

PENSKE AUTOMOTIVE GROUP, INC.

Form 10-Q

July 30, 2010

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**  
**Washington, D.C. 20549**  
**Form 10-Q**

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

**For the quarterly period ended June 30, 2010**

**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 1-12297**

**Penske Automotive Group, Inc.**

*(Exact name of registrant as specified in its charter)*

**Delaware**

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

**22-3086739**

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

**2555 Telegraph Road,  
Bloomfield Hills, Michigan**

*(Address of principal executive offices)*

**48302-0954**

*(Zip Code)*

**Registrant's telephone number, including area code:**

**(248) 648-2500**

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 has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

As of July 26, 2010, there were 92,074,157 shares of voting common stock outstanding.

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**PENSKE AUTOMOTIVE GROUP, INC.  
CONSOLIDATED CONDENSED BALANCE SHEETS**

	<b>June 30, 2010</b>	<b>December 31, 2009</b>
	<b>(Unaudited)</b>	
	<b>(In thousands, except per share amounts)</b>	
<b>ASSETS</b>		
Cash and cash equivalents	\$ 17,664	\$ 13,999
Accounts receivable, net of allowance for doubtful accounts of \$1,797 and \$1,689	351,013	321,226
Inventories	1,364,718	1,302,495
Other current assets	106,479	95,426
Assets held for sale	572	10,625
Total current assets	1,840,446	1,743,771
Property and equipment, net	707,832	726,808
Goodwill	795,366	810,047
Franchise value	199,581	201,756
Equity method investments	280,847	295,473
Other long-term assets	14,591	18,152
Total assets	\$ 3,838,663	\$ 3,796,007
 <b>LIABILITIES AND EQUITY</b>		
Floor plan notes payable	\$ 818,339	\$ 769,657
Floor plan notes payable non-trade	499,410	423,316
Accounts payable	209,535	189,989
Accrued expenses	218,716	227,294
Current portion of long-term debt	16,551	12,442
Liabilities held for sale	501	7,675
Total current liabilities	1,763,052	1,630,373
Long-term debt	844,292	933,966
Deferred tax liabilities	159,872	157,500
Other long-term liabilities	109,713	128,129
Total liabilities	2,876,929	2,849,968
Commitments and contingent liabilities		
<b>Equity</b>		
Penske Automotive Group stockholders' equity:		
Preferred Stock, \$0.0001 par value; 100 shares authorized; none issued and outstanding		

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Common Stock, \$0.0001 par value, 240,000 shares authorized; 92,142 shares issued and outstanding at June 30, 2010; 91,618 shares issued and outstanding at December 31, 2009

Non-voting Common Stock, \$0.0001 par value, 7,125 shares authorized; none issued and outstanding

Class C Common Stock, \$0.0001 par value, 20,000 shares authorized; none issued and outstanding

Additional paid-in-capital	738,611	737,198
Retained earnings	246,000	196,205
Accumulated other comprehensive income	(26,567)	9,049

Total Penske Automotive Group stockholders' equity	958,053	942,461
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Non-controlling interest	3,681	3,578
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Total equity	961,734	946,039
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Total liabilities and equity	\$ 3,838,663	\$ 3,796,007
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See Notes to Consolidated Condensed Financial Statements

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**PENSKE AUTOMOTIVE GROUP, INC.**  
**CONSOLIDATED CONDENSED STATEMENTS OF INCOME**

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	2009	2010	2009
	(Unaudited)			
	(In thousands, except per share amounts)			
Revenue:				
New vehicle	\$ 1,355,813	\$ 1,090,127	\$ 2,588,136	\$ 2,061,323
Used vehicle	749,669	658,787	1,446,337	1,275,286
Finance and insurance, net	63,558	54,674	122,992	103,137
Service and parts	332,160	331,106	666,183	658,009
Distribution	19,933	53,152	27,869	133,265
Fleet and wholesale vehicle	182,555	130,849	337,850	245,975
 Total revenues	 2,703,688	 2,318,695	 5,189,367	 4,476,995
 Cost of sales:				
New vehicle	1,244,630	1,004,151	2,375,452	1,903,990
Used vehicle	689,552	599,526	1,329,500	1,160,009
Service and parts	141,655	148,692	287,275	298,867
Distribution	17,227	45,702	24,949	114,016
Fleet and wholesale	180,280	126,869	331,819	238,319
 Total cost of sales	 2,273,344	 1,924,940	 4,348,995	 3,715,201
 Gross profit	 430,344	 393,755	 840,372	 761,794
Selling, general and administrative expenses	355,177	327,389	695,691	640,055
Depreciation	12,054	13,811	24,428	26,692
 Operating income	 63,113	 52,555	 120,253	 95,047
Floor plan interest expense	(8,321)	(8,969)	(16,842)	(18,431)
Other interest expense	(12,542)	(13,687)	(25,262)	(28,187)
Debt discount amortization	(2,428)	(3,135)	(5,343)	(6,773)
Equity in earnings of affiliates	4,784	3,466	4,355	4,180
Gain on debt repurchase	422		1,027	10,429
 Income from continuing operations before income taxes	 45,028	 30,230	 78,188	 56,265
Income taxes	(15,625)	(10,329)	(28,060)	(20,074)
 Income from continuing operations	 29,403	 19,901	 50,128	 36,191
Gain (loss) from discontinued operations, net of tax	281	(5,734)	(112)	(5,822)
 Net income	 29,684	 14,167	 50,016	 30,369
Less: Income attributable to non-controlling interests	243	88	221	8

Net income attributable to Penske Automotive Group common stockholders	\$ 29,441	\$ 14,079	\$ 49,795	\$ 30,361
<b>Basic earnings per share attributable to Penske Automotive Group common stockholders:</b>				
Continuing operations	\$ 0.32	\$ 0.22	\$ 0.54	\$ 0.40
Discontinued operations	(0.00)	(0.06)	(0.00)	(0.06)
Net income	\$ 0.32	\$ 0.15	\$ 0.54	\$ 0.33
Shares used in determining basic earnings per share	92,142	91,531	92,016	91,506
<b>Diluted earnings per share attributable to Penske Automotive Group common stockholders:</b>				
Continuing operations	\$ 0.32	\$ 0.22	\$ 0.54	\$ 0.40
Discontinued operations	(0.00)	(0.06)	(0.00)	(0.06)
Net income	\$ 0.32	\$ 0.15	\$ 0.54	\$ 0.33
Shares used in determining diluted earnings per share	92,206	91,592	92,086	91,537
<b>Amounts attributable to Penske Automotive Group common stockholders:</b>				
Income from continuing operations	\$ 29,403	\$ 19,901	\$ 50,128	\$ 36,191
Less: Income attributable to non-controlling interests	243	88	221	8
Income from continuing operations, net of tax	29,160	19,813	49,907	36,183
Gain (loss) from discontinued operations, net of tax	281	(5,734)	(112)	(5,822)
Net income	\$ 29,441	\$ 14,079	\$ 49,795	\$ 30,361
Cash dividends per share	\$	\$	\$	\$

See Notes to Consolidated Condensed Financial Statements

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**PENSKE AUTOMOTIVE GROUP, INC.**  
**CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS**

	<b>Six Months Ended</b>	
	<b>June 30,</b>	
	<b>2010</b>	<b>2009</b>
	<b>(Unaudited)</b>	
	<b>(In thousands)</b>	
<b>Operating Activities:</b>		
Net income	\$ 50,016	\$ 30,369
Adjustments to reconcile net income to net cash from continuing operating activities:		
Depreciation	24,428	26,692
Debt discount amortization	5,343	6,773
Undistributed earnings of equity method investments	(4,355)	(4,180)
Loss from discontinued operations, net of tax	112	5,822
Deferred income taxes	11,398	21,037
Gain on debt repurchase	(1,027)	(10,733)
Changes in operating assets and liabilities:		
Accounts receivable	(25,714)	(26,927)
Inventories	(33,856)	340,656
Floor plan notes payable	27,057	(188,134)
Accounts payable and accrued expenses	12,036	32,906
Other	4,155	6,824
Net cash from continuing operating activities	69,593	241,105
<b>Investing Activities:</b>		
Purchase of equipment and improvements	(37,622)	(43,979)
Dealership acquisitions net, including repayment of sellers' floor plan notes payable of \$7,231 and \$2,940, respectively	(12,277)	(8,610)
Other		12,679
Net cash from continuing investing activities	(49,899)	(39,910)
<b>Financing Activities:</b>		
Proceeds from borrowings under U.S. credit agreement revolving credit line	320,600	276,800
Repayments under U.S. credit agreement revolving credit line	(292,600)	(276,800)
Repayments under U.S. credit agreement term loan		(10,000)
Repurchase of 3.5% senior subordinated convertible notes	(113,604)	(51,425)
Net repayments of other long-term debt	(9,497)	(47,768)
Net borrowings (repayments) of floor plan notes payable - non-trade	76,094	(78,608)
Proceeds from exercises of options, including excess tax benefit	211	
Net cash from continuing financing activities	(18,796)	(187,801)
Discontinued operations:		
Net cash from discontinued operating activities	(6,489)	(643)
Net cash from discontinued investing activities	9,463	(2,605)



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Net cash from discontinued financing activities	(207)	(7,085)
Net cash from discontinued operations	2,767	(10,333)
Net change in cash and cash equivalents	3,665	3,061
Cash and cash equivalents, beginning of period	13,999	17,108
Cash and cash equivalents, end of period	\$ 17,664	\$ 20,169

**Supplemental disclosures of cash flow information:**

Cash paid for:

Interest	\$ 43,876	\$ 49,368
Income taxes	14,121	4,655

See Notes to Consolidated Condensed Financial Statements

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**PENSKE AUTOMOTIVE GROUP, INC.**  
**CONSOLIDATED CONDENSED STATEMENT OF EQUITY**

	Common Stock	Additional	Accumulated	Total				
	Issued	Paid-in	Other	Stockholders				
	Shares	Capital	Retained	Equity	to Penske	Non-controlling	Total	
	Amount		Earnings	Attributable	Automotive	Interest	Equity	
			(Unaudited)	Income	Group			
			(Loss)	(Loss)				
			(Dollars in thousands)	(Loss)				
Balance, January 1, 2010	91,617,746	\$ 9 \$ 737,198	\$ 196,205	\$ 9,049	\$ 942,461	\$ 3,578	\$ 946,039	
Equity compensation	499,751	5,837			5,837		5,837	
Exercise of options, including tax benefit of \$108	25,000	211			211		211	
Repurchase of 3.5% senior subordinated convertible notes		(4,635)			(4,635)		(4,635)	
Distributions to non-controlling interests						(118)	(118)	
Foreign currency translation				(42,831)	(42,831)		(42,831)	
Other				7,215	7,215		7,215	
Net income			49,795		49,795	221	50,016	
Balance, June 30, 2010	92,142,497	\$ 9 \$ 738,611	\$ 246,000	\$ (26,567)	\$ 958,053	\$ 3,681	\$ 961,734	

See Notes to Consolidated Condensed Financial Statements

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**PENSKE AUTOMOTIVE GROUP, INC.**  
**NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS**  
**(Unaudited)**  
**(In thousands, except per share amounts)**

**1. Interim Financial Statements**

***Business Overview***

Penske Automotive Group, Inc. (the Company) is the second largest automotive retailer headquartered in the U.S. as measured by total revenues. As of June 30, 2010, the Company owned and operated 171 franchises in the U.S. and 152 franchises outside of the U.S., primarily in the U.K. During the six months ended June 30, 2010, we acquired 6 franchises, including Volkswagen and Audi franchises in Santa Ana, California and a group of BMW franchises in Augsburg, Germany through the dissolution of a joint venture. We were awarded 9 franchises, including Audi and Mercedes franchises in Chantilly, Virginia, two Mini franchises in the western U.S. and four Mercedes Sprinter commercial van franchises in the U.S. We also disposed of 5 franchises, including our Toyota/Scion business in Warren, Michigan and our Ford business in Goodyear, Arizona.

Each of the Company's dealerships offers a wide selection of new and used vehicles for sale. In addition to selling new and used vehicles, the Company generates higher-margin revenue at each of its dealerships through maintenance and repair services and the sale and placement of higher-margin products, such as third party finance and insurance products, third-party extended service contracts and replacement and aftermarket automotive products. In 2007, the Company established a wholly-owned subsidiary, smart USA Distributor, LLC (smart USA), which is the exclusive distributor of the smart fortwo vehicle in the U.S. and Puerto Rico. The Company also holds a 9.0% limited partnership interest in Penske Truck Leasing Co., L.P. (PTL), a leading global transportation services provider.

***Basis of Presentation***

The following unaudited consolidated condensed financial statements of the Company have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and disclosures normally included in the Company's annual financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted pursuant to the SEC rules and regulations. The information presented as of June 30, 2010 and December 31, 2009 and for the three and six month periods ended June 30, 2010 and 2009 is unaudited, but includes all adjustments which the management of the Company believes to be necessary for the fair presentation of results for the periods presented. The consolidated condensed financial statements for prior periods have been revised for entities which have been treated as discontinued operations through June 30, 2010, and the results for interim periods are not necessarily indicative of results to be expected for the year. These consolidated condensed financial statements should be read in conjunction with the Company's audited financial statements for the year ended December 31, 2009, which are included as part of the Company's Annual Report on Form 10-K.

Results for three and six months ended June 30, 2010 include a \$422 and \$1,027 pre-tax gain relating to the repurchase of \$41,548 and \$112,658 aggregate principal amount of the Company's 3.5% senior subordinated convertible notes (Convertible Notes), respectively. Results for the six months ended June 30, 2009 include a \$10,429 pre-tax gain relating to the repurchase of \$68,740 aggregate principal amount of the Convertible Notes.

***Discontinued Operations***

The Company accounts for dispositions as discontinued operations when the operations and cash flows of the business being disposed of will be eliminated from on-going operations and that the Company will not have any significant continuing involvement in its operations.

In evaluating whether the cash flows of a dealership in its Retail reportable segment will be eliminated from ongoing operations, the Company considers whether it is likely that customers will migrate to similar franchises that it owns in the same geographic market. The Company's consideration includes an evaluation of the brands sold at other dealerships it operates in the market and their proximity to the disposed dealership. When the Company disposes of franchises, it typically does not have continuing brand representation in that market. If the franchise being disposed of is located in a complex of Company owned dealerships, the Company does not treat the disposition as a discontinued operation if the Company believes that the cash flows previously generated by the disposed franchise will be replaced

by expanded operations of the remaining franchises. The results of operations during the three and six months ended June 30, 2010 and 2009 and the net assets as of June 30, 2010 and December 31, 2009 of dealerships accounted for as discontinued operations were immaterial.

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**PENSKE AUTOMOTIVE GROUP, INC.**  
**NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS**

***Estimates***

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The accounts requiring the use of significant estimates include accounts receivable, inventories, income taxes, intangible assets and certain reserves.

***Estimated Useful Lives of Assets***

The Company changed the useful lives of certain fixed assets during the first quarter of 2010 as part of a review of assumptions related to the expected utilization of those assets by the Company. The Company accounted for the change in useful lives as a change in estimate prospectively effective January 1, 2010, which resulted in a reduction of depreciation expense of \$1,410 and \$2,820 for the three and six month periods ended June 30, 2010, respectively.

***Fair Value of Financial Instruments***

Financial instruments consist of cash and cash equivalents, accounts receivable, accounts payable, debt, floor plan notes payable, and interest rate swaps used to hedge future cash flows. Other than our subordinated notes, the carrying amount of all significant financial instruments approximates fair value due either to length of maturity, the existence of variable interest rates that approximate prevailing market rates, or as a result of mark to market accounting. A summary of the fair value of the subordinated notes as of June 30, 2010, based on level one market data follows:

	<b>Carrying Value</b>	<b>Fair Value</b>
7.75% senior subordinated notes due 2016	\$ 375,000	\$ 350,625
3.5% senior subordinated convertible notes due 2026	187,157	194,570

**2. Inventories**

Inventories consisted of the following:

	<b>June 30, 2010</b>	<b>December 31, 2009</b>
New vehicles	\$ 956,879	\$ 898,110
Used vehicles	330,895	325,707
Parts, accessories and other	76,944	78,678
 Total inventories	 \$ 1,364,718	 \$ 1,302,495

The Company receives non-refundable floor plan interest and advertising assistance credits from certain vehicle manufacturers that reduce cost of sales when the vehicles are sold. These floor plan interest and advertising assistance credits amounted to \$13,176 and \$8,975 during the six months ended June 30, 2010 and 2009, respectively.

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**PENSKE AUTOMOTIVE GROUP, INC.**  
**NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS**

**3. Business Combinations**

The Company's retail operations acquired three and five franchises during the six months ended June 30, 2010 and 2009, respectively. The Company's financial statements include the results of operations of the acquired dealerships from the date of acquisition. The fair value of the assets acquired and liabilities assumed have been recorded in the Company's consolidated condensed financial statements, and may be subject to adjustment pending completion of final valuation. A summary of the aggregate consideration paid and the aggregate amounts of the assets acquired and liabilities assumed in the six months ended June 30, 2010 and 2009 follows:

	<b>June 30, 2010</b>	<b>June 30, 2009</b>
Inventory	\$ 8,595	\$ 2,935
Other current assets	17	129
Property and equipment	187	3,250
Goodwill	3,510	1,746
Franchise value		749
Current liabilities	(32)	(199)
Cash used in dealership acquisitions	\$ 12,277	\$ 8,610

In the first quarter of 2010, the Company exited one of its German joint ventures by exchanging its 50% interest in the joint venture for 100% ownership in three BMW franchises previously held by the joint venture. The Company recorded \$13,331 of intangible assets in connection with this transaction.

**4. Intangible Assets**

The following is a summary of the changes in the carrying amount of goodwill and franchise value during the six months ended June 30, 2010:

	<b>Goodwill</b>	<b>Franchise Value</b>
Balance January 1, 2010	\$ 810,047	\$ 201,756
Additions	13,051	3,703
Foreign currency translation	(27,732)	(5,878)
Balance June 30, 2010	\$ 795,366	\$ 199,581

**5. Floor Plan Notes Payable Trade and Non-trade**

The Company finances substantially all of its new and a portion of its used vehicle inventories under revolving floor plan arrangements with various lenders, primarily through captive finance companies associated with automotive manufacturers. In the U.S., the floor plan arrangements are due on demand; however, the Company has not historically been required to repay floor plan advances prior to the sale of the vehicles that have been financed. The Company typically makes monthly interest payments on the amount financed. Outside the U.S., substantially all of the floor plan arrangements are payable on demand or have an original maturity of 90 days or less, and the Company is generally required to repay floor plan advances at the earlier of the sale of the vehicles that have been financed or the stated maturity.

The floor plan agreements typically grant a security interest in substantially all of the assets of the Company's dealership subsidiaries, and in the U.S. are guaranteed by the Company. Interest rates under the floor plan arrangements are variable and increase or decrease based on changes in the prime rate, defined London Interbank Offered Rate (LIBOR), Finance House Base Rate, or Euro Interbank Offered Rate. The Company classifies floor plan

notes payable to a party other than the manufacturer of a particular new vehicle, and all floor plan notes payable relating to pre-owned vehicles, as floor plan notes payable non-trade on its consolidated condensed balance sheets, and classifies related cash flows as a financing activity on its consolidated condensed statements of cash flows.

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**PENSKE AUTOMOTIVE GROUP, INC.**  
**NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS**

**6. Earnings Per Share**

Basic earnings per share is computed using net income attributable to Penske Automotive Group common stockholders and the number of weighted average shares of voting common stock outstanding, including outstanding unvested restricted stock awards which contain rights to non-forfeitable dividends. Diluted earnings per share is computed using net income attributable to Penske Automotive Group common stockholders and the number of weighted average shares of voting common stock outstanding, adjusted for the dilutive effect of non-participatory equity compensation. A reconciliation of the number of shares used in the calculation of basic and diluted earnings per share for the three and six months ended June 30, 2010 and 2009 follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	2009	2010	2009
Weighted average number of common shares outstanding	92,142	91,531	92,016	91,506
Effect of non-participatory equity compensation	64	61	70	31
Weighted average number of common shares outstanding, including effect of dilutive securities	92,206	91,592	92,086	91,537

There were no anti-dilutive stock options outstanding during the three and six months ended June 30, 2010 which were excluded from the calculation of diluted earnings per share. During the three and six months ended June 30, 2009, 3 and 222 stock options, respectively, were excluded from the calculation of diluted earnings per share because the effect of such securities was anti-dilutive. In addition, the Company has senior subordinated convertible notes outstanding which, under certain circumstances discussed in Note 7, may be converted to voting common stock. As of June 30, 2010 and 2009, no shares related to the senior subordinated convertible notes were included in the calculation of diluted earnings per share because the effect of such securities was anti-dilutive.

**7. Long-Term Debt**

Long-term debt consisted of the following:

	<b>June 30, 2010</b>	<b>December 31, 2009</b>
U.S. credit agreement revolving credit line	\$ 28,000	\$
U.S. credit agreement term loan	149,000	149,000
U.K. credit agreement revolving credit line	44,817	59,803
U.K. credit agreement term loan	10,545	17,115
U.K. credit agreement overdraft line of credit	12,259	12,048
7.75% senior subordinated notes due 2016	375,000	375,000
3.5% senior subordinated convertible notes due 2026, net of debt discount	187,157	289,344
Mortgage facilities	46,608	41,358
Other	7,457	2,740
Total long-term debt	860,843	946,408
Less: current portion	(16,551)	(12,442)
Net long-term debt	\$ 844,292	\$ 933,966



***U.S. Credit Agreement***

The Company is party to a credit agreement with DCFS USA LLC and Toyota Motor Credit Corporation, as amended (the U.S. Credit Agreement), which, as of June 30, 2010, provided for up to \$250,000 in revolving loans for working capital, acquisitions, capital expenditures, investments and other general corporate purposes, a non-amortizing term loan with a remaining balance of \$149,000, and for an additional \$10,000 of availability for letters of credit, through September 30, 2012. As of June 30, 2010, the revolving loans bore interest at a defined LIBOR plus 2.50%, subject to an incremental 0.50% for uncollateralized borrowings in excess of a defined borrowing base. The term loan, which bears interest at defined LIBOR plus 2.50%, may be prepaid at any time, but then may not be re-borrowed.

The U.S. Credit Agreement is fully and unconditionally guaranteed on a joint and several basis by the Company's domestic subsidiaries and contains a number of significant covenants that, among other things, restrict the Company's ability to dispose of assets, incur additional indebtedness, repay other indebtedness, pay dividends, create liens on assets, make investments or acquisitions and engage in mergers or consolidations. The Company is also required to comply with specified financial and other tests and ratios, each as defined in the U.S. Credit Agreement, including: a ratio of current assets to current liabilities, a fixed charge coverage ratio, a ratio of debt to stockholders' equity and a ratio of debt to EBITDA. A breach of these requirements would give rise to certain remedies under the agreement, the most severe of which is the termination of the agreement and acceleration of the amounts owed. As of June 30, 2010, the Company was in compliance with all covenants under the U.S. Credit Agreement.

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The U.S. Credit Agreement also contains typical events of default, including change of control, non-payment of obligations and cross-defaults to the Company's other material indebtedness. Substantially all of the Company's domestic assets are subject to security interests granted to lenders under the U.S. Credit Agreement. As of June 30, 2010, \$149,000 of term loans, \$1,250 of letters of credit, and \$28,000 of revolver borrowings were outstanding under the U.S. Credit Agreement.

In July 2010, the Company amended the U.S. Credit Agreement to (1) increase the borrowing capacity under the revolving credit line by \$50.0 million, (2) increase the interest rate on secured revolving borrowings by 25 basis points, and (3) increase the rate on unsecured revolving borrowings by 50 basis points.

***U.K. Credit Agreement***

The Company's subsidiaries in the U.K. (the "U.K. Subsidiaries") are party to an agreement with the Royal Bank of Scotland plc, as agent for National Westminster Bank plc, which provides for a funded term loan, a revolving credit agreement and a seasonally adjusted overdraft line of credit (collectively, the "U.K. Credit Agreement") to be used for working capital, acquisitions, capital expenditures, investments and general corporate purposes. The U.K. Credit Agreement provides for (1) up to £100,000 in revolving loans through August 31, 2013, which bears interest between a defined LIBOR plus 1.1% and defined LIBOR plus 3.0%, (2) a term loan which bears interest between 6.39% and 8.29% and is payable ratably in quarterly intervals until fully repaid on June 30, 2011, and (3) a demand seasonally adjusted overdraft line of credit for up to £20,000 that bears interest at the Bank of England Base Rate plus 1.75%. The U.K. Credit Agreement is fully and unconditionally guaranteed on a joint and several basis by the U.K.

Subsidiaries, and contains a number of significant covenants that, among other things, restrict the ability of the U.K. Subsidiaries to pay dividends, dispose of assets, incur additional indebtedness, repay other indebtedness, create liens on assets, make investments or acquisitions and engage in mergers or consolidations. In addition, the U.K. Subsidiaries are required to comply with specified ratios and tests, each as defined in the U.K. Credit Agreement, including: a ratio of EBITDAR to interest plus rental payments (as defined), a measurement of maximum capital expenditures, and a debt to EBITDA ratio (as defined). A breach of these requirements would give rise to certain remedies under the agreement, the most severe of which is the termination of the agreement and acceleration of the amounts owed. As of June 30, 2010, the U.K. subsidiaries were in compliance with all covenants under the U.K. Credit Agreement.

The U.K. Credit Agreement also contains typical events of default, including change of control and non-payment of obligations and cross-defaults to other material indebtedness of the U.K. Subsidiaries. Substantially all of the U.K. Subsidiaries' assets are subject to security interests granted to lenders under the U.K. Credit Agreement. As of June 30, 2010, outstanding loans under the U.K. Credit Agreement amounted to £45,265 (\$67,621), including £7,059 (\$10,545) under the term loan. In July 2010, the Company amended the U.K. Credit Agreement in connection with a reorganization of our European operations.

***7.75% Senior Subordinated Notes***

In December 2006, the Company issued \$375,000 aggregate principal amount of 7.75% senior subordinated notes due 2016 (the "7.75% Notes"). The 7.75% Notes are unsecured senior subordinated notes and are subordinate to all existing and future senior debt, including debt under the Company's credit agreements, mortgages and floor plan indebtedness. The 7.75% Notes are guaranteed by substantially all of the Company's wholly-owned domestic subsidiaries on an unsecured senior subordinated basis. Those guarantees are full and unconditional and joint and several. The Company can redeem all or some of the 7.75% Notes at its option beginning in December 2011 at specified redemption prices, or prior to December 2011 at 100% of the principal amount of the notes plus an applicable "make-whole" premium, as defined. Upon certain sales of assets or specific kinds of changes of control, the Company is required to make an offer to purchase the 7.75% Notes. The 7.75% Notes also contain customary negative covenants and events of default. As of June 30, 2010, the Company was in compliance with all negative covenants and there were no events of default.

***Senior Subordinated Convertible Notes***

On January 31, 2006, the Company issued \$375,000 aggregate principal amount of 3.50% senior subordinated convertible notes due 2026 (the "Convertible Notes"), of which \$193,602 were outstanding at June 30, 2010. The

Convertible Notes mature on April 1, 2026, unless earlier converted, redeemed or purchased by the Company, as discussed below. The Convertible Notes are unsecured senior subordinated obligations and are subordinate to all future and existing senior debt, including debt under the Company's credit agreements, mortgages and floor plan indebtedness. The Convertible Notes are guaranteed on an unsecured senior subordinated basis by substantially all of the Company's wholly-owned domestic subsidiaries. Those guarantees are full and unconditional and joint and several. The Convertible Notes also contain customary negative covenants and events of default. As of June 30, 2010, the Company was in compliance with all negative covenants and there were no events of default.

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**PENSKE AUTOMOTIVE GROUP, INC.**

**NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS**

Holders of the Convertible Notes may convert them based on a conversion rate of 42.7796 shares of common stock per \$1,000 principal amount of the Convertible Notes (which is equal to a conversion price of approximately \$23.38 per share), subject to adjustment, only under the following circumstances: (1) in any quarterly period, if the closing price of the common stock for twenty of the last thirty trading days in the prior quarter exceeds \$28.05 (subject to adjustment), (2) for specified periods, if the trading price of the Convertible Notes falls below specific thresholds, (3) if the Convertible Notes are called for redemption, (4) if specified distributions to holders of common stock are made or specified corporate transactions occur, (5) if a fundamental change (as defined) occurs, or (6) during the ten trading days prior to, but excluding, the maturity date.

Upon conversion of the Convertible Notes, for each \$1,000 principal amount of the Convertible Notes, a holder will receive an amount in cash, equal to the lesser of (i) \$1,000 or (ii) the conversion value, determined in the manner set forth in the related indenture covering the Convertible Notes, of the number of shares of common stock equal to the conversion rate. If the conversion value exceeds \$1,000, the Company will also deliver, at its election, cash, common stock or a combination of cash and common stock with respect to the remaining value deliverable upon conversion. In the event of a conversion due to a change of control on or before April 6, 2011, the Company will, in certain circumstances, pay a make-whole premium by increasing the conversion rate used in that conversion. In addition, the Company will pay additional cash interest, commencing with six-month periods beginning on April 1, 2011, if the average trading price of a Convertible Note for certain periods in the prior six-month period equals 120% or more of the principal amount of the Convertible Notes. On or after April 6, 2011, the Company may redeem the Convertible Notes, in whole at any time or in part from time to time, for cash at a redemption price of 100% of the principal amount of the Convertible Notes to be redeemed, plus any accrued and unpaid interest to the applicable redemption date.

Holders of the Convertible Notes may require the Company to purchase all or a portion of their Convertible Notes for cash on each of April 1, 2011, April 1, 2016 or April 1, 2021 at a purchase price equal to 100% of the principal amount of the Convertible Notes to be purchased, plus accrued and unpaid interest, if any, to the applicable purchase date. Because the Company expects to be required to redeem the Convertible Notes in April 2011, it is reviewing alternatives to refinance or repay the Convertible Notes, which may include the issuance of additional securities. In the absence of a refinancing of the Convertible Notes, the Company expects to utilize cash flow from operations, working capital and availability under the U.S. Credit Agreement to repay the Convertible Notes. Based on the ability and intent to refinance any redemption or repayment of the Convertible Notes, the Company has classified them as long-term in the Consolidated Condensed Balance Sheet as of June 30, 2010. In the event the outstanding balance of the Convertible Notes exceeds or was expected to exceed the revolving capacity under the U.S. Credit Agreement, any such excess would have been classified as current.

In the second quarter of 2010, the Company repurchased \$41,548 principal amount of its outstanding Convertible Notes, which had a book value, net of debt discount, of \$40,013 for \$41,859. The Company allocated \$2,438 of the total consideration to the reacquisition of the equity component of the Convertible Notes. In connection with the transactions, the Company wrote off \$170 of unamortized deferred financing costs. As a result, the Company recorded a \$422 pre-tax gain in connection with the repurchases. In total during the first six months of 2010, the Company repurchased \$112,658 principal amount of its outstanding Convertible Notes, which had a book value, net of debt discount, of \$107,530 for \$113,603. The Company allocated \$7,667 of the total consideration to the reacquisition of the equity component of the Convertible Notes. In connection with the transactions, the Company wrote off \$567 of unamortized deferred financing costs. As a result, the Company has recorded an aggregate \$1,027 pre-tax gain in connection with the repurchases during 2010.

In the first quarter of 2009, the Company repurchased \$68,740 principal amount of its outstanding Convertible Notes, which had a book value, net of debt discount, of \$62,831 for \$51,425. In connection with the transaction, the Company wrote off \$672 of unamortized deferred financing costs and incurred \$305 of transaction costs. No element of the consideration was allocated to the reacquisition of the equity component because the consideration paid was less than the fair value of the liability component prior to extinguishment. As a result, the Company recorded a

\$10,429 pre-tax gain in connection with the repurchase.

The liability and equity components related to the Convertible Notes consist of the following:

	<b>June 30, 2010</b>	<b>December 31, 2009</b>
Carrying amount of the equity component	\$ 38,458	\$ 43,093
Principal amount of the liability component	\$ 193,602	\$ 306,260
Unamortized debt discount	6,445	16,916
Net carrying amount of the liability component	\$ 187,157	\$ 289,344

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**NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS**

The unamortized debt discount will be amortized as additional interest expense through April 1, 2011, the date the Company expects to be required to redeem the Convertible Notes. The annual effective interest rate on the liability component is 8.25%.

In July 2010, the Company repurchased an additional \$43,000 principal amount of the Convertible Notes for \$43,215. As a result, there is an aggregate of \$150,602 principal amount of the Convertible Notes currently outstanding.

***Mortgage Facilities***

The Company is party to several mortgages, including a \$42,400 mortgage facility with respect to certain of its dealership properties that matures on October 1, 2015. This facility bears interest at a defined rate, requires monthly principal and interest payments, and includes the option to extend the term for successive periods of five years up to a maximum term of twenty-five years. In the event the Company exercises its options to extend the term, the interest rate will be renegotiated at each renewal period. This mortgage facility also contains typical events of default, including non-payment of obligations, cross-defaults to the Company's other material indebtedness, certain change of control events, and the loss or sale of certain franchises operated at the property. Substantially all of the buildings, improvements, fixtures and personal property of the properties under the mortgage facility are subject to security interests granted to the lender. As of June 30, 2010, \$46,608 was outstanding under these facilities.

**8. Interest Rate Swaps**

The Company uses interest rate swaps to manage interest rate risk associated with the Company's variable rate floor plan debt. The Company is party to interest rate swap agreements through January 2011, pursuant to which the LIBOR portion of \$300,000 of the Company's floating rate floor plan debt was fixed at 3.67%. We may terminate these arrangements at any time, subject to the settlement of the then current fair value of the swap arrangements.

The Company designated \$290,000 of the swap agreements as cash flow hedges of future interest payments of LIBOR based U.S. floor plan borrowings and the effective portion of the gain or loss on that \$290,000 of the swap agreements is reported as a component of other comprehensive income and reclassified into earnings when the hedged transaction affects earnings. Settlements and changes in the fair value related to the undesignated \$10,000 of the swap agreements will be recorded as realized and unrealized gains/losses within interest expense.

The Company used Level 2 inputs to estimate the fair value of the interest rate swap agreements. As of June 30, 2010, the fair value of the swaps designated as hedging instruments was estimated to be a liability of \$5,729, which is recorded in accrued expenses. As of December 31, 2009, the fair value of the swaps designated as hedging instruments was estimated to be a liability of \$9,963, of which \$9,250 and \$713 were recorded in accrued expenses and other long-term liabilities, respectively. As of June 30, 2010, the fair value of the swaps not designated as hedging instruments was estimated to be a liability of \$198, which is recorded in accrued expenses. As of December 31, 2009, the fair value of the swaps not designated as hedging instruments was estimated to be a liability of \$344, of which \$319 and \$25 were recorded in accrued expenses and other long-term liabilities, respectively.

During the six months ended June 30, 2010, the Company recognized a net gain of \$1,328 related to the effective portion of the interest rate swap agreements designated as hedging instruments in accumulated other comprehensive income, and reclassified \$2,207 of the existing derivative losses from accumulated other comprehensive income into floor plan interest expense. During the six months ended June 30, 2009, the Company recognized a net gain of \$1,464 related to the effective portion of the interest rate swap agreements designated as hedging instruments in accumulated other comprehensive income, and reclassified \$4,894 of existing derivative losses from accumulated other comprehensive income into floor plan interest expense. The Company expects approximately \$4,248 associated with the swaps to be recognized as an increase of interest expense as the hedged interest payments become due through the swap agreement's maturity in January 2011. During the six months ended June 30, 2010 and 2009, the swaps increased the weighted average interest rate on the Company's floor plan borrowings by approximately 0.8% and 0.6%, respectively.

**9. Commitments and Contingent Liabilities**

The Company is involved in litigation which may relate to claims brought by governmental authorities, issues with customers and employment related matters, including class action claims and purported class action claims. As of

June 30, 2010, the Company is not party to any legal proceedings, including class action lawsuits, that individually or in the aggregate, are reasonably expected to have a material adverse effect on the Company's results of operations, financial condition or cash flows. However, the results of these matters cannot be predicted with certainty, and an unfavorable resolution of one or more of these matters could have a material adverse effect on the Company's results of operations, financial condition or cash flows.

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The Company has historically structured its operations so as to minimize ownership of real property. As a result, the Company leases or subleases substantially all of its facilities. These leases are generally for a period between five and 20 years, and are typically structured to include renewal options at the Company's election. Pursuant to the leases for some of the Company's larger facilities, the Company is required to comply with specified financial ratios, including a rent coverage ratio and a debt to EBITDA ratio, each as defined. For these leases, non-compliance with the ratios may require the Company to post collateral in the form of a letter of credit. A breach of the other lease covenants give rise to certain remedies by the landlord, the most severe of which include the termination of the applicable lease and acceleration of the total rent payments due under the lease. As of June 30, 2010, the Company was in compliance with all covenants under these leases.

The Company has sold a number of dealerships to third parties and, as a condition to certain of those sales, remains liable for the lease payments relating to the properties on which those businesses operate in the event of non-payment by the buyer. The Company is also party to lease agreements on properties that it no longer uses in its retail operations that it has sublet to third parties. The Company relies on subtenants to pay the associated rent and maintain the property at these locations. In the event the subtenant does not perform as expected, the Company may not be able to recover amounts owed to it and the Company could be required to fulfill these obligations.

The Company is potentially subject to additional purchase commitments pursuant to its smart distribution agreement, smart franchise agreement and state franchise laws in the event of franchise terminations, none of which have historically had a material adverse effect on its results of operations, financial condition or cash flows. The Company does not anticipate that the purchase commitments will have a material adverse effect on its future results of operations, financial condition or cash flows, although such an outcome is possible.

The Company has \$20,891 of letters of credit outstanding as of June 30, 2010, which are required by certain of our lenders and insurance providers. In addition, the Company has \$14,382 of surety bonds posted by dealerships in the ordinary course of business.

**10. Equity*****Comprehensive income (loss)***

Other comprehensive income (loss) includes foreign currency translation gains and losses, as well as changes relating to other immaterial items, including certain defined benefit plans in the U.K. and changes in the fair value of interest rate swap agreements, each of which has been excluded from net income and reflected in equity. Total comprehensive income (loss) is summarized as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	2009	2010	2009
Attributable to Penske Automotive Group:				
Net income	\$ 29,441	\$ 14,079	\$ 49,795	\$ 30,361
Other comprehensive income (loss):				
Foreign currency translation	(15,123)	52,357	(42,831)	54,565
Other	4,029	1,472	7,215	1,635
Total attributable to Penske Automotive Group	18,347	67,908	14,179	86,561
Attributable to the non-controlling interest:				
Net income	243	88	221	8
Total comprehensive income (loss)	\$ 18,590	\$ 67,996	\$ 14,400	\$ 86,569



In July 2010, the Company repurchased 68 shares at an average price of \$10.97 for a total of \$751.

**11. Segment Information**

The Company's operations are organized by management into operating segments by line of business and geography. The Company has determined it has three reportable segments as defined in general accounting principles for segment reporting, including: (i) Retail, consisting of our automotive retail operations, (ii) Distribution, consisting of our distribution of the smart fortwo vehicle, parts and accessories in the U.S. and Puerto Rico and (iii) PAG Investments, consisting of our investments in non-automotive retail operations. The Retail reportable segment includes all automotive dealerships and all departments relevant to the operation of the dealerships. The individual dealership operations included in the Retail reportable segment have been grouped into five geographic operating segments, which have been aggregated into one reportable segment as their operations (A) have similar economic characteristics (all are automotive dealerships having similar margins), (B) offer similar products and services (all sell new and used vehicles, service, parts and third-party finance and insurance products), (C) have similar target markets and customers (generally individuals) and (D) have similar distribution and marketing practices (all distribute products and services through dealership facilities that market to customers in similar fashions).

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The following table summarizes revenues and income from continuing operations before certain non-recurring items and income taxes, which is the measure by which management allocates resources to its segments, and which we refer to as adjusted segment income, for each of our reportable segments. Adjusted segment income excludes the item in the table below in order to enhance the comparability of segment income from period to period.

Three Months Ended June 30

	Retail	Distribution	PAG Investments	Intersegment Elimination	Total
Revenues					
2010	\$ 2,684,068	\$ 32,063	\$	\$ (12,443)	\$ 2,703,688
2009	2,265,625	58,878		(5,808)	2,318,695
Adjusted segment income					
2010	44,294	(3,610)	4,103	(181)	44,606
2009	26,802	967	2,520	(59)	30,230

Six Months Ended June 30

	Retail	Distribution	PAG Investments	Intersegment Elimination	Total
Revenues					
2010	\$ 5,162,123	\$ 47,187	\$	\$ (19,943)	\$ 5,189,367
2009	4,343,812	147,509		(14,326)	4,476,995
Adjusted segment income					
2010	83,030	(9,202)	3,597	(264)	77,161
2009	35,660	7,272	3,126	(222)	45,836

The following table reconciles total adjusted segment income to consolidated income from continuing operations before income taxes for the three and six month periods ended June 30, 2010 and 2009.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	2009	2010	2009
Adjusted segment income	\$ 44,606	\$ 30,230	\$ 77,161	\$ 45,836
Gain on debt repurchase	422		1,027	10,429
Income from continuing operations before income taxes	\$ 45,028	\$ 30,230	\$ 78,188	\$ 56,265

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The following tables include consolidating condensed financial information as of June 30, 2010 and December 31, 2009 and for the three and six month periods ended June 30, 2010 and 2009 for Penske Automotive Group, Inc. (as the issuer of the Convertible Notes and the 7.75% Notes), guarantor subsidiaries and non-guarantor subsidiaries (primarily representing foreign entities). The condensed consolidating financial information includes certain allocations of balance sheet, income statement and cash flow items which are not necessarily indicative of the financial position, results of operations or cash flows of these entities on a stand-alone basis.

**CONSOLIDATING CONDENSED BALANCE SHEET**  
**June 30, 2010**

	<b>Total Company</b>	<b>Eliminations</b>	<b>Penske Automotive Group, Inc. (In thousands)</b>	<b>Guarantor Subsidiaries</b>	<b>Non-Guarantor Subsidiaries</b>
Cash and cash equivalents	\$ 17,664	\$	\$	\$ 13,540	\$ 4,124
Accounts receivable, net	351,013	(250,655)	250,655	206,509	144,504
Inventories	1,364,718			850,026	514,692
Other current assets	106,479		863	66,670	38,946
Assets held for sale	572			572	
<b>Total current assets</b>	<b>1,840,446</b>	<b>(250,655)</b>	<b>251,518</b>	<b>1,137,317</b>	<b>702,266</b>
Property and equipment, net	707,832		5,024	449,485	253,323
Intangible assets	994,947			572,940	422,007
Equity method investments	280,847		232,015		48,832
Other long-term assets	14,591	(1,241,648)	1,245,377	9,252	1,610
<b>Total assets</b>	<b>\$ 3,838,663</b>	<b>\$ (1,492,303)</b>	<b>\$ 1,733,934</b>	<b>\$ 2,168,994</b>	<b>\$ 1,428,038</b>
Floor plan notes payable	\$ 818,339	\$	\$	\$ 501,158	\$ 317,181
Floor plan notes payable non-trade	499,410		29,900	300,139	169,371
Accounts payable	209,535		1,994	82,788	124,753
Accrued expenses	218,716	(250,655)	1,149	125,777	342,445
Current portion of long-term debt	16,551			1,239	15,312
Liabilities held for sale	501			501	
<b>Total current liabilities</b>	<b>1,763,052</b>	<b>(250,655)</b>	<b>33,043</b>	<b>1,011,602</b>	<b>969,062</b>
Long-term debt	844,292	(59,194)	739,157	50,087	114,242
Deferred tax liabilities	159,872			148,563	11,309
Other long-term liabilities	109,713			92,416	17,297

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Total liabilities	2,876,929	(309,849)	772,200	1,302,668	1,111,910
Total equity	961,734	(1,182,454)	961,734	866,326	316,128
Total liabilities and equity	\$ 3,838,663	\$ (1,492,303)	\$ 1,733,934	\$ 2,168,994	\$ 1,428,038

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**PENSKE AUTOMOTIVE GROUP, INC.**  
**NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS**  
**CONSOLIDATING CONDENSED BALANCE SHEET**  
**December 31, 2009**

	<b>Total Company</b>	<b>Eliminations</b>	<b>Penske Automotive Group, Inc. (In thousands)</b>	<b>Guarantor Subsidiaries</b>	<b>Non-Guarantor Subsidiaries</b>
Cash and cash equivalents	\$ 13,999	\$	\$	\$ 12,344	\$ 1,655
Accounts receivable, net	321,226	(230,299)	230,299	195,748	125,478
Inventories	1,302,495			776,887	525,608
Other current assets	95,426		1,725	61,640	32,061
Assets held for sale	10,625			10,625	
<b>Total current assets</b>	<b>1,743,771</b>	<b>(230,299)</b>	<b>232,024</b>	<b>1,057,244</b>	<b>684,802</b>
Property and equipment, net	726,808		6,007	450,116	270,685
Intangible assets	1,011,803			570,282	441,521
Equity method investments	295,473		231,897		63,576
Other long-term assets	18,152	(1,287,938)	1,293,067	10,848	2,175
<b>Total assets</b>	<b>\$ 3,796,007</b>	<b>\$ (1,518,237)</b>	<b>\$ 1,762,995</b>	<b>\$ 2,088,490</b>	<b>\$ 1,462,759</b>
Floor plan notes payable	\$ 769,657	\$	\$	\$ 448,069	\$ 321,588
Floor plan notes payable non-trade	423,316			254,807	168,509
Accounts payable	189,989		3,268	74,610	112,111
Accrued expenses	227,294	(230,299)	344	111,800	345,449
Current portion of long-term debt	12,442			1,033	11,409
Liabilities held for sale	7,675			7,675	
<b>Total current liabilities</b>	<b>1,630,373</b>	<b>(230,299)</b>	<b>3,612</b>	<b>897,994</b>	<b>959,066</b>
Long-term debt	933,966	(59,706)	813,344	43,066	137,262
Deferred tax liabilities	157,500			145,551	11,949
Other long-term liabilities	128,129			123,154	4,975
<b>Total liabilities</b>	<b>2,849,968</b>	<b>(290,005)</b>	<b>816,956</b>	<b>1,209,765</b>	<b>1,113,252</b>
Total equity	946,039	(1,228,232)	946,039	878,725	349,507
<b>Total liabilities and equity</b>	<b>\$ 3,796,007</b>	<b>\$ (1,518,237)</b>	<b>\$ 1,762,995</b>	<b>\$ 2,088,490</b>	<b>\$ 1,462,759</b>



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**PENSKE AUTOMOTIVE GROUP, INC.**  
**NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS**  
**CONSOLIDATING CONDENSED STATEMENT OF INCOME**  
**Three Months Ended June 30, 2010**

	<b>Total</b>		<b>Penske</b>	<b>Guarantor</b>	<b>Non-Guarantor</b>
	<b>Company</b>	<b>Eliminations</b>	<b>Automotive</b>	<b>Subsidiaries</b>	<b>Subsidiaries</b>
			<b>Group,</b>		
			<b>Inc.</b>		
			<b>(In thousands)</b>		
Revenues	\$ 2,703,688	\$	\$	\$ 1,618,487	\$ 1,085,201
Cost of sales	2,273,344			1,347,980	925,364
Gross profit	430,344			270,507	159,837
Selling, general, and administrative expenses	355,177		3,494	225,414	126,269
Depreciation	12,054		300	6,984	4,770
Operating income (loss)	63,113		(3,794)	38,109	28,798
Floor plan interest expense	(8,321)			(6,167)	(2,154)
Other interest expense	(12,542)		(8,343)	(33)	(4,166)
Debt discount amortization	(2,428)		(2,428)		
Equity in earnings of affiliates	4,784		3,937		847
Gain on debt repurchase	422		422		
Equity in earnings of subsidiaries		(54,991)	54,991		
Income from continuing operations before income taxes	45,028	(54,991)	44,785	31,909	23,325
Income taxes	(15,625)	19,186	(15,625)	(12,548)	(6,638)
Income from continuing operations	29,403	(35,805)	29,160	19,361	16,687
Loss from discontinued operations, net of tax	281	(281)	281	281	
Net income	29,684	(36,086)	29,441	19,642	16,687
Less: Income attributable to the non-controlling interests	243				243
Net income attributable to Penske Automotive Group	\$ 29,441	\$ (36,086)	\$ 29,441	\$ 19,642	\$ 16,444

common stockholders



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**PENSKE AUTOMOTIVE GROUP, INC.**  
**NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS**  
**CONSOLIDATING CONDENSED STATEMENT OF INCOME**  
**Three Months Ended June 30, 2009**

	<b>Total</b>		<b>Penske</b>	<b>Guarantor</b>	<b>Non-Guarantor</b>
	<b>Company</b>	<b>Eliminations</b>	<b>Automotive</b>	<b>Subsidiaries</b>	<b>Subsidiaries</b>
			<b>Group,</b>		
			<b>Inc.</b>		
			<b>(In thousands)</b>		
Revenues	\$ 2,318,695	\$	\$	\$ 1,374,689	\$ 944,006
Cost of sales	1,924,940			1,133,537	791,403
Gross profit	393,755			241,152	152,603
Selling, general, and administrative expenses	327,389		6,229	201,348	119,812
Depreciation	13,811		290	8,636	4,885
Operating income (loss)	52,555		(6,519)	31,168	27,906
Floor plan interest expense	(8,969)			(6,233)	(2,736)
Other interest expense	(13,687)		(10,754)	(35)	(2,898)
Debt discount amortization	(3,135)		(3,135)		
Equity in income of affiliates	3,466		2,381		1,085
Equity in earnings of subsidiaries		(48,169)	48,169		
Income from continuing operations before income taxes	30,230	(48,169)	30,142	24,900	23,357
Income taxes	(10,329)	16,512	(10,329)	(9,894)	(6,618)
Income from continuing operations	19,901	(31,657)	19,813	15,006	16,739
Loss from discontinued operations, net of tax	(5,734)	5,734	(5,734)	(3,369)	(2,365)
Net income	14,167	(25,923)	14,079	11,637	14,374
Less: Income attributable to the non-controlling interests	88				88
Net income attributable to Penske Automotive Group common stockholders	\$ 14,079	\$ (25,923)	\$ 14,079	\$ 11,637	\$ 14,286



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**PENSKE AUTOMOTIVE GROUP, INC.**  
**NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS**  
**CONSOLIDATING CONDENSED STATEMENT OF INCOME**  
**Six Months Ended June 30, 2010**

	<b>Total</b>		<b>Penske</b>	<b>Guarantor</b>	<b>Non-Guarantor</b>
	<b>Company</b>	<b>Eliminations</b>	<b>Automotive</b>	<b>Subsidiaries</b>	<b>Subsidiaries</b>
			<b>Group,</b>		
			<b>Inc.</b>		
			<b>(In thousands)</b>		
Revenues	\$ 5,189,367	\$	\$	\$ 3,006,952	\$ 2,182,415
Cost of sales	4,348,995			2,494,595	1,854,400
Gross profit	840,372			512,357	328,015
Selling, general, and administrative expenses	695,691		8,087	433,106	254,498
Depreciation	24,428		590	13,944	9,894
Operating income (loss)	120,253		(8,677)	65,307	63,623
Floor plan interest expense	(16,842)			(12,228)	(4,614)
Other interest expense	(25,262)		(16,390)	(589)	(8,283)
Debt discount amortization	(5,343)		(5,343)		
Equity in earnings of affiliates	4,355		4,283		72
Gain on debt repurchase	1,027		1,027		
Equity in earnings of subsidiaries		(103,067)	103,067		
Income from continuing operations before income taxes	78,188	(103,067)	77,967	52,490	50,798
Income taxes	(28,060)	37,093	(28,060)	(22,948)	(14,145)
Income from continuing operations	50,128	(65,974)	49,907	29,542	36,653
Loss from discontinued operations, net of tax	(112)	112	(112)	(112)	
Net income	50,016	(65,862)	49,795	29,430	36,653
Less: Income attributable to the non-controlling interests	221				221
Net income attributable to Penske Automotive Group	\$ 49,795	\$ (65,862)	\$ 49,795	\$ 29,430	\$ 36,432

common stockholders

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**PENSKE AUTOMOTIVE GROUP, INC.**  
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**CONSOLIDATING CONDENSED STATEMENT OF INCOME**  
**Six Months Ended June 30, 2009**

	<b>Total</b>		<b>Penske</b>	<b>Guarantor</b>	<b>Non-Guarantor</b>
	<b>Company</b>	<b>Eliminations</b>	<b>Automotive</b>	<b>Subsidiaries</b>	<b>Subsidiaries</b>
			<b>Group,</b>		
			<b>Inc.</b>		
			<b>(In thousands)</b>		
Revenues	\$ 4,476,995	\$	\$	\$ 2,645,760	\$ 1,831,235
Cost of sales	3,715,201			2,179,823	1,535,378
Gross profit	761,794			465,937	295,857
Selling, general, and administrative expenses	640,055		9,547	398,390	232,118
Depreciation	26,692		580	16,924	9,188
Operating income (loss)	95,047		(10,127)	50,623	54,551
Floor plan interest expense	(18,431)			(12,471)	(5,960)
Other interest expense	(28,187)		(22,226)	(64)	(5,897)
Debt discount amortization	(6,773)		(6,773)		
Equity in earnings of affiliates	4,180		2,964		1,216
Gain on debt repurchase	10,429		10,429		
Equity in earnings of subsidiaries		(81,990)	81,990		
Income from continuing operations before income taxes	56,265	(81,990)	56,257	38,088	43,910
Income taxes	(20,074)	29,269	(20,074)	(16,978)	(12,291)
Income from continuing operations	36,191	(52,721)	36,183	21,110	31,619
Loss from discontinued operations, net of tax	(5,822)	5,822	(5,822)	(3,465)	(2,357)
Net income	30,369	(46,899)	30,361	17,645	29,262
Less: Income attributable to the non-controlling interests	8				8
Net income attributable to Penske Automotive Group	\$ 30,361	\$ (46,899)	\$ 30,361	\$ 17,645	\$ 29,254

common stockholders

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**PENSKE AUTOMOTIVE GROUP, INC.**  
**NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS**  
**CONSOLIDATING CONDENSED STATEMENT OF CASH FLOWS**  
**Six Months Ended June 30, 2010**

	<b>Total Company</b>	<b>Penske Automotive Group, Inc.</b>	<b>Guarantor Subsidiaries</b>	<b>Non-Guarantor Subsidiaries</b>
	(In thousands)			
Net cash from continuing operating activities	\$ 69,593	\$ 55,493	\$ (23,636)	\$ 37,736
Investing activities:				
Purchase of property and equipment	(37,622)		(27,809)	(9,813)
Dealership acquisitions, net	(12,277)		(12,277)	
Other			83	(83)
Net cash from continuing investing activities	(49,899)		(40,003)	(9,896)
Financing activities:				
Proceeds from borrowings under U.S. credit agreement revolving credit line	320,600	320,600		
Repayment under U.S. credit agreement revolving credit line	(292,600)	(292,600)		
Net borrowings (repayments) of long-term debt	(9,497)		7,739	(17,236)
Repurchase 3.5% senior subordinated convertible notes	(113,604)	(113,604)		
Proceeds from exercises of options, including excess tax benefit	211	211		
Net (repayments) borrowings of floor plan notes payable non-trade	76,094	29,900	53,856	(7,662)
Distributions from (to) parent			473	(473)
Net cash from continuing financing activities	(18,796)	(55,493)	62,068	(25,371)
Net cash from discontinued operations	2,767		2,767	
Net change in cash and cash equivalents	3,665		1,196	2,469
Cash and cash equivalents, beginning of period	13,999		12,344	1,655
Cash and cash equivalents, end of period	\$ 17,664	\$	\$ 13,540	\$ 4,124





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**PENSKE AUTOMOTIVE GROUP, INC.**  
**NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS**  
**CONSOLIDATING CONDENSED STATEMENT OF CASH FLOWS**  
**Six Months Ended June 30, 2009**

	<b>Total</b>	<b>Penske</b>	<b>Guarantor</b>	<b>Non-Guarantor</b>
	<b>Company</b>	<b>Automotive</b>	<b>Subsidiaries</b>	<b>Subsidiaries</b>
		<b>Group,</b>		
		<b>Inc.</b>		
		<b>(In thousands)</b>		
Net cash from continuing operating activities	\$ 241,105	\$ 49,940	\$ 50,923	\$ 140,242
Investing activities:				
Purchase of property and equipment	(43,979)		(26,223)	(17,756)
Dealership acquisitions, net	(8,610)		(690)	(7,920)
Other	12,679	11,485		1,194
Net cash from continuing investing activities	(39,910)	11,485	(26,913)	(24,482)
Financing activities:				
Repayments under U.S. credit agreement term loan	(10,000)	(10,000)		
Repurchase 3.5% senior subordinated convertible notes	(51,425)	(51,425)		
Net borrowings (repayments) of long-term debt	(47,768)		(8,080)	(39,688)
Net (repayments) borrowings of floor plan notes payable non-trade	(78,608)		(6,863)	(71,745)
Distributions from (to) parent			20	(20)
Net cash from continuing financing activities	(187,801)	(61,425)	(14,923)	(111,453)
Net cash from discontinued operations	(10,333)		(6,689)	(3,644)
Net change in cash and cash equivalents	3,061		2,398	663
Cash and cash equivalents, beginning of period	17,108		14,126	2,982
Cash and cash equivalents, end of period	\$ 20,169	\$	\$ 16,524	\$ 3,645



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

*This Management's Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements that involve risks and uncertainties. Our actual results may differ materially from those discussed in the forward-looking statements as a result of various factors, including those discussed in Forward Looking Statements. We have acquired and initiated a number of businesses since inception. Our financial statements include the results of operations of those businesses from the date acquired or when they commenced operations. This Management's Discussion and Analysis of Financial Condition and Results of Operations has been updated to reflect the revision of our financial statements for entities which have been treated as discontinued operations through June 30, 2010.*

**Overview**

We are the second largest automotive retailer headquartered in the U.S. as measured by total revenues. As of June 30, 2010, we owned and operated 171 franchises in the U.S. and 152 franchises outside of the U.S., primarily in the U.K. We offer a full range of vehicle brands with 95% of our total retail revenue in 2010 generated from brands of non-U.S. based manufacturers, and 64% generated from premium brands, such as Audi, BMW, Cadillac, Mercedes-Benz and Porsche. Each of our dealerships offer a wide selection of new and used vehicles for sale. In addition to selling new and used vehicles, we generate higher-margin revenue at each of our dealerships through maintenance and repair services and the sale and placement of higher-margin products, such as third party finance and insurance products, third-party extended service contracts and replacement and aftermarket automotive products. We are also diversified geographically, with 65% of our total revenues in 2010 generated by operations in the U.S. and Puerto Rico and 35% generated from our operations outside the U.S. (predominately in the U.K.).

We are also, through smart USA Distributor, LLC ( smart USA ), a wholly-owned subsidiary, the exclusive distributor of the smart fortwo vehicle in the U.S. and Puerto Rico. The smart fortwo is manufactured by Mercedes-Benz Cars and is a Daimler brand. This technologically advanced vehicle achieves more than 40 miles per gallon on the highway and is an ultra-low emissions vehicle as certified by the State of California Air Resources Board. As of June 30, 2010, smart USA has certified a network of more than 75 smart dealerships, ten of which are owned and operated by us. The smart fortwo offers five different versions, the *pure*, *passion coupe*, *passion cabriolet*, *BRABUS coupe* and *BRABUS cabriolet*, with base retail prices currently ranging from \$11,990 to \$20,990. smart USA wholesaled 2,996 and 9,373 smart fortwo vehicles during the six months ended June 30, 2010 and 2009, respectively.

We also hold a 9.0% limited partnership interest in Penske Truck Leasing Co., L.P. ( PTL ), a leading global transportation services provider. PTL operates and maintains more than 200,000 vehicles and serves customers in North America, South America, Europe and Asia. Product lines include full-service leasing, contract maintenance, commercial and consumer truck rental and logistics services, including, transportation and distribution center management and supply chain management. The general partner of PTL is Penske Truck Leasing Corporation, a wholly-owned subsidiary of Penske Corporation, which together with other wholly-owned subsidiaries of Penske Corporation, owns 41.1% of PTL. The remaining 49.9% of PTL is owned by GE Capital.

**Outlook**

Since September 2008, general economic conditions have impacted consumer traffic, vehicle sales and vehicle service work at our dealerships. While we have experienced increased sales in the six months ended June 30 when compared with the prior year, volumes are still below historical levels. We believe general economic conditions, while improving, will continue to impact traffic and sales in the markets in which we operate throughout 2010.

**Operating Overview**

New and used vehicle revenues include sales to retail customers and to leasing companies providing consumer automobile leasing. We generate finance and insurance revenues from sales of third-party extended service contracts, sales of third-party insurance policies, commissions relating to the sale of finance and lease contracts to third parties and the sales of certain other products. Service and parts revenues include fees paid for repair, maintenance and collision services, and the sale of replacement parts and other aftermarket accessories. During the three and six months ended June 30, 2010, we experienced year over year increases in same store new and used retail unit sales, resulting in retail revenue growth, including finance and insurance revenues. Our same store service and parts business also experienced a benefit during these periods due to Toyota recall activity.

Our gross profit tends to vary with the mix of revenues we derive from the sale of new vehicles, used vehicles, finance and insurance products, service and parts transactions, and the distribution of the smart fortwo. Our gross profit varies across product lines, with vehicle sales usually resulting in lower gross profit margins and our other revenues resulting in higher gross profit margins. Factors such as inventory and vehicle availability, customer demand, consumer confidence, unemployment, general economic conditions, seasonality, weather, credit availability, fuel prices and manufacturers' advertising and incentives may impact the mix of our revenues, and therefore influence our gross profit margin. Aggregate gross profit increased \$36.6 million, or 9.3%, and \$78.6 million, or 10.3%, during the three and six month periods, respectively, as compared to the same periods of the prior year. The increase in gross profit is largely attributable to increases in new and used unit sales and related finance and insurance sales. Our retail gross margin percentage declined from 17.9% during the three months ended June 30, 2009 to 17.0% during the three months ended June 30, 2010 and declined from 17.9% during the six months ended June 30, 2009 to 17.2% during the six months ended June 30, 2010, due primarily to an increase in the percentage of our revenues generated by lower margin vehicle sales.

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Our selling expenses consist of advertising and compensation for sales personnel, including commissions and related bonuses. General and administrative expenses include compensation for administration, finance, legal and general management personnel, rent, insurance, utilities and other outside services. A significant portion of our selling expenses are variable, and we believe a significant portion of our general and administrative expenses are subject to our control, allowing us to adjust them over time to reflect economic trends. Our selling, general, and administrative expenses increased on a same store basis, due in large part to increases in variable compensation as a result of the increase in same store retail gross profit versus the prior year and cost of living increases relating to our lease agreements. However, selling, general and administrative expenses as a percentage of gross profit decreased by 61 basis points to 82.5% in the second quarter of 2010 as compared to the prior year.

Floor plan interest expense relates to financing incurred in connection with the acquisition of new and used vehicle inventories that is secured by those vehicles. Other interest expense consists of interest charges on all of our interest-bearing debt, other than interest relating to floor plan financing. The cost of our variable rate indebtedness is based on the prime rate, defined London Interbank Offered Rate ( LIBOR ), the Bank of England Base Rate, the Finance House Base Rate, or the Euro Interbank Offered Rate. Our floor plan and other interest expenses have decreased during the three and six months ended June 30, 2010 as a result of decreases in average floor plan balances outstanding, term loan repayments and repurchases of our 3.5% senior subordinated convertible notes.

Equity in earnings of affiliates represents our share of the earnings from our investments in joint ventures and other non-consolidated investments, including PTL. It is our expectation that operating conditions as outlined above in the Outlook section will similarly impact these businesses throughout 2010.

The future success of our business will likely be dependent on, among other things, general economic and industry conditions, our ability to consummate and integrate acquisitions, the level of vehicle sales in our markets, our ability to increase sales of higher margin products, especially service and parts services, our ability to realize returns on our significant capital investment in new and upgraded dealership facilities, the success of our distribution business, and the return realized from our investments in various joint ventures and other non-consolidated investments. See

Forward-Looking Statements.

**Critical Accounting Policies and Estimates**

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires the application of accounting policies that often involve making estimates and employing judgments. Such judgments influence the assets, liabilities, revenues and expenses recognized in our financial statements. Management, on an ongoing basis, reviews these estimates and assumptions. Management may determine that modifications in assumptions and estimates are required, which may result in a material change in our results of operations or financial position.

The following are the accounting policies applied in the preparation of our financial statements that management believes are most dependent upon the use of estimates and assumptions.

***Revenue Recognition******Vehicle, Parts and Service Sales***

We record revenue when vehicles are delivered and title has passed to the customer, when vehicle service or repair work is completed and when parts are delivered to our customers. Sales promotions that we offer to customers are accounted for as a reduction of revenues at the time of sale. Rebates and other incentives offered directly to us by manufacturers are recognized as a reduction of cost of sales. Reimbursements of qualified advertising expenses are treated as a reduction of selling, general and administrative expenses. The amounts received under certain manufacturer rebate and incentive programs are based on the attainment of program objectives, and such earnings are recognized either upon the sale of the vehicle for which the award was received, or upon attainment of the particular program goals if not associated with individual vehicles. During the six months ended June 30, 2010 and 2009, we earned \$170.7 million and \$145.6 million, respectively, of rebates, incentives and reimbursements from manufacturers, of which \$166.6 million and \$143.3 million was recorded as a reduction of cost of sales.

***Finance and Insurance Sales***

Subsequent to the sale of a vehicle to a customer, we sell our installment sale contracts to various financial institutions on a non-recourse basis (with specified exceptions) to mitigate the risk of default. We receive a commission from the

lender equal to either the difference between the interest rate charged to the customer and the interest rate set by the financing institution or a flat fee. We also receive commissions for facilitating the sale of various third-party insurance products to customers, including credit and life insurance policies and extended service contracts. These commissions are recorded as revenue at the time the customer enters into the contract.

**Table of Contents*****Impairment Testing***

Franchise value impairment is assessed as of October 1 every year and upon the occurrence of an indicator of impairment through a comparison of its carrying amount and estimated fair value. An indicator of impairment exists if the carrying value of a franchise exceeds its estimated fair value and an impairment loss may be recognized up to that excess. The fair value of franchise value is determined using a discounted cash flow approach, which includes assumptions that include revenue and profitability growth, franchise profit margins, and our cost of capital. We also evaluate our franchise agreements in connection with the annual impairment testing to determine whether events and circumstances continue to support our assessment that the franchise agreements have an indefinite life.

Goodwill impairment is assessed at the reporting unit level as of October 1 every year and upon the occurrence of an indicator of impairment. We have determined that the dealerships in each of our operating segments within the Retail reportable segment are components that are aggregated into five geographical reporting units for the purpose of goodwill impairment testing, as they (A) have similar economic characteristics (all are automotive dealerships having similar margins), (B) offer similar products and services (all sell new and used vehicles, service, parts and third-party finance and insurance products), (C) have similar target markets and customers (generally individuals) and (D) have similar distribution and marketing practices (all distribute products and services through dealership facilities that market to customers in similar fashions). There is no goodwill recorded in our Distribution or PAG Investments reportable segments. An indicator of goodwill impairment exists if the carrying amount of the reporting unit, including goodwill, is determined to exceed its estimated fair value. The fair value of goodwill is determined using a discounted cash flow approach, which includes assumptions that include revenue and profitability growth, franchise profit margins, residual values and our cost of capital. If an indication of goodwill impairment exists, an analysis reflecting the allocation of the fair value of the reporting unit to all assets and liabilities, including previously unrecognized intangible assets, is performed. The impairment is measured by comparing the implied fair value of the reporting unit goodwill with its carrying amount and an impairment loss may be recognized up to any excess of the carrying value over the implied fair value.

***Investments***

We account for each of our investments under the equity method, pursuant to which we record our proportionate share of the investee's income each period. The net book value of our investments was \$280.8 million and \$295.5 million as of June 30, 2010 and December 31, 2009, respectively. Investments for which there is not a liquid, actively traded market are reviewed periodically by management for indicators of impairment. If an indicator of impairment were to be identified, management estimates the fair value of the investment using a discounted cash flow approach, which includes assumptions relating to revenue and profitability growth, profit margins, residual values and our cost of capital. Declines in investment values that are deemed to be other than temporary may result in an impairment charge reducing the investments' carrying value to fair value.

***Self-Insurance***

We retain risk relating to certain of our general liability insurance, workers' compensation insurance, auto physical damage insurance, property insurance, employment practices liability insurance, directors and officers insurance and employee medical benefits in the U.S. As a result, we are likely to be responsible for a significant portion of the claims and losses incurred under these programs. The amount of risk we retain varies by program, and, for certain exposures, we have pre-determined maximum loss limits for certain individual claims and/or insurance periods. Losses, if any, above the pre-determined loss limits are paid by third-party insurance carriers. Our estimate of future losses is prepared by management using our historical loss experience and industry-based development factors. Aggregate reserves relating to retained risk were \$23.8 million and \$21.5 million as of June 30, 2010 and December 31, 2009, respectively. Changes in the reserve estimate during 2010 relate primarily to current year activity in our general liability and workers compensation programs.

***Income Taxes***

Tax regulations may require items to be included in our tax returns at different times than the items are reflected in our financial statements. Some of these differences are permanent, such as expenses that are not deductible on our tax return, and some are temporary differences, such as the timing of depreciation expense. Temporary differences create deferred tax assets and liabilities. Deferred tax assets generally represent items that will be used as a tax deduction or

credit in our tax returns in future years which we have already recorded in our financial statements. Deferred tax liabilities generally represent deductions taken on our tax returns that have not yet been recognized as expense in our financial statements. We establish valuation allowances for our deferred tax assets if the amount of expected future taxable income is not likely to allow for the use of the deduction or credit. A valuation allowance of \$7.7 million has been recorded relating to net operating losses and credit carryforwards in the U.S. based on our determination that it is more likely than not that they will not be utilized.



**Table of Contents*****Classification of Franchises in Continuing and Discontinued Operations***

We classify the results of our operations in our consolidated financial statements based on general accounting principles for discontinued operations, which requires judgment in determining whether a franchise will be reported within continuing or discontinued operations. Such judgments include whether a franchise will be divested, the period required to complete the divestiture, and the likelihood of changes to the divestiture plans. If we determine that a franchise should be either reclassified from continuing operations to discontinued operations or from discontinued operations to continuing operations, our consolidated financial statements for prior periods are revised to reflect such reclassification.

**Results of Operations**

The following tables present comparative financial data relating to our operating performance in the aggregate and on a same store basis. Dealership results are only included in same store comparisons when we have consolidated the acquired entity during the entirety of both periods being compared. As an example, if a dealership was acquired on January 15, 2008, the results of the acquired entity would be included in annual same store comparisons beginning with the year ended December 31, 2010 and in quarterly same store comparisons beginning with the quarter ended June 30, 2009.

***Three Months Ended June 30, 2010 Compared to Three Months Ended June 30, 2009 (dollars in millions, except per unit amounts)*****New Vehicle Data**

	<b>2010 vs. 2009</b>			
	<b>2010</b>	<b>2009</b>	<b>Change</b>	<b>% Change</b>
New retail unit sales	39,676	33,176	6,500	19.6%
Same store new retail unit sales	38,091	33,140	4,951	14.9%
New retail sales revenue	\$ 1,355.8	\$ 1,090.1	\$ 265.7	24.4%
Same store new retail sales revenue	\$ 1,301.7	\$ 1,088.4	\$ 213.3	19.6%
New retail sales revenue per unit	\$ 34,172	\$ 32,859	\$ 1,313	4.0%
Same store new retail sales revenue per unit	\$ 34,175	\$ 32,841	\$ 1,334	4.1%
Gross profit new	\$ 111.2	\$ 86.0	\$ 25.2	29.3%
Same store gross profit new	\$ 106.3	\$ 85.8	\$ 20.5	23.9%
Average gross profit per new vehicle retailed	\$ 2,802	\$ 2,591	\$ 211	8.1%
Same store average gross profit per new vehicle retailed	\$ 2,791	\$ 2,588	\$ 203	7.8%
Gross margin % new	8.2%	7.9%	0.3%	3.8%
Same store gross margin % new	8.2%	7.9%	0.3%	3.8%

**Units**

Retail unit sales of new vehicles increased 6,500 units, or 19.6%, from 2009 to 2010. The increase is due a 4,951 unit, or 14.9%, increase in same store retail unit sales during the period, coupled with a 1,549 unit increase from net dealership acquisitions. The same store increase was due primarily to unit sales increases in our volume foreign brand stores in the U.S. and premium brand stores in the U.S. and U.K., and reflect the improved consumer confidence levels and credit availability in 2010 compared to the prior year.

**Revenues**

New vehicle retail sales revenue increased \$265.7 million, or 24.4%, from 2009 to 2010. The increase is due to a \$213.3 million, or 19.6%, increase in same store revenues, coupled with a \$52.4 million increase from net dealership acquisitions. The same store revenue increase is due primarily to the 14.9% increase in retail unit sales, which increased revenue by \$169.2 million, coupled with a \$1,334, or 4.1%, increase in average selling prices per unit which increased revenue by \$44.1 million.

**Gross Profit**

Retail gross profit from new vehicle sales increased \$25.2 million, or 29.3%, from 2009 to 2010. The increase is due to a \$20.5 million, or 23.9%, increase in same store gross profit, coupled with a \$4.7 million increase from net

dealership acquisitions. The same store increase is due primarily to the 14.9% increase in retail unit sales, which increased gross profit by \$13.8 million, coupled with a \$203, or 7.8%, increase in the average gross profit per new vehicle retailed, which increased gross profit by \$6.7 million.

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	<b>2010 vs. 2009</b>			
	<b>2010</b>	<b>2009</b>	<b>Change</b>	<b>% Change</b>
Used retail unit sales	29,232	26,100	3,132	12.0%
Same store used retail unit sales	28,239	26,070	2,169	8.3%
Used retail sales revenue	\$ 749.7	\$ 658.8	\$ 90.9	13.8%
Same store used retail sales revenue	\$ 727.4	\$ 657.9	\$ 69.5	10.6%
Used retail sales revenue per unit	\$ 25,645	\$ 25,241	\$ 404	1.6%
Same store used retail sales revenue per unit	\$ 25,760	\$ 25,237	\$ 523	2.1%
Gross profit used	\$ 60.1	\$ 59.3	\$ 0.8	1.3%
Same store gross profit used	\$ 59.1	\$ 59.2	\$ (0.1)	(0.2%)
Average gross profit per used vehicle retailed	\$ 2,056	\$ 2,271	\$ (215)	(9.5%)
Same store average gross profit per used vehicle retailed	\$ 2,095	\$ 2,272	\$ (177)	(7.8%)
Gross margin % used	8.0%	9.0%	(1.0%)	(11.1%)
Same store gross margin % used	8.1%	9.0%	(0.9%)	(10.0%)

**Units**

Retail unit sales of used vehicles increased 3,132 units, or 12.0%, from 2009 to 2010. The increase is due to a 2,169 unit, or 8.3%, increase in same store retail unit sales, coupled with a 963 unit increase from net dealership acquisitions. The same store increase was due primarily to unit sales increases in premium and volume foreign brand stores in the U.S., and reflect the improved consumer confidence levels and credit availability in 2010 compared to the prior year.

**Revenues**

Used vehicle retail sales revenue increased \$90.9 million, or 13.8%, from 2009 to 2010. The increase is due to a \$69.5 million, or 10.6%, increase in same store revenues, coupled with a \$21.4 million increase from net dealership acquisitions. The same store revenue increase is due to a \$523, or 2.1%, increase in comparative average selling prices per unit, which increased revenue by \$13.6 million, coupled with the 8.3% increase in same store retail unit sales which increased revenue by \$55.9 million.

**Gross Profit**

Retail gross profit from used vehicle sales increased \$0.8 million, or 1.3%, from 2009 to 2010. The increase is due to a \$0.9 million increase from net dealership acquisitions, offset by a \$0.1 million, or 0.2%, decrease in same store gross profit. The decrease in same store gross profit is due to a \$177, or 7.8%, decrease in average gross profit per used vehicle retailed, which decreased retail gross profit by \$4.6 million, offset by a 8.3% increase in used retail unit sales, which increased gross profit by \$4.5 million.

**Finance and Insurance Data**

	<b>2010 vs. 2009</b>			
	<b>2010</b>	<b>2009</b>	<b>Change</b>	<b>% Change</b>
Finance and insurance revenue	\$ 63.6	\$ 54.7	\$ 8.9	16.3%
Same store finance and insurance revenue	\$ 62.1	\$ 54.6	\$ 7.5	13.7%
Finance and insurance revenue per unit	\$ 922	\$ 922	\$	
Same store finance and insurance revenue per unit	\$ 937	\$ 922	\$ 15	1.6%

Finance and insurance revenue increased \$8.9 million, or 16.3%, from 2009 to 2010. The increase is due to a \$7.5 million, or 13.7%, increase in same store revenues during the period, coupled with a \$1.4 million increase from net dealership acquisitions. The same store revenue increase is due to a 12.0% increase in total retail unit sales, which increased revenue by \$6.7 million, coupled with a \$15, or 1.6%, increase in comparative average finance and insurance revenue per unit which increased revenue by \$0.8 million.



**Table of Contents****Service and Parts Data**

	<b>2010 vs. 2009</b>			
	<b>2010</b>	<b>2009</b>	<b>Change</b>	<b>% Change</b>
Service and parts revenue	\$ 332.2	\$ 331.1	\$ 1.1	0.3%
Same store service and parts revenue	\$ 321.9	\$ 329.5	\$ (7.6)	(2.3%)
Gross profit	\$ 190.5	\$ 182.4	\$ 8.1	4.4%
Same store gross profit	\$ 184.8	\$ 181.6	\$ 3.2	1.8%
Gross margin	57.4%	55.1%	2.3%	4.2%
Same store gross margin	57.4%	55.1%	2.3%	4.2%

**Revenues**

Service and parts revenue increased \$1.1 million, or 0.3%, from 2009 to 2010. The increase is due to a \$8.7 million increase from net dealership acquisitions, offset by a \$7.6 million, or 2.3%, decrease in same store revenues during the period. We believe the same store decline is due in large part to a decline in vehicle sales over the last several years compared to historical levels in addition to a decrease in warranty due to the improvement in the quality of vehicles being produced today, offset somewhat by the significant Toyota recall actions in 2010.

**Gross Profit**

Service and parts gross profit increased \$8.1 million, or 4.4%, from 2009 to 2010. The increase is due to a \$3.2 million, or 1.8%, increase in same store gross profit during the period, coupled with a \$4.9 million increase from net dealership acquisitions. The same store gross profit increase is due to a 2.3% increase in gross margin, which increased gross profit by \$7.5 million, offset by the \$7.6 million, or 2.3%, decrease in same store revenues, which decreased gross profit by \$4.3 million. Service and parts margin in 2010 has been positively impacted by the significant Toyota recall actions.

**Distribution**

Distribution units wholesaled during the quarter decreased 1,619 units, or 44.2%, from 3,659 in 2009 to 2,040 in 2010. During the three months ended June 30, 2010, smart USA recorded \$0.4 million of incentives relating to 2009 model year inventory which decreased gross profit. Due largely to the reduction in wholesale unit sales and the incentives on 2009 model year inventory, distribution segment revenue decreased \$26.8 million, or 45.5%, to \$32.1 million in 2010, and segment gross profit decreased \$4.6 million, or 61.3%, to \$2.9 million in 2010. In total, the distribution segment generated a loss of \$3.6 million in 2010 compared with income of \$1.0 million in 2009.

**Selling, General and Administrative**

Selling, general and administrative expenses ( SG&A ) increased \$27.8 million, or 8.5%, from \$327.4 million to \$355.2 million. The aggregate increase is due primarily to a \$17.3 million, or 5.3%, increase in same store SG&A, coupled with a \$10.5 million increase from net dealership acquisitions. The increase in same store SG&A is due to (1) a net increase in variable selling expenses, including increases in variable compensation, as a result of the 8.2% increase in same store retail gross profit versus the prior year and (2) increased rent and other costs relating to our ongoing facility improvement and expansion programs. SG&A expenses decreased as a percentage of gross profit from 83.2% to 82.5%.

**Depreciation**

Depreciation decreased \$1.7 million, or 12.7%, from \$13.8 million to \$12.1 million. The decrease is due to a \$2.0 million, or 14.7%, decrease in same store depreciation, offset by a \$0.3 million increase from net dealership acquisitions. The same store decrease was primarily due to a \$1.4 million impact from a change in the estimated useful lives of certain fixed assets effective January 1, 2010.

**Table of Contents****Floor Plan Interest Expense**

Floor plan interest expense, including the impact of swap transactions, decreased \$0.7 million, or 7.2%, from \$9.0 million to \$8.3 million. The decrease is due to a \$0.8 million, or 9.3%, decrease in same store floor plan interest expense, offset by a \$0.1 million increase from net dealership acquisitions. The same store decrease is due to primarily to decreases in average outstanding floor plan balances.

**Other Interest Expense**

Other interest expense decreased \$1.2 million, or 8.4%, from \$13.7 million to \$12.5 million. The decrease is due primarily to the repurchase of \$112.7 million aggregate principal amount of our 3.5% senior subordinated convertible notes during the six months ended June 30, 2010.

**Debt Discount Amortization**

Debt discount amortization decreased \$0.7 million, from \$3.1 million to \$2.4 million, due primarily to the write off of a portion of our aggregate debt discount in connection with the repurchase of a portion of our outstanding 3.5% senior subordinated convertible notes.

**Equity in Earnings of Affiliates**

Equity in earnings of affiliates increased \$1.3 million, from \$3.5 million to \$4.8 million. The increase from 2009 to 2010 is primarily related to the overall improvement in the performance of those businesses, which is consistent with our overall operating results.

**Gain on Debt Repurchase**

During the three months ended June 30, 2010, we repurchased \$41.5 million principal amount of our Convertible Notes, which had a book value, net of debt discount, of \$40.0 million for \$41.9 million. We allocated \$2.4 million of the total consideration to the reacquisition of the equity component of the Convertible Notes. In connection with the transactions, we wrote off \$0.2 million of unamortized deferred financing costs. As a result, we recorded a \$0.4 million pre-tax gain in connection with the repurchases.

**Income Taxes**

Income taxes increased \$5.3 million, or 51.3%, from \$10.3 million to \$15.6 million. The increase from 2009 to 2010 is due to the increase in our pre-tax income versus the prior year, coupled with an increase in our overall effective income tax rate resulting from the relative strength of our operations in domestic markets with higher tax rates.

**Six Months Ended June 30, 2010 Compared to Six Months Ended June 30, 2009 (dollars in millions, except per unit amounts)**

Our results for the six months ended June 30, 2009 include a gain of \$10.4 million (\$6.5 million after-tax), or \$0.07 per share, relating to the repurchase of \$68.7 million aggregate principal amount of our 3.5% senior subordinated convertible notes.

**New Vehicle Data**

	2010	2009	2010 vs. 2009	
			Change	% Change
New retail unit sales	75,815	63,911	11,904	18.6%
Same store new retail unit sales	73,482	63,750	9,732	15.3%
New retail sales revenue	\$ 2,588.1	\$ 2,061.3	\$ 526.8	25.6%
Same store new retail sales revenue	\$ 2,498.4	\$ 2,049.2	\$ 449.2	21.9%
New retail sales revenue per unit	\$ 34,137	\$ 32,253	\$ 1,884	5.8%
Same store new retail sales revenue per unit	\$ 34,000	\$ 32,145	\$ 1,855	5.8%
Gross profit new	\$ 212.7	\$ 157.3	\$ 55.4	35.2%
Same store gross profit new	\$ 204.2	\$ 156.0	\$ 48.2	30.9%
Average gross profit per new vehicle retailed	\$ 2,805	\$ 2,462	\$ 343	13.9%
Same store average gross profit per new vehicle retailed	\$ 2,779	\$ 2,447	\$ 332	13.6%
Gross margin % new	8.2%	7.6%	0.6%	7.9%
Same store gross margin % new	8.2%	7.6%	0.6%	7.9%

*Units*

Retail unit sales of new vehicles increased 11,904 units, or 18.6%, from 2009 to 2010. The increase is due a 9,732 unit, or 15.3%, increase in same store retail unit sales during the period, coupled with a 2,172 unit increase from net dealership acquisitions. The same store increase was due primarily to unit sales increases in our volume foreign brand stores in the U.S. and premium brand stores in the U.S. and U.K., and reflect the improved consumer confidence levels and credit availability in 2010 compared to the prior year.

**Table of Contents****Revenues**

New vehicle retail sales revenue increased \$526.8 million, or 25.6%, from 2009 to 2010. The increase is due to a \$449.2 million, or 21.9%, increase in same store revenues, coupled with a \$77.6 million increase from net dealership acquisitions. The same store revenue increase is due primarily to the 15.3% increase in retail unit sales, which increased revenue by \$330.9 million, coupled with a \$1,855, or 5.8%, increase in average selling prices per unit which increased revenue by \$118.3 million.

**Gross Profit**

Retail gross profit from new vehicle sales increased \$55.4 million, or 35.2%, from 2009 to 2010. The increase is due to a \$48.2 million, or 30.9%, increase in same store gross profit, coupled with a \$7.2 million increase from net dealership acquisitions. The same store increase is due primarily to the 15.3% increase in retail unit sales, which increased gross profit by \$27.0 million, coupled with a \$332, or 13.6%, increase in the average gross profit per new vehicle retailed which increased gross profit by \$21.2 million.

**Used Vehicle Data**

	<b>2010 vs. 2009</b>			
	<b>2010</b>	<b>2009</b>	<b>Change</b>	<b>% Change</b>
Used retail unit sales	55,996	53,090	2,906	5.5%
Same store used retail unit sales	54,512	52,854	1,658	3.1%
Used retail sales revenue	\$ 1,446.3	\$ 1,275.3	\$ 171.0	13.4%
Same store used retail sales revenue	\$ 1,396.2	\$ 1,261.9	\$ 134.3	10.6%
Used retail sales revenue per unit	\$ 25,829	\$ 24,021	\$ 1,808	7.5%
Same store used retail sales revenue per unit	\$ 25,612	\$ 23,875	\$ 1,737	7.3%
Gross profit used	\$ 116.8	\$ 115.3	\$ 1.5	1.3%
Same store gross profit used	\$ 114.1	\$ 114.2	\$ (0.1)	(0.1%)
Average gross profit per used vehicle retailed	\$ 2,086	\$ 2,171	\$ (85)	(3.9%)
Same store average gross profit per used vehicle retailed	\$ 2,093	\$ 2,160	\$ (67)	(3.1%)
Gross margin % used	8.1%	9.0%	(0.9%)	(10.0%)
Same store gross margin % used	8.2%	9.0%	(0.8%)	(8.9%)

**Units**

Retail unit sales of used vehicles increased 2,906 units, or 5.5%, from 2009 to 2010. The increase is due to a 1,658 unit, or 3.1%, increase in same store retail unit sales, coupled with a 1,248 unit increase from net dealership acquisitions. The same store increase was due primarily to unit sales increases in premium and volume foreign brand stores in the U.S., and reflect the improved consumer confidence levels and credit availability in 2010 compared to the prior year.

**Revenues**

Used vehicle retail sales revenue increased \$171.0 million, or 13.4%, from 2009 to 2010. The increase is due to a \$134.3 million, or 10.6%, increase in same store revenues, coupled with a \$36.7 million increase from net dealership acquisitions. The same store revenue increase is due to a \$1,737, or 7.3%, increase in comparative average selling prices per unit, which increased revenue by \$91.8 million, coupled with the 3.1% increase in same store retail unit sales which increased revenue by \$42.5 million.

**Gross Profit**

Retail gross profit from used vehicle sales increased \$1.5 million, or 1.3%, from 2009 to 2010. The increase is due to a \$1.6 million increase from net dealership acquisitions, offset by a \$0.1 million, or 0.1%, decrease in same store gross profit. The decrease in same store gross profit is due to a \$67, or 3.1%, decrease in average gross profit per used vehicle retailed, which decreased retail gross profit by \$3.5 million, offset by the 3.1% increase in used retail unit sales which increased gross profit by \$3.4 million.





**Table of Contents****Finance and Insurance Data**

	<b>2010 vs. 2009</b>			
	<b>2010</b>	<b>2009</b>	<b>Change</b>	<b>% Change</b>
Finance and insurance revenue	\$ 123.0	\$ 103.1	\$ 19.9	19.3%
Same store finance and insurance revenue	\$ 119.7	\$ 102.7	\$ 17.0	16.6%
Finance and insurance revenue per unit	\$ 933	\$ 882	\$ 51	5.8%
Same store finance and insurance revenue per unit	\$ 936	\$ 880	\$ 56	6.4%

Finance and insurance revenue increased \$19.9 million, or 19.3%, from 2009 to 2010. The increase is due to a \$17.0 million, or 16.6%, increase in same store revenues during the period, coupled with a \$2.9 million increase from net dealership acquisitions. The same store revenue increase is due to a 9.8% increase in retail unit sales, which increased revenue by \$10.6 million, coupled with a \$56, or 6.4%, increase in comparative average finance and insurance revenue per unit which increased revenue by \$6.4 million.

**Service and Parts Data**

	<b>2010 vs. 2009</b>			
	<b>2010</b>	<b>2009</b>	<b>Change</b>	<b>% Change</b>
Service and parts revenue	\$ 666.2	\$ 658.0	\$ 8.2	1.2%
Same store service and parts revenue	\$ 649.7	\$ 652.5	\$ (2.8)	(0.4%)
Gross profit	\$ 378.9	\$ 359.1	\$ 19.8	5.5%
Same store gross profit	\$ 369.6	\$ 356.4	\$ 13.2	3.7%
Gross margin	56.9%	54.6%	2.3%	4.2%
Same store gross margin	56.9%	54.6%	2.3%	4.2%

**Revenues**

Service and parts revenue increased \$8.2 million, or 1.2%, from 2009 to 2010. The increase is due to an \$11.0 million increase from net dealership acquisitions, offset by a \$2.8 million, or 0.4%, decrease in same store revenues during the period. We believe the same store decline is due in large part to a decline in vehicle sales over the last several years compared to historical levels in addition to a decrease in warranty due to the improvement in the quality of vehicles being produced today, offset somewhat by the significant Toyota recall actions in 2010.

**Gross Profit**

Service and parts gross profit increased \$19.8 million, or 5.5%, from 2009 to 2010. The increase is due to a \$13.2 million, or 3.7%, increase in same store gross profit during the period, coupled with a \$6.6 million increase from net dealership acquisitions. The same store gross profit increase is due to a 2.3% increase in gross margin, which increased gross profit by \$14.8 million, offset by the \$2.8 million, or 0.4%, decrease in same store revenues, which decreased gross profit by \$1.6 million. Service and parts margin in 2010 has been positively impacted by the significant Toyota recall actions.

**Distribution**

Distribution units wholesaled decreased 6,377 units, or 68.0%, from 9,373 in 2009 to 2,996 in 2010. During the six months ended June 30, 2010, smart USA recorded \$1.5 million of incentives relating to 2009 model year inventory which decreased gross profit. Due largely to the reduction in wholesale unit sales and the incentives on 2009 model year inventory, distribution segment revenue decreased \$100.3 million, or 68.0%, to \$47.2 million in June 30, 2010, and segment gross profit decreased \$16.4 million, or 84.1%, to \$3.1 million in 2010. In total, the distribution segment generated a loss of \$9.2 million in 2010 compared with income of \$7.3 million in 2009.

**Selling, General and Administrative**

Selling, general and administrative expenses ( SG&A ) increased \$55.6 million, or 8.7%, from \$640.1 million to \$695.7 million. The aggregate increase is due primarily to a \$40.1 million, or 6.3%, increase in same store SG&A, coupled with a \$15.5 million increase from net dealership acquisitions. The increase in same store SG&A is due to (1) a net increase in variable selling expenses, including increases in variable compensation, as a result of a 10.8% increase in same store retail gross profit versus the prior year and (2) increased rent and other costs relating to our

ongoing facility improvement and expansion programs. SG&A expenses decreased as a percentage of gross profit from 84.0% to 82.8%.

**Depreciation**

Depreciation decreased \$2.3 million, or 8.5%, from \$26.7 million to \$24.4 million. The decrease is due to a \$2.6 million, or 10.0%, decrease in same store depreciation, offset by a \$0.3 million increase from net dealership acquisitions. The same store decrease was due to a \$2.8 million decrease due to a change in the estimated useful lives of certain fixed assets effective January 1, 2010.

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### **Floor Plan Interest Expense**

Floor plan interest expense, including the impact of swap transactions, decreased \$1.6 million, or 8.6%, from \$18.4 million to \$16.8 million. The decrease is due to a \$1.8 million, or 10.1%, decrease in same store floor plan interest expense, offset by a \$0.2 million increase from net dealership acquisitions. The same store decrease is due in large part to decreases in average outstanding floor plan balances.

### **Other Interest Expense**

Other interest expense decreased \$2.9 million, or 10.4%, from \$28.2 million to \$25.3 million. The decrease is due primarily to the repurchases of \$112.7 million aggregate principal amount of Convertible Notes during the six months ended June 30, 2010.

### **Debt Discount Amortization**

Debt discount amortization decreased \$1.5 million, from \$6.8 million to \$5.3 million, due primarily to the write off of a portion of our aggregate debt discount in connection with the repurchase of a portion of Convertible Notes.

### **Gain on Debt Repurchase**

In total during 2010, we repurchased \$112.7 million principal amount of Convertible Notes, which had a book value, net of debt discount, of \$107.5 million for \$113.6 million. We allocated \$7.7 million of the total consideration to the reacquisition of the equity component of the Convertible Notes. In connection with the transactions, we wrote off \$0.6 million of unamortized deferred financing costs. As a result, we recorded a \$1.0 million pre-tax gain in connection with the repurchases.

In the first quarter of 2009, we repurchased \$68.7 million principal amount of Convertible Notes, which had a book value, net of debt discount, of \$62.8 million for \$51.4 million. In connection with the transaction, we wrote off \$0.7 million of unamortized deferred financing costs and incurred \$0.3 million of transaction costs. No element of the consideration was allocated to the reacquisition of the equity component of the Convertible Notes because the consideration paid was less than the fair value of the liability component prior to extinguishment. As a result, we recorded a \$10.4 million pre-tax gain in connection with the repurchase.

### **Income Taxes**

Income taxes increased \$8.0 million, or 39.8%, from \$20.1 million to \$28.1 million. The increase from 2009 to 2010 is due to the increase in our pre-tax income versus the prior year. Our effective tax rate was 35.9% for the six months ended June 30, 2010 and 35.7% for the six months ended June 30, 2009.

### **Liquidity and Capital Resources**

Our cash requirements are primarily for working capital, inventory financing, the acquisition of new businesses, the improvement and expansion of existing facilities, the construction of new facilities, debt service and repayments, and potentially for dividends and repurchases of our outstanding securities under the program discussed below.

Historically, these cash requirements have been met through cash flow from operations, borrowings under our credit agreements and floor plan arrangements, the issuance of debt securities, sale-leaseback transactions, mortgages, dividends from joint venture investments or the issuance of equity securities.

As discussed in more detail below, we had \$193.6 million of Convertible Notes outstanding as of June 30, 2010, and presently have \$150.6 million outstanding. Because we currently expect to be required to redeem these notes in April 2011, we are reviewing alternatives to refinance or repay these notes, which may include the issuance of additional securities. In the absence of a refinancing of these notes, we expect to utilize cash flow from operations, working capital and available capacity under the U.S. credit agreement to repay the Convertible Notes. See Forward Looking Statements. As of June 30, 2010, we had working capital of \$77.4 million, including \$17.7 million of cash, available to fund our operations and capital commitments. In addition, we had \$222.0 million and £43.4 million (\$64.8 million) available for borrowing under our U.S. credit agreement and our U.K. credit agreement, respectively, each of which is discussed below.

We have historically expanded our retail automotive operations through organic growth and the acquisition of retail automotive dealerships. In addition, one of our subsidiaries is the exclusive distributor of smart fortwo vehicles in the U.S. and Puerto Rico. We believe that cash flow from operations, dividends from our joint venture investments and our existing capital resources, including the liquidity provided by our credit agreements and floor plan financing arrangements, will be sufficient to fund our operations and commitments for at least the next twelve months. In the

event we pursue additional significant acquisitions, other expansion opportunities, significant repurchases of our outstanding securities; reinstate our quarterly cash dividends; or refinance or repay existing debt (including the Convertible Notes), we may need to raise additional capital either through the public or private issuance of equity or debt securities or through additional borrowings, which sources of funds may not necessarily be available on terms acceptable to us, if at all. In addition, our liquidity could be negatively impacted in the event we fail to comply with the covenants under our various financing and operating agreements or in the event our floor plan financing is withdrawn. For a discussion of these possible events, see the discussion below with respect to our financing agreements.

**Table of Contents*****Securities Repurchases***

From time to time, our Board of Directors has authorized securities repurchase programs pursuant to which we may, from time to time and as market conditions warrant, purchase our outstanding common stock, debt or convertible debt on the open market, in privately negotiated transactions, via a tender offer, or a pre-arranged trading plan. We have historically funded any such repurchases through cash flow from operations and borrowings under our U.S. credit facility. The decision to make repurchases will be based on factors such as the market price of the relevant security versus our view of its intrinsic value, the potential impact of such repurchases on our capital structure, and alternative uses of capital, such as for strategic investments in our current businesses, as well as any then-existing limits imposed by our finance agreements and securities trading policy. During the six months ended June 30, 2010, we repurchased a total of \$112.7 aggregate principal amount of Convertible Notes for \$113.6 million.

In July 2010, the Company repurchased an additional \$43.0 million principal amount of its outstanding convertible notes for \$43.2 million as well as 68 thousand shares of our common stock at an average price of \$10.97 per share. Subsequent to these purchases, our Board of Directors increased our authorized repurchase authority to \$150.0 million.

***Dividends***

In February 2009, we announced the suspension of our quarterly cash dividend. Future quarterly or other cash dividends will depend upon a variety of factors considered relevant by our Board of Directors which may include our earnings, capital requirements, restrictions on any then existing indebtedness, financial condition, our ability to repay or earlier refinance the expected April 2011 redemption of our \$150.6 million of Convertible Notes and other factors.

***Inventory Financing***

We finance substantially all of our new and a portion of our used vehicle inventories under revolving floor plan arrangements with various lenders, primarily through captive finance companies associated with automotive manufacturers. In the U.S., the floor plan arrangements are due on demand; however, we have not historically been required to repay floor plan advances prior to the sale of the vehicles that have been financed. We typically make monthly interest payments on the amount financed. Outside of the U.S., substantially all of our floor plan arrangements are payable on demand or have an original maturity of 90 days or less and we are generally required to repay floor plan advances at the earlier of the sale of the vehicles that have been financed or the stated maturity. The floor plan agreements typically grant a security interest in substantially all of the assets of our dealership subsidiaries, and in the U.S. are guaranteed by us. Interest rates under the floor plan arrangements are variable and increase or decrease based on changes in the prime rate, defined LIBOR, Finance House Base Rate, or Euro Interbank Offered Rate. We receive non-refundable credits from certain of our vehicle manufacturers, which are treated as a reduction of cost of sales as vehicles are sold. To date, we have not experienced any material limitation with respect to the amount or availability of financing from any institution providing us vehicle financing.

***U.S. Credit Agreement***

We are party to a credit agreement with DCFS USA LLC and Toyota Motor Credit Corporation, as amended (the U.S. credit agreement), which, as of June 30, 2010, provided for up to \$250.0 million in revolving loans for working capital, acquisitions, capital expenditures, investments and other general corporate purposes, a non-amortizing term loan with a remaining balance of \$149.0 million, and for an additional \$10.0 million of availability for letters of credit, through September 30, 2012. As of June 30, 2010, the revolving loans bore interest at a defined LIBOR plus 2.50%, subject to an incremental 0.50% for uncollateralized borrowings in excess of a defined borrowing base. The term loan, which bears interest at defined LIBOR plus 2.50%, may be prepaid at any time, but then may not be re-borrowed. The U.S. credit agreement is fully and unconditionally guaranteed on a joint and several basis by our domestic subsidiaries and contains a number of significant covenants that, among other things, restrict our ability to dispose of assets, incur additional indebtedness, repay other indebtedness, pay dividends, create liens on assets, make investments or acquisitions and engage in mergers or consolidations. We are also required to comply with specified financial and other tests and ratios, each as defined in the U.S. credit agreement, including: a ratio of current assets to current liabilities, a fixed charge coverage ratio, a ratio of debt to stockholders' equity and a ratio of debt to EBITDA. A breach of these requirements would give rise to certain remedies under the agreement, the most severe of which is the termination of the agreement and acceleration of the amounts owed. As of June 30, 2010, we were in compliance

with all covenants under the U.S. credit agreement, and we believe we will remain in compliance with such covenants for the next twelve months. In making such determination, we have considered the current margin of compliance with the covenants and our expected future results of operations, working capital requirements, acquisitions, capital expenditures and investments. See Forward Looking Statements .

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The U.S. credit agreement also contains typical events of default, including change of control, non-payment of obligations and cross-defaults to our other material indebtedness. Substantially all of our domestic assets are subject to security interests granted to lenders under the U.S. credit agreement. As of June 30, 2010, \$149.0 of term loans, \$28.0 million of borrowings under our revolving credit agreement and \$1.3 million of letters of credit were outstanding under the U.S. credit agreement.

In July 2010, we amended the U.S. Credit Agreement to (1) increase the borrowing capacity under the revolving agreement by \$50.0 million, (2) increase the interest rate on secured revolving borrowings by 25 basis points, and (3) increase the rate on unsecured revolving borrowings by 50 basis points.

***U.K. Credit Agreement***

Our subsidiaries in the U.K. (the U.K. subsidiaries) are party to an agreement, as amended, with the Royal Bank of Scotland plc, as agent for National Westminster Bank plc, which provides for a funded term loan, a revolving credit agreement and a seasonally adjusted overdraft line of credit (collectively, the U.K. credit agreement) to be used for working capital, acquisitions, capital expenditures, investments and other general corporate purposes. The U.K. credit agreement provides for (1) up to £100.0 million in revolving loans through August 31, 2013, which bears interest between a defined LIBOR plus 1.1% and defined LIBOR plus 3.0%, (2) a term loan which bears interest between 6.39% and 8.29% and is payable ratably in quarterly intervals until fully repaid on June 30, 2011, and (3) a demand seasonally adjusted overdraft line of credit for up to £20.0 million that bears interest at the Bank of England Base Rate plus 1.75%.

The U.K. credit agreement is fully and unconditionally guaranteed on a joint and several basis by our U.K. subsidiaries, and contains a number of significant covenants that, among other things, restrict the ability of our U.K. subsidiaries to pay dividends, dispose of assets, incur additional indebtedness, repay other indebtedness, create liens on assets, make investments or acquisitions and engage in mergers or consolidations. In addition, our U.K. subsidiaries are required to comply with specified ratios and tests, each as defined in the U.K. credit agreement, including: a ratio of EBITDAR to interest plus rental payments (as defined), a measurement of maximum capital expenditures, and a debt to EBITDA ratio (as defined). A breach of these requirements would give rise to certain remedies under the agreement, the most severe of which is the termination of the agreement and acceleration of the amounts owed. As of June 30, 2010, our U.K. subsidiaries were in compliance with all covenants under the U.K. credit agreement and we believe they will remain in compliance with such covenants for the next twelve months. In making such determination, we have considered the current margin of compliance with the covenants and our expected future results of operations, working capital requirements, acquisitions, capital expenditures and investments in the U.K. See [Forward Looking Statements](#).

The U.K. credit agreement also contains typical events of default, including change of control and non-payment of obligations and cross-defaults to other material indebtedness of our U.K. subsidiaries. Substantially all of our U.K. subsidiaries' assets are subject to security interests granted to lenders under the U.K. credit agreement. As of June 30, 2010, outstanding loans under the U.K. credit agreement amounted to £45.3 million (\$67.6 million), including £7.1 million (\$10.5 million) under the term loan. In July 2010, we amended the U.K. Credit Agreement in connection with a reorganization of our European operations.

***7.75% Senior Subordinated Notes***

On December 7, 2006 we issued \$375.0 million aggregate principal amount of 7.75% senior subordinated notes due 2016 (the 7.75% Notes). The 7.75% Notes are unsecured senior subordinated notes and are subordinate to all existing and future senior debt, including debt under our credit agreements, mortgages and floor plan indebtedness. The 7.75% Notes are guaranteed by substantially all of our wholly-owned domestic subsidiaries on an unsecured senior subordinated basis. Those guarantees are full and unconditional and joint and several. We can redeem all or some of the 7.75% Notes at our option beginning in December 2011 at specified redemption prices, or prior to December 2011 at 100% of the principal amount of the notes plus an applicable make-whole premium, as defined. Upon certain sales of assets or specific kinds of changes of control, we are required to make an offer to purchase the 7.75% Notes. The 7.75% Notes also contain customary negative covenants and events of default. As of June 30, 2010, we were in compliance with all negative covenants and there were no events of default.

***Senior Subordinated Convertible Notes***



In January 2006, we issued \$375.0 million aggregate principal amount of 3.50% senior subordinated convertible notes due 2026 (the Convertible Notes ), of which \$193.6 million were outstanding at June 30, 2010 and \$150.6 million are presently outstanding. The Convertible Notes mature on April 1, 2026, unless earlier converted, redeemed or purchased by us, as discussed below. The Convertible Notes are unsecured senior subordinated obligations and are subordinate to all future and existing debt under our credit agreements, mortgages and floor plan indebtedness. The Convertible Notes are guaranteed on an unsecured senior subordinated basis by substantially all of our wholly-owned domestic subsidiaries. The guarantees are full and unconditional and joint and several. The Convertible Notes also contain customary negative covenants and events of default. As of June 30, 2010, we were in compliance with all negative covenants and there were no events of default.

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Holders of the Convertible Notes may convert them based on a conversion rate of 42.7796 shares of our common stock per \$1,000 principal amount of the Convertible Notes (which is equal to a conversion price of approximately \$23.38 per share), subject to adjustment, only under the following circumstances: (1) in any quarterly period, if the closing price of our common stock for twenty of the last thirty trading days in the prior quarter exceeds \$28.05 (subject to adjustment), (2) for specified periods, if the trading price of the Convertible Notes falls below specific thresholds, (3) if the Convertible Notes are called for redemption, (4) if specified distributions to holders of our common stock are made or specified corporate transactions occur, (5) if a fundamental change (as defined) occurs, or (6) during the ten trading days prior to, but excluding, the maturity date.

Upon conversion of the Convertible Notes, for each \$1,000 principal amount of the Convertible Notes, a holder will receive an amount in cash, equal to the lesser of (i) \$1,000 or (ii) the conversion value, determined in the manner set forth in the indenture covering the Convertible Notes, of the number of shares of common stock equal to the conversion rate. If the conversion value exceeds \$1,000, we will also deliver, at our election, cash, common stock or a combination of cash and common stock with respect to the remaining value deliverable upon conversion.

In the event of a conversion due to a change of control on or before April 6, 2011, we will, in certain circumstances, pay a make-whole premium by increasing the conversion rate used in that conversion. In addition, we will pay additional cash interest commencing with six-month periods beginning on April 1, 2011, if the average trading price of a Convertible Note for certain periods in the prior six-month period equals 120% or more of the principal amount of the Convertible Notes. On or after April 6, 2011, we may redeem the Convertible Notes, in whole at any time or in part from time to time, for cash at a redemption price of 100% of the principal amount of the Convertible Notes to be redeemed, plus any accrued and unpaid interest to the applicable redemption date.

Holders of the Convertible Notes may require us to purchase all or a portion of their Convertible Notes for cash on April 1, 2011, April 1, 2016 or April 1, 2021 at a purchase price equal to 100% of the principal amount of the Convertible Notes to be purchased, plus accrued and unpaid interest, if any, to the applicable purchase date. Because we expect to be required to redeem the Convertible Notes in April 2011, we are reviewing alternatives to refinance or repay these notes, which may include the issuance of additional securities. In the absence of a refinancing of the Convertible Notes, we expect to utilize cash flow from operations, working capital and availability under the U.S. credit agreement to repay the Convertible Notes. See *Forward Looking Statements* .

In the second quarter of 2010, we repurchased \$41.5 million principal amount of its outstanding Convertible Notes for \$41.9 million. In total during the first six months of 2010, we repurchased \$112.7 million principal amount of our outstanding Convertible Notes for \$113.6 million.

In July 2010, we repurchased an additional \$43.0 million principal amount of Convertible Notes for \$43.2 million resulting in \$150.6 million presently outstanding.

***Mortgage Facilities***

We are party to several mortgages, including a \$42.4 million mortgage facility with respect to certain of our dealership properties that matures in October 2015. This facility bears interest at a defined rate, requires monthly principal and interest payments, and includes the option to extend the term for successive periods of five years up to a maximum term of twenty-five years. In the event we exercise our options to extend the term, the interest rate will be renegotiated at each renewal period. This mortgage facility also contains typical events of default, including non-payment of obligations, cross-defaults to our other material indebtedness, certain change of control events, and loss or sale of certain franchises operated at the property. Substantially all of the buildings, improvements, fixtures and personal property of the properties under the mortgage facility are subject to security interests granted to the lender. As of June 30, 2010, \$46.6 million was outstanding under these facilities.

***Interest Rate Swaps***

We use interest rate swaps to manage interest rate risk associated with our variable rate floor plan debt. We are party to interest rate swap agreements through January 2011 pursuant to which the LIBOR portion of \$300.0 million of our floating rate floor plan debt was fixed at 3.67%. We may terminate these arrangements at any time, subject to the settlement of the then current fair value of the swap arrangements. During the six months ended June 30, 2010 and 2009, the swaps increased the weighted average interest rate on floor plan borrowings by approximately 0.8% and 0.6%, respectively.

***PTL Dividends***

We own a 9.0% limited partnership interest in Penske Truck Leasing. During the six months ended June 30, 2010 and 2009, respectively, we received \$8.8 million and \$20.0 million of pro rata cash dividends from this investment. We currently expect to continue to receive future dividends from PTL subject in amount and timing on its performance.

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***Operating Leases***

We have historically structured our operations so as to minimize our ownership of real property. As a result, we lease or sublease substantially all of our facilities. These leases are generally for a period between five and 20 years, and are typically structured to include renewal options at our election. Pursuant to the leases for some of our larger facilities, we are required to comply with specified financial ratios, including a rent coverage ratio and a debt to EBITDA ratio, each as defined. For these leases, non-compliance with the ratios may require us to post collateral in the form of a letter of credit. A breach of our other lease covenants give rise to certain remedies by the landlord, the most severe of which include the termination of the applicable lease and acceleration of the total rent payments due under the lease. As of June 30, 2010, we were in compliance with all covenants under these leases.

***Sale/Leaseback Arrangements***

We have in the past and expect in the future to enter into sale-leaseback transactions to finance certain property acquisitions and capital expenditures, pursuant to which we sell property and/or leasehold improvements to third parties and agree to lease those assets back for a certain period of time. Such sales generate proceeds which vary from period to period. In light of current market conditions, this financing option has become more expensive and thus we may utilize these arrangements less in the near term.

***Off-Balance Sheet Arrangements***

We have sold a number of dealerships to third parties and, as a condition to certain of those sales, remain liable for the lease payments relating to the properties on which those businesses operate in the event of non-payment by the buyer. We are also party to lease agreements on properties that we no longer use in our retail operations that we have sublet to third parties. We rely on subtenants to pay the rent and maintain the property at these locations. In the event a subtenant does not perform as expected, we may not be able to recover amounts owed to us and we could be required to fulfill these obligations.

***smart USA***

We are subject to purchase commitments pursuant to the smart distribution agreement, which requires us to purchase a number of vehicles to be negotiated on an ongoing basis. In addition, we are potentially subject to a purchase commitment with respect to unsold inventories and other items pursuant to the smart franchise agreement and state franchise laws in the event of franchise terminations.

***Cash Flows***

Cash and cash equivalents increased by \$3.7 million and \$3.1 million during the six months ended June 30, 2010 and 2009, respectively. The major components of these changes are discussed below.

***Cash Flows from Continuing Operating Activities***

Cash provided by operating activities was \$69.6 million and \$241.1 million during the six months ended June 30, 2010 and 2009, respectively. Cash flows from continuing operating activities include net income, as adjusted for non-cash items, and the effects of changes in working capital.

We finance substantially all of our new and a portion of our used vehicle inventories under revolving floor plan notes payable with various lenders. We retain the right to select which, if any, financing source to utilize in connection with the procurement of vehicles. Many vehicle manufacturers provide vehicle financing for the dealers representing their brands, however, it is not a requirement that dealers utilize this financing. Historically, our floor plan finance source has been based on aggregate pricing considerations.

In accordance with general accounting principles relating to the statement of cash flows, we report all cash flows arising in connection with floor plan notes payable with the manufacturer of a particular new vehicle as an operating activity in our statement of cash flows, and all cash flows arising in connection with floor plan notes payable to a party other than the manufacturer of a particular new vehicle and all floor plan notes payable relating to pre-owned vehicles as a financing activity in our statement of cash flows.

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We believe that changes in aggregate floor plan liabilities are typically linked to changes in vehicle inventory and, therefore, are an integral part of understanding changes in our working capital and operating cash flow. As a result, we have presented the following reconciliation of cash flow from operating activities as reported in our condensed consolidated statement of cash flows as if all changes in vehicle floor plan were classified as an operating activity for informational purposes:

	<b>Six Months Ended June 30,</b>	
	<b>2010</b>	<b>2009</b>
Net cash from continuing operating activities as reported	\$ 69,593	\$ 241,105
Floor plan notes payable non-trade as reported	76,094	(78,608)
Net cash from continuing operating activities, adjusted to include all floor plan notes payable	\$ 145,687	\$ 162,497

***Cash Flows from Continuing Investing Activities***

Cash used in continuing investing activities was \$49.9 million and \$39.9 million during the six months ended June 30, 2010 and 2009, respectively. Cash flows from continuing investing activities consist primarily of cash used for capital expenditures and net expenditures for acquisitions and other investments. Capital expenditures were \$37.6 million and \$44.0 million during the six months ended June 30, 2010 and 2009, respectively. Capital expenditures relate primarily to improvements to our existing dealership facilities and the construction of new facilities. As of June 30, 2010, we do not have material commitments related to our planned or ongoing capital projects. We currently expect to finance our capital expenditures with operating cash flows or borrowings under our U.S. or U.K. credit facilities. Cash used in acquisitions and other investments, net of cash acquired, was \$12.3 million and \$8.6 million during the six months ended June 30, 2010 and 2009, respectively, and included cash used to repay sellers floor plan liabilities in such business acquisitions of \$7.2 million and \$2.9 million, respectively. The six months ended June 30, 2009 include \$12.7 million of proceeds from other investing activities.

***Cash Flows from Continuing Financing Activities***

Cash used in continuing financing activities was \$18.8 million and \$187.8 million during the six months ended June 30, 2010 and 2009, respectively. Cash flows from continuing financing activities include net borrowings or repayments of long-term debt, repurchases of securities, net borrowings or repayments of floor plan notes payable non-trade and the exercise of stock options. During the six months ended June 30, 2009, we repaid \$10.0 of our U.S. credit agreement term loan. We had net repayments of other long-term debt of \$9.5 million and \$47.8 million during the six months ended June 30, 2010 and 2009, respectively. We used \$113.6 million to repurchase \$112.7 million aggregate principal amount of Convertible Notes during the six months ended June 30, 2010 and used \$51.4 million to repurchase \$68.7 million aggregate principal amount of Convertible Notes during the six months ended June 30, 2009. We had net borrowings of floor plan notes payable non-trade of \$76.1 million during the six months ended June 30, 2010 and repayments of floor plan notes payable non-trade of \$78.6 million during the six months ended June 30, 2009. During the six months ended June 30, 2010, we received proceeds of \$0.2 million from the exercise of stock options.

***Cash Flows from Discontinued Operations***

Cash flows relating to discontinued operations are not currently considered, nor are they expected to be, material to our liquidity or our capital resources.

**Related Party Transactions*****Stockholders Agreement***

Several of our directors and officers are affiliated with Penske Corporation or related entities. Roger S. Penske, our Chairman of the Board and Chief Executive Officer, is also Chairman of the Board and Chief Executive Officer of Penske Corporation, and through entities affiliated with Penske Corporation, our largest stockholder owning approximately 35% of our outstanding common stock. Mitsui & Co., Ltd. and Mitsui & Co. (USA), Inc. (collectively,

Mitsui ) own approximately 17% of our outstanding common stock. Mitsui, Penske Corporation and certain other affiliates of Penske Corporation are parties to a stockholders agreement pursuant to which the Penske affiliated companies agreed to vote their shares for one director who is a representative of Mitsui. In turn, Mitsui agreed to vote their shares for up to fourteen directors voted for by the Penske affiliated companies. This agreement terminates in March 2014, upon the mutual consent of the parties, or when either party no longer owns any of our common stock.

***Other Related Party Interests and Transactions***

Roger S. Penske is also a managing member of Transportation Resource Partners, an organization that invests in transportation-related industries. Richard J. Peters, one of our directors, is a managing director of Transportation Resource Partners and is a director of Penske Corporation. One of our directors, Hiroshi Ishikawa, serves as our Executive Vice President International Business Development and serves in a similar capacity for Penske Corporation. Robert H. Kurnick, Jr., our President and a director, is also the President and a director of Penske Corporation.

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We sometimes pay to and/or receive fees from Penske Corporation, its subsidiaries, and its affiliates for services rendered in the normal course of business, or to reimburse payments made to third parties on each others behalf. These transactions are reviewed periodically by our Audit Committee and reflect the provider s cost or an amount mutually agreed upon by both parties.

We are a 9.0% limited partner of PTL, a leading global transportation services provider. PTL operates and maintains more than 200,000 vehicles and serves customers in North America, South America, Europe and Asia. Product lines include full-service leasing, contract maintenance, commercial and consumer truck rental and logistics services, including, transportation and distribution center management and supply chain management. The general partner of PTL is Penske Truck Leasing Corporation, a wholly-owned subsidiary of Penske Corporation, which together with other wholly-owned subsidiaries of Penske Corporation, owns 41.1% of PTL. The remaining 49.9% of PTL is owned by GE Capital. Among other things, the partnership agreement provides us with specified partner distribution and governance rights and restricts our ability to transfer our interests. We have also entered into other joint ventures with certain related parties as more fully discussed below.

**Joint Venture Relationships**

We are party to a number of joint ventures pursuant to which we own and operate automotive dealerships together with other investors. We may provide these dealerships with working capital and other debt financing at costs that are based on our incremental borrowing rate. As of June 30, 2010, our automotive retail joint venture relationships were as follows:

<b>Location</b>	<b>Dealerships</b>	<b>Ownership Interest</b>
Fairfield, Connecticut	Audi, Mercedes-Benz, Porsche, smart	87.95%(A)(B)
Edison, New Jersey	Ferrari, Maserati	70.00%(B)
Las Vegas, Nevada	Ferrari, Maserati	50.00%(C)
Frankfurt, Germany	Lexus, Toyota	50.00%(C)
Aachen, Germany	Audi, Lexus, Skoda, Toyota, Volkswagen	50.00%(C)

(A) An entity controlled by one of our directors, Lucio A. Noto (the Investor ), owns a 12.05% interest in this joint venture which entitles the Investor to 20% of the joint venture s operating profits. In addition, the Investor has an option to purchase up to a 20% interest in the joint venture for specified

amounts.

- (B) Entity is consolidated in our financial statements.
- (C) Entity is accounted for using the equity method of accounting.

In the first quarter of 2010, the Company exited one of its German joint ventures by exchanging its 50% interest in the joint venture for 100% ownership in three BMW franchises previously held by the joint venture.

**Cyclicality**

Unit sales of motor vehicles, particularly new vehicles, historically have been cyclical, fluctuating with general economic cycles. During economic downturns, the automotive retailing industry tends to experience periods of decline and recession similar to those experienced by the general economy. We believe that the industry is influenced by general economic conditions and particularly by consumer confidence, the level of personal discretionary spending, fuel prices, interest rates and credit availability.

**Seasonality**

Our business is modestly seasonal overall. Our U.S. operations generally experience higher volumes of vehicle sales in the second and third quarters of each year due in part to consumer buying trends and the introduction of new vehicle models. Also, vehicle demand, and to a lesser extent demand for service and parts, is generally lower during the winter months than in other seasons, particularly in regions of the U.S. where dealerships may be subject to severe winters. Our U.K. operations generally experience higher volumes of vehicle sales in the first and third quarters of each year, due primarily to vehicle registration practices in the U.K.

**Effects of Inflation**

We believe that inflation rates over the last few years have not had a significant impact on revenues or profitability. We do not expect inflation to have any near-term material effects on the sale of our products and services; however, we cannot be sure there will be no such effect in the future. We finance substantially all of our inventory through various revolving floor plan arrangements with interest rates that vary based on various benchmarks. Such rates have historically increased during periods of increasing inflation.



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**Forward Looking Statements**

This quarterly report on Form 10-Q contains forward-looking statements which generally can be identified by the use of terms such as may, will, should, expect, anticipate, believe, intend, plan, estimate, predict, continue or variations of such terms, or the use of these terms in the negative. Forward-looking statements include statements regarding our current plans, forecasts, estimates, beliefs or expectations, including, without limitation, statements with respect to:

- our future financial and operating performance, including sales of the smart fortwo;
- future acquisitions;
- future potential capital expenditures and securities repurchases;
- our ability to realize cost savings and synergies;
- our ability to respond to economic cycles;
- trends in the automotive retail industry and in the general economy in the various countries in which we operate;
- our ability to access the remaining availability under our credit agreements;
- our liquidity, including our ability to refinance our outstanding senior subordinated convertible notes;
- future foreign exchange rates;
- trends affecting our future financial condition or results of operations; and
- our business strategy.

Forward-looking statements involve known and unknown risks and uncertainties and are not assurances of future performance. Actual results may differ materially from anticipated results due to a variety of factors, including the factors identified in our 2009 annual report on Form 10-K filed February 24, 2010. Important factors that could cause actual results to differ materially from our expectations include the following:

- our business and the automotive retail industry in general are susceptible to adverse economic conditions, including changes in interest rates, foreign exchange rates, consumer demand, consumer confidence, fuel prices, unemployment rates and credit availability;
- the number of new and used vehicles sold in our markets;
- automobile manufacturers exercise significant control over our operations, and we depend on them in order to operate our business;
- we depend on the success and popularity of the brands we sell, and adverse conditions affecting one or more automobile manufacturers, such as the recent Toyota recalls, may negatively impact our revenues and profitability;
- a restructuring of any significant automotive manufacturers, as well as the automotive sector as a whole;
- we may not be able to satisfy our capital requirements for acquisitions, dealership renovation projects, financing the purchase of our inventory, or refinancing of our debt when it becomes due (including our \$150.6 million of outstanding senior subordinated convertible notes expected to be repaid in April 2011);
- our failure to meet a manufacturer's consumer satisfaction requirements may adversely affect our ability to acquire new dealerships, our ability to obtain incentive payments from manufacturers;
- although we typically purchase vehicles and parts in the local functional currency, changes in foreign exchange rates may impact manufacturers, as many of the component parts of vehicles are manufactured in foreign markets, which could lead to an increase in our costs which we may not be able to pass on to the consumer;
- changes in tax, financial or regulatory rules or requirements;

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with respect to PTL, changes in the financial health of its customers, labor strikes or work stoppages by its employees, a reduction in PTL's asset utilization rates and industry competition;

if we lose key personnel, especially our Chief Executive Officer, or are unable to attract additional qualified personnel;

import product restrictions and foreign trade risks that may impair our ability to sell foreign vehicles profitably;

new or enhanced regulations relating to automobile dealerships;

if state dealer laws in the U.S. are repealed or weakened, our automotive dealerships may be subject to increased competition and may be more susceptible to termination, non-renewal or renegotiation of their franchise agreements;

non-compliance with the financial ratios and other covenants under our credit agreements and operating leases;

our distribution of the smart fortwo vehicle is dependent upon continued availability of and customer demand for the smart fortwo;

our dealership operations may be affected by severe weather or other periodic business interruptions;

some of our directors and officers may have conflicts of interest with respect to certain related party transactions and other business interests;

our level of indebtedness may limit our ability to obtain financing generally and may require that a significant portion of our cash flow be used for debt service;

we may be involved in legal proceedings that could have a material adverse effect on our business; and

our operations outside of the U.S. subject our profitability to fluctuations relating to changes in foreign currency valuations.

In addition:

the price of our common stock is subject to substantial fluctuation, which may be unrelated to our performance; and

shares eligible for future sale, or issuable under the terms of our convertible notes, may cause the market price of our common stock to drop significantly, even if our business is doing well.

We urge you to carefully consider these risk factors in evaluating all forward-looking statements regarding our business. Readers of this report are cautioned not to place undue reliance on the forward-looking statements contained in this report. All forward-looking statements attributable to us are qualified in their entirety by this cautionary statement. Except to the extent required by the federal securities laws and Securities and Exchange Commission rules and regulations, we have no intention or obligation to update publicly any forward-looking statements whether as a result of new information, future events or otherwise.

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

*Interest Rates.* We are exposed to market risk from changes in the interest rates on a significant portion of our outstanding debt. Outstanding revolving balances under our credit agreements bear interest at variable rates based on a margin over defined LIBOR or the Bank of England Base Rate. Based on the amount outstanding under these facilities as of June 30, 2010, a 100 basis point change in interest rates would result in an approximate \$2.3 million change to our annual other interest expense. Similarly, amounts outstanding under floor plan financing arrangements bear interest at a variable rate based on a margin over the prime rate, defined LIBOR, the Finance House Base Rate, or the Euro Interbank Offered Rate. We are currently party to swap agreements pursuant to which a notional \$300.0 million of our floating rate floor plan debt was exchanged for fixed rate debt through January 2011. Based on an average of the aggregate amounts outstanding under our floor plan financing arrangements subject to variable interest payments during the trailing twelve months ended June 30, 2010, adjusted to exclude the notional value of the hedged swap agreements, a 100 basis point change in interest rates would result in an approximate \$9.2 million change to our annual floor plan interest expense.



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We evaluate our exposure to interest rate fluctuations and follow established policies and procedures to implement strategies designed to manage the amount of variable rate indebtedness outstanding at any point in time in an effort to mitigate the effect of interest rate fluctuations on our earnings and cash flows. These policies include:

- the maintenance of our overall debt portfolio with targeted fixed and variable rate components;
- the use of authorized derivative instruments;
- the prohibition of using derivatives for trading or other speculative purposes; and
- the prohibition of highly leveraged derivatives or derivatives which we are unable to reliably value, or for which we are unable to obtain a market quotation.

Interest rate fluctuations affect the fair market value of our fixed rate debt, including our swaps, mortgages, the 7.75% Notes, the Convertible Notes, and certain seller financed promissory notes, but, with respect to such fixed rate debt instruments, do not impact our earnings or cash flows.

*Foreign Currency Exchange Rates.* As of June 30, 2010, we had dealership operations in the U.K. and Germany. In each of these markets, the local currency is the functional currency. Due to our intent to remain permanently invested in these foreign markets, we do not hedge against foreign currency fluctuations. In the event we change our intent with respect to the investment in any of our international operations, we would expect to implement strategies designed to manage those risks in an effort to mitigate the effect of foreign currency fluctuations on our earnings and cash flows. A ten percent change in average exchange rates versus the U.S. Dollar would have resulted in an approximate \$192.8 million change to our revenues for the six months ended June 30, 2010.

In common with other automotive retailers, we purchase certain of our new vehicle and parts inventories from foreign manufacturers. Although we purchase the majority of our inventories in the local functional currency, our business is subject to certain risks, including, but not limited to, differing economic conditions, changes in political climate, differing tax structures, other regulations and restrictions and foreign exchange rate volatility which may influence such manufacturers' ability to provide their products at competitive prices in the local jurisdictions. Our future results could be materially and adversely impacted by changes in these or other factors.

### ***Item 4. Controls and Procedures***

Under the supervision and with the participation of our management, including the principal executive and financial officers, we conducted an evaluation of the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act)), as of the end of the period covered by this report. Our disclosure controls and procedures are designed to ensure that information required to be disclosed by us in the reports we file under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to management, including our principal executive and financial officers, to allow timely discussions regarding required disclosure.

Based upon this evaluation, the Company's principal executive and financial officers concluded that our disclosure controls and procedures were effective as of the end of the period covered by this report. In addition, we maintain internal controls designed to provide us with the information required for accounting and financial reporting purposes. There were no changes in our internal control over financial reporting that occurred during the most recent quarter that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**Table of Contents****PART II OTHER INFORMATION****Item 1. Legal Proceedings**

We are involved in litigation which may relate to claims brought by governmental authorities, issues with customers, and employment related matters, including class action claims and purported class action claims. As of June 30, 2010, we are not party to any legal proceedings, including class action lawsuits, that, individually or in the aggregate, are reasonably expected to have a material adverse effect on our results of operations, financial condition or cash flows. However, the results of these matters cannot be predicted with certainty, and an unfavorable resolution of one or more of these matters could have a material adverse effect on our results of operations, financial condition or cash flows.

**Item 5. Other Information**

On July 27, 2010, we, DCFS USA LLC and Toyota Motor Credit Corporation amended our U.S. credit agreement to (1) increase the borrowing capacity under the revolving agreement by \$50.0 million to a total of \$300.00 million, (2) increase the interest rate on secured revolving borrowings by 25 basis points, and (3) increase the rate on unsecured revolving borrowings by 50 basis points. We purchase motor vehicles from Daimler AG and Toyota Motor Corporation, affiliates of the respective lenders under the Credit Agreement, for sale at certain of our dealerships. The lenders also provide us with floor-plan financing and consumer financing. On July 27, 2010, we also amended our U.K. credit agreement to facilitate a reorganization of our European operations. Our UK operations also sell motor vehicles to an affiliate of RBS which provides other banking services to Sytner Group.

**Item 6. Exhibits**

- |      |  |
|------|--|
| 4.1  | Second Amendment dated July 27, 2010 to Amended and Restated Credit Agreement, dated as of October 30, 2008 among Penske Automotive Group, Inc., Toyota Motor Credit Corporation and DCFS USA LLC, as agent.   |
| 4.2  | Amendment dated July 27, 2010 to multi-option credit agreement, fixed rate credit agreement and overdraft facility agreement each dated August 31, 2006 between Sytner Group Limited and The Royal Bank of Scotland, plc, as agent for National Westminster Bank Plc.  |
| 12   | Computation of Ratio of Earnings to Fixed Charges  |
| 31.1 | Rule 13(a)-14(a)/15(d)-14(a) Certification.  |
| 31.2 | Rule 13(a)-14(a)/15(d)-14(a) Certification.  |
| 32   | Section 1350 Certification.  |
| 101  | The following materials from Penske Automotive Group's Quarterly Report on Form 10-Q for the quarter ended June 30, 2010, formatted in XBRL (eXtensible Business Reporting Language): (i) the Consolidated Condensed Balance Sheets as of June 30, 2010 and December 31, 2009, (ii) the Consolidated Condensed Statements of Income for the three and six months ended June 30, 2010 and 2009, (iii) the Consolidated Condensed Statements of Cash Flows for the six months ended June 30, 2010 and 2009, (iv) the Consolidated Condensed Statement of Equity for the six months ended June 30, 2010, and (v) the Notes to Consolidated Condensed Financial Statements, tagged as blocks of text.* |

\* Pursuant to Rule 406T of Regulation S-T, the Interactive Data Files on Exhibit 101 hereto are deemed not filed or part of a registration

statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, are deemed not filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and otherwise are not subject to liability under those sections.

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**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.

PENSKE AUTOMOTIVE GROUP, INC.

By: /s/ Roger S. Penske  
Roger S. Penske  
*Chief Executive Officer*

Date: July 30, 2010

By: /s/ Robert T. O Shaughnessy  
Robert T. O Shaughnessy  
*Chief Financial Officer*

Date: July 30, 2010

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<b>Exhibit No.</b>	<b>Description</b>
4.1	Second Amendment dated July 27, 2010 to Amended and Restated Credit Agreement, dated as of October 30, 2008 among Penske Automotive Group, Inc., Toyota Motor Credit Corporation and DCFS USA LLC, as agent.
4.2	Amendment dated July 27, 2010 to multi-option credit agreement, fixed rate credit agreement and overdraft facility agreement each dated August 31, 2006 between Sytner Group Limited and The Royal Bank of Scotland, plc, as agent for National Westminster Bank Plc.
12	Computation of Ratio of Earnings to Fixed Charges
31.1	Rule 13(a)-14(a)/15(d)-14(a) Certification.
31.2	Rule 13(a)-14(a)/15(d)-14(a) Certification.
32	Section 1350 Certification.
101	The following materials from Penske Automotive Group's Quarterly Report on Form 10-Q for the quarter ended June 30, 2010, formatted in XBRL (eXtensible Business Reporting Language): (i) the Condensed Balance Sheets as of June 30, 2010 and December 31, 2009, (ii) the Condensed Statements of Income for the three and six months ended June 30, 2010 and 2009, (iii) the Condensed Statements of Cash Flows for the six months ended June 30, 2010 and 2009, (iv) the Consolidated Condensed Statement of Equity for the six months ended June 30, 2010, and (v) the Notes to Consolidated Condensed Financial Statements, tagged as blocks of text*.

\* Pursuant to Rule 406T of Regulation S-T, the Interactive Data Files on Exhibit 101 hereto are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, are deemed not filed for purposes of Section 18 of the Securities Exchange Act of 1934, as



amended, and otherwise are not subject to liability under those sections.