | 1                                 |               | 81,047                    |
| Shareholders equity                                  | 569,358           | 569,358                   | 93,667                            | (663,025 )    | 569,358                   |
| Total liabilities and shareholders equity            | \$ 569,358        | \$ 1,906,857              | \$ 165,022                        | \$ (663,025 ) | \$ 1,978,212              |

**Condensed Consolidating Balance Sheet**  
**As of December 31, 2006**  
(In thousands)

|                                                      | Parent<br>Company | Guarantor<br>Subsidiaries | Non-<br>guarantor<br>Subsidiaries | Eliminations  | Condensed<br>Consolidated |
|------------------------------------------------------|-------------------|---------------------------|-----------------------------------|---------------|---------------------------|
| <b>ASSETS</b>                                        |                   |                           |                                   |               |                           |
| Current assets:                                      |                   |                           |                                   |               |                           |
| Cash and cash equivalents                            | \$                | \$ 129,170                | \$                                | \$            | \$ 129,170                |
| Inventories                                          |                   | 719,350                   | 55,963                            |               | 775,313                   |
| Other current assets                                 |                   | 311,134                   | 51,500                            |               | 362,634                   |
| Assets held for sale                                 |                   | 25,947                    |                                   |               | 25,947                    |
| Total current assets                                 |                   | 1,185,601                 | 107,463                           |               | 1,293,064                 |
| Property and equipment, net                          |                   | 196,017                   | 6,567                             |               | 202,584                   |
| Goodwill                                             |                   | 394,794                   | 53,202                            |               | 447,996                   |
| Other assets                                         |                   | 86,919                    | 274                               |               | 87,193                    |
| Investment in subsidiaries                           | 611,833           | 83,198                    |                                   | (695,031 )    |                           |
| Total assets                                         | \$ 611,833        | \$ 1,946,529              | \$ 167,506                        | \$ (695,031 ) | \$ 2,030,837              |
| <b>LIABILITIES AND SHAREHOLDERS EQUITY</b>           |                   |                           |                                   |               |                           |
| Current Liabilities:                                 |                   |                           |                                   |               |                           |
| Floor plan notes payable manufacturer affiliated     | \$                | \$ 319,896                | \$                                | \$            | \$ 319,896                |
| Floor plan notes payable non-manufacturer affiliated |                   | 330,026                   | 50,855                            |               | 380,881                   |
| Other current liabilities                            |                   | 142,983                   | 33,408                            |               | 176,391                   |
| Liabilities associated with assets held for sale     |                   | 3,887                     |                                   |               | 3,887                     |
| Total current liabilities                            |                   | 796,792                   | 84,263                            |               | 881,055                   |
| Long-term debt                                       |                   | 453,966                   | 44                                |               | 454,010                   |
| Other liabilities                                    |                   | 83,938                    | 1                                 |               | 83,939                    |
| Shareholders equity                                  | 611,833           | 611,833                   | 83,198                            | (695,031 )    | 611,833                   |
| Total liabilities and shareholders equity            | \$ 611,833        | \$ 1,946,529              | \$ 167,506                        | \$ (695,031 ) | \$ 2,030,837              |

**Condensed Consolidating Statement of Income**  
**For the Three Months Ended March 31, 2007**  
(In thousands)

|                                     | Parent<br>Company | Guarantor<br>Subsidiaries | Non-<br>guarantor<br>Subsidiaries | Eliminations | Condensed<br>Consolidated |
|-------------------------------------|-------------------|---------------------------|-----------------------------------|--------------|---------------------------|
| Revenues                            | \$                | \$ 1,246,436              | \$ 173,084                        | \$ (3,950 )  | \$ 1,415,570              |
| Cost of sales                       |                   | 1,050,645                 | 144,812                           | (3,950 )     | 1,191,507                 |
| Gross profit                        |                   | 195,791                   | 28,272                            |              | 224,063                   |
| Operating expenses:                 |                   |                           |                                   |              |                           |
| Selling, general and administrative |                   | 156,724                   | 19,662                            |              | 176,386                   |
| Depreciation and amortization       |                   | 4,880                     | 448                               |              | 5,328                     |
| Income from operations              |                   | 34,187                    | 8,162                             |              | 42,349                    |
| Other income (expense):             |                   |                           |                                   |              |                           |
| Floor plan interest expense         |                   | (10,470 )                 | (746 )                            |              | (11,216 )                 |
| Other interest expense              |                   | (9,886 )                  | (1,900 )                          |              | (11,786 )                 |
| Other income (expense), net         |                   | (15,727 )                 | 247                               |              | (15,480 )                 |
| Equity in earnings of subsidiaries  | 433               | 3,590                     |                                   | (4,023 )     |                           |
| Total other expense, net            | 433               | (32,493 )                 | (2,399 )                          | (4,023 )     | (38,482 )                 |
| Income before income taxes          | 433               | 1,694                     | 5,763                             | (4,023 )     | 3,867                     |
| Income tax (benefit) expense        |                   | (715 )                    | 2,173                             |              | 1,458                     |
| Income from continuing operations   | 433               | 2,409                     | 3,590                             | (4,023 )     | 2,409                     |
| Discontinued operations, net of tax |                   | (1,976 )                  |                                   |              | (1,976 )                  |
| Net income                          | \$ 433            | \$ 433                    | \$ 3,590                          | \$ (4,023 )  | \$ 433                    |



**Condensed Consolidating Statement of Income**  
**For the Three Months Ended March 31, 2006**  
(In thousands)

|                                     | Parent<br>Company | Guarantor<br>Subsidiaries | Non-<br>guarantor<br>Subsidiaries | Eliminations | Condensed<br>Consolidated |
|-------------------------------------|-------------------|---------------------------|-----------------------------------|--------------|---------------------------|
| Revenues                            | \$                | \$ 1,207,724              | \$ 159,840                        | \$ (1,813 )  | \$ 1,365,751              |
| Cost of sales                       |                   | 1,022,814                 | 135,831                           | (1,813 )     | 1,156,832                 |
| Gross profit                        |                   | 184,910                   | 24,009                            |              | 208,919                   |
| Operating expenses:                 |                   |                           |                                   |              |                           |
| Selling, general and administrative |                   | 145,623                   | 17,668                            |              | 163,291                   |
| Depreciation and amortization       |                   | 4,513                     | 442                               |              | 4,955                     |
| Income from operations              |                   | 34,774                    | 5,899                             |              | 40,673                    |
| Other income (expense):             |                   |                           |                                   |              |                           |
| Floor plan interest expense         |                   | (8,282 )                  | (655 )                            |              | (8,937 )                  |
| Other interest expense              |                   | (9,429 )                  | (1,474 )                          |              | (10,903 )                 |
| Other income, net                   |                   | 986                       | 85                                |              | 1,071                     |
| Equity in earnings of subsidiaries  | 12,553            | 2,409                     |                                   | (14,962 )    |                           |
| Total other expense, net            | 12,553            | (14,316 )                 | (2,044 )                          | (14,962 )    | (18,769 )                 |
| Income before income taxes          | 12,553            | 20,458                    | 3,855                             | (14,962 )    | 21,904                    |
| Income tax expense                  |                   | 6,768                     | 1,446                             |              | 8,214                     |
| Income from continuing operations   | 12,553            | 13,690                    | 2,409                             | (14,962 )    | 13,690                    |
| Discontinued operations, net of tax |                   | (1,137 )                  |                                   |              | (1,137 )                  |
| Net income                          | \$ 12,553         | \$ 12,553                 | \$ 2,409                          | \$ (14,962 ) | \$ 12,553                 |

**Condensed Consolidating Statement of Cash Flows**  
**For the Three Months Ended March 31, 2007**  
(In thousands)

|                                                     | Parent<br>Company | Guarantor<br>Subsidiaries | Non-<br>guarantor<br>Subsidiaries | Eliminations | Condensed<br>Consolidated |
|-----------------------------------------------------|-------------------|---------------------------|-----------------------------------|--------------|---------------------------|
| Net cash (used in) provided by operating activities | \$                | \$ (76,477 )              | \$ 32,117                         | \$           | \$ (44,360 )              |
| Cash flow from investing activities:                |                   |                           |                                   |              |                           |
| Capital expenditures                                |                   | (12,537 )                 | (380 )                            |              | (12,917 )                 |
| Other investing activities                          |                   | 6,551                     | 11                                |              | 6,562                     |
| Net cash used in investing activities               |                   | (5,986 )                  | (369 )                            |              | (6,355 )                  |
| Cash flow from financing activities:                |                   |                           |                                   |              |                           |
| Floor Plan Borrowings non-manufacturer affiliated   |                   | 553,361                   | 109,641                           |              | 663,002                   |
| Floor Plan Repayments non-manufacturer affiliated   |                   | (487,313 )                | (114,695 )                        |              | (602,008 )                |
| Payment of dividends                                |                   | (6,708 )                  |                                   |              | (6,708 )                  |
| Proceeds from borrowings                            |                   | 265,000                   |                                   |              | 265,000                   |
| Payments of debt issuance costs                     |                   | (7,250 )                  |                                   |              | (7,250 )                  |
| Sale-leaseback agreements                           |                   | 3,181                     |                                   |              | 3,181                     |
| Repayments of debt                                  |                   | (253,914 )                | (5 )                              |              | (253,919 )                |
| Intercompany financing, net                         |                   | 26,689                    | (26,689 )                         |              |                           |
| Other financing activities                          |                   | (45,256 )                 |                                   |              | (45,256 )                 |
| Net cash provided by (used in) financing activities |                   | 47,790                    | (31,748 )                         |              | 16,042                    |
| Net decrease in cash and cash equivalents           |                   | (34,673 )                 |                                   |              | (34,673 )                 |
| Cash and cash equivalents, beginning of period      |                   | 129,170                   |                                   |              | 129,170                   |
| Cash and cash equivalents, end of period            | \$                | \$ 94,497                 | \$                                | \$           | \$ 94,497                 |

**Condensed Consolidating Statement of Cash Flows**  
**For the Three Months Ended March 31, 2006**  
(In thousands)

|                                                      | Parent<br>Company | Guarantor<br>Subsidiaries | Non-<br>guarantor<br>Subsidiaries | Eliminations | Condensed<br>Consolidated |
|------------------------------------------------------|-------------------|---------------------------|-----------------------------------|--------------|---------------------------|
| Net cash provided by operating activities            | \$                | \$ 71,459                 | \$ 2,227                          | \$           | \$ 73,686                 |
| Cash flow from investing activities:                 |                   |                           |                                   |              |                           |
| Capital expenditures                                 |                   | (11,285                   | ) (659                            | )            | (11,944                   |
| Other investing activities                           |                   | 8,746                     |                                   |              | 8,746                     |
| Net cash used in investing activities                |                   | (2,539                    | ) (659                            | )            | (3,198                    |
| Cash flow from financing activities:                 |                   |                           |                                   |              |                           |
| Floor Plan Borrowings non-manufacturer<br>Affiliated |                   | 575,672                   | 101,577                           |              | 677,249                   |
| Floor Plan Repayments non-manufacturer<br>affiliated |                   | (643,929                  | ) (103,757                        | )            | (747,686                  |
| Proceeds from borrowings                             |                   | 902                       |                                   |              | 902                       |
| Repayments of debt                                   |                   | (1,547                    | ) (7                              | )            | (1,554                    |
| Intercompany financing                               |                   | (619                      | ) 619                             |              |                           |
| Other financing activities                           |                   | 3,281                     |                                   |              | 3,281                     |
| Net cash used in financing activities                |                   | (66,240                   | ) (1,568                          | )            | (67,808                   |
| Net increase in cash and cash equivalents            |                   | 2,680                     |                                   |              | 2,680                     |
| Cash and cash equivalents, beginning of period       |                   | 57,194                    |                                   |              | 57,194                    |
| Cash and cash equivalents, end of period             | \$                | \$ 59,874                 | \$                                | \$           | \$ 59,874                 |

**14. SUBSEQUENT EVENTS**

During the second quarter of 2007, we completed the acquisition of three franchises (three dealership locations) representing annual revenues of approximately \$144.0 million for approximately \$29.0 million (including \$10.7 million borrowed from our floor plan facility for the purchase of inventory).

On May 4, 2007, our board of directors declared a \$0.20 per share cash dividend. This was the fourth consecutive quarter that a \$0.20 per share dividend was paid.

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors and Shareholders of Asbury Automotive Group, Inc.:

We have reviewed the accompanying condensed consolidated balance sheet of Asbury Automotive Group, Inc. and subsidiaries (the Company) as of March 31, 2007, and the related condensed consolidated statements of income and cash flow for the three-month periods ended March 31, 2007 and 2006. These interim financial statements are the responsibility of the Company'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 the 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 consolidated 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 standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of the Company as of December 31, 2006, and the related consolidated statements of income, shareholders' equity, and cash flows for the year then ended (not presented herein); and in our report dated March 15, 2007, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of December 31, 2006 is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ DELOITTE & TOUCHE LLP  
New York, New York  
May 8, 2007

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

We are one of the largest automotive retailers in the United States operating 112 franchises (85 dealership locations) in 21 metropolitan markets within 10 states as of March 31, 2007. We offer an extensive range of automotive products and services, including new and used vehicles, vehicle maintenance, replacement parts, collision repair services, and financing, insurance and service contracts. We offer 33 domestic and foreign brands of new vehicles, including four heavy truck brands. We also operate 23 collision repair centers that serve our markets.

We developed our dealership portfolio through the acquisition of large, locally branded dealership groups operating throughout the United States. We complemented these large dealership groups with the purchase of numerous single point dealerships and small dealership groups in our existing market areas (referred to as tuck-in acquisitions). We continue to use tuck-in acquisitions to increase the number of vehicle brands we offer in a particular market area and to create a larger gross profit base over which to spread overhead costs. Our retail network is currently organized into four regions and includes nine dealership groups: (i) Florida (comprising our Coggin dealerships, operating primarily in Jacksonville and Orlando, and our Courtesy dealerships operating in Tampa), (ii) West (comprising our McDavid dealerships operating throughout Texas and our California dealerships operating in Los Angeles, Sacramento and Fresno), (iii) Mid-Atlantic (comprising our Crown dealerships operating in North Carolina, South Carolina and Southern Virginia), and (iv) South (comprising our Nalley dealerships operating in Atlanta, Georgia and our North Point dealerships operating in Little Rock, Arkansas). Our Plaza dealerships operating in St. Louis, Missouri and our Gray Daniels dealerships operating in Jackson, Mississippi, remain standalone operations.

Our revenues are derived primarily from four offerings: (i) the sale of new vehicles to individual retail customers (new retail) and the sale of new vehicles to commercial customers (fleet) (the terms new retail and fleet being collectively referred to as new); (ii) the sale of used vehicles to individual retail customers (used retail) and the sale of used vehicles to other dealers at auction (wholesale) (the terms used retail and wholesale being collectively referred to as used); (iii) maintenance and collision repair services and the sale of automotive parts (collectively referred to as fixed operations); and (iv) the arrangement of vehicle financing and the sale of various insurance and warranty products (collectively referred to as F&I). We evaluate the results of our new and used vehicle sales based on unit volumes and gross profit per vehicle retailed (PVR), our fixed operations based on aggregate gross profit, and F&I based on dealership generated F&I PVR. We assess the organic growth of our revenue and gross profit by comparing the year-to-year results of stores that we have operated for at least twelve full months.

The organic growth of our business is dependent upon the execution of our balanced automotive retailing and service business strategy, as well as our strong brand mix, which is heavily weighted towards luxury and mid-line import brands. Sales of vehicles (particularly new vehicles) have historically fluctuated with general macroeconomic conditions, including consumer confidence, availability of consumer credit and fuel prices. We believe that any future negative trends in new vehicle sales will be mitigated by (i) the stability of our fixed operations, (ii) increased used vehicle sales, (iii) our variable cost structure and (iv) our advantageous brand mix. Historically, our brand mix has been less affected by market volatility than the U.S. automobile industry as a whole. We expect the recent industry-wide gain in market share of the luxury and mid-line import brands to continue in the near future.

Our gross profit margin varies with our revenue mix. The sale of new vehicles generally results in lower gross profit margin than used vehicle sales and fixed operations. As a result, when used vehicles and fixed operations revenue increases as a percentage of total revenue, we expect our overall gross profit margin to increase. We continue to implement new initiatives specifically designed to accelerate the growth of our high margin businesses and to leverage our selling, general and administrative (SG&A) expense structure.

SG&A expenses consist primarily of fixed and incentive-based compensation, advertising, rent, insurance, utilities and other customary operating expenses. A significant portion of our selling expenses is variable (such as sales commissions), or controllable expenses (such as advertising), generally allowing our cost structure to adapt in response to trends in our business. We evaluate commissions paid to salespeople as a percentage of retail vehicle gross profit and all other SG&A expenses in the aggregate as a percentage of total gross profit.

Our operations are generally subject to seasonal variations as we tend to generate more revenue and operating income in the second and third quarters than in the first and fourth quarters of the calendar year. Generally, the seasonal variations in our operations are caused by factors relating to weather conditions, changes in manufacturer incentive programs, model changeovers and consumer buying patterns, among other things. Over the past several years, certain automobile manufacturers have used a combination of vehicle pricing and financing incentive programs to generate increased customer demand for new vehicles. We anticipate that the manufacturers will continue to use these incentive programs to drive demand for their product offerings.

**RESULTS OF OPERATIONS**

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Three Months Ended March 31, 2007, Compared to the Three Months Ended March 31, 2006

|                                                             | For the Three Months Ended<br>March 31, |                         |                  |                         |                        |  |             |          |
|-------------------------------------------------------------|-----------------------------------------|-------------------------|------------------|-------------------------|------------------------|--|-------------|----------|
|                                                             | 2007                                    | % of<br>Gross<br>Profit | 2006             | % of<br>Gross<br>Profit | Increase<br>(Decrease) |  | % Change    |          |
|                                                             | (In thousands)                          |                         |                  |                         |                        |  |             |          |
| <b>REVENUES:</b>                                            |                                         |                         |                  |                         |                        |  |             |          |
| New vehicle                                                 | \$ 824,451                              |                         | \$ 809,657       |                         | \$ 14,794              |  | 2           | %        |
| Used vehicle                                                | 378,147                                 |                         | 352,415          |                         | 25,732                 |  | 7           | %        |
| Parts, service and collision repair                         | 174,288                                 |                         | 168,529          |                         | 5,759                  |  | 3           | %        |
| Finance and insurance, net                                  | 38,684                                  |                         | 35,150           |                         | 3,534                  |  | 10          | %        |
| Total revenues                                              | 1,415,570                               |                         | 1,365,751        |                         | 49,819                 |  | 4           | %        |
| <b>COST OF SALES</b>                                        | <b>1,191,507</b>                        |                         | <b>1,156,832</b> |                         | <b>34,675</b>          |  | <b>3</b>    | <b>%</b> |
| <b>GROSS PROFIT</b>                                         | <b>224,063</b>                          | <b>100 %</b>            | <b>208,919</b>   | <b>100 %</b>            | <b>15,144</b>          |  | <b>7</b>    | <b>%</b> |
| <b>OPERATING EXPENSES:</b>                                  |                                         |                         |                  |                         |                        |  |             |          |
| Selling, general and administrative                         | 176,386                                 | 79 %                    | 163,291          | 79 %                    | 13,095                 |  | 8           | %        |
| Depreciation and amortization                               | 5,328                                   | 2 %                     | 4,955            | 2 %                     | 373                    |  | 8           | %        |
| Income from operations                                      | 42,349                                  | 19 %                    | 40,673           | 19 %                    | 1,676                  |  | 4           | %        |
| <b>OTHER INCOME (EXPENSE):</b>                              |                                         |                         |                  |                         |                        |  |             |          |
| Floor plan interest expense                                 | (11,216 )                               | (5 )%                   | (8,937 )         | (4 )%                   | 2,279                  |  | 26          | %        |
| Other interest expense                                      | (11,786 )                               | (5 )%                   | (10,903 )        | (5 )%                   | 883                    |  | 8           | %        |
| Interest income                                             | 1,965                                   | 1 %                     | 727              |                         | 1,238                  |  | 170         | %        |
| Loss on extinguishment of long-term debt                    | (17,737 )                               | (8 )%                   |                  |                         | 17,737                 |  | NM          |          |
| Other income, net                                           | 292                                     |                         | 344              |                         | (52 )                  |  | (15)        | %        |
| Total other expense, net                                    | (38,482 )                               | (17 )%                  | (18,769 )        | (9 )%                   | 19,713                 |  | 105         | %        |
| Income before income taxes                                  | 3,867                                   | 2 %                     | 21,904           | 10 %                    | (18,037 )              |  | (82)        | %        |
| <b>INCOME TAX EXPENSE</b>                                   | <b>1,458</b>                            | <b>1 %</b>              | <b>8,214</b>     | <b>3 %</b>              | <b>(6,756 )</b>        |  | <b>(82)</b> | <b>%</b> |
| <b>INCOME FROM CONTINUING OPERATIONS</b>                    |                                         |                         |                  |                         |                        |  |             |          |
|                                                             | 2,409                                   | 1 %                     | 13,690           | 7 %                     | (11,281 )              |  | (82)        | %        |
| <b>DISCONTINUED OPERATIONS, net of tax</b>                  |                                         |                         |                  |                         |                        |  |             |          |
|                                                             | (1,976 )                                | (1 )%                   | (1,137 )         | (1 )%                   | (839 )                 |  | (74)        | %        |
| <b>NET INCOME</b>                                           | <b>\$ 433</b>                           | <b>%</b>                | <b>\$ 12,553</b> | <b>6 %</b>              | <b>\$ (12,120 )</b>    |  | <b>(97)</b> | <b>%</b> |
| Income from continuing operations per common share- Diluted |                                         |                         |                  |                         |                        |  |             |          |
|                                                             | \$ 0.07                                 |                         | \$ 0.41          |                         | \$ (0.34 )             |  | (83)        | %        |
| Net income per common share- Diluted                        |                                         |                         |                  |                         |                        |  |             |          |
|                                                             | \$ 0.01                                 |                         | \$ 0.37          |                         | \$ (0.36 )             |  | (97)        | %        |

Net income was \$0.4 million, or \$0.01 per diluted share, for the three months ended March 31, 2007, as compared to \$12.6 million, or \$0.37 per diluted share for the three months ended March 31, 2006. Net income for the three months ended March 31, 2007 includes \$11.1 million (net of tax) of costs associated with the refinancing of our long-term debt and \$1.8 million of costs associated with the retirement of our current CEO, Kenneth B. Gilman.

Income from continuing operations was \$2.4 million, or \$0.07 per diluted share, for the three months ended March 31, 2007, as compared to \$13.7 million, or \$0.41 per diluted share, for the three months ended March 31, 2006. Excluding the long-term debt refinancing and retirement of our current CEO mentioned above, adjusted income from continuing operations increased \$1.6 million (12%) to \$15.3 million for the three months ended March 31, 2007 from \$13.7 million for the three months ended March 31, 2006. We believe that excluding these items provides a more accurate representation of our year over year financial performance.

The 12% increase in adjusted income from continuing operations resulted from a balanced performance across all four of our business lines and continued improvement in the SG&A expense as a percent of gross profit. Our results during the three months ended March 31, 2007 include (i) a \$5.4 million (6%) increase in fixed operations gross profit and a \$3.7 million (12%) increase in used vehicle gross profit as a result of our continued focus on our high margin businesses; (ii) \$3.5 million (10%) increase in finance and insurance gross profit driven by improved dealership generated F&I PVR, partially





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resulting from our re-negotiated contract with our primary service contract provider, (iii) a \$2.5 million (4%) increase in new vehicle gross profit as a result of increased demand for certain new luxury vehicles and improved gross profit margin on mid-line import vehicles as we capitalized on manufacturer incentive programs, and (iv) an 80 basis point improvement in adjusted SG&A expenses (excluding the retirement benefits discussed above) as a percentage of gross profit, as we continue to leverage our fixed overhead and organizational structure. These factors were partially offset by a 26% increase in floor plan interest expense principally resulting from a 65 basis point increase in short-term interest rates and higher inventories of heavy trucks.

Total revenues increased \$49.8 million (4%) to \$1.4 billion for the three months ended March 31, 2007. The increase in total revenues was a result of a \$25.7 million (7%) increase in used vehicle revenue and a \$14.8 million (2%), increase in new vehicle revenue.

Total gross profit increased \$15.2 million (7%), to \$224.1 million for the three months ended March 31, 2007, from \$208.9 million for the three months ended March 31, 2006. The increase in total gross profit was a result of strong performances across all of our business lines, in particular our higher margin fixed operations and F&I businesses, which contributed to a 50 basis point increase in our total gross profit margin.

| New Vehicle                                        | For the Three Months Ended                   |       |            |       |           |       | Increase<br>(Decrease) | %<br>Change |
|----------------------------------------------------|----------------------------------------------|-------|------------|-------|-----------|-------|------------------------|-------------|
|                                                    | March 31,<br>2007                            |       | 2006       |       |           |       |                        |             |
|                                                    | (In thousands, except for unit and PVR data) |       |            |       |           |       |                        |             |
| <b>Revenue:</b>                                    |                                              |       |            |       |           |       |                        |             |
| New retail revenue same store(1)                   |                                              |       |            |       |           |       |                        |             |
| Luxury                                             | \$ 264,958                                   | 34 %  | \$ 248,221 | 33 %  | \$ 16,737 | 7 %   |                        |             |
| Mid-line import                                    | 320,005                                      | 42 %  | 317,170    | 42 %  | 2,835     | 1 %   |                        |             |
| Mid-line domestic                                  | 118,026                                      | 15 %  | 122,029    | 16 %  | (4,003)   | (3) % |                        |             |
| Value                                              | 10,594                                       | 1 %   | 10,252     | 1 %   | 342       | 3 %   |                        |             |
| Total passenger vehicle retail revenue- same store | 713,583                                      |       | 697,672    |       | 15,911    | 2 %   |                        |             |
| Heavy trucks                                       | 58,730                                       | 8 %   | 63,135     | 8 %   | (4,405)   | (7) % |                        |             |
| Total new retail revenue same store(1)             | 772,313                                      | 100 % | 760,807    | 100 % | 11,506    | 2 %   |                        |             |
| New retail revenue acquisitions                    | 1,167                                        |       |            |       |           |       |                        |             |
| Total new retail revenues                          | 773,480                                      |       | 760,807    |       | 12,673    | 2 %   |                        |             |
| Fleet revenue same store(1)                        | 50,971                                       |       | 48,850     |       | 2,121     | 4 %   |                        |             |
| Fleet revenue acquisitions                         |                                              |       |            |       |           |       |                        |             |
| Total fleet revenue                                | 50,971                                       |       | 48,850     |       | 2,121     | 4 %   |                        |             |
| New vehicle revenue, as reported                   | \$ 824,451                                   |       | \$ 809,657 |       | \$ 14,794 | 2 %   |                        |             |
| <b>New retail units:</b>                           |                                              |       |            |       |           |       |                        |             |
| New retail units same store(1)                     |                                              |       |            |       |           |       |                        |             |
| Luxury                                             | 5,519                                        | 23 %  | 5,507      | 23 %  | 12        |       |                        |             |
| Mid-line import                                    | 13,083                                       | 54 %  | 12,764     | 53 %  | 319       | 2 %   |                        |             |
| Mid-line domestic                                  | 4,101                                        | 17 %  | 4,294      | 18 %  | (193)     | (4) % |                        |             |
| Value                                              | 517                                          | 2 %   | 482        | 2 %   | 35        | 7 %   |                        |             |
| Total passenger vehicle retail units- same store   | 23,220                                       |       | 23,047     |       | 173       | 1 %   |                        |             |
| Heavy trucks                                       | 1,017                                        | 4 %   | 1,076      | 4 %   | (59)      | (5) % |                        |             |
| Total new retail units same store(1)               | 24,237                                       | 100 % | 24,123     | 100 % | 114       |       |                        |             |
| New retail units acquisitions                      | 55                                           |       |            |       |           |       |                        |             |
| Retail units actual                                | 24,292                                       |       | 24,123     |       | 169       | 1 %   |                        |             |
| <b>New revenue PVR</b>                             |                                              |       |            |       |           |       |                        |             |
| New revenue PVR same store(1)                      | \$ 31,865                                    |       | \$ 31,539  |       | \$ 326    | 1 %   |                        |             |
| New revenue PVR actual                             | \$ 31,841                                    |       | \$ 31,539  |       | \$ 302    | 1 %   |                        |             |

(1) Same store amounts include the results of dealerships for the identical months for each period presented in the comparison, commencing with the first full month in which the dealership was owned by us.



|                                                         | For the Three Months Ended<br>March 31,<br>2007<br>(In thousands, except for unit and PVR data) |        |     |   |    |        | 2006 |   | Increase<br>(Decrease) | %<br>Change |      |   |   |
|---------------------------------------------------------|-------------------------------------------------------------------------------------------------|--------|-----|---|----|--------|------|---|------------------------|-------------|------|---|---|
| <b>Gross Profit:</b>                                    |                                                                                                 |        |     |   |    |        |      |   |                        |             |      |   |   |
| New retail gross profit same store(1)                   |                                                                                                 |        |     |   |    |        |      |   |                        |             |      |   |   |
| Luxury                                                  | \$                                                                                              | 21,565 | 37  | % | \$ | 19,790 | 35   | % | \$                     | 1,775       | 9    | % |   |
| Mid-line import                                         |                                                                                                 | 24,060 | 41  | % |    | 22,846 | 41   | % |                        | 1,214       | 5    | % |   |
| Mid-line domestic                                       |                                                                                                 | 8,794  | 15  | % |    | 9,905  | 18   | % |                        | (1,111)     | (11) | % |   |
| Value                                                   |                                                                                                 | 738    | 1   | % |    | 928    | 2    | % |                        | (190)       | (20) | % |   |
| Total passenger vehicle retail gross profit- same store |                                                                                                 | 55,157 |     |   |    | 53,469 |      |   |                        | 1,688       | 3    | % |   |
| Heavy trucks                                            |                                                                                                 | 3,252  | 6   | % |    | 2,760  | 4    | % |                        | 492         | 18   | % |   |
| Total new retail gross profit same store(1)             |                                                                                                 | 58,409 | 100 | % |    | 56,229 | 100  | % |                        | 2,180       | 4    | % |   |
| New retail gross profit acquisitions                    |                                                                                                 | 63     |     |   |    |        |      |   |                        |             |      |   |   |
| Total retail gross profit                               |                                                                                                 | 58,472 |     |   |    | 56,229 |      |   |                        | 2,243       | 4    | % |   |
| Fleet gross profit same store(1)                        |                                                                                                 | 1,065  |     |   |    | 821    |      |   |                        | 244         | 30   | % |   |
| Fleet gross profit acquisitions                         |                                                                                                 |        |     |   |    |        |      |   |                        |             |      |   |   |
| Total fleet gross profit                                |                                                                                                 | 1,065  |     |   |    | 821    |      |   |                        | 244         | 30   | % |   |
| New vehicle gross profit, as reported                   | \$                                                                                              | 59,537 |     |   | \$ | 57,050 |      |   | \$                     | 2,487       | 4    | % |   |
| New gross profit PVR same store(1)                      | \$                                                                                              | 2,410  |     |   | \$ | 2,331  |      |   | \$                     | 79          | 3    | % |   |
| New gross profit PVR actual                             | \$                                                                                              | 2,407  |     |   | \$ | 2,331  |      |   | \$                     | 76          | 3    | % |   |
| New retail gross margin same store(1)                   |                                                                                                 | 7.6    | %   |   |    | 7.4    | %    |   |                        | 0.2         | %    | 3 | % |
| New retail gross margin actual                          |                                                                                                 | 7.6    | %   |   |    | 7.4    | %    |   |                        | 0.2         | %    | 3 | % |

(1) Same store amounts include the results of dealerships for the identical months for each period presented in the comparison, commencing with the first full month in which the dealership was owned by us.

New vehicle revenues increased \$14.8 million (2%) to \$0.8 billion for the three months ended March 31, 2007. The increase in new vehicle revenues was a result of a \$19.6 million (3%) increase in our same store new retail revenue from luxury and mid-line import brands, partially offset by a \$4.0 million (3%) decrease in mid-line domestic sales, as these brands continue to lose market share; and a \$4.4 million (7%) decrease in heavy trucks as a result of lower demand from changes in emission laws effective January 2007. Same store new vehicle retail revenues excluding heavy trucks (passenger vehicle) increased \$15.9 million (2%) for the three months ended March 31, 2007, compared with the three months ended March 31, 2006. Our same store passenger vehicle retail unit sales increased 1% despite a 1% decrease in the overall U.S. passenger retail vehicle industry. We continue to benefit from our strong brand mix, heavily weighted toward luxury and mid-line import brands that continue to increase their market share.

New vehicle gross profit increased \$2.4 million (4%) to \$59.5 million for the three months ended March 31, 2007, from \$57.1 million for the three months ended March 31, 2006. New retail gross profit increased \$2.2 million (4%) driven by a \$3.0 million (7%) increase in luxury and mid-line import same store retail gross profit as a result of (i) increased demand for certain new luxury vehicles, (ii) the continued increase in mid-line import market share and (iii) our ability to capitalize on manufacturer incentive programs from mid-line import brands. These increases in same store retail gross profit were partially offset by the performance of our mid-line domestic and value brands, which were down 11% and 20%, respectively, with the majority of the decrease resulting from the continued loss of market share for the domestic brands.

