

UNITED AUTO GROUP INC

Form 8-K

August 07, 2002

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SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, DC 20549

FORM 8-K  
CURRENT REPORT

Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Date of Report (Date of Earliest Event Reported): August 7, 2002

UNITED AUTO GROUP, INC.

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(Exact Name of Registrant as Specified in its Charter)

DELAWARE

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(State or Other Jurisdiction of Incorporation)

1-12297

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(Commission File Number)

13400 OUTER DRIVE WEST  
DETROIT, MI

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(Address of Principal Executive Offices)

313-592-7311

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(Registrant's Telephone Number, Including Area Code)

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**RISK FACTORS**

*Our substantial amount of indebtedness may limit our ability to obtain financing for acquisitions, make us more vulnerable to adverse economic conditions and make it more difficult for us to make payments on the New Notes and our other indebtedness.*

We are highly leveraged. As of March 31, 2002, we had approximately \$585.2 million of total debt outstanding and \$758.2 million of floor plan notes payable outstanding. As of August 1, 2002, \$305.7 million was outstanding under our credit agreement.

Our substantial debt could have important consequences to you. For example, it could:

make it more difficult for us to obtain additional financing in the future for our acquisitions and operations, working capital requirements, capital expenditures, debt service or other general corporate requirements;

require us to dedicate a substantial portion of our cash flows from operations to the repayment of our debt and the interest associated with our debt rather than to other areas of our business;

limit our operating flexibility due to financial and other restrictive covenants, including restrictions on incurring additional debt, creating liens on our properties, making acquisitions and paying dividends;

make it more difficult for us to satisfy our obligations with respect to the New Notes;

subject us to the risks that interest rates and our interest expense will increase;

place us at a competitive disadvantage compared to our competitors that have less debt; and

make us more vulnerable in the event of adverse economic and industry conditions or a downturn in our business.

In addition, an event of default under our principal credit agreement and certain of our floor plan financing arrangements would occur to the extent that Penske Capital Partners, LLC and/or Penske Corporation do not control our board of directors.

Our ability to meet our debt service obligations depends on our future financial and operating performance, which will be impacted by general economic conditions and by financial, business and other competitive factors, many of which are beyond our control. These factors could include operating difficulties, increased operating costs, the response of competitors, regulatory developments and delays in implementing our growth strategies. Our ability to meet our debt service and other obligations may depend in significant part on the extent to which we can successfully implement our business strategy. We may not be able to implement our business strategy and the anticipated results of our strategy may not be realized.

If our business does not generate sufficient cash flow from operations or future borrowings cease to be available to us under our credit agreement or from other sources in an amount sufficient to enable us to service our debt, including the New Notes, we may be unable to fund our other liquidity needs. If we are unable to service our debt, due to inadequate liquidity or otherwise, we may have to delay or cancel acquisitions, sell equity securities, sell assets or restructure or refinance our indebtedness. We cannot assure you that, if we are unable to service our debt, we will be able to sell our equity securities, sell our assets or restructure or refinance our debt on a timely basis or on satisfactory terms or at all. In addition, the terms of our existing or future franchise agreements, agreements with manufacturers or debt agreements, including the indenture governing the Original Notes and New Notes and our credit agreement, may prohibit us from adopting any of these alternatives.

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Our debt instruments, including the credit agreement and the indenture governing the Original Notes and New Notes, also permit us to incur additional debt in the future. Any such additional debt could be senior to the Original Notes and New Notes. In addition, the entities we may acquire in the future could have significant amounts of debt outstanding which we would be required to assume in connection with the acquisition.

***The New Notes will be junior to our senior debt and the guarantees will be junior to guarantor senior debt, which could result in the holders of the New Notes not being paid after a default under the senior debt, or in the holders of the New Notes receiving less, ratably, than our other unsecured general creditors in a bankruptcy, liquidation, reorganization or similar proceeding relating to us.***

The New Notes will be unsecured senior subordinated obligations and will be junior to all of our existing and future senior indebtedness, including indebtedness under our credit agreement and floor plan financing. As of March 31, 2002, we had \$242.5 million of outstanding senior indebtedness (not including our guarantees of subsidiary floor plan debt) ranking senior to the New Notes and \$3.7 million of senior subordinated indebtedness ranking equal with the New Notes.

Substantially all of our domestic subsidiaries will guarantee the New Notes. These guarantees will be unsecured senior subordinated obligations and will be junior to all existing and future senior debt of the guarantors. As of March 31, 2002, the guarantors had \$587.1 million of senior indebtedness (not including subsidiary guarantees of debt under our credit agreement) ranking senior to the senior subordinated guarantees.

We may also incur significant additional senior indebtedness under the terms of our credit agreement and floorplan financing. As of March 31, 2002, we had a maximum of \$433.5 million available under our credit agreement which, if borrowed, would be senior indebtedness. This availability is subject to the credit agreement's borrowing base collateral limitation (in general, the borrowing base equals certain of our allowable tangible assets plus \$300.0 million). If we become bankrupt, liquidate or dissolve, our assets would be available to pay obligations on the New Notes only after our senior indebtedness has been paid. Similarly, if one of our guarantor subsidiaries becomes bankrupt, liquidates or dissolves, that subsidiary's assets would be available to pay obligations on its guarantee only after payments have been made on its senior indebtedness.

If we fail to pay any of our senior indebtedness, we may make payments on the New Notes only if either we first pay our senior debt or the holders of our senior debt waive the payment default. Moreover, if any non-payment default exists under our senior indebtedness, we may not make any cash payments on the New Notes for a period of up to 179 days in any 360-day period, unless we cure the non-payment default, the holders of the senior indebtedness waive the default or rescind acceleration of the indebtedness or we repay the indebtedness in full. In the event of a non-payment default we may not have sufficient assets to pay amounts due on the New Notes.

In the event of a bankruptcy, liquidation, reorganization or similar proceeding relating to us, holders of the New Notes will participate ratably with all of our general unsecured creditors. However, because the indenture requires that, until all of our senior debt is repaid, amounts otherwise payable to holders of the New Notes in a bankruptcy or similar proceeding be paid to holders of senior debt instead, holders of the New Notes may receive less, ratably, than our other general unsecured creditors in any such proceeding. In any of these cases, we may not have sufficient funds to pay all of our creditors, including the holders of the New Notes.

***Because the New Notes will be effectively junior to the liabilities of our current and future non-guarantor subsidiaries, in a bankruptcy, liquidation or dissolution of those subsidiaries, their assets will not be available to us or the holders of the New Notes until their liabilities have been paid.***

The New Notes also will be effectively junior to all existing and future debt and other liabilities of our subsidiaries that are not guarantors, which will include our foreign subsidiaries and one immaterial joint venture. Sytner will not be a guarantor under the New Notes, and the New Notes will be effectively junior to

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Sytner's debt and to any loan notes issued by UAG U.K. Holdings Limited in connection with the Sytner acquisition. If one of our nonguarantor subsidiaries becomes bankrupt, liquidates or dissolves, that nonguarantor subsidiary's assets would not be available to us or the holders of the New Notes until after payments have been made on all of its liabilities. As a result, the payment of principal, premium and interest on the New Notes is effectively subordinated in right of payment to all indebtedness and liabilities of the non-guarantor subsidiaries.

***The New Notes will not be secured by any of our assets. However, our credit agreement and floor plan financing are secured by substantially all of our assets. As a result, if we became insolvent, secured lenders will have a prior claim on our assets.***

In addition to being subordinated to all of our senior indebtedness, the New Notes will not be secured by any of our assets. However, our floorplan financing is secured by substantially all of our subsidiaries' assets, and our credit agreement is secured by substantially all of our assets and a pledge of the capital stock of many of our subsidiaries. Additionally, the terms of the indenture and our credit facility permit us to incur additional secured debt in the future. Accordingly, the payment of principal, premium and interest on the New Notes will be effectively subordinated in right of payment to all of our secured indebtedness, and the payment under the guarantees will effectively be subordinated in right of payment to all secured indebtedness of the guarantors.

If we become insolvent or are liquidated, or if payment under any of the instruments governing our secured debt is accelerated, the lenders under these instruments will be entitled to exercise the remedies available to a secured lender under applicable law and pursuant to instruments governing such debt. Accordingly, such lenders will have a prior claim on our assets. In that event, because the New Notes will not be secured by any of our assets, it is possible that there will be no assets remaining from which claims of holders of the New Notes can be satisfied or, if any assets remain, the remaining assets might be insufficient to satisfy those claims in full.

***The agreements governing our debt, including the New Notes and our credit agreement, contain various covenants that limit our discretion in the operation of our business, could prohibit us from engaging in transactions we believe to be beneficial and could lead to the acceleration of our debt.***

Our existing and future debt agreements impose and will impose operating and financial restrictions on our activities. These restrictions require us to comply with or maintain certain financial tests and ratios and restrict our ability and our subsidiaries' ability to:

incur additional debt;

create liens;

make acquisitions;

redeem and/or prepay certain debt;

sell preferred stock of subsidiaries or other assets;

make certain investments;

enter new lines of business;

engage in consolidations, mergers and acquisitions;

repurchase or redeem capital stock;

guarantee obligations;

engage in certain transactions with affiliates; and

pay dividends and make other distributions.





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The credit agreement also requires us to comply with certain financial ratios, including a maximum funded debt to stockholders' equity ratio, a maximum non-floor plan debt to stockholders' equity ratio, and a maximum funded debt to EBITDA ratio. These restrictions on our ability to operate our business could seriously harm our business by, among other things, limiting our ability to take advantage of financing, merger and acquisition and other corporate opportunities.

***Failure to comply with covenants in our existing or future financing agreements could result in cross-defaults under some of our financing agreements which could jeopardize our ability to pay the New Notes.***

Various risks, uncertainties and events beyond our control could affect our ability to comply with these covenants and maintain the financial tests and ratios required by the instruments governing our financing arrangements. Failure to comply with any of the covenants in our existing or future financing agreements could result in a default under those agreements and under other agreements containing cross-default provisions. A default would permit lenders to cease to make further extensions of credit, accelerate the maturity of the debt under these agreements and foreclose upon any collateral securing that debt. Under these circumstances, we might not have sufficient funds or other resources to satisfy all of our obligations, including our obligations under the New Notes. In addition, the limitations imposed by financing agreements on our ability to incur additional debt and to take other actions might significantly impair our ability to obtain other financing. We also may amend the provisions and limitations of our credit facility from time to time without the consent of the holders of New Notes.

The aggregate amount outstanding at August 1, under all such indebtedness was \$305.7 million. Such indebtedness contains optional redemption or acceleration rights at the election of the holders upon a covenant default or change in control, which, if exercised, would constitute an event of default under the Indenture. It is possible that we would be unable to fulfill all of these obligations and make payments on the New Notes simultaneously.

***We may be unable to make a change of control offer required by the indenture governing the Original Notes and New Notes, which would cause defaults under the indenture governing the Original Notes and New Notes and our credit agreement.***

The terms of the New Notes will require us to make an offer to repurchase the New Notes upon the occurrence of a change of control at a purchase price equal to 101% of the principal amount of the New Notes, plus accrued interest to the date of the purchase. We are prohibited by the credit agreement, and may be prohibited under future financing agreements, from purchasing any notes prior to their stated maturity. In such circumstances, we will be required to repay or obtain the requisite consent from the affected lenders to permit the repurchase of the New Notes. If we are unable to repay all of such debt or are unable to obtain the necessary consents, we will be unable to offer to repurchase the New Notes, which would constitute an event of default under the indenture governing the Original Notes and New Notes, which itself would also constitute a default under our credit agreement and our other existing financing arrangements, and could constitute a default under the terms of any future debt that we may incur. In addition, we may not have sufficient funds available at the time of any change of control to repurchase the New Notes.