We expect our passenger vehicle unit sales, revenue and gross profit to outperform the U.S. passenger retail unit sales environment as we believe the luxury and mid-line import brands will continue to increase market share. However, we expect heavy trucks unit sales, revenue and gross profit to decrease significantly in 2007 as the new emission laws have significantly increased the price of heavy trucks, resulting in a temporary reduction in demand for heavy trucks produced in the near future. We believe we will mitigate some of this decrease as we strategically increased our inventory of 2006 model year heavy trucks because 2006 model year heavy trucks will not be required to adhere to the new emission laws.



| Used Vehicle                           | For the Three Months Ended |            | Increase (Decrease) | % Change |    |
|----------------------------------------|----------------------------|------------|---------------------|----------|----|
|                                        | March 31, 2007             | 2006       |                     |          |    |
| <b>Revenue:</b>                        |                            |            |                     |          |    |
| Retail revenues same store(1)          | \$ 295,794                 | \$ 266,367 | \$ 29,427           | 11       | %  |
| Retail revenues acquisitions           | 722                        |            |                     |          |    |
| Total used retail revenues             | 296,516                    | 266,367    | 30,149              | 11       | %  |
| Wholesale revenues same store(1)       | 81,407                     | 86,048     | (4,641 )            | (5)      | )% |
| Wholesale revenues acquisitions        | 224                        |            |                     |          |    |
| Total wholesale revenues               | 81,631                     | 86,048     | (4,417 )            | (5)      | )% |
| Used vehicle revenue, as reported      | \$ 378,147                 | \$ 352,415 | \$ 25,732           | 7        | %  |
| <b>Gross Profit:</b>                   |                            |            |                     |          |    |
| Retail gross profit same store(1)      | \$ 35,576                  | \$ 32,033  | \$ 3,543            | 11       | %  |
| Retail gross profit acquisitions       | 77                         |            |                     |          |    |
| Total used retail gross profit         | 35,653                     | 32,033     | 3,620               | 11       | %  |
| Wholesale gross profit same store(1)   | 494                        | 400        | 94                  | 24       | %  |
| Wholesale gross profit acquisitions    | 22                         |            |                     |          |    |
| Total wholesale gross profit           | 516                        | 400        | 116                 | 29       | %  |
| Used vehicle gross profit, as reported | \$ 36,169                  | \$ 32,433  | \$ 3,736            | 12       | %  |
| Used retail units same store(1)        | 16,568                     | 15,219     | 1,349               | 9        | %  |
| Used retail units acquisitions         | 57                         |            |                     |          |    |
| Used retail units actual               | 16,625                     | 15,219     | 1,406               | 9        | %  |
| Used revenue PVR same store(1)         | \$ 17,853                  | \$ 17,502  | \$ 351              | 2        | %  |
| Used revenue PVR actual                | \$ 17,836                  | \$ 17,502  | \$ 334              | 2        | %  |
| Used gross profit PVR same store(1)    | \$ 2,147                   | \$ 2,105   | \$ 42               | 2        | %  |
| Used gross profit PVR actual           | \$ 2,145                   | \$ 2,105   | \$ 40               | 2        | %  |
| Used retail gross margin same store(1) | 12.0                       | % 12.0     | %                   | %        | %  |
| Used retail gross margin actual        | 12.0                       | % 12.0     | %                   | %        | %  |

(1) Same store amounts include the results of dealerships for the identical months for each period presented in the comparison, commencing with the first full month in which the dealership was owned by us.

Used vehicle revenues increased \$25.7 million (7%) to \$0.4 billion for the three months ended March 31, 2007. The increase in used vehicle revenues was a result of a 9% increase in used retail unit sales. Used vehicle gross profit increased \$3.8 million (12%) to \$36.2 million for the three months ended March 31, 2007, from \$32.4 million for the three months ended March 31, 2006. Used retail gross profit increased \$3.7 million (11%) to \$35.7 million as a result of a 9% increase in used retail unit sales.

The increases in our used retail units sales and used gross profit is a result of our investment in technology to better value trade-ins and improve inventory management, sharing of best practices and the execution by our regional management teams dedicated to the used vehicle business. We expect used vehicle revenues and gross profit to continue to increase in the future as we execute our current initiatives, increase our focus on sub-prime customers and increase our focus on our training initiatives.

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| Fixed Operations                                              | For the Three Months Ended |            | Increase<br>(Decrease) | %<br>Change |
|---------------------------------------------------------------|----------------------------|------------|------------------------|-------------|
|                                                               | March 31,<br>2007          | 2006       |                        |             |
| <b>Revenue:</b>                                               |                            |            |                        |             |
| Revenues same store(1)                                        |                            |            |                        |             |
| Parts and service                                             | \$ 158,231                 | \$ 152,475 | \$ 5,756               | 4 %         |
| Collision repair                                              | 15,984                     | 16,054     | (70 )                  | %           |
| Total revenue same store(1)                                   | 174,215                    | 168,529    | 5,686                  | 3 %         |
| Revenues acquisitions                                         |                            |            |                        |             |
| Parts, service and collision repair revenue, as reported      | \$ 174,288                 | \$ 168,529 | \$ 5,759               | 3 %         |
| <b>Gross Profit:</b>                                          |                            |            |                        |             |
| Gross profit same store(1)                                    |                            |            |                        |             |
| Parts and service                                             | \$ 80,885                  | \$ 75,852  | \$ 5,033               | 7 %         |
| Collision repair                                              | 8,719                      | 8,434      | 285                    | 3 %         |
| Total gross profit same store(1)                              | 89,604                     | 84,286     | 5,318                  | 6 %         |
| Gross profit acquisitions                                     |                            |            |                        |             |
| Parts, service and collision repair gross profit, as reported | \$ 89,673                  | \$ 84,286  | \$ 5,387               | 6 %         |
| Parts and service gross margin same store(1)                  | 51.1                       | % 49.7     | % 1.4                  | % 3 %       |
| Collision repair gross margin same store(1)                   | 54.5                       | % 52.5     | % 2.0                  | % 4 %       |

(1) Same store amounts include the results of dealerships for the identical months for each period presented in the comparison, commencing with the first full month in which the dealership was owned by us.

Fixed operations revenues increased \$5.8 million (3%) to \$174.3 million for the three months ended March 31, 2007, from \$168.5 million for the three months ended March 31, 2006. Fixed operations revenues increased primarily due to an 8% increase in our customer pay parts and service businesses. The growth in our customer pay business is a result of our investments in facility expansion and equipment upgrades, increased capacity utilization, and continued focus on customer retention initiatives.

Fixed operations gross profit increased \$5.4 million (6%) to \$89.7 million for the three months ended March 31, 2007, from \$84.3 million for the three months ended March 31, 2006. The increase in fixed operations gross profit is primarily a result of an 11% increase in gross profit from our customer pay parts and service businesses.

We expect our fixed operations sales to continue to grow as we (i) continue to invest in additional service capacity, (ii) upgrade equipment, (iii) expand our product offerings, (iv) capitalize on our regional training programs and (v) add service advisors and skilled technicians to meet anticipated future demand, especially from the increased market share of the mid-line import and luxury import brands.

| Finance and Insurance, net                                 | For the Three Months Ended |           | Increase<br>(Decrease) | %<br>Change |
|------------------------------------------------------------|----------------------------|-----------|------------------------|-------------|
|                                                            | March 31,<br>2007          | 2006      |                        |             |
| <b>Dealership generated F&amp;I same store(1)</b>          |                            |           |                        |             |
| Dealership generated F&I acquisitions                      | \$ 38,609                  | \$ 34,157 | \$ 4,452               | 13 %        |
| Dealership generated F&I, net                              | 75                         |           |                        |             |
| Corporate generated F&I                                    | 38,684                     | 34,157    | 4,527                  | 13 %        |
| Finance and insurance, net as reported                     |                            | 993       | (993 )                 | NM          |
| Finance and insurance, net as reported                     | \$ 38,684                  | \$ 35,150 | \$ 3,534               | 10 %        |
| <b>Dealership generated F&amp;I PVR-same store (1) (2)</b> |                            |           |                        |             |
| Dealership generated F&I PVR-actual (2)                    | \$ 946                     | \$ 868    | \$ 78                  | 9 %         |
| F&I PVR-actual                                             | \$ 945                     | \$ 893    | \$ 52                  | 6 %         |

(1) Same store amounts include the results of dealerships for the identical months for each period presented in the comparison, commencing with the first full month in which the dealership was owned by us.

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(2) Refer to Reconciliation of Non-GAAP Financial Information for further discussion regarding dealership generated F&I gross profit PVR.

F&I increased \$3.5 million (10%) to \$38.7 million for the three months ended March 31, 2007, from \$35.2 million for the three months ended March 31, 2006. Approximately \$3.0 million of the increase in F&I was a result of the \$77 (9%) increase in dealership generated F&I PVR, \$1.4 million from a 4% increase in retail units, partially offset by the \$1.0 million reduction in corporate generated F&I. The increase in dealership generated F&I PVR was a result of a renegotiated contract with our primary service contract provider in the second quarter of 2006, which contributed an incremental \$35 PVR. During the second quarter of 2006 we sold our remaining interest in a pool of extended service contracts. As a result of this sale, we no longer receive any corporate generated F&I.

Dealership generated F&I, which excludes corporate generated F&I, increased \$4.5 million (13%) to \$38.7 million for the three months ended March 31, 2007, from \$34.2 million for the three months ended March 31, 2006. The increase in dealership generated F&I was primarily a result of a 9% increase in dealership generated F&I PVR. We anticipate F&I will increase in the future as a result of (i) increased retail unit sales, (ii) the maturation of new F&I programs and (iii) improvement of the F&I operations at our under-performing franchises.

| Selling, General and Administrative          | For the Three Months Ended<br>March 31, |                         |            |                         | % of<br>Gross<br>Profit | % of<br>Gross<br>Profit<br>Increase<br>(Decrease) | % of<br>Gross<br>Profit %<br>Change |  |
|----------------------------------------------|-----------------------------------------|-------------------------|------------|-------------------------|-------------------------|---------------------------------------------------|-------------------------------------|--|
|                                              | 2007                                    | % of<br>Gross<br>Profit | 2006       | % of<br>Gross<br>Profit |                         |                                                   |                                     |  |
| Personnel costs                              | \$ 80,926                               | 36.1 %                  | \$ 77,561  | 37.1 %                  | (1.0)                   | (3)                                               | %                                   |  |
| Sales compensation                           | 25,196                                  | 11.2 %                  | 23,131     | 11.1 %                  | 0.1                     | 1                                                 | %                                   |  |
| Share-based compensation                     | 1,895                                   | 0.8 %                   | 1,369      | 0.7 %                   | 0.1                     | 14                                                | %                                   |  |
| Retirement benefits expense                  | 2,950                                   | 1.3 %                   |            |                         | 1.3                     | NM                                                | %                                   |  |
| Outside services                             | 15,196                                  | 6.8 %                   | 13,157     | 6.3 %                   | 0.5                     | 8                                                 | %                                   |  |
| Advertising                                  | 12,545                                  | 5.6 %                   | 11,562     | 5.5 %                   | 0.1                     | 2                                                 | %                                   |  |
| Rent                                         | 13,941                                  | 6.2 %                   | 12,994     | 6.2 %                   |                         |                                                   | %                                   |  |
| Utilities                                    | 4,775                                   | 2.1 %                   | 4,863      | 2.3 %                   | (0.2)                   | (9)                                               | %                                   |  |
| Insurance                                    | 3,563                                   | 1.7 %                   | 3,864      | 1.9 %                   | (0.2)                   | (11)                                              | %                                   |  |
| Other                                        | 15,399                                  | 6.9 %                   | 14,790     | 7.1 %                   | (0.2)                   | (3)                                               | %                                   |  |
| Selling, general and administrative          | \$ 176,386                              | 78.7 %                  | \$ 163,291 | 78.2 %                  | 0.5                     | 1                                                 | %                                   |  |
| <i>Adjustments to SG&amp;A:</i>              |                                         |                         |            |                         |                         |                                                   |                                     |  |
| Retirement benefits expense                  | (2,950)                                 | (1.3 %)                 |            |                         |                         |                                                   |                                     |  |
| Adjusted selling, general and administrative | \$ 173,436                              | 77.4 %                  | \$ 163,291 | 78.2 %                  | (0.8)                   | (1)                                               | %                                   |  |
| Gross Profit                                 | \$ 224,063                              |                         | \$ 208,919 |                         |                         |                                                   |                                     |  |

SG&A expenses were \$176.4 million for the three month ended March 31, 2007, as compared to \$163.3 million for the three months ended March 31, 2006. SG&A expenses during the three months ended March 31, 2007 include \$3.0 million of costs associated with the retirement of our current CEO, Kenneth B. Gilman. Excluding this item, adjusted SG&A expense as a percentage of gross profit decreased 80 basis points to 77.4% for the three months ended March 31, 2007, from 78.2% for the three months ended March 31, 2006. The improvement in adjusted SG&A as a percentage of adjusted gross profit is a result of several expense control initiatives and continued leveraging of our fixed overhead and organizational structure by increasing total gross profit by \$15.1 million (7%) during the three months ended March 31, 2007, as compared to the three months ended March 31, 2006. We anticipate that we will continue to lower our SG&A expense as a percentage of gross profit in the future as we continue to consolidate certain back office functions and continue to leverage our fixed cost structure, partially offset by increased rent expense as we continue to add service capacity.

*Depreciation and Amortization*



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Depreciation and amortization expense increased \$0.3 million (8%) to \$5.3 million for the three months ended March 31, 2007 from \$5.0 million for the three months ended March 31, 2006. This increase is primarily related to property and equipment acquired during 2007 and 2006. We expect depreciation and amortization to increase in the future as a result of previous and future capital expenditure projects to remodel and upgrade our facilities and expand our service capacity.

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*Other Income (Expense)*

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Floor plan interest expense increased \$2.3 million (26%) to \$11.2 million for the three months ended March 31, 2007, from \$8.9 million for the three months ended March 31, 2006. Approximately 43% of this increase was the result of a 65 basis point increase in short-term interest rates over last year, approximately 43% of the increase was the result of higher average inventory levels during the three months ended March 31, 2007 as compared to the three months ended March 31, 2006 and the remaining 14% was primarily the result of the amortization of two cash flow swaps, which were terminated in March of 2006. The increase in the average inventory levels are primarily a result of increased inventories of heavy trucks as we have strategically increased our inventories of 2006 model heavy trucks due to the change in emission laws effective January 2007. We expect floor plan expense to fluctuate with changes in our inventory levels in the near future as we anticipate that short-term interest rates will remain at their current level.

Other interest expense increased \$0.9 million (8%) to \$11.8 million for the three months ended March 31, 2007, from \$10.9 million for the three months ended March 31, 2006. Approximately \$0.2 million of the increase in other interest expense is a result of a higher effective interest rate on our 8% Notes due to the termination of a fair value swap on our 8% Notes in March of 2006. As a result, our 8% Notes, which had a variable rate while the fair value swap was in place, became fixed at 8% in March 2006 and will remain fixed until maturity in 2014. The amortization of the swap termination costs increased other interest expense by \$0.2 million for the three months ended March 31, 2007.

During the three months ended March 31, 2007, we recognized a \$17.7 million loss on the extinguishment of \$238.1 million of our 9% Notes and \$3.0 million of our 8% Notes in connection with the refinancing of our long-term debt. Included in the \$17.7 million loss are (i) a \$12.4 million premium on the repurchase of the 9% Notes and 8% Notes, (ii) \$5.2 million of costs associated with a pro-rata write-off of unamortized debt issuance costs associated with the 9% Notes and 8% Notes, and (iii) \$0.1 million of costs associated with a pro-rata write-off of the unamortized value of our terminated fair value swap associated with the 8% Notes. Other interest expense will decrease by \$7.9 million on an annual basis as a result of this debt refinancing. In addition, our board of directors has authorized us to repurchase up to an additional \$19.4 million of our senior subordinated notes.

Interest income increased \$1.3 million (170%) to \$2.0 million for the three months ended March 31, 2007 from \$0.7 million for the three months ended March 31, 2006. The increase in interest income is a result of higher average cash balances during the three months ended March 31, 2007 as compared to the three months ended March 31, 2006 and a 65 basis point increase in short-term interest rates.

### *Income Tax Expense*

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Income tax expense decreased \$6.7 million (82%), to \$1.5 million for the three months ended March 31, 2007, compared to \$8.2 million for the three months ended March 31, 2006. Our effective tax rate for the three months ended March 31, 2007, was 37.7% compared to 37.5% for the three months ended March 31, 2006, an increase of 20 basis points principally as a result of tax law changes in the state of Texas. As we operate nationally, our effective tax rate is dependent upon our geographic revenue mix. We evaluate our effective tax rate periodically based on our revenue sources. We will continue to evaluate our effective tax rate in the future, and expect that our future annual effective tax rate will be between 37.5% and 38.5%.

### *Discontinued Operations*

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|                                                                                              | For the Three Months Ended |             |
|----------------------------------------------------------------------------------------------|----------------------------|-------------|
|                                                                                              | March 31,                  |             |
|                                                                                              | 2007                       | 2006        |
|                                                                                              | (Dollars in thousands)     |             |
| Franchises                                                                                   | 2                          | 12          |
| Net losses from sold or closed franchises, net of tax                                        | \$ (664 )                  | \$ (1,170 ) |
| Net divestiture income (expense) including net gain (loss) on sale of franchises, net of tax | (1,312 )                   | 33          |
| Discontinued operations, net of tax                                                          | \$ (1,976 )                | \$ (1,137 ) |

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During the three months ended March 31, 2007, we sold two franchises (two dealership locations). The \$2.0 million loss from discontinued operations is a result of (i) \$1.3 million, net of tax, of divestiture expense associated with the two franchises mentioned above (ii) \$0.1 million, net of tax, of net losses of franchises sold in 2007 and (iii) \$0.6 million, net of tax, of additional divestiture costs and certain recurring costs associated with franchises sold prior to 2007. The \$1.1 million loss from discontinued operations for the three months ended March 31, 2006, includes \$1.2 million, net of tax, of losses of franchises sold or closed in 2007 and 2006 and \$0.1 million, net of tax, of net divestiture income associated with franchises sold during the three months ended March 31, 2006.

We continuously evaluate the financial and operating results of our dealerships, specifically the 10% contributing the least amount of operating income, and we will look to divest dealerships that do not meet our expectations. We do not currently have any franchises held for sale and based on the performance of our current brand mix, we do not anticipate a significant amount of divestitures in the near future.

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## LIQUIDITY AND CAPITAL RESOURCES

We require cash to fund working capital needs, finance acquisitions of new dealerships and fund capital expenditures. We believe that our cash and cash equivalents on hand as of March 31, 2007, our funds generated through future operations and the funds available for borrowings under our Committed Credit Facility (as defined below), floor plan facilities, mortgage notes payable and proceeds from sale-leaseback transactions will be sufficient to fund our debt service and working capital requirements, commitments and contingencies, acquisitions, capital expenditures, current divided commitments and any seasonal operating requirements for the foreseeable future.

As of March 31, 2007, we had cash and cash equivalents of approximately \$94.5 million and working capital of \$387.7 million. In addition, we had \$125.0 million available for borrowings under our committed credit facility for working capital, general corporate purposes and acquisitions.

### *Long-term Debt Refinancing*

During the three months ended March 31, 2007, we initiated a refinancing of our long-term debt which included (i) a cash tender offer for all of our \$250.0 million 9% Senior Subordinated Notes due 2012 ( 9% Notes ), (ii) the issuance of \$115.0 million of 3% Senior Subordinated Convertible Notes due 2012 ( 3% Notes ), which have an initial conversion price of \$33.99 and (iii) the issuance of \$150.0 million of 7.625% Senior Subordinated Notes due 2017. As of March 31, 2007, we had completed the issuance of our 3% Notes and 7.625% Notes and repurchased \$238.1 million of our 9% Notes through our tender offer. We plan to call the remaining \$11.9 million of our 9% Notes on the first call date of June 15, 2007. Upon completion of our long-term debt refinancing, we expect our annual interest expense will decrease by approximately \$7.9 million.

In connection with the issuance of our 3% Notes, we paid \$19.3 million for convertible note hedge and sold warrants to purchase shares of our common stock for proceeds of \$8.9 million. The convertible note hedge and warrant transactions are separate contracts and are not part of the terms of the 3% Notes and will not affect the holders' rights under the 3% Notes. Holders of the 3% Notes will not have any rights with respect to the convertible note hedge and warrant transactions. These equity transactions require the counterparties to deliver shares to holders of our 3% Notes who convert when the fair market value of our common stock is between \$33.99 and \$45.09, effectively increasing the conversion price of the 3% Notes to \$45.09, which is a 62.50% premium over the market price of our common stock at the time of pricing. The convertible note hedge transactions are expected to offset the potential dilution upon conversion of the 3% Notes in the event that the market value per share of our common stock at the time of exercise is greater than the strike price of the convertible note hedge transactions.

### *3% Senior Subordinated Convertible Notes due 2012*

On March 16, 2007, we issued \$115.0 million in aggregate principal amount of our 3% Notes, receiving net proceeds of \$111.4 million. The sale of the notes was exempt from registration pursuant to Rule 144A under the Securities Act of 1933. During the second quarter of 2007, we expect to file a shelf registration statement with the Securities and Exchange Commission covering the resale of the notes and the underlying common stock. The costs related to the issuance of these notes were capitalized and are being amortized to other interest expense over the term of the notes. We pay interest on these notes on March 15 and September 15 of each year until their maturity on September 15, 2012. If and when these notes are converted, we will pay cash for the principal amount of each note and, if applicable, shares of our common stock based on a daily conversion value calculated on a proportionate basis for each volume weighted average price ( VWAP ) trading day (as defined in the notes) and the relevant 30 VWAP trading day observation period. The initial conversion rate for the notes will be 29.4172 shares of common stock per \$1,000 principal amount of notes, which is equivalent to an initial conversion price of \$33.99 per share. The conversion rate will be subject to adjustment in some events but will not be adjusted for accrued interest.

Our 3% Notes are guaranteed by all our wholly-owned current subsidiaries and all of our future domestic subsidiaries that have outstanding, incur or guarantee any other indebtedness. The terms of our 3% Notes, in certain circumstances, restrict our ability to, among other things, sell all or substantially all of our assets.

### *7.625% Senior Subordinated Notes due 2017*

On March 26, 2007, we issued \$150.0 million of our 7.625% Notes, receiving net proceeds of \$146.3 million. The sale of the notes was exempt from registration pursuant to Rule 144A and Regulation S under the Securities Act of 1933, as amended. During the second quarter of 2007, we expect to file a registration statement with the Securities

and Exchange Commission in connection with an exchange offer to exchange the notes for new notes with substantially identical terms that are registered under the Securities Act of 1933 and, therefore, will generally be freely transferable. The costs related to the issuance of these notes were capitalized and are being amortized to other interest expense over the term of the notes. We pay interest on these notes on March 15 and September 15 of each year until their maturity on March 15, 2017. At any time during the term of the 7.625% Notes we may, at our option, choose to redeem all or a portion of these notes at a price equal to 100% of their principal amount plus the applicable premium set forth in the 7.625% Notes indenture. On or before March 15, 2010, we may, at our option, use the net proceeds of one or more equity offerings to redeem up to 35% of the aggregate principal amount of these notes at a redemption price equal to 107.625% of their principal amount plus accrued and unpaid interest thereon.

Our 7.625% Notes are guaranteed by all of our wholly-owned current subsidiaries and all of our future domestic subsidiaries that have outstanding, incur or guarantee any other indebtedness. The terms of our 7.625% Notes, in certain circumstances, restrict our ability to, among other things, incur additional indebtedness, pay dividends, repurchase our common stock and merge or sell all or substantially all our assets.

#### *Share Repurchase and Dividends*

In January 2007, our board of directors declared a \$0.20 per share dividend, which was the third consecutive quarter that a \$0.20 per share dividend was paid.

In February 2007, our board of directors approved a 1.3 million share repurchase program with the objective of offsetting earnings per share dilution resulting from employee share-based compensation programs. In connection with the refinancing of our long-term debt, we elected to purchase all of the 1.3 million shares at \$27.75 per share for \$36.1 million.

#### *Committed Credit Facility*



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We have a committed credit facility (the Committed Credit Facility) with JPMorgan Chase Bank, N.A., and 18 other financial institutions (the Syndicate), which provides us with \$125.0 million of working capital borrowing capacity and \$425.0 million of financing for all of our new and used vehicle inventory with the exception of our (i) Ford, Lincoln, Mercury, Mazda, Volvo and Rover dealerships (Ford Trustmark), (ii) General Motors dealerships and (iii) Mercedes, Chrysler, Dodge and Jeep dealerships (DaimlerChrysler Dealerships) through March 2009. Ford Motor Credit Corporation (FMCC) provides us with \$150.0 million of floor plan financing outside of the Syndicate to finance inventory at our Ford Trustmark dealerships while General Motors Acceptance Corporation (GMAC) and DaimlerChrysler Financial Services (DCFS) each provides us with \$100.0 million of floor plan financing outside of the Syndicate to finance inventory at our General Motors dealerships and DaimlerChrysler Dealerships, respectively.

### *Floor Plan Financing-*

We finance substantially all of our new vehicle inventory and, at our option, have the ability to finance a portion of our used vehicle inventory. We consider floor plan notes payable to a party that is affiliated with vehicle manufacturers from which we purchase new vehicle inventory Floor plan notes payable manufacturer affiliated and all other floor plan notes payable Floor plan notes payable non-manufacturer affiliated. As of March 31, 2007, total borrowing capacity under the floor plan financing agreements with our vehicle floor plan providers totaled \$795.0 million. In addition, as of March 31, 2007, we had total borrowing capacity of \$56.0 million under ancillary floor plan financing agreements with Comerica Bank and Navistar Financial for our heavy trucks business in Atlanta, Georgia. As of March 31, 2007, we had \$671.4 million, outstanding to lenders affiliated and non-affiliated with the vehicle manufacturers from which we purchase our vehicle inventory.

Amounts borrowed under the Committed Credit Facility are secured by certain of our tangible and intangible assets and the guarantees of each of our subsidiaries, other than our Toyota and Lexus subsidiaries.

### *Debt Covenants-*

We are subject to certain financial covenants in connection with our debt and lease agreements, including the financial covenants described below. Our Committed Credit Facility includes certain financial ratios with the following requirements: (i) an adjusted current ratio of at least 1.2 to 1, of which our ratio was 1.6 to 1 as of March 31, 2007; (ii) a fixed charge coverage ratio of at least 1.2 to 1, of which our ratio was 1.6 to 1 as of March 31, 2007; (iii) an adjusted leverage ratio of not more than 4.5 to 1, of which our ratio was 2.9 to 1 as of March 31, 2007 and (iv) a minimum adjusted net worth of not less than \$350.0 million, of which our adjusted net worth was \$467.7 million as of March 31, 2007. A breach of these covenants could cause an acceleration of repayment of our Committed Credit Facility if not otherwise waived or cured.

Certain of our lease agreements include financial ratios with the following requirements: (i) a liquidity ratio of at least 1.2 to 1, of which our ratio was 1.5 to 1 as of March 31, 2007 and (ii) an EBITDA based coverage ratio of at least 1.5 to 1, of which our ratio was 3.2 to 1 as of March 31, 2007. A breach of these covenants would give rise to certain lessor remedies under our various lease agreements, the most severe of which include the following: (a) termination of the applicable lease, (b) termination of certain of the tenant's lease rights, such as renewal rights and rights of first offer or negotiation relating to the purchase of the premises, and/or (c) a liquidated damages claim equal to the amount to which the accelerated rents under the applicable lease for the remainder of the lease term exceed the fair market rent over the same periods. As of March 31, 2007, we were in compliance with all our debt and lease agreement covenants.

#### Cash Flows for the Three Months Ended March 31, 2007 Compared to the Three Months Ended March 31, 2006

Floor plan borrowings are required by all vehicle manufacturers for the purchase of new vehicles, and our agreements with our floor plan providers require us to repay amounts borrowed for the purchase of a vehicle immediately after that vehicle is sold. As a result, changes in floor plan notes payable are directly linked to changes in new vehicle inventory and therefore are an integral part of understanding changes in our working capital and operating cash flow. Consequently, we have provided a reconciliation of cash flow from operating activities and financing activities, as if all changes in floor plan notes payable were classified as an operating activity.

| (In thousands)                                                                                                                       | For the Three Months Ended |              |
|--------------------------------------------------------------------------------------------------------------------------------------|----------------------------|--------------|
|                                                                                                                                      | March 31,<br>2007          | 2006         |
| <i>Reconciliation of Cash (used in) provided by Operating Activities to Adjusted Cash provided by Operating Activities</i>           |                            |              |
| Cash (used in) provided by operating activities as reported                                                                          | \$ (44,360 )               | \$ 73,686    |
| Floor plan notes payable non-manufacturer affiliated, net                                                                            | 60,994                     | (70,437 )    |
| Cash provided by operating activities as adjusted                                                                                    | \$ 16,634                  | \$ 3,249     |
| <i>Reconciliation of Cash provided by (used in) Financing Activities to Adjusted Cash (used in) provided by Financing Activities</i> |                            |              |
| Cash provided by (used in) financing activities as reported                                                                          | \$ 16,042                  | \$ (67,808 ) |
| Floor plan borrowings non-manufacturer affiliated                                                                                    | (663,002 )                 | (677,249 )   |
| Floor plan repayments non-manufacturer affiliated                                                                                    | 602,008                    | 747,686      |
| Cash (used in) provided by financing activities as adjusted                                                                          | \$ (44,952 )               | \$ 2,629     |

#### *Operating Activities-*

Net cash used in operating activities totaled \$44.4 million for the three months ended March 31, 2007. Net cash provided by operating activities totaled \$73.7 million for the three months ended March 31, 2006. Net cash provided by operating activities, as adjusted, totaled \$16.6 million and \$3.2 million for the three months ended March 31, 2007 and 2006, respectively. Cash provided by operating activities, as adjusted, includes net income adjusted for non-cash items and changes in working capital, including changes in floor plan notes payable and inventory. The increase in our cash provided by operating activities, as adjusted, for the three months ended March 31, 2007, as compared to the three months ended March 31, 2006, was a result of a \$9.6 million increase in net income adjusted for non-cash items and \$5.6 million related to the timing of payments of accounts payable, accrued liabilities and prepaid assets.

#### *Investing Activities*

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Net cash used in investing activities totaled \$6.4 million and \$3.2 million for the three months ended March 31, 2007 and 2006, respectively. Cash flows from investing activities relate primarily to capital expenditures, acquisition and divestiture activity, sale of property and equipment and construction reimbursements from lessors in connection with our sale-leaseback agreements.

Capital expenditures were \$12.9 million and \$11.9 million for the three months ended March 31, 2007 and 2006, respectively, of which \$2.7 million and \$6.4 million, were financed or were pending financing through sale-leaseback agreements for the three months ended March 31, 2007 and 2006, respectively. Our capital investments consisted of upgrades of our existing facilities, equipment purchases and construction of new facilities. Future capital expenditures will relate primarily to upgrading existing dealership facilities and operational improvements that we expect will provide us with acceptable rates of return on our investments. We expect that capital expenditures during 2007 will total between \$70 million and \$80 million, of which we intend to finance approximately 50% to 60% principally through sale-leaseback agreements.

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Proceeds from the sale of assets totaled \$8.4 million and \$9.3 million for the three months ended March 31, 2007 and 2006, respectively. Included in the proceeds from the sale of assets for the three months ended March 31, 2007 and 2006, was \$5.4 million and \$5.9 million of proceeds that were paid directly to our floor plan providers associated with the sale of inventory in connection with our divestitures. We continuously monitor the profitability and market value of our dealerships and, under certain conditions, may strategically divest non-profitable dealerships.

*Financing Activities*

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Net cash provided by financing activities totaled \$16.0 million for the three months ended March 31, 2007. Net cash used in financing activities totaled \$67.8 million for the three months ended March 31, 2006. Net cash used in financing activities, as adjusted, totaled \$45.0 million for the three months ended March 31, 2007. Net cash provided by financing activities, as adjusted, totaled \$2.6 million for the three months ended March 31, 2006.

During the three months ended March 31, 2007, and 2006, proceeds from borrowings totaled \$265.0 million and \$0.9 million, respectively. Proceeds from borrowings during the three months ended March 31, 2007 include the issuance of our 3% Notes and 7.625% Notes. In addition we incurred \$7.3 million of debt issuance costs associated with issuance of our 3% Notes and 7.625% Notes.

During the three months ended March 31, 2007, and 2006, we repaid debt of \$253.9 million and \$1.6 million, respectively. Included in the \$253.9 million of debt repayments above was \$250.4 million related to the repurchase of \$238.1 million of our 9% Notes and \$3.1 million related to the repurchase of \$3.0 million of our 8% Notes. In addition, our board of directors has authorized us to repurchase up to an additional \$19.4 million of our senior subordinated notes.

During the three months ended March 31, 2007, in connection with the 3% Notes we paid \$19.3 million for a convertible bond hedge and sold warrants to purchase shares of our common stock at \$45.09 per share for proceeds of \$8.9 million.

During the three months ended March 31, 2007, we paid a \$0.20 per share dividend totaling \$6.7 million. This was the third consecutive quarter that a \$0.20 per share dividend was paid.

During the three months ended March 31, 2007, in connection with the issuance of convertible debt, we purchased 1.3 million shares of our common stock at \$27.75 per share for \$36.1 million.

During the three months ended March 31, 2007, we received net proceeds of \$3.2 million from the sale of real estate associated with sale-leaseback transactions. We consider these particular transactions financing activities as we owned the real estate and related improvements prior to the sale-leaseback transaction and continue to use the dealership facilities and related real estate in our operations. We have entered into long-term lease agreements for use of the dealership facilities with the lessors.

During the three months ended March 31, 2007 and 2006, we received net proceeds from the exercise or vesting of share-based equity awards totaling \$0.3 million and \$2.9 million, respectively. The \$0.3 million of proceeds for the three months ended March 31, 2007, includes the payment of \$0.7 million of employee tax withholdings in connection with a net share settlement of equity awards.

### **Off-Balance Sheet Transactions**

We had no material off-balance sheet transactions during the periods presented other than those disclosed in Note 14 of our condensed consolidated financial statements.

### **Stock Repurchase and Dividend Restrictions**

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Pursuant to the indentures governing our 9% Senior Subordinated Notes due 2012, our 8% Senior Subordinated Notes due 2014, our 7.625% Senior Subordinated Notes due 2017 and our Committed Credit Facility, our ability to repurchase shares of our common stock and pay cash dividends is limited. As of March 31, 2007, our ability to repurchase shares and pay cash dividends was limited to \$34.8 million due to these restrictions.

### **CRITICAL ACCOUNTING ESTIMATES**

Preparation of financial statements in conformity with accounting principles generally accepted in the United States

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of America requires management to make estimates and assumptions that affect amounts of assets and liabilities and disclosures of contingent assets and liabilities as of the date of the financial statements and reported amounts of revenues and expenses during the periods presented. Actual amounts could differ from those estimates. On an ongoing basis, management evaluates its estimates and assumptions and the effects of revisions are reflected in the financial statements in the period in which they are determined to be necessary. The accounting policies described below are those that most frequently require management to make estimates and judgments, and therefore are critical to understanding our results of operations. Senior management has discussed the development and selection of these accounting estimates and the related disclosures with the audit committee of our board of directors.

#### *Inventories*

Our inventories are stated at the lower of cost or market. We use the specific identification method to value our vehicle inventories and the first-in, first-out method ( FIFO ) to account for our parts inventories. We maintain a reserve for specific inventory units where cost basis exceeds fair value. In assessing lower of cost or market for new and used vehicles, we consider (i) the aging of new and used vehicles, (ii) loss histories of new and used vehicles, (iii) the timing of annual and model changeovers of new vehicles and (iv) current market conditions. We very rarely sell new vehicles that have been in inventory for less than 300 days at a loss. Our new vehicle loss histories have indicated that our losses range between 1% to 6% of our new vehicle inventory that exceeded 300 days old. As of March 31, 2007, our new vehicle loss reserve was \$0.6 million or 5.6% of new vehicle inventory over 300 days old. Each 1% change in our estimate would change our new vehicle reserve approximately \$0.1 million. Our used vehicle loss histories have indicated that our losses range between 2% to 4% of our used vehicle inventory. As of March 31, 2007, our used vehicle loss reserve was \$3.5 million or 2.8% of used vehicle inventory. A 1% change in our estimate of used vehicle losses during the three months ended March 31, 2007 would change Used Vehicle Cost of Sales by approximately \$1.2 million.

#### *Notes Receivable Finance Contracts*

As of March 31, 2007 and December 31, 2006, we had outstanding notes receivable from finance contracts of \$17.5 million and \$17.9 million, respectively. These notes have initial terms ranging from 12 to 60 months, and are collateralized by the related vehicles. The assessment of our allowance for credit losses considers historical loss ratios and the performance of the current portfolio with respect to past due accounts. We continually analyze our current portfolio against our historical performance. In addition, we attribute minimal value to the underlying collateral in our assessment of the reserve. Our loss histories indicate our future credit losses will be approximately 16% of notes receivable. Our allowance for credit losses was \$3.3 million and \$3.1 million as of March 31, 2007 and December 31, 2006, respectively. A 1% change in our estimate of notes receivable losses during the three months ended March 31, 2007 would change our Finance and Insurance, net by approximately \$0.3 million.

#### *F&I Chargeback Reserve*

We receive commissions from the sale of vehicle service contracts, credit life insurance and disability insurance to customers. In addition, we receive commissions from financing institutions for arranging customer financing. We may be charged back ( chargebacks ) for finance, insurance or vehicle service contract commissions in the event a contract is terminated. The revenues from financing fees and commissions are recorded at the time the vehicles are sold and a reserve for future chargebacks is established based on historical operating results and the termination provisions of the applicable contracts. This data is evaluated on a product-by-product basis. Our loss histories vary depending on the product but generally range between 7% and 21%. Our chargeback reserves were \$14.5 million and \$14.1 million as of March 31, 2007 and December 31, 2006, respectively. A 1% change in chargebacks of all our products during the three months ended March 31, 2007 would change Finance and Insurance, net by approximately \$0.4 million.

#### *Self Insurance Reserves*

We are self insured for certain employee medical, workers compensation and general liability claims. We maintain stop loss insurance for individual and aggregate claims. We maintain and frequently review claim and loss histories to help us assess our future liability for these claims. In addition, we use professional service providers such as account administrators and actuaries to help us accumulate and assess this information. As of March 31, 2007, we had \$7.4 million of insurance reserves for both known and unknown employee medical, workers compensation and general liability claims.

### *Goodwill and Other Intangible Assets*

Goodwill represents the excess cost of the businesses acquired over the fair market value of the identifiable net assets. We have determined that based on how we operate our business, allocate resources, and regularly review our financial data and operating results that we qualify as a single reporting unit for purposes of testing goodwill for impairment. We evaluate our operations and financial results in the aggregate by dealership. The dealership general managers are responsible for customer facing activities, including inventory management and advertising and personnel decisions; and have the flexibility to respond to local market conditions. The corporate management team, with input from the regional management teams, is responsible for infrastructure and general strategy decisions.

The fair market value of our manufacturer franchise rights is determined at the acquisition date through discounting the projected cash flows specific to each franchise. We have determined that manufacturer franchise rights have an indefinite life as there are no legal, contractual, economic or other factors that limit their useful lives and they are expected to generate cash flows indefinitely due to the historically long lives of the manufacturers' brand names. Due to the fact that manufacturer franchise rights are specific to the location in which we acquire a dealership, we have determined that the dealership is the reporting unit for purposes of testing for impairment.

In accordance with SFAS No. 142, *Goodwill and Other Intangible Assets*, we do not amortize goodwill and other intangible assets that are deemed to have indefinite lives. We review goodwill and indefinite lived manufacturer franchise rights for impairment annually on October 1st of each year, or more often if events or circumstances indicate that impairment may have occurred. We are subject to financial statement risk to the extent that intangible assets become impaired due to decreases in the related fair market value of our underlying businesses.

### **RECENT ACCOUNTING PRONOUNCEMENTS**

In June 2006, the FASB issued FASB Interpretation (FIN) No. 48 *Accounting for Uncertainty in Income Taxes* an interpretation of FASB Statement No. 109. FIN 48 establishes a single model to address accounting for uncertain tax positions. FIN 48 clarifies the accounting for income taxes by prescribing a minimum recognition threshold a tax position is required to meet before being recognized as well as providing guidance on derecognition, measurement classification, interest and penalties and disclosure.

We adopted the provisions of FIN 48 effective January 1, 2007 and recognized no material adjustment in our liability for unrecognized tax benefits. As of January 1, 2007, we had \$3.6 million of total unrecognized tax benefits. Of that amount \$2.4 million, net of the federal effect, if recognized would favorably impact our effective rate in future periods. We do not expect these amounts to change materially in the next twelve months.

In connection with the adoption of FIN 48, we analyzed our filing positions in all of the federal and state jurisdictions where we are required to file tax returns, as well as all open years in these jurisdictions. We have uncertain tax positions in certain of the states in which we do business; however, none of the states individually constitute a major tax jurisdiction, as defined. Years subject to audit range as far back as 2003. The Internal Revenue Service commenced examinations of our consolidated federal returns for the years 2004 and 2005 in the first quarter of 2007, and certain of our subsidiary returns for 2003, 2004 and 2005 in the fourth quarter 2006. In addition, we have various state audits for years 2003, 2004 and 2005, being performed as of March 31, 2007. To date, no material adjustments have been proposed and we do not anticipate that these examinations will result in a material change to our financial position or results of operations.

We recognize interest and penalties related to income tax matters in income tax expense. As of March 31, 2007, we had approximately \$0.7 million of accrued interest related to uncertain tax positions and no accrual for penalties. We do not expect the amount of accrued interest to change materially in the next twelve months.

### **RECONCILIATION OF NON-GAAP FINANCIAL INFORMATION**

#### *Adjusted cash provided by (used in) operating and financing activities*

Floor plan borrowings are required by all vehicle manufacturers for the purchase of new vehicles, and our agreements with our floor plan providers require us to repay amounts borrowed for the purchase of a vehicle immediately after that vehicle is sold. As a result, changes in floor plan notes payable are directly linked to changes in new vehicle inventory and therefore are an integral part of understanding changes in our working capital and operating cash flow.





Consequently, we have provided a reconciliation of cash flow from operating activities and financing activities, as if all changes in floor plan notes payable were classified as an operating activity.

| (In thousands)                                                                                                                       | For the Three Months Ended |              |
|--------------------------------------------------------------------------------------------------------------------------------------|----------------------------|--------------|
|                                                                                                                                      | March 31,<br>2007          | 2006         |
| <i>Reconciliation of Cash (used in) provided by Operating Activities to Adjusted Cash provided by Operating Activities</i>           |                            |              |
| Cash (used in) provided by operating activities as reported                                                                          | \$ (44,360 )               | \$ 73,686    |
| Floor plan notes payable non-manufacturer affiliated, net                                                                            | 60,994                     | (70,437 )    |
| Cash provided by operating activities as adjusted                                                                                    | \$ 16,634                  | \$ 3,249     |
| <i>Reconciliation of Cash provided by (used in) Financing Activities to Adjusted Cash (used in) provided by Financing Activities</i> |                            |              |
| Cash provided (used in) by financing activities as reported                                                                          | \$ 16,042                  | \$ (67,808 ) |
| Floor plan borrowings non-manufacturer affiliated                                                                                    | (663,002 )                 | (677,249 )   |
| Floor plan repayments non-manufacturer affiliated                                                                                    | 602,008                    | 747,686      |
| Cash (used in) provided by financing activities as adjusted                                                                          | \$ (44,952 )               | \$ 2,629     |

#### *Dealership generated Finance and Insurance Gross Profit PVR-*

We evaluate our finance and insurance gross profit performance on a PVR basis by dividing our total finance and insurance gross profit by the number of retail vehicles sold. During 2003, our corporate office renegotiated a contract with one of our third party finance and insurance product providers, which resulted in the recognition of revenue during the three months ended March 31, 2006, that was attributable to retail vehicles sold during prior periods. We believe that dealership generated finance and insurance gross profit, which excludes the additional commissions derived from this contract, provides a more accurate measure of our finance and insurance operating performance.

The following table reconciles finance and insurance gross profit to dealership generated finance and insurance gross profit, and provides the necessary components to calculate dealership generated finance and insurance gross profit PVR:

| (In thousands, except for unit and per vehicle data)                                                                    | For the Three Months Ended |           |
|-------------------------------------------------------------------------------------------------------------------------|----------------------------|-----------|
|                                                                                                                         | March 31,<br>2007          | 2006      |
| <i>Reconciliation of Finance and Insurance Gross Profit to Dealership Generated Finance and Insurance Gross Profit:</i> |                            |           |
| Finance and insurance gross profit, net (as reported)                                                                   | \$ 38,684                  | \$ 35,150 |
| Less: Corporate generated finance and insurance gross profit                                                            |                            | (993 )    |
| Dealership generated finance and insurance gross profit                                                                 | \$ 38,684                  | \$ 34,157 |
| Dealership generated finance and insurance gross profit PVR                                                             | \$ 945                     | \$ 868    |
| Retail units sold:                                                                                                      |                            |           |
| New retail units                                                                                                        | 24,292                     | 24,123    |
| Used retail units                                                                                                       | 16,625                     | 15,219    |
| Total                                                                                                                   | 40,917                     | 39,342    |

#### *Adjusted SG&A Expense and Adjusted Income from Continuing Operations*

Our selling, general and administrative expenses for the three months ended March 31, 2007 were impacted by expenses related to the retirement benefits of current CEO Kenneth B. Gilman. We believe that a more accurate comparison of selling, general and administrative expenses can be made by adjusting for this item.

|                                                                          | <b>For the Three Months Ended March 31,</b> |             |
|--------------------------------------------------------------------------|---------------------------------------------|-------------|
|                                                                          | <b>2007</b>                                 | <b>2006</b> |
| <i>Adjusted SG&amp;A expenses excluding retirement benefits expense:</i> |                                             |             |
| SG&A expenses                                                            | \$ 176,386                                  | \$ 163,291  |
| Retirement benefits expense                                              | (2,950 )                                    |             |
| Adjusted SG&A expenses                                                   | \$ 173,436                                  | \$ 163,291  |
| Gross profit                                                             | \$ 224,063                                  | \$ 208,919  |
| Adjusted SG&A expenses as a percentage of gross profit                   | 77.4                                        | % 78.2      |

Our income from continuing operations for the three months ended March 31, 2007, was impacted by expenses related to the retirement benefit of current CEO Kenneth B. Gilman and costs associated with our long-term debt refinancing. We believe that a more accurate comparison of our income from continuing operations can be made by adjusting for these items.

|                                                                                                                                           | <b>For the Three Months Ended March 31,</b> |             |
|-------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------|-------------|
|                                                                                                                                           | <b>2007</b>                                 | <b>2006</b> |
| <i>Adjusted income from continuing operations excluding retirement benefits expense and loss on the extinguishment of long-term debt:</i> |                                             |             |
| Net income                                                                                                                                | \$ 433                                      | \$ 12,553   |
| Discontinued operations, net of tax                                                                                                       | 1,976                                       | 1,137       |
| Income from continuing operations                                                                                                         | 2,409                                       | 13,690      |
| Retirement benefits expense, net of tax                                                                                                   | 1,838                                       |             |
| Loss on extinguishment of long-term debt, net of tax                                                                                      | 11,050                                      |             |
| Adjusted income from continuing operations                                                                                                | \$ 15,297                                   | \$ 13,690   |

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

#### Interest Rate Risk

We are exposed to market risk from changes in interest rates on a significant portion of our outstanding indebtedness. Based on \$557.1 million of total variable rate debt (including floor plan notes payable) outstanding as of March 31, 2007, a 1% change in interest rates would result in a change of approximately \$5.6 million to our annual other interest expense.

We received \$7.4 million of interest credit assistance from certain automobile manufacturers during the three months ended March 31, 2007. Interest credit assistance reduced cost of sales for the three months ended March 31, 2007 by \$7.1 million and reduced new vehicle inventory by \$4.4 million and \$4.1 million as of March 31, 2007 and December 31, 2006, respectively. Although we can provide no assurance as to the amount of future floor plan credits, it is our expectation, based on historical data, that an increase in prevailing interest rates would result in increased interest credit assistance from certain automobile manufacturers.

#### Hedging Risk

In November 2006, we entered into an interest rate swap agreement with a notional principal amount of \$150.0 million as a hedge against the changes in interest rates of our variable rate floor plan notes payable for a period of two years beginning in November 2006. The swap agreement was designated and qualifies as a cash flow hedge of future changes in interest rates of our variable rate floor plan notes payable and is not expected to contain any ineffectiveness. As of March 31, 2007, the swap agreement had a fair value of \$0.4 million, which was included in Other Long-Term Liabilities on the accompanying Condensed Consolidated Balance Sheet.

Three of our interest rate swap agreements terminated in March 2006, which resulted in a cash payment of \$13.7 million, which equaled the fair market value of the swap agreements. Included in Accumulated Other Comprehensive Loss on our Condensed Consolidated Balance Sheet as of March 31, 2007, was \$3.1 million (\$2.0 million, net of tax) of unrecognized amortization related to our two terminated cash flow swaps, which are being amortized through March 2014 as a component of Floor Plan Interest Expense on the accompanying Condensed Consolidated Statements of Income. Amortization of these terminated cash flow swaps will total \$0.9 million for the year ended December 31, 2007. In addition, included as a reduction to our 8% Notes as of March 31, 2007, was \$7.5 million of unrecognized amortization related to our



terminated fair value swap, which is being amortized through March 2014 as a component of Other Interest Expense on the accompanying Condensed Consolidated Statements of Income. Amortization of this terminated fair value swap will total \$1.1 million for the year ended December 31, 2007.

We have an interest rate swap with a current notional principal amount of \$14.0 million. The swap was designed to provide a hedge against changes in interest rates of our variable rate mortgage notes payable through maturity in June 2011. This interest rate swap qualifies for cash flow hedge accounting treatment and will contain minor ineffectiveness. Under the terms of the swap agreement, we make payments based on a fixed rate of 6.08% and receive a variable rate cash flows based on one-month LIBOR. As of March 31, 2007 and December 31, 2006, the swap agreement had a fair value of \$0.3 million, which was included in Other Long-Term Assets on the accompanying Condensed Consolidated Balance Sheets.

**Item 4. Controls and Procedures**

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As of the end of the period covered by this report, the Company conducted an evaluation, under the supervision and with the participation of the Company's chief executive officer and chief financial officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures as defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act). Based on this evaluation, the Company's chief executive officer and chief financial officer concluded that as of the end of such period such disclosure controls and procedures (i) were reasonably designed to ensure that information required to be disclosed by the Company in reports it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time period specified in the rules and forms of the Securities and Exchange Commission and (ii) were effective.

There have not been any changes in the Company's internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the fiscal quarter to which this report relates that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

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### Forward-Looking Statements

This report contains forward-looking statements as that term is defined in the Private Securities Litigation Reform Act of 1995. The forward-looking statements include statements relating to goals, plans and projections regarding our financial position, results of operations, market position, product development and business strategy. Such statements include, but are not limited to our expectations that the mid-line import and luxury brands will continue to take market share and the impact that will have on our operations; that the vehicle manufacturers will continue their incentive programs; that our increased service expansion will drive future revenue increases; that we will continue to acquire dealerships and the impact those acquisitions on our operations; that our initiatives in F&I will increase revenues; our capital expenditure projections and the impact they will have on our operations, our ability to complete our bond repurchase plan and the impact that plan will have on our operations; the impact that our high margin business will have on our future operations; and our ability to continue to pay dividends.

These statements are based on management's current expectations and involve significant risks and uncertainties that may cause results to differ materially from those set forth in the statements. These risks and uncertainties include, among other things:

- market factors;
- our relationships with vehicle manufacturers and other suppliers;
- the amount of our indebtedness;
- risks related to pending and potential future acquisitions;
- general economic conditions both nationally and locally;
- our ability to successfully implement our strategies,
- governmental regulations and legislation; and

- automotive retail industry trends.

There can be no guarantees that our plans for future operations will be successfully implemented or that they will prove to be commercially successful or that we will be able to continue paying dividends in the future at the current rate or at all. These and other risk factors are discussed in our Annual Report on Form 10-K and in our other filings with the Securities and Exchange Commission. We undertake no obligation to publicly update any forward-looking statement, whether as a result of new information, future events or otherwise.

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**PART II. OTHER INFORMATION****Item 6. Exhibits**

Exhibits required to be filed by Item 601 of Regulation S-K:

**Exhibit**

| <b>Number</b> | <b>Description of Documents</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                  |
|---------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 4.1           | Indenture, dated as of March 16, 2007, among Asbury Automotive Group, Inc., the subsidiary guarantors listed on Schedule I thereto, and The Bank of New York, as Trustee, relating to the 3% Senior Subordinated Convertible Notes due 2012                                                                                                                                                                                                                                                                                                                                                                                      |
| 4.2           | Form of 3% Senior Subordinated Convertible Notes due 2012                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                        |
| 4.3           | Indenture, dated as of March 26, 2007, among Asbury Automotive Group, Inc., the subsidiary guarantors listed on Schedule I thereto, and The Bank of New York, as Trustee, relating to the 7.625% Senior Subordinated Notes due 2017                                                                                                                                                                                                                                                                                                                                                                                              |
| 4.4           | Form of 7.625% Senior Subordinated Notes due 2017                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                |
| 4.5           | Fifth Supplemental Indenture, dated as of March 8, 2007, among Asbury Automotive Group, Inc. and The Bank of New York, as Trustee, related to the 9% Senior Subordinated Notes due 2012 of Asbury Automotive Group, Inc. (filed as Exhibit 4.1 to Asbury Automotive Group's Current Report on Form 8-K filed with the Securities and Exchange Commission on March 13, 2007)*                                                                                                                                                                                                                                                     |
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| 10.11         | Third Amendment to Credit Agreement dated August 1, 2006, effective as of March 8, 2007, among Asbury Automotive Group, Inc., each of the subsidiaries of the Company listed on the signature pages thereto, each of the Lenders listed on the signature pages thereto (the "Lenders"), JPMorgan Chase Bank, N.A., as Administrative Agent for the Lenders, JPMorgan Chase Bank, N.A., as Floor Plan Agent for the Lenders, and Bank of America, N.A., as Syndication Agent (filed as Exhibit 10.1 to Asbury Automotive Group's Current Report on Form 8-K filed with the Securities and Exchange Commission on March 13, 2007)* |
| 10.12         | Form of Performance Share Unit Award Agreement (filed as Exhibit 10.1 to Asbury Automotive Group's Current Report on Form 8-K filed with the Securities and Exchange Commission on February 28, 2007)*                                                                                                                                                                                                                                                                                                                                                                                                                           |
| 15.1          | Awareness letter from Deloitte & Touche LLP                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |
| 31.1          | Certificate of Chief Executive Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, dated May 8, 2007                                                                                                                                                                                                                                                                                                                                                                                                                      |
| 31.2          | Certificate of Chief Financial Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    |





- 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, dated May 8, 2007
- 32.1 Certificate of Chief Executive Officer pursuant to Rule 13a-14(b)/15d-14(b) of the Securities Exchange Act of 1934 and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, dated May 8, 2007
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\* Incorporated by reference

#### 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.

#### Asbury Automotive Group, Inc. (Registrant)

Date: May 8, 2007

By: /s/ CHARLES R. OGLESBY  
Name: Charles R. Oglesby  
Title: Chief Executive Officer and President

Date: May 8, 2007

By: /s/ J. GORDON SMITH  
Name: J. Gordon Smith  
Title: Senior Vice President and Chief Financial Officer  
(Principal Financial Officer)

## INDEX TO EXHIBITS

| Exhibit<br>Number | Description of Documents                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       |
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