One of the events which would trigger a change of control is a sale of all or substantially all of our assets. The phrase all or substantially all as used in the definition of change of control has not been interpreted under New York law (which is the governing law of the Indenture) to represent a specific quantitative test. As a consequence, investors may not be able to determine when a change of control has occurred giving rise to the repurchase obligations under the Indenture. It is possible, therefore, that there could be a disagreement between us and some or all holders of the New Notes over whether a specific asset sale or sales triggers a change of control offer and that holders of the New Notes might not receive a change of control offer in respect of that transaction. In addition, in the event the holders of the New Notes elected to exercise their rights under the Indenture and the Company elected to contest such election, there could be no assurance as to how a court interpreting New York law would interpret the phrase all or substantially all.

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*We could enter into various transactions, such as acquisitions, refinancings, recapitalizations or other highly leveraged transactions, which would not constitute a change of control, but which could nevertheless increase the amount of our outstanding debt at such time, or adversely affect our capital structure or credit ratings, or otherwise adversely affect holders of the Notes.*

Under the terms of the Notes, a variety of acquisition, refinancing, recapitalization or other highly leveraged transactions are not considered change in control transactions. As a result, we could enter into any such transaction without being required to make an offer to repurchase the Notes even though the transaction could increase the total amount of our outstanding indebtedness, adversely affect our capital structure or credit ratings or otherwise adversely affect the holders of the New Notes.

*We are a holding company and as a result rely on the receipt of payments from our subsidiaries in order to meet our cash needs and service our indebtedness, including the New Notes. Our subsidiaries are subject to restrictions on payment of dividends under their franchise agreements, dealer agreements, floor plan agreements and other agreements which restrict our ability to apply profits generated from one subsidiary for use in others or the parent company; this could adversely affect our ability to make payments on the New Notes.*

We are a holding company and our principal assets consist of the shares of capital stock or other equity instruments of our subsidiaries. As a holding company without independent means of generating operating revenues, we depend on dividends, distributions and other payments, including payments of management fees and pursuant to tax sharing arrangements, from our subsidiaries to fund our obligations and meet our cash needs. If the operating results of our subsidiaries at any given time are not sufficient to make distributions to us we would be unable to make payments on the New Notes. Our expenses include salaries of our executive officers, insurance, professional fees and payment of certain indebtedness that may be outstanding from time to time. Most of our subsidiaries are subject to restrictions on the payment of dividends under certain circumstances pursuant to their franchise agreements, dealer agreements, other agreements with manufacturers and floor plan agreements. For example, most of the agreements contain minimum working capital or net worth requirements and some manufacturers' dealer agreements specifically prohibit distribution to us if the distribution would cause the dealership to fail to meet such manufacturer's capitalization guidelines, including net working capital. These restrictions limit our ability to apply profits generated from one subsidiary for use in other subsidiaries or, in some cases, at the parent company.

*Federal and state statutes allow courts, under specific circumstances, to void guarantees of the New Notes. In such event, holders of New Notes would be structurally subordinated to creditors of the issuer of the voided guarantee.*

Federal and state statutes allow courts, under specific circumstances, to void guarantees, subordinate claims under the guarantees to the guarantor's other debt or take other action detrimental to holders of the guarantees of notes. Under the federal bankruptcy law and comparable provisions of state fraudulent transfer laws, the guarantees made by our subsidiaries could be voided or subordinated to other debt if, among other things:

any subsidiary guarantor issued the guarantee to delay, hinder or defraud present or future creditors; or

any subsidiary guarantor received less than reasonably equivalent value or fair consideration for issuing such subsidiary guarantee and, at the time it issued its subsidiary guarantee, any subsidiary guarantor

was insolvent or rendered insolvent by reason of such incurrence; or

was engaged in a business or transaction for which such guarantor's remaining unencumbered assets constituted unreasonably small capital; or

intended to incur, or believed that it would incur, debts beyond its ability to pay such debts as they mature; or

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was a defendant in an action for money damages, or had a judgment for money damages docketed against it if, in either case, after final judgment, the judgment is unsatisfied.

Among other things, a legal challenge of a guarantee on fraudulent conveyance grounds may focus on the benefits, if any, realized by the guarantor as a result of our issuance of the New Notes. The measures of insolvency for purposes of these fraudulent transfer laws will vary depending upon the law applied in any proceeding to determine whether a fraudulent transfer has occurred. Generally, however, a subsidiary guarantor would be considered insolvent if, at the time it incurred the indebtedness,

the sum of its debts is greater than the fair value of all of its assets;

the present fair saleable value of its assets was less than the amount that would be required in order to pay its probable liability on its existing debts and liabilities, including contingent liabilities, as they become absolute and mature; or

it could not pay or is generally not paying its debts as they become due.

There is no way to predict with certainty what standards a court would apply to determine whether a guarantor was solvent at the relevant time. It is possible that a court could view the issuance of guarantees as a fraudulent conveyance. To the extent that a guarantee were to be avoided as a fraudulent conveyance or held unenforceable for any other reason, holders of the New Notes would cease to have any claim in respect of the guarantor and would be creditors solely of ours and of the guarantors whose guarantees had not been avoided or held unenforceable. In this event, the claims of the holders of the New Notes against the issuer of an invalid guarantee would be subject to the prior payment in full of all liabilities of the guarantor thereunder. After providing for all prior claims, there may not be sufficient assets to satisfy the claims of the holders of the New Notes relating to the voided guarantees. We have not separately obtained a solvency opinion in connection with this transaction.

The guarantees may be released under certain circumstances upon resale, exchange or transfer by us of the stock of the related guarantor or all or substantially all of the assets of the guarantor to a non-affiliate.

***If you do not exchange your Original Notes for New Notes, you will continue to be subject to restrictions on transfer of your Original Notes.***

If you do not exchange your Original Notes for the New Notes pursuant to the Exchange Offer, you will continue to be subject to the restrictions on transfer of your Original Notes described in the legend on your Original Notes. The restrictions on transfer of your Original Notes arise because we issued the Original Notes pursuant to exemptions from, or in transactions not subject to, the registration requirements of the Securities Act and applicable state securities laws. In general, you may only offer to sell the Original Notes if they are registered under the Securities Act and applicable state securities laws, or offered and sold pursuant to an exemption from such requirements. We do not intend to register the Original Notes under the Securities Act. In addition, if you exchange your Original Notes in the Exchange Offer for the purpose of participating in a distribution of the New Notes, you may be deemed to have received restricted securities and, if so, will be required to comply with the registration and prospectus delivery requirements of the Securities Act in connection with any resale transaction. To the extent Original Notes are tendered and accepted in the Exchange Offer, the trading market, if any, for the Original Notes would be adversely affected.

***If you do not comply with the specified exchange procedures described in this prospectus, you may be unable to obtain registered notes.***

We will issue the New Notes in exchange for the Original Notes pursuant to this Exchange Offer only after we have timely received such Original Notes, along with a properly completed and duly executed Letter of Transmittal and all other required documents. Therefore, if you want to tender your Original Notes in exchange for New Notes, you should allow sufficient time to ensure timely delivery. Neither the Exchange Agent nor the Company is under any duty to give notification of defects or irregularities with respect to the tender of Original Notes for exchange. The Exchange Offer will expire at 12:00 a.m., New York City time, on \_\_\_\_\_, 2002, or on a later extended date and time as we may decide (the Expiration Date ).

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Original Notes that are not tendered or are tendered but not accepted for exchange will, following the Expiration Date and the consummation of this Exchange Offer, continue to be subject to the existing restrictions upon transfer thereof. In general, the Original Notes may not be offered or sold, unless registered under the Securities Act or except pursuant to an exemption from or in a transaction not subject to, the Securities Act. In addition, if you are still holding any Original Notes after the Expiration Date and the Exchange Offer has been consummated, subject to certain exceptions, you will not be entitled to any rights to have such Original Notes registered under the Securities Act or to any similar rights under the Registration Rights Agreement (subject to limited exceptions, if applicable). We do not currently anticipate that we will register the Original Notes under the Securities Act.

The New Notes and any Original Notes having the same maturity which remain outstanding after consummation of the Exchange Offer will vote together as a single class for purposes of determining whether Holders of the requisite percentage thereof have taken certain actions or exercised certain rights under the Indenture.

### **Requirements for Transfer of New Notes**

Based on interpretations by staff of the SEC, as set forth in no-action letters issued to third parties, we believe that you may offer for resale, resell and otherwise transfer the New Notes without compliance with the registration and prospectus delivery provisions of the Securities Act, subject to certain limitations. These limitations include that you are not an affiliate of ours within the meaning of Rule 405 under the Securities Act, that you acquire your New Notes in the ordinary course of your business and that you have no arrangement with any person to participate in the distribution of such New Notes. However, we have not submitted a no-action letter to the SEC regarding this Exchange Offer and we cannot assure you that the SEC would make a similar determination with respect to the Exchange Offer as in such other circumstances. If you are an affiliate of the Company, are engaged in or intend to engage in or have any arrangement or understanding with respect to a distribution of the New Notes to be acquired pursuant to the Exchange Offer, you

may not rely on the applicable interpretations of the staff of the SEC and

must comply with the registration and prospectus delivery requirements of the Securities Act in connection with any resale transaction.

Each broker-dealer that receives New Notes for its own account pursuant to the Exchange Offer must acknowledge that it will deliver a prospectus meeting the requirements under the Securities Act in connection with any resale of such New Notes. The Letter of Transmittal states that by so acknowledging and delivering a prospectus, a broker-dealer will not be deemed to admit that it is an underwriter within the meaning of the Securities Act. This Prospectus, as it may be amended or supplemented from time to time, may be used by a broker-dealer in connection with resales of New Notes where the Original Notes exchanged for such New Notes were acquired by such broker-dealer as a result of market-making activities or other trading activities. We have agreed to use our best efforts to make this Prospectus available to any participating broker-dealer for use in connection with any such resale. However, to comply with the securities laws of certain jurisdictions, if applicable, the New Notes may not be offered or sold unless they have been registered or qualified for sale in such jurisdictions or an exemption from registration or qualification is available.

### **Risks Relating to the Business**

*Automobile manufacturers exercise significant control over our operations and we depend on them in order to operate our business. Significant declines in sales of new vehicles manufactured by BMW, DaimlerChrysler, Ford, General Motors, Honda, Nissan or Toyota, or the loss of deterioration of our relationship with one or more of these manufacturers, could have a material adverse effect on our revenues and profitability.*

Each of our dealerships operates pursuant to franchise agreements with automobile manufacturers or manufacturer-authorized distributors. We are dependent on our relationships with these automobile

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manufacturers because, without a franchise agreement, we cannot obtain new vehicles from a manufacturer. A large number of our vehicles are manufactured by BMW, DaimlerChrysler, Ford, General Motors, Honda, Nissan and Toyota. A significant decline in the sale of new vehicles manufactured by these manufacturers, or the loss or deterioration of our relationships with one or more of these manufacturers, could have a material adverse effect on our revenues and profitability.

Manufacturers exercise a great degree of control over the operations of our dealerships. For example, manufacturers can require our dealerships to meet specified standards of appearance and quality, require individual dealerships to meet specified financial criteria such as maintenance of minimum net working capital and, in some cases, minimum net worth, impose minimum customer service and satisfaction standards, set standards regarding the maintenance of inventories of vehicles and parts, require dealerships to provide financial statements as often as monthly, and govern the extent to which our dealerships can utilize the manufacturers' names and trademarks. In many cases the manufacturer must consent to the replacement of the dealership's general manager.

Our franchise agreements worldwide may be terminated or not renewed by the automobile manufacturers for a variety of reasons, including any unapproved change of ownership or management and other material breaches of the franchise agreements. We have from time to time been in non-compliance with various provisions of some of our franchise agreements. If any of our significant existing franchise agreements or a large number of franchise agreements are not renewed or the terms and conditions of any such renewals is materially unfavorable to us, there may be a material adverse effect on our revenues and profitability. In addition, actions taken by manufacturers to exploit their bargaining position in negotiating the terms of renewals of franchise agreements or otherwise could also have a material adverse effect on our revenues and profitability.

In addition, we depend on manufacturers to provide us with a desirable mix of popular new vehicles, which produce the highest profit margins and tend to be the most difficult to obtain from manufacturers. Manufacturers generally allocate their vehicles among dealerships based on the sales history of each dealership. If we cannot obtain sufficient quantities of the most popular models, whether due to sales declines at our dealerships or otherwise, our new vehicle sales and profitability may be adversely affected. Sales of less profitable models may reduce our profit margins.

Our dealerships also depend on the manufacturers for sales incentives, warranties and other programs that are intended to promote and support new vehicle sales by our dealerships. Some of these programs include customer rebates on new vehicles, dealer incentives on new vehicles, special financing or leasing terms, warranties on new and used vehicles and sponsorship of used vehicle sales by authorized new vehicle dealers. Manufacturers have historically made many changes to their incentive programs during each year. A reduction or discontinuation of a manufacturer's incentive programs could materially adversely affect our new vehicle sales volume and our profitability.

Our franchise agreements do not give us the exclusive right to sell a manufacturer's product within a given geographic area. Accordingly, a manufacturer may, subject to any protection of state law, grant another dealer a franchise to start a new dealership near one of our locations, or an existing dealer may move its dealership to a location which would compete directly with us. The location of new dealerships near our existing dealerships could materially adversely affect our operations, revenues and profitability.

***Because we depend on the success and popularity of the brands we sell, adverse conditions affecting one or more automobile manufacturers may negatively impact our revenues and profitability.***

Our success depends on the overall success of the line of vehicles that each of our dealerships sells. As a result, our success depends to a great extent on the automobile manufacturers' financial condition, marketing, vehicle design, production and distribution capabilities, reputation, management and labor relations. In 2001, Toyota, DaimlerChrysler, General Motors, Honda and Ford accounted for 28%, 18%, 14%, 12% and 11%, respectively, of our total revenues. No other manufacturer accounted for more than 10% of our total 2001 revenues. Events such as labor strikes that may adversely affect a manufacturer may also adversely affect us. In particular, labor strikes at a manufacturer that continue for a substantial period of time

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could have a material adverse effect on our business. Similarly, the delivery of vehicles from manufacturers at a time later than scheduled, which may occur particularly during periods of new product introductions, could lead to reduced sales during those periods. This has been experienced at some of our dealerships from time to time. In addition, any event that causes adverse publicity involving one or more automobile manufacturers or their vehicles may have an adverse effect on our revenues and profitability regardless of whether that event involves any of our dealerships.

*If we are unable to complete additional acquisitions and successfully integrate acquisitions, we will be unable to achieve desired results from our acquisition strategy.*

Growth in our revenues and earnings depends substantially on our ability to acquire and successfully operate dealerships. We cannot guarantee that we will be able to identify and acquire dealerships in the future. Moreover, acquisitions, including the Sytner acquisition, involve a number of risks, including:

incurring significantly higher capital expenditures and operating expenses;

failing to integrate the operations and personnel of the acquired dealerships;

entering new markets with which we are not familiar;

incurring undiscovered liabilities at acquired dealerships;

disrupting our ongoing business;

failing to retain key personnel of the acquired dealerships;

impairing relationships with employees, manufacturers and customers; and

incorrectly valuing acquired entities.

In addition, managing and integrating additional dealerships into our existing mix of dealerships may result in substantial costs, diversion of our management resources or other operational or financial problems. Unforeseen expenses, difficulties, complications and delays frequently encountered in connection with the integration of acquired entities and the rapid expansion of operations could inhibit our growth, result in our failure to achieve acquisition synergies and require us to focus resources on integration rather than more profitable areas.

Acquired entities may subject us to unforeseen liabilities that we are unable to detect prior to completing the acquisition or liabilities that turn out to be greater than those we had expected. These liabilities may include liabilities that arise from non-compliance with environmental laws by prior owners for which we, as a successor owner, will be responsible. Until we assume operating control of acquired entities, we may not be able to ascertain the actual value of the acquired entity.

There can be no assurance that we will identify acquisition candidates that would result in the most successful combinations or that we will be able to complete acquisitions on acceptable terms on a timely basis. The magnitude, timing and nature of future acquisitions will depend upon various factors, including the availability of suitable acquisition candidates, the negotiation of acceptable terms, our financial capabilities, the availability of skilled employees to manage the acquired companies and general economic and business conditions. Further, covenants contained in our debt instruments impose limitations on our ability to acquire additional dealerships and future debt instruments may impose additional restrictions.

Our future growth via acquisition of automobile dealerships in the United States and abroad will depend on our ability to obtain the requisite manufacturer approvals. We must obtain the consent of a manufacturer prior to the acquisition of any of its dealership franchises anywhere in the world. Obtaining the consent of a manufacturer for the acquisition of a dealership could take a significant amount of time or be rejected entirely. In addition, under many franchise agreements or under state law, a manufacturer will have a right of first refusal to acquire a dealership that we seek to acquire. Alternatively, in connection with acquisitions by us, one or more manufacturers may seek to impose various conditions on us in connection with their approval of an acquisition. If the conditions are not satisfied, we may be precluded from acquiring, either directly or



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through acquisitions, additional franchises. In addition, factors outside our control may cause a manufacturer to reject our application to make acquisitions. In determining whether to approve an acquisition, manufacturers may consider many factors, including the moral character and business experience of the dealership principals and the financial condition, ownership structure, the number of current franchises owned, sales performance and customer satisfaction index scores of our dealerships. In addition, manufacturers limit the total number of their dealerships that we may own nationally or in a particular geographic area or metropolitan region and, in some cases, the total number of their vehicles that we may sell as a percentage of that manufacturer's overall sales. Manufacturers also limit the ownership of stores in contiguous markets, the dualing of a franchise with another brand, and the frequency of acquisitions. Although to date we have only reached these ceilings with one manufacturer, our growth strategy may be affected by these limits.

***We may not be able to satisfy our capital requirements for making acquisitions and financing the purchase of our inventory, which could have a material adverse effect on our operations and hinder our ability to achieve our growth strategy.***

We require substantial capital in order to acquire automobile dealerships. This capital might be raised through public or private financing, including through the issuance of our equity securities as full or partial consideration for acquisitions, as well as borrowings and other sources. Other than our credit agreement, we do not have any commitments or immediate plans with respect to acquisition financing. Availability under our credit agreement is limited by a collateral-based borrowing base calculated using our net tangible assets. There can be no assurance that additional or sufficient financing will be available, or, if available, that it will be available on acceptable terms. If we raise additional funds by issuing our equity securities, dilution to then existing stockholders may result. The extent to which we will be able or willing to issue equity securities for acquisitions will depend on the market value of our common stock and the willingness of our potential acquisition candidates to accept equity securities as partial or full consideration for the sale of their businesses. The number of shares of common stock that we issue in connection with acquisitions could be large. In addition, a decline in the market price of our common stock for any reason, including, without limitation, a perception that sales of substantial amounts of common stock which are not then publicly registered could occur, may increase the amount of cash required by us to finance acquisitions. If adequate funds are not available, we may be required to significantly curtail our acquisition program, which would materially and adversely affect our growth strategy.

We depend to a significant extent on our ability to finance the purchase of inventory, which in the automotive retail industry involves borrowing significant sums of money in the form of floor plan financing. Floor plan financing is the vehicle through which dealerships finance the purchase of new vehicles from a manufacturer. The dealership borrows money to buy a particular vehicle from the manufacturer and pays off the loan when it sells the particular vehicle, paying interest during the interim period. In connection with acquisitions of dealerships, we must either obtain new floor plan financing or obtain consents to assume that financing. Our floor plan financing is secured by substantially all of the assets of our automotive dealership subsidiaries and, in some cases, a guarantee from us. Our remaining assets are pledged to secure our credit agreement. This may impede our ability to borrow from other sources. Most of our floor plan lenders are associated with manufacturers with whom we have franchise agreements. Consequently, the deterioration of our relationship with a manufacturer could adversely affect our relationship with the affiliated floor plan lender and vice versa.

Any inability to obtain floor plan financing on customary terms, or the termination of our floor plan financing arrangements by our floor plan lenders, would have a material adverse effect on our operations.

***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 and our profitability.***

Many manufacturers attempt to measure customers' satisfaction with their sales and warranty service experiences through systems which vary from manufacturer to manufacturer but which are generally known as customer satisfaction indices, or CSI. These manufacturers may use a dealership's CSI scores as a factor in



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evaluating applications for additional dealership acquisitions. The components of CSI have been modified by various manufacturers from time to time in the past, and these components might be further modified or replaced by different systems in the future. To date, we have not been materially adversely affected by these standards and have not been denied approval of any acquisition based on low CSI scores, although certain of our dealerships have had difficulty from time to time meeting their manufacturers' CSI standards. However, we cannot be sure that we will be able to comply with these standards in the future. A manufacturer may refuse to consent to an acquisition of one of its franchises if it determines that our dealerships do not comply with the manufacturer's CSI standards. This could materially adversely affect our acquisition strategy. In addition, because we receive payments from the manufacturers based in part on CSI scores, future payments could be materially reduced or eliminated if our CSI scores decline.

***Automobile manufacturers impose limits on our ability to issue additional equity and on the ownership of our common stock by third parties, which may hamper our ability to meet our financing needs.***

A number of manufacturers impose restrictions on the sale and transfer of our common stock. The most prohibitive restrictions provide that, under specified circumstances, we may be forced to sell or surrender franchises (1) if a competitor automobile manufacturer acquires a 5% or greater ownership interest in us if the manufacturer objects to that acquisition within 60 days or (2) if an individual or entity that has a criminal record in connection with business dealings with any automobile manufacturer, distributor or dealer or who has been convicted of a felony acquires a 5% or greater ownership interest in us and the manufacturer objects to that acquisition within 60 days. Similarly, several manufacturers, such as Nissan, Toyota, Mercedes, General Motors, Infiniti and Isuzu, have the right to approve the acquisition by a third party of 20% or more of our voting equity, and a number of manufacturers, including BMW, Toyota, Honda, DaimlerChrysler, Ford, General Motors, and Jaguar, continue to prohibit changes in ownership that may affect control of our company. One manufacturer (Ferrari North America) can repurchase its dealerships if Roger Penske's ownership falls below 37.6% or if Mr. Penske is no longer our chief executive officer.

Actions by our stockholders or prospective stockholders that would violate any of the above restrictions are generally outside our control. If we are unable to renegotiate these restrictions, we may be forced to terminate or sell one or more franchises, which could have a material adverse effect on us. This may also inhibit our ability to acquire dealership groups. These restrictions also may prevent or deter prospective acquirers from acquiring control of us and, therefore, may adversely impact the value of our common stock. These restrictions also may impede our ability to raise required capital or to issue our stock as consideration for future acquisitions.

***Our business and the automotive retail industry in general are susceptible to adverse economic conditions, including changes in consumer confidence, fuel prices and credit availability, which could have a material adverse effect on our business, revenues and profitability and make it difficult to attain our growth strategy.***

We believe that the automotive retail industry is influenced by general economic conditions and particularly by consumer confidence, the level of personal discretionary spending, interest rates, fuel prices, unemployment rates and credit availability. Historically, unit sales of motor vehicles, particularly new vehicles, have been cyclical, fluctuating with general economic cycles. During economic downturns, retail new vehicle sales tend to experience periods of decline characterized by oversupply and weak demand. The current economic outlook in the aftermath of the September 11, 2001 attacks is uncertain. The automotive retail industry may experience sustained periods of decline in vehicle sales in the future. In addition, changes in interest rates could significantly impact our vehicle sales because a significant portion of vehicle buyers finance their purchases. Any decline or change of this type could have a material adverse effect on our business, revenues and profitability.

In addition, local economic, competitive and other conditions affect the performance of our dealerships. Our revenues and profitability depend substantially on general economic conditions and spending habits in those regions of the United States where we maintain most of our operations.

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*Substantial competition in automotive sales and services may adversely affect our profitability due to our need to lower prices to sustain sales and profitability.*

The automotive retail industry is highly competitive. Depending on the geographic market, we compete with:

franchised automotive dealerships in our markets that sell the same or similar makes of new and used vehicles that we offer and occasionally at lower prices than us;

other national or regional affiliated groups of franchised dealerships;

private market buyers and sellers of used vehicles;

Internet-based vehicle brokers that sell vehicles obtained from franchised dealers directly to consumers;

service center chain stores; and

independent service and repair shops.

We also compete with regional and national vehicle rental companies that sell their used rental vehicles. In addition, automobile manufacturers may directly enter the retail market in the future, which could have a material adverse effect on us. As we seek to acquire dealerships in new markets, we may face significant competition as we strive to gain market share. Some of our competitors have greater financial, marketing and personnel resources and lower overhead and sales costs than us. We do not have any cost advantage in purchasing new vehicles from the automobile manufacturers and typically rely on advertising, merchandising, sales expertise, service reputation and dealership location in order to sell new vehicles. Our franchise agreements do not grant us the exclusive right to sell a manufacturer's product within a given geographic area. Our revenues and profitability may be materially and adversely affected if competing dealerships expand their market share or are awarded additional franchises by manufacturers that supply our dealerships.

In addition to competition for vehicle sales, our dealerships compete with franchised dealerships to perform warranty repairs and with other automotive dealers, franchised and independent service center chains and independent garages for non-warranty repair and routine maintenance business. Our dealerships compete with other automotive dealers, service stores and auto parts retailers in their parts operations. We believe that the principal competitive factors in service and parts sales are price, the use of factory-approved replacement parts, the familiarity with a manufacturer's brands and models and the quality of customer service. A number of regional or national chains offer selected parts and services at prices that may be lower than our dealerships' prices. We also compete with a broad range of financial institutions in arranging financing for our customers' vehicle purchases.

Some automobile manufacturers have begun to acquire automotive dealerships or may do so in the future. Our revenues and profitability could be materially adversely affected by the efforts of manufacturers to enter the retail arena.

In addition, the Internet is becoming a significant part of the sales process in our industry. We believe that customers are using the Internet as part of the sales process to compare pricing for cars and related finance and insurance services, which may reduce gross profit margins for new and used cars and profits for related finance and insurance services. Some websites offer vehicles for sale over the Internet without the benefit of having a dealership franchise, although they must currently source their vehicles from a franchised dealer. If Internet new vehicle sales are allowed to be conducted without the involvement of franchised dealers, or if dealerships are able to effectively use the Internet to sell outside of their markets, our business could be materially adversely affected. We would also be materially adversely affected to the extent that Internet companies acquire dealerships or ally themselves with our competitors' dealerships.

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***Because automotive retailing is a mature industry with limited growth potential in new vehicle sales, our growth and earnings will depend significantly on acquisitions and consolidations and expansion of our higher margin businesses.***

The U.S. automotive retail industry is considered a mature industry in which minimal growth in unit sales of new vehicles is expected. Accordingly, growth in our revenues and earnings will depend significantly on our ability to acquire and consolidate profitable dealerships, grow our higher-margin businesses and expand our automobile financing and other aftermarket business.

***If we lose key personnel or are unable to attract additional qualified personnel, our business could be adversely affected because we rely on the industry knowledge and relationships of our key personnel.***

We believe that our success depends to a significant extent upon the efforts and abilities of our executive management and key employees, including, in particular, Roger S. Penske. Additionally, our business is dependent upon our ability to continue to attract and retain qualified personnel, such as managers, as well as retaining executive management in connection with acquisitions. We generally have not entered into employment agreements with our key personnel. The loss of the services of one or more members of our senior management team, including, in particular, Roger S. Penske, could have a material adverse effect on us and materially impair the efficiency and productivity of our operations. We do not have key man insurance for any of our executive officers or key personnel. In addition, the loss of any of our key employees or the failure to attract qualified managers could have a material adverse effect on our business and may materially impact the ability of our dealerships to conduct their operations in accordance with our national standards.

***Our quarterly operating results may fluctuate due to seasonality in the automotive retail business and other factors.***

The automobile industry experiences seasonal variations in revenues. Demand for automobiles is generally lower during the winter months than in other seasons, particularly in regions of the United States associated with harsh winters. A higher amount of vehicle sales generally occurs in the second and third fiscal quarters of each year due in part to consumer buying trends and the introduction of new vehicle models. Therefore, if conditions surface in the second or third quarters that depress or affect automotive sales, such as high fuel costs, depressed economic conditions or similar adverse conditions, our revenues for the year will be disproportionately adversely affected. Our dealerships located in the northeastern states are affected by seasonality more than our dealerships in other regions.

In addition, the U.K. retail automotive industry typically experiences peak sales activity during March and September of each year. This seasonality results from the perception in the U.K. that the resale value of a vehicle may be determined by the date that the vehicle is registered. Because new vehicle registration periods begin on March 1 and September 1 each year, vehicles with comparable mileage that were registered in March may have an equivalent used vehicle value to vehicles registered in August of the same year.

***Our business may be adversely affected by import product restrictions and foreign trade risks that may impair our ability to sell foreign vehicles profitably.***

A significant portion of our new vehicle business involves the sale of vehicles, vehicle parts or vehicles composed of parts that are manufactured outside the United States. As a result, our operations are subject to customary risks associated with imported merchandise, including fluctuations in the relative value of currencies, import duties, exchange controls, differing tax structures, trade restrictions, transportation costs, work stoppages and general political and economic conditions in foreign countries.

The United States or the countries from which our products are imported may, from time to time, impose new quotas, duties, tariffs or other restrictions, or adjust presently prevailing quotas, duties or tariffs on imported merchandise. Any of those impositions or adjustments could materially affect our operations and our ability to purchase imported vehicles and parts at reasonable prices, which could have a material adverse effect on our business.

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***Our automotive dealerships are subject to substantial regulation which may adversely affect our profitability and significantly increase our costs in the future.***

A number of foreign, federal, state and local regulations affect our business of marketing, selling, financing and servicing automobiles. We also are subject to laws and regulations relating to business corporations generally.

Under the laws of states in which we currently operate or into which we may expand, we typically must obtain a license in order to establish, operate or relocate a dealership or operate an automotive repair service, including dealer, sales, finance and insurance-related licenses issued by state authorities. These laws also regulate our conduct of business, including our advertising, operating, financing, employment and sales practices. Other laws and regulations include state franchise laws and regulations and other extensive laws and regulations applicable to new and used motor vehicle dealers, as well as federal and state wage-hour, anti-discrimination and other employment practices laws. Our operations are also subject to the National Traffic and Motor Vehicle Safety Act, the Magnusson-Moss Warranty Act, Federal Motor Vehicle Safety Standards promulgated by the United States Department of Transportation and various state motor vehicle regulatory agencies.

Our operations are also subject to consumer protection laws known as Lemon Laws. These laws typically require a manufacturer or dealer to replace a new vehicle or accept it for a full refund within one year after initial purchase if the vehicle does not conform to the manufacturer's express warranties and the dealer or manufacturer, after a reasonable number of attempts, is unable to correct or repair the defect. Federal laws require various written disclosures to be provided on new vehicles, including mileage and pricing information.

The imported automobiles purchased by us are subject to U.S. customs duties and, in the ordinary course of our business, we may, from time to time, be subject to claims for duties, penalties, liquidated damages, or other charges.

Our financing activities with customers are subject to federal truth-in-lending, consumer leasing and equal credit opportunity regulations as well as state and local motor vehicle finance laws, installment finance laws, insurance laws, usury laws and other installment sales laws. Some states regulate finance fees that may be paid as a result of vehicle sales.

Possible penalties for violation of any of these laws or regulations include revocation or suspension of our licenses and civil or criminal fines and penalties. In addition, many laws may give customers a private cause of action.

Violation of these laws or costs of compliance with these laws or changes in these laws could result in adverse financial consequences to us.

***If state dealer laws in the United States are repealed or weakened, our automotive dealerships will be more susceptible to termination, non-renewal or renegotiation of their franchise agreements.***

State dealer laws generally provide that a manufacturer may not terminate or refuse to renew a franchise agreement unless it has first provided the dealer with written notice setting forth good cause and stating the grounds for termination or non-renewal. Some state dealer laws allow dealers to file protests or petitions or to attempt to comply with the manufacturer's criteria within the notice period to avoid the termination or non-renewal. Though unsuccessful to date, manufacturers' lobbying efforts may lead to the repeal or revision of state dealer laws. If dealer laws are repealed in the states in which we operate, manufacturers may be able to terminate our franchises without providing advance notice, an opportunity to cure or a showing of good cause. Without the protection of state dealer laws, it may also be more difficult for our dealers to renew their franchise agreements upon expiration. In addition, Europe does not have state dealer laws and, as a result, our European operations will be required to operate without these protections.

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***Our automotive dealerships are subject to foreign, federal, state and local environmental regulations that may result in claims and liabilities, which could be material.***

We are subject to a wide range of foreign, federal, state and local environmental laws and regulations, including those governing discharges into the air and water, the operation and removal of underground and aboveground storage tanks, the use, handling, storage and disposal of hazardous substances and other materials and the investigation and remediation of contamination. As with automotive dealerships generally, and service, parts and body shop operations in particular, our business involves the use, storage, handling and contracting for recycling or disposal of hazardous materials or wastes and other environmentally sensitive materials. Operations involving the management of hazardous and non-hazardous materials are subject to requirements of the federal Resource Conservation and Recovery Act, or RCRA, and comparable state statutes. Our business also involves the operation of storage tanks containing such materials. Storage tanks are subject to periodic testing, containment, upgrading and removal under RCRA and comparable statutes. Furthermore, investigation or remediation may be necessary in the event of leaks or other discharges from current or former underground or aboveground storage tanks. We may also have liability in connection with materials that were sent to third-party recycling, treatment, and/or disposal facilities under the Comprehensive Environmental Response, Compensation and Liability Act, and comparable state statutes, which impose liability for investigation and remediation of contamination without regard to fault or the legality of the conduct that contributed to the contamination. Similar to many of our competitors, we have incurred and will continue to incur, capital and operating expenditures and other costs in complying with such laws and regulations.

However, soil and groundwater contamination is known to exist at some of our current or former properties. Further, environmental laws and regulations are complex and subject to change. In addition, in connection with our acquisitions, it is possible that we will assume or become subject to new or unforeseen environmental costs or liabilities, some of which may be material. In connection with our dispositions, or prior dispositions made by companies we acquire, we may retain exposure for environmental costs and liabilities, some of which may be material. Compliance with current or amended, or new or more stringent, laws or regulations, stricter interpretations of existing laws or the future discovery of environmental conditions could require additional expenditures by us, and those expenditures could be material. See Business Environmental Matters.

***Our principal stockholders have substantial influence over us and may make decisions with which you disagree. Some of our directors and officers may have conflicts of interest with respect to certain related party transactions and other business interests.***

As a result of the equity offering on March 18, 2002, Penske Corporation, Penske Capital Partners, L.L.C. and various of their affiliates beneficially owns over 55% of our outstanding common stock. In addition, these entities have entered into a stockholders agreement with several of our other stockholders in which they have agreed to elect five nominees of Penske Capital Partners to our board of directors. As a result, these persons have the ability to control us and direct our affairs and business.

This concentration of ownership, as well as various provisions contained in our agreements with manufacturers, our certificate of incorporation and bylaws and the Delaware General Corporation Law, could have the effect of discouraging, delaying or preventing a change in control of us or unsolicited acquisition proposals. These provisions include the stock ownership limits imposed by various manufacturers, the classified structure of our board of directors, our ability to issue blank check preferred stock and the interested stockholder provisions of Section 203 of Delaware law.

Some of our executive officers affiliated with our largest stockholder hold executive positions at companies other than our company. Roger S. Penske, our Chairman and Chief Executive Officer, is also Chairman and Chief Executive Officer of Penske Corporation, a diversified transportation services company, and Chairman of Penske Truck Leasing Corporation. Robert H. Kurnick, Jr., our Executive Vice President and General Counsel, is also Executive Vice President of Penske Corporation and General Counsel of Penske Capital Partners, LLC and Paul H. Walters, our Executive Vice President Human Resources, is also

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Executive Vice President Administration of Penske Corporation. Much of the compensation of these officers is generally paid by Penske Corporation and not by us, and while these officers have historically devoted a substantial majority of their time to our matters, these officers are not required to spend any specific amount of time on our matters. In addition, James A. Hislop, one of our directors, is President and Chief Executive Officer of Penske Capital Partners, LLC and a director of Penske Corporation, and Richard J. Peters, one of our directors, is the President and a director of Penske Corporation. In addition, Penske Corporation is the owner of Penske Automotive Group, a privately-held automotive dealership company with operations in southern California. Due to their relationships with their related entities, Messrs. Penske, Kurnick, Walters, Hislop and Peters may have a conflict of interest in making any decision related to transactions between their related entities and us or with respect to allocations of corporate opportunities. To date, all affiliated transactions have been approved by an affirmative vote of a majority of the disinterested members of our board of directors.

***Due to the nature of the automotive retailing business, we may be involved in legal proceedings or suffer losses that could have a material adverse effect on our business.***

We will generally continue to be involved in legal proceedings in the ordinary course of business. A significant judgment against us, the loss of a significant license or permit or the imposition of a significant fine could have a material adverse effect on our business, financial condition and future prospects. In addition, it is possible that we could suffer losses at individual dealerships due to fraud or theft.

***Changes in the European Commission's regulations regarding automobile manufacturers may have an adverse effect on Sytner and result in greater competition and decreased profitability.***

European automobile manufacturers and distributors have, for the past sixteen years, benefited from successive European Commission Block Exemptions. The current Block Exemption has been in place since 1995. It gives European vehicle companies and dealers immunity from a number of antitrust restrictions on distribution and servicing agreements and has allowed vehicle manufacturers to sell vehicles only through selected dealers, each with exclusive territories.

The Block Exemption will expire on September 30, 2002 and a new draft Regulation, approved by the European Commission on February 5, 2002, has been proposed as a replacement regime governing the relationship between European automobile manufacturers and dealers.

The European Commission adopted an evaluation report on the operation of the current Block Exemption which concluded that several of the underlying aims of the Block Exemption had not been achieved. It concluded that European consumers found it hard to exercise their rights under the single market and to take advantage of price differentials between member states, that competition between dealers is not strong enough and that dealers remain too dependent on vehicle manufacturers.

The new draft Regulation does not prescribe a single rigid model for vehicle distribution, but rather leaves a set of choices open to vehicle manufacturers, distributors and dealers. Its key features are:

vehicle manufacturers may choose between exclusive distribution, where each dealer approved by the manufacturer is allowed a sales territory, and selective distribution, where dealers are selected according to a set of criteria;

there are no prescriptions about the type of criteria that might be used or the way distribution networks are organized, other than a defined blacklist of severely anti-competitive restrictions;

retailers will have a choice about whether they sell more than one brand of car;

dealers in a selective distribution system may engage in active sales throughout the European Union, or set up other sales outlets or delivery points in any member state; and

dealers may choose whether they wish to carry out repairs themselves, or subcontract them to another authorized member of the manufacturer's network (independent repairers may become authorized repairers without being obliged to sell new vehicles).

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The draft Regulation will be further considered by the Advisory Committee on Restrictive Practices and Dominant Positions in March 2002 with a view to being formally adopted by the European Commission before the summer and to come into force on October 1, 2002. It is then expected to remain in place until May 31, 2010.

*The Sytner acquisition exposes us to the risks involved in international operations, including currency fluctuation risks, which could have a material effect on our results of operations or financial position as reported in U.S. dollars.*

The acquisition of Sytner has been our largest expansion outside of the United States. We do not have significant experience operating dealerships outside of the United States and strategies that have succeeded in the U.S. may not achieve similar results in the United Kingdom. Moreover, our international expansion has exposed us generally to the risks involved in foreign operations, including:

changes in international tax laws and treaties, including increases of withholding and other taxes on remittances and other payments by subsidiaries;

currency and exchange risks;

tariffs, trade barriers, and restrictions on the transfer of funds between nations;

changes in U.K. governmental regulations;

the impact of local economic and political conditions;

the impact of European Commission regulation and the relationship between the U.K. and continental Europe; and

increased competition and the impact on vehicle pricing resulting from the expiration of the Block Exemption.

In addition, Sytner's results of operations and financial position are reported in British pounds sterling and will then be translated into U.S. dollars at the applicable foreign currency exchange rate for inclusion in our consolidated financial statements. As exchange rates between the U.K. and the U.S. fluctuate, the translation effect of such fluctuations may have a material effect on our results of operations or financial position as reported in U.S. dollars.

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ITEM 7. FINANCIAL STATEMENTS

**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.*

**General**

We are the third largest publicly-held automotive retailer in the United States as measured by total revenues. As of March 31, 2002, we owned and operated 123 franchises in the United States and 66 franchises internationally, primarily in the United Kingdom. As an integral part of our dealership operations, we retail new and used automobiles and light trucks, operate service and parts departments, operate collision repair centers and sell various aftermarket products, including finance, warranty, extended service and other insurance contracts.

New vehicle revenues include sales to retail customers and to leasing companies providing consumer automobile leasing. Used vehicle revenues include amounts received for used vehicles sold to retail customers, leasing companies providing consumer leasing and other dealers. We generate finance and insurance revenues from sales of warranty policies, extended service contracts, other insurance policies, and accessories, as well as from fees for placing finance and lease contracts. Service and parts revenues include fees paid for repair and maintenance service, the sale of replacement parts and body shop repairs.

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, and service and parts services. Our gross profit generally varies across product lines, with new vehicle sales usually resulting in lower gross profit margins and our other products resulting in higher gross profit margins. Factors such as seasonality, weather, cyclicalities and manufacturers' advertising and incentives may impact the mix of our revenues, and therefore influence our gross profit margin.

Our selling expenses consist of advertising and compensation for sales department personnel, including commissions and related bonuses. General and administrative expenses include compensation for administration, finance, legal and general management personnel, depreciation, amortization, rent, insurance, utilities and other outside services. A significant portion of our selling expenses are variable (such as sales commissions), and a significant portion of our general and administrative expenses are subject to our control (such as advertising), allowing us to adjust them over time to reflect economic trends.

Floor plan interest expense relates to floor plan financing. Other interest expense consists of interest charges on all of our interest-bearing debt, other than interest relating to floor plan financing.

We have made a number of dealership acquisitions in each year since 1999. Each of these acquisitions has been accounted for using the purchase method of accounting. As a result, our financial statements include the results of operations of the acquired dealerships from the date of acquisition.

**Critical Accounting Policies**

The preparation of financial statements in accordance with accounting standards generally accepted in the United States of America requires the application of accounting policies that often involve a significant amount of judgment. Such judgments influence the reported amounts of the assets, liabilities, revenues and expenses in the Company's consolidated financial statements. Management, on an ongoing basis, reviews estimates and assumptions. If management determines, as a result of its consideration of facts and circumstances, that modifications in assumptions and estimates are appropriate, results of operations and financial position as reported in the consolidated financial statements may change significantly.

Following is a summary of the accounting policies applied in the preparation of our consolidated financial statements that management believes are most dependent upon the use of estimates and assumptions.





**Table of Contents*****Finance and Insurance Revenue Recognition***

The Company arranges financing for customers through various financial institutions and receives a commission from the lender equal to the difference between the interest rates charged to customers over the predetermined interest rates set by the financing institution. The Company also receives commissions from the sale of various insurance products to customers, including credit, life, and health insurance policies and extended service contracts. The Company receives fee income from the placement of these contracts at the time the customer enters into the contract. The Company is not the obligor under any of these contracts. In the case of finance contracts, a customer may prepay, or fail to pay, thereby terminating the contract. Customers may also terminate extended warranty contracts with the underlying warranty provider, which are fully paid at purchase, and become eligible for refunds of unused premiums. If the customer terminates a retail finance contract or cancels an extended warranty or other insurance product prior to scheduled maturity, a portion of these fees may be charged back to us based on the relevant terms of the contracts. The revenue we record relating to these fees is net of an estimate of the ultimate amount of chargebacks we will be required to pay. Such estimate of ultimate chargeback exposure is based on our historical chargeback expense, including the impact of refinance and default rates on retail finance contracts and cancellation rates on extended warranty contracts and other insurance products, arising from similar contracts.

**Results of Operations*****Three Months Ended March 31, 2002 Compared to Three Months Ended March 31, 2001***

**Revenues.** Retail revenues, which exclude revenues relating to fleet and wholesale transactions, increased by \$252.8 million, or 20.3%, from \$1.2 billion to \$1.5 billion. The overall increase in retail revenues is due primarily to: (1) a \$73.7 million, or 6.4%, increase in retail revenues at dealerships owned prior to January 1, 2001, and (2) dealership acquisitions made subsequent to January 1, 2001, partially offset by a decrease in revenues resulting from the divestiture of certain dealerships. The overall increase in retail revenues at dealerships owned prior to January 1, 2001 reflects 7.3%, 2.3%, 12.4% and 7.7% increases in new retail vehicle, used retail vehicle, finance and insurance and service and parts revenues, respectively. Revenues of \$134.8 million from fleet and wholesale transactions represent a 6.9% increase versus the prior year. The increase in fleet and wholesale revenues is due to acquisitions subsequent to January 1, 2001, offset by a \$5.1 million, or 4.6% decrease at stores owned prior to January 1, 2001.

Retail sales of new vehicles increased by \$171.9 million, or 21.3%, from \$805.9 million to \$977.8 million. The increase is due primarily to: (1) a \$54.6 million, or 7.3%, increase at dealerships owned prior to January 1, 2001 and (2) acquisitions made subsequent to January 1, 2001, partially offset by a decrease resulting from the divestiture of certain dealerships. The increase at dealerships owned prior to January 1, 2001, is due primarily to a 4.7% increase in new retail unit sales which increased revenue by \$34.8 million and a 2.5% increase in comparative average selling prices per vehicle which increased revenue by \$19.8 million. The Company believes that this increase is due in part to its favorable brand mix, which includes a higher concentration of foreign nameplates which have been steadily increasing market share in the United States. Approximately 90% of the increase in new retail unit sales at dealerships owned prior to January 1, 2001 results from sales of these foreign nameplates. Aggregate retail unit sales of new vehicles increased by 16.0%, due principally to: (1) the net increase at dealerships owned prior to January 1, 2001 and (2) acquisitions made subsequent to January 1, 2001, partially offset by the decrease due to divested dealerships. We retailed 36,007 new vehicles (66.5% of total retail vehicle sales) during the three months ended March 31, 2002, compared with 31,035 new vehicles (65.3% of total retail vehicle sales) during the three months ended March 31, 2001.

Retail sales of used vehicles increased by \$46.1 million, or 17.3%, from \$266.0 million to \$312.0 million. The increase is due primarily to: (1) a \$5.6 million, or 2.3%, increase at dealerships owned prior to January 1, 2001 and (2) acquisitions made subsequent to January 1, 2001, partially offset by a decrease resulting from the divestiture of certain dealerships. The increase at dealerships owned prior to January 1, 2001, is due primarily to a 2.7% increase in used retail unit sales which increased revenue by \$6.6 million, offset by a decrease in comparative average selling prices per vehicle which reduced revenue by

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\$1.0 million. Aggregate retail unit sales of used vehicles increased by 10.2%, due principally to: (1) the net increase at dealerships owned prior to January 1, 2001, and (2) acquisitions made subsequent to January 1, 2001, partially offset by the decrease due to divested dealerships. We retailed 18,169 used vehicles (33.5% of total retail vehicle sales) during the three months ended March 31, 2002, compared with 16,486 used vehicles (34.7% of total retail vehicle sales) during the three months ended March 31, 2001.

Finance and insurance revenues increased by \$6.1 million, or 18.3%, from \$33.0 million to \$39.1 million. The increase is due primarily to: (1) a \$3.4 million, or 12.4%, increase at dealerships owned prior to January 1, 2001 and (2) acquisitions made subsequent to January 1, 2001, partially offset by a decrease resulting from the divestiture of certain dealerships. The increase at dealerships owned prior to January 1, 2001 is primarily due to a revenue increase of \$50 per retail vehicle sold, which increased revenue by \$2.3 million, and a 4% increase in retail vehicles sold, which increased revenue by \$1.1 million.

Service and parts revenues increased by \$28.8 million, or 20.5%, from \$140.6 million to \$169.4 million. The increase is due primarily to: (1) a \$10.1 million, or 7.7%, increase at dealerships owned prior to January 1, 2001 and (2) acquisitions made subsequent to January 1, 2001, partially offset by a decrease resulting from the divestiture of certain dealerships. The Company believes that its service and parts business is being positively impacted by the complexity of today's vehicles, manufacturers' warranty programs for both new and certified used vehicles and increases in retail unit sales at our dealerships.

Fleet revenues decreased \$3.2 million, or 8.5%, versus the comparable prior year period. The decrease in fleet revenues is due primarily to: (1) a \$3.7 million, or 11.9%, decrease in fleet sales revenues at dealerships owned prior to January 1, 2001 and (2) a decrease resulting from the divestiture of certain dealerships, partially offset by an increase due to acquisitions made subsequent to January 1, 2001.

Wholesale revenues increased \$11.9 million, or 13.4%, versus the comparable prior year period. The increase in wholesale revenues is due primarily to acquisitions made subsequent to January 1, 2001, partially offset by (1) a \$1.5 million, or 1.8%, decrease at dealerships owned prior to January 1, 2001 and (2) a decrease resulting from the divestiture of certain dealerships.

*Gross Profit.* Retail gross profit, which excludes gross profit on fleet and wholesale transactions, increased \$44.5 million, or 23.3%, from \$191.5 million to \$236.0 million. The increase in gross profit is due to: (1) a \$16.9 million, or 9.8%, increase in retail gross profit at stores owned prior to January 1, 2001, and (2) acquisitions made subsequent to January 1, 2001, partially offset by a decrease resulting from the divestiture of certain dealerships. Gross profit as a percentage of revenues on retail transactions increased from 14.0% to 14.5%. Gross profit as a percentage of revenues for new vehicle retail, used vehicle retail, finance and insurance and service and parts revenues was 8.6%, 11.1%, 100.0%, and 46.0%, respectively, compared with 8.4%, 10.5%, 100.0% and 44.8% in the comparable prior year period. The increase in gross profit as a percentage of revenues on retail transactions is primarily attributable to: (1) increased gross profit margins on new vehicle revenues, (2) increased gross profit margins on used vehicle revenues and (3) increased gross profit margins on service and parts revenues, partially offset by an increase in the relative proportion of lower margin new vehicle sales revenues to total retail vehicle revenues. Aggregate gross profit on fleet and wholesale transactions increased by \$0.7 million to \$1.0 million.

*Selling, General and Administrative Expenses.* Selling, general and administrative expenses increased by \$35.9 million, or 22.8%, from \$157.9 million to \$193.8 million. Such expenses increased as a percentage of total revenue from 11.5% to 11.9%, and decreased as a percentage of gross profit from 82.3% to 81.8%. The aggregate increase in selling, general and administrative expenses is due principally to: (1) a \$16.1 million, or 11.8%, increase at dealerships owned prior to January 1, 2001, and (2) acquisitions made subsequent to January 1, 2001, partially offset by (1) a \$4.6 million decrease in goodwill amortization due to the adoption of SFAS No. 142, and (2) a decrease resulting from the divestiture of certain dealerships. The increase in selling, general and administrative expenses at stores owned prior to January 1, 2001 is due in large part to increased selling expenses, including increases in variable compensation as a result of the 9.8% increase in retail gross profit over the prior year, depreciation, healthcare costs, and other insurance costs versus the prior year.

*Floor Plan Interest Expense.* Floor plan interest expense decreased by \$4.0 million, or 31.5%, from \$12.6 million to \$8.6 million. The decrease in floor plan interest expense is due to (1) a \$6.7 million, or

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62.6%, decrease at stores owned prior to January 1, 2001 and (2) a decrease relating to the divestiture of certain dealerships, partially offset by acquisitions made subsequent to January 1, 2001. The decrease at stores owned prior to January 1, 2001 is due primarily to a decrease in inventory at dealerships owned prior to January 1, 2001, coupled with a decrease in our weighted average borrowing rate on floor plan indebtedness during 2002.

*Other Interest Expense.* Other interest expense decreased by \$1.8 million, or 18.6%, from \$9.7 million to \$7.9 million. The decrease is due primarily to increased acquisition related indebtedness, offset in part by (1) a decrease in our weighted average borrowing rate during 2002 and (2) the pay-down of indebtedness with proceeds from equity offerings subsequent to December 31, 2001.

*Income Taxes.* Income taxes increased by \$5.5 million from \$5.1 million to \$10.6 million. The increase is due to an increase in pre-tax income compared with 2001, partially offset by a decrease in our estimated effective annual tax rate.

***Year Ended December 31, 2001 Compared to Year Ended December 31, 2000***

*Revenues.* Retail revenues, which exclude revenues relating to fleet and wholesale transactions, increased by \$1.3 billion, or 28.5%, from \$4.4 billion to \$5.7 billion. The overall increase in retail revenues is due primarily to: (1) a \$328.9 million, or 9.1%, increase in retail revenues at dealerships owned prior to January 1, 2000, and (2) dealership acquisitions made subsequent to January 1, 2000, partially offset by a decrease in revenues resulting from the divestiture of certain dealerships. The overall increase in retail revenues at dealerships owned prior to January 1, 2000 reflects 10.3%, 6.2%, 19.4% and 4.2% increases in new retail vehicle, used retail vehicle, finance and insurance and service and parts revenues, respectively. Revenues of \$520.1 million from fleet and wholesale transactions represent a 16.6% increase versus the prior year. The increase in fleet and wholesale revenues is due to acquisitions subsequent to January 1, 2000.

Retail sales of new vehicles, which exclude fleet transactions, increased by \$865.9 million, or 30.5%, from \$2.8 billion to \$3.7 billion. The increase is due primarily to: (1) a \$237.9 million, or 10.3%, increase at dealerships owned prior to January 1, 2000 and (2) acquisitions made subsequent to January 1, 2000, partially offset by a decrease resulting from the divestiture of certain dealerships. The increase at dealerships owned prior to January 1, 2000, is due primarily to a 7.6% increase in new retail unit sales which increased revenue by \$176.8 million and a 2.5% increase in comparative average selling prices per vehicle which increased revenue by \$61.1 million. The Company believes that the increase is due in part to its favorable brand mix, which includes a higher concentration of foreign nameplates, which have been steadily increasing market share in the United States. Approximately 114% of the increase in new retail vehicle sales at dealerships owned prior to January 1, 2000 results from sales of these foreign nameplates. Aggregate retail unit sales of new vehicles increased by 25.2%, due principally to: (1) the net increase at dealerships owned prior to January 1, 2000 and (2) acquisitions made subsequent to January 1, 2000, partially offset by the decrease due to divested dealerships. We retailed 141,056 new vehicles (67.1% of total retail vehicle sales) during the year ended December 31, 2001, compared with 112,676 new vehicles (65.9% of total retail vehicle sales) during the year ended December 31, 2000. Fleet revenues increased \$29.4 million, or 22.5%, versus the comparable prior year period. The increase in fleet revenues is due primarily to: (1) a \$10.9 million, or 8.7%, increase in fleet sales revenues at dealerships owned prior to January 1, 2000 and (2) acquisitions made subsequent to January 1, 2000, partially offset by a decrease resulting from the divestiture of certain dealerships.

Retail sales of used vehicles, which exclude wholesale transactions, increased by \$216.0 million, or 23.7%, from \$912.0 million to \$1.1 billion. The increase is due primarily to: (1) a \$47.4 million, or 6.2%, increase at dealerships owned prior to January 1, 2000 and (2) acquisitions made subsequent to January 1, 2000, partially offset by a decrease resulting from the divestiture of certain dealerships. The increase at dealerships owned prior to January 1, 2000, is due primarily to a 5.2% increase in used retail unit sales which increased revenue by \$40.2 million and a 0.9% increase in comparative average selling prices per vehicle which increased revenue by \$7.2 million. Aggregate retail unit sales of used vehicles increased by 19.0%, due principally to: (1) the net increase at dealerships owned prior to January 1, 2000, and (2) acquisitions made subsequent to January 1, 2000, partially offset by the decrease due to divested dealerships. We retailed 69,302 used vehicles (32.9% of total retail vehicle sales) during the year ended December 31, 2001, compared with

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58,252 used vehicles (34.1% of total retail vehicle sales) during the year ended December 31, 2000. Wholesale revenues increased \$44.5 million, or 14.1%, versus the comparable prior year period. The increase in wholesale revenues is due primarily to: acquisitions made subsequent to January 1, 2000; partially offset by (1) a \$13.1 million, or 5.1%, decrease at dealerships owned prior to January 1, 2000 and (2) a decrease resulting from the divestiture of certain dealerships.

Finance and insurance revenues increased by \$60.6 million, or 31.4%, from \$193.1 million to \$253.7 million. The increase is due primarily to: (1) a \$26.8 million, or 19.4%, increase at dealerships owned prior to January 1, 2000 and (2) acquisitions made subsequent to January 1, 2000, partially offset by a decrease resulting from the divestiture of certain dealerships. The increase at dealerships owned prior to January 1, 2000 is primarily due to a revenue increase of \$114 per retail vehicle sold, which increased revenue by \$17.4 million, and a 6.8% increase in retail vehicles sold which increased revenue by \$9.4 million.

Service and parts revenues increased by \$120.4 million, or 24.5%, from \$491.8 million to \$612.2 million. The increase is due primarily to: (1) a \$16.8 million, or 4.2%, increase at dealerships owned prior to January 1, 2000 and (2) acquisitions made subsequent to January 1, 2000, partially offset by a decrease resulting from the divestiture of certain dealerships. The Company believes that its service and parts business is being positively impacted by the complexity of today's vehicles, manufacturer warranty programs for both new and certified used vehicles and increases in retail vehicle sales at our dealerships.

*Gross Profit.* Retail gross profit, which excludes gross profit on fleet and wholesale transactions, increased \$176.0 million, or 26.0%, from \$675.5 million to \$851.5 million. The increase in gross profit is due to: (1) a \$45.9 million, or 8.5%, increase in retail gross profit at stores owned prior to January 1, 2000, and (2) acquisitions made subsequent to January 1, 2000, partially offset by a decrease resulting from the divestiture of certain dealerships. Gross profit as a percentage of revenues on retail transactions decreased from 15.2% to 14.9%. Gross profit as a percentage of revenues for new vehicle retail, used vehicle retail, finance and insurance and service and parts revenues was 8.3%, 10.6%, 58.5%, and 44.9%, respectively, compared with 8.8%, 10.7%, 58.7% and 43.8% in the comparable prior year period. The decrease in gross profit as a percentage of revenues on retail transactions is primarily attributable to: (1) an increase in the relative proportion of lower margin new vehicle sales revenues to total retail vehicle revenues, (2) a decrease in the percentage of higher margin finance and insurance and service and parts revenues to total retail revenues, (3) decreased gross profit margins on new retail vehicle revenues, and (4) decreased gross profit margins on used retail vehicle revenues, partially offset by increased gross profit margins on service and parts revenues. Aggregate gross profit on fleet and wholesale transactions decreased by \$2.8 million to a loss of \$0.3 million.

*Selling, General and Administrative Expenses.* Selling, general and administrative expenses increased by \$153.6 million, or 28.5%, from \$539.7 million to \$693.3 million. Such expenses as a percentage of total revenue were 11.1%, which is consistent with the prior year, and increased as a percentage of gross profit from 79.6% to 81.5%. The aggregate increase in selling, general and administrative expenses is due principally to: (1) a \$45.6 million, or 11.0%, increase at dealerships owned prior to January 1, 2000, and (2) acquisitions made subsequent to January 1, 2000, partially offset by a decrease resulting from the divestiture of certain dealerships. The increase in selling, general and administrative expenses at stores owned prior to January 1, 2000 is due in large part to increased selling expenses, including increased variable compensation, as a result of the 8.5% increase in retail gross profit over the prior year.

*Floor Plan Interest Expense.* Floor plan interest expense decreased by \$2.0 million, or 4.4%, from \$44.4 million to \$42.4 million. The decrease in floor plan interest expense is due to (1) a \$10.1 million, or 29.4%, decrease at stores owned prior to January 1, 2000 and (2) a decrease relating to the divestiture of certain dealerships, partially offset by acquisitions made subsequent to January 1, 2000. The decrease at stores owned prior to January 1, 2000 is due primarily to a decrease in inventory at dealerships owned prior to January 1, 2000, coupled with a decrease in our weighted average borrowing rate on floor plan indebtedness during 2001.

*Other Interest Expense.* Other interest expense increased by \$2.0 million, or 6.1%, from \$32.8 million to \$34.8 million. The increase is due primarily to increased acquisition related indebtedness, offset in part by

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(1) a decrease in our weighted average borrowing rate during 2001, (2) the effect of refinancing our 11.0% senior subordinated notes due 2007 and certain other indebtedness with lower interest borrowings under our amended and restated credit agreement, dated as of December 22, 2000 and (3) the paydown of indebtedness with proceeds from equity offerings subsequent to December 31, 2000.

*Income Taxes.* Income taxes increased by \$8.5 million from \$26.6 million to \$35.1 million. The increase is due to an increase in pre-tax income compared with 2000.

*Extraordinary Item.* The 2000 extraordinary loss of \$4.0 million, net of \$3.1 million of tax, represents a loss resulting from the redemption premium paid for the subordinated notes and the write-off of unamortized deferred financing costs relating thereto.

***Year Ended December 31, 2000 Compared to Year Ended December 31, 1999***

*Revenues.* Retail revenues, which exclude revenues relating to fleet and wholesale transactions, increased by \$855.7 million, or 23.9%, from \$3.6 billion to \$4.4 billion. The overall increase in retail revenues is due primarily to: (1) a \$196.1 million, or 6.2%, increase in retail revenues at dealerships owned prior to January 1, 1999 and (2) dealership acquisitions made subsequent to January 1, 1999, partially offset by a decrease in revenues resulting from the divestiture of some dealerships. The overall increase in retail revenues at dealerships owned prior to January 1, 1999, reflects 6.3%, 5.1%, 7.3% and 7.9% increases in new retail vehicle, used retail vehicle, finance and insurance and service and parts revenues, respectively. Revenues of \$446.2 million from fleet and wholesale transactions were consistent with the prior year.

Retail sales of new vehicles, which exclude fleet sale transactions, increased by \$593.0 million, or 26.4%, from \$2.2 billion to \$2.8 billion. The increase is due primarily to: (1) a \$125.0 million, or 6.3%, increase at dealerships owned prior to January 1, 1999, and (2) acquisitions made subsequent to January 1, 1999, partially offset by a decrease resulting from the divestiture of some dealerships. The increase at dealerships owned prior to January 1, 1999, is due primarily to a 4.0% increase in new retail unit sales which increased revenue by \$80.3 million and a 2.2% increase in comparative average selling prices per vehicle which increased revenue by \$44.7 million. Aggregate retail unit sales of new vehicles increased by 20.8%, due principally to: (1) the net increase at dealerships owned prior to January 1, 1999, and (2) acquisitions made subsequent to January 1, 1999, partially offset by the decrease due to divested dealerships. We retailed 112,676 new vehicles (65.9% of total retail vehicle sales) during the year ended December 31, 2000, compared with 93,259 new vehicles (64.2% of total retail vehicle sales) during the year ended December 31, 1999. Fleet sales decreased \$39.5 million, or 23.2%, compared to the comparable prior year period due primarily to a 31.9% decrease in fleet unit sales.

Retail sales of used vehicles, which exclude wholesale transactions, increased by \$142.3 million, or 18.5%, from \$769.6 million to \$912.0 million. The increase is due primarily to: (1) a \$35.2 million, or 5.1%, increase at dealerships owned prior to January 1, 1999, and (2) acquisitions made subsequent to January 1, 1999, partially offset by a decrease resulting from the divestiture of certain dealerships. The increase at dealerships owned prior to January 1, 1999, is due primarily to a 1.5% increase in used retail unit sales which increased revenue by \$10.1 million and a 3.6% increase in comparative average selling prices per vehicle which increased revenue by \$25.1 million. The Company believes that the increase is due in part to its favorable brand mix, which includes a higher concentration of foreign nameplates, which have been steadily increasing market share in the United States. Approximately 196% of the increase in new retail vehicle sales at dealerships owned prior to January 1, 1999 results from the sales of foreign nameplates. Aggregate retail unit sales of used vehicles increased by 12.0%, due principally to: (1) the net increase at dealerships owned prior to January 1, 1999, and (2) acquisitions made subsequent to January 1, 1999, partially offset by the decrease due to divested dealerships. We retailed 58,252 used vehicles (34.1% of total retail vehicle sales) during the year ended December 31, 2000, compared with 52,027 used vehicles (35.8% of total retail vehicle sales) during the year ended December 31, 1999. Wholesale revenues increased \$45.2 million, or 16.7%, compared to the comparable prior year period. The increase in wholesale revenues is due primarily to: acquisitions made subsequent to January 1, 1999, offset in part by (1) an \$8.2 million, or 3.5%, decrease at

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dealerships owned prior to January 1, 1999, and (2) a decrease resulting from the divestiture of some dealerships.

Finance and insurance revenues increased by \$27.4 million, or 16.5%, from \$165.8 million to \$193.1 million. The increase is due primarily to: (1) an \$8.8 million, or 7.3%, increase at dealerships owned prior to January 1, 1999, and (2) acquisitions made subsequent to January 1, 1999, partially offset by a decrease resulting from the divestiture of certain dealerships. The increase at dealerships owned prior to January 1, 1999 is primarily due to a revenue increase of \$39 per retail vehicle sold, which increased revenue by \$5.2 million, and a 3.0% increase in retail vehicles sold which increased revenue by \$3.6 million.

Service and parts revenues increased by \$93.0 million, or 23.3%, from \$398.8 million to \$491.8 million. The increase is due primarily to: (1) a \$27.1 million, or 7.9%, increase at dealerships owned prior to January 1, 1999, and (2) acquisitions made subsequent to January 1, 1999, partially offset by a decrease resulting from the divestiture of some dealerships. The Company believes that its service and parts business is being positively impacted by the complexity of today's vehicles, manufacturer warranty programs for both new and used vehicles and increases in vehicle sales at our dealerships.

*Gross Profit.* Retail gross profit, which excludes gross profit on fleet and wholesale transactions, increased \$125.9 million, or 22.9%, from \$549.6 million to \$675.5 million. The increase in gross profit is due to: (1) a \$30.6 million, or 6.5%, increase in retail gross profit at stores owned prior to January 1, 1999, and (2) acquisitions made subsequent to January 1, 1999, partially offset by a decrease resulting from the divestiture of some dealerships. Gross profit as a percentage of revenues on retail transactions decreased from 15.3% to 15.2%. Gross profit as a percentage of revenues for new vehicle retail, used vehicle retail, finance and insurance and service and parts revenues was 8.8%, 10.7%, 58.7%, and 43.8%, respectively, compared with 8.6%, 11.1%, 58.8% and 43.4% in the comparable prior year period. The decrease in gross profit as a percentage of revenues on retail transactions is primarily attributable to: (1) an increase in the relative proportion of lower margin new vehicle sales revenues to total retail revenues during 2000 and (2) decreases in gross profit margins on used retail vehicle revenues; partially offset by increases in gross profit margins on new retail vehicle and service and parts revenues and an increase in service and parts revenues as a percentage of total revenues. Aggregate gross profit on fleet and wholesale transactions increased \$2.6 million to \$2.4 million.

*Selling, General and Administrative Expenses.* Selling, general and administrative expenses increased by \$94.6 million, or 21.2%, from \$445.1 million to \$539.7 million. These expenses as a percentage of total revenues were 11.1%, which is consistent with the prior year, and decreased as a percentage of gross profit from 81.0% to 79.6%. The aggregate increase in selling, general and administrative expenses is due principally to: (1) a \$26.6 million, or 7.3%, increase at stores owned prior to January 1, 1999 and (2) acquisitions made subsequent to January 1, 1999, partially offset by a decrease resulting from the divestiture of some dealerships. The increase in selling, general and administrative expense at stores owned prior to January 1, 1999 is due in large part to increased selling expenses, including increased variable compensation, as a result of the 6.5% increase in retail gross profit over the prior year.

*Floor Plan Interest Expense.* Floor plan interest expense increased by \$15.7 million, or 54.9%, from \$28.7 million to \$44.4 million. The increase in floor plan interest expense is due to: (1) a \$6.0 million, or 24.3%, increase at stores owned prior to January 1, 1999 and (2) acquisitions made subsequent to January 1, 1999, offset in part by decreases relating to (1) the effect of our interest rate swaps hedging floor plan interest rates and (2) the divestiture of certain dealerships. The increase at stores owned prior to January 1, 1999 is due to an increase in inventory levels compared to 1999 and an increase in our weighted average borrowing rate during 2000.

*Other Interest Expense.* Other interest expense increased by \$3.4 million, or 11.7%, from \$29.3 million to \$32.8 million. The increase is due primarily to increased acquisition related indebtedness, offset in part by (1) the effect of refinancing the subordinated notes and certain other indebtedness with lower interest borrowings under our credit agreement and (2) the paydown of indebtedness with proceeds from equity offerings during 1999.

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*Income Taxes.* Income taxes increased by \$5.1 million from \$21.4 million to \$26.6 million. The increase is due to an increase in pre-tax income compared with 1999, offset in part by a decrease in our estimated annual effective income tax rate. The decrease in the comparative effective rate is due primarily to a decrease in our estimated effective state tax rate resulting from certain tax planning initiatives and a change in the geographic mix of our earnings.

*Extraordinary Item.* The \$4.0 million extraordinary item in 2000 represents a loss resulting from the redemption premium paid for the subordinated notes and the write-off of unamortized deferred financing costs relating to the subordinated notes. The \$0.7 million extraordinary item in 1999 represents the after tax gain arising from the retirement of \$49.0 million of subordinated notes, offset in part by the write-off of a portion of the deferred financing costs relating to the subordinated notes.

**Quarterly Financial Data**

The following table shows selected income statement data for the last nine quarters:

	<b>Three Months Ended</b>			
	<b>March 31</b>			
<b>2002</b>				
Total revenues	\$ 1,633.1			
Gross profit	237.0			
Net income	15.7			
Net income per diluted common share	\$ 0.40			
<b>Three Months Ended</b>				
	<b>March 31</b>	<b>June 30</b>	<b>September 30</b>	<b>December 31</b>
(in millions, except per share data)				
<b>2001</b>				
Total revenues	\$ 1,395.0	\$ 1,615.2	\$ 1,595.8	\$ 1,614.7
Gross profit	191.8	219.0	221.1	219.3
Net income	6.6	13.4	13.5	11.3
Net income per diluted common share	\$ 0.21	\$ 0.40	\$ 0.38	\$ 0.32
<b>Three Months Ended</b>				
	<b>March 31</b>	<b>June 30(1)</b>	<b>September 30</b>	<b>December 31</b>
(in millions, except per share data)				
<b>2000(2)</b>				
Total revenues	\$ 1,110.8	\$ 1,204.1	\$ 1,331.2	\$ 1,237.9
Gross profit	152.1	166.8	182.6	176.5
Net income	5.6	7.1	11.2	6.1
Net income per diluted common share	\$ 0.19	\$ 0.24	\$ 0.40	\$ 0.21

(1) We recorded a \$4.0 million extraordinary loss in the second quarter of 2000 resulting from the redemption premium paid for the subordinated notes and the write-off of unamortized financing costs relating to the subordinated notes.

(2) The per share amounts are calculated independently for each of the quarters presented. As a result, the sum of the quarters is not equal to the full year per share amounts.

**Liquidity and Capital Resources**



## Edgar Filing: UNITED AUTO GROUP INC - Form 8-K

Our cash requirements are primarily for working capital, the acquisition of new dealerships, the improvement and expansion of existing facilities and the construction of new facilities. Historically, these cash requirements have been met through borrowings under our credit agreement, the issuance of debt

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securities, including floor plan notes payable, sale-leaseback transactions, the issuance of equity securities and cash flow from operations. At March 31, 2002, we had working capital of \$145.0 million.

We finance the majority of our new and a portion of our used vehicle inventory under revolving floor plan financing arrangements into which our subsidiaries have entered with various lenders. We make monthly interest payments on the amount financed, but are generally not required to make loan principal repayments prior to the sale of the new and used vehicles we have financed. The floor plan agreements grant a security interest in substantially all of the assets of our domestic automotive dealership subsidiaries. Interest rates on the floor plan arrangements are variable and increase or decrease based on movements in the prime rate or LIBOR. As of March 31, 2002, our outstanding borrowings under floor plan arrangements amounted to \$758.2 million.

Our credit agreement with DaimlerChrysler Services North America LLC and Toyota Motor Credit Corporation provides for revolving loans to be used for acquisitions, working capital, the repurchase of common stock and general corporate purposes. Our borrowing capacity under the revolving portion of the credit agreement is \$700.0 million and, in addition, we have use of a standby letter of credit facility in the amount of \$50.0 million. Our credit agreement also provided for a term loan of \$161.0 million, all of which was used during 1999 and 2000 to repurchase our senior subordinated notes. Loans under the credit agreement bear interest between LIBOR plus 2.00% and LIBOR plus 3.00%. The credit agreement is fully and unconditionally guaranteed on a joint and several basis by our domestic automotive dealership subsidiaries (and will be guaranteed by domestic automotive dealership subsidiaries acquired or established by us in the future) and contains a number of significant covenants that, among other things, restrict our ability to 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, we are required to comply with specified ratios and tests, including debt to equity, debt to EBITDA (as defined) and minimum working capital covenants. Under the terms of our credit agreement, we are required to comply with minimum manufacturer working capital standards at each of our dealerships. We are also required to maintain a total debt (including floor plan borrowings) to stockholders' equity ratio of less than 2.75:1, a non floor plan debt to stockholders' equity ratio of less than 1.30:1, and a senior debt (non floor plan debt less subordinated debt) to EBITDA ratio of less than 3.75:1. EBITDA is based upon the preceding twelve months and, as defined, is pro forma to include twelve months EBITDA for acquired entities. Our credit agreement also contains typical events of default including change of control and non-payment of obligations. Substantially all of our assets are subject to security interests granted to lenders under the credit agreement. The availability under the revolving portion of the credit agreement is subject to a collateral-based borrowing limitation which is determined based on certain of our allowable tangible assets (which does not include foreign assets). Revolving loans mature on August 3, 2005. As of March 31, 2002, our outstanding borrowings under the credit agreement amounted to \$242.5 million. The \$161.0 million of term loans were repaid in March. As of May 10, 2002, our outstanding borrowings under the credit agreement amounted to \$261.5 million.

In October 2001, we entered into swap agreements of approximately four years duration pursuant to which a notional \$400.0 million of our floating rate debt was exchanged for fixed rate debt. The fixed rate interest to be paid by us is based on LIBOR and amounts to approximately 4.23%. During 2000, we entered into a swap agreement of five years duration pursuant to which a notional \$200.0 million of our floating rate debt was exchanged for fixed rate debt for five years. The fixed rate interest to be paid by us is based on LIBOR and amounts to approximately 7.1%. In order to rebalance the ratio of our fixed to floating rate indebtedness after the equity and debt financings in March 2002 discussed below, we terminated the \$400.0 million swap agreements originally entered into in October 2001.

In 1997, we issued \$200.0 million of 11.0% senior subordinated notes due 2007. In 1999, we redeemed \$49.0 million of the notes. In 2000 we completed a tender offer in which we repurchased \$147.3 million of the notes at a redemption price of 101% of the principal amount of the subordinated notes. The indentures governing the subordinated notes require us to comply with specified debt service coverage ratio levels in order to incur incremental indebtedness. Such indentures also limit our ability to pay dividends based on a formula that takes into account, among other things, our consolidated net income, and contain other covenants which restrict our ability to purchase capital stock, incur liens, sell assets and enter into other transactions.

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The subordinated notes are fully and unconditionally guaranteed on a joint and several basis by certain of our domestic automotive dealership subsidiaries. The \$3.7 million of these notes outstanding as of March 31, 2002 become redeemable at our option, with payment of a premium, in July 2002.

In March 2002, we issued \$300.0 million of 9.625% senior subordinated notes due 2012 pursuant to Rule 144A and Regulation S under the Securities Act, as amended. Proceeds from the offering of \$292.2 million were used to repay borrowings under the Company's credit agreement. The notes are unsecured senior subordinated notes and rank behind all of our existing and future senior debt, including debt under our credit agreement. The notes are guaranteed by substantially all of our domestic subsidiaries on a senior subordinated basis. We can redeem all or some of the notes at our option beginning in 2007 at specified redemption prices. In addition, until 2005 we are allowed to redeem up to 35% of the notes with the net cash proceeds from specified public equity offerings. Upon a change of control each holder of notes will be able to require us to repurchase all or some of the notes at a redemption price of 101% of the principal amount of the notes. The notes also contain customary negative covenants and events of default. We are obligated to use our best efforts to commence a registered exchange offer for the notes or to register resales of the notes under the Securities Act, but we cannot assure you that such a registration will be completed or that any trading market will develop after completion of such a registration.

In March 2002, we completed an offering of 6,000,000 shares of our common stock for \$22.00 per share pursuant to an underwritten registered offering, of which 3,000,000 shares were sold by the Company and 3,000,000 were sold by selling stockholders. Proceeds to the Company from the offering of \$61.5 million were used to repay borrowings under the Company's credit agreement.

On April 12, 1999, we entered into a securities purchase agreement with International Motor Cars Group I, L.L.C. and International Motor Cars Group II, L.L.C., Delaware limited liability companies controlled by Penske Capital Partners, L.L.C. (together, the PCP Entities), pursuant to which the PCP Entities agreed to purchase (1) an aggregate of 7,903,124 shares of our Series A convertible preferred stock, par value \$0.0001 per share, (2) an aggregate of 396,876 shares of our Series B convertible preferred stock, par value \$0.0001 per share, and (3) warrants to purchase (a) 3,898,665 shares of common stock and (b) 1,101,335 shares of our non-voting common stock, par value \$0.0001 per share, for \$83.0 million.

The shares of Series A preferred stock and Series B preferred stock entitle the PCP Entities to dividends at a rate of 6.5% per year. The dividends were payable in kind for the first two years after issuance and are, to the extent still outstanding, currently payable in cash. The Series B preferred stock is convertible into an aggregate of 648,588 shares of non-voting common stock (after giving effect to payable in kind dividends). The Series A preferred stock was converted into 7,033,031 shares of our voting common stock on May 2, 2002. We are entitled, at our sole discretion, under certain circumstances to redeem the Series B preferred stock after August 8, 2002 for an amount per share equal to the liquidation preference. The liquidation preference is currently \$10,000 per share plus accrued and unpaid dividends. It is currently the Company's intention to redeem the Series B preferred stock in August 2002, unless earlier converted by the holders of the Series B preferred stock, with cash flow from operations supplemented by borrowings under our credit agreement.

The warrants, as originally issued to the PCP Entities, were exercisable at a price of \$12.50 per share until February 3, 2002, and \$15.50 per share thereafter until May 2, 2004. Pursuant to the anti-dilution provisions of the warrants and as a result of the sale of equity to Mitsui & Co. in 2001, (a) the number of warrants to purchase common stock was increased from 3,898,665 shares to 3,915,580 shares, (b) the number of warrants to purchase non-voting common stock was increased from 1,101,335 shares to 1,106,113 shares, and (c) the warrant exercise price was lowered from \$12.50 to \$12.45. On February 1, 2002, the PCP Entities exercised the warrants in full and paid us the full exercise price of \$62.5 million. The proceeds of the warrant exercise were used to repay borrowings under the Company's credit agreement.

In September 2001, we announced that our board of directors authorized the repurchase of up to three million shares of our outstanding common stock. Pursuant to that authorization, we repurchased 387,092 shares through open market purchases and negotiated transactions at an aggregate cost of \$5.8 million during 2001. The share repurchase program remains open and the Company continually evaluates market conditions

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and internal financing considerations when contemplating purchasing shares. The Company has not repurchased any shares in 2002.

In March 2002, we acquired Sytner Group plc, a publicly traded automotive retailer operating 60 franchises in the United Kingdom, pursuant to an all cash tender offer for all of Sytner's outstanding share capital for approximately £95.3 million in cash. In addition, we assumed approximately £15.8 million of Sytner's debt. As an alternative to receiving all or any part of the £95.3 million of the cash consideration receivable under the offer, Sytner shareholders could elect to receive £1 of loan notes in lieu of every £1 of consideration otherwise receivable under the offer. A total of £26.4 million of such loan notes were issued pursuant to this election. The loan notes bear interest at approximately 3.9% and mature in July 2003. The funds which will be used to repay these notes are being held in escrow by the Royal Bank of Scotland for the benefit of the noteholders.

During 2002, net cash provided by operations amounted to \$5.6 million. Net cash used in investing activities during 2002 totaled \$135.9 million, including \$36.4 million related to capital expenditures and \$149.5 million for acquisitions which includes approximately \$140.0 million relating to the Sytner acquisition, offset by \$50.0 million in proceeds from sale-leaseback transactions. Net cash provided by financing activities during 2002 totaled \$127.5 million, relating to: (1) borrowings of \$178.0 million for capital expenditures and acquisitions which includes approximately \$140.0 million relating to the Sytner acquisition, (2) borrowings of \$300.0 million in connection with the issuance of the senior subordinated notes due 2012 in March and (3) \$126.8 million relating to the issuance of voting common stock, offset by \$477.4 million used to repay borrowings under the Company's credit agreement.

We have a number of capital projects planned or underway relating to the expansion and renovation of our retail automotive operations. Gross cash expenditures during 2002 relating to such projects are estimated to aggregate to \$130.0 million, a portion of which has already been spent. Historically, we have financed such capital expenditures with borrowings under our credit agreement and cash flow from operations. In the past, we have also entered into sale-leaseback transactions with Automotive Group Realty, LLC (AGR), a wholly owned subsidiary of Penske Corporation. We sold certain properties to AGR in 2002 for consideration of \$50.0 million and made lease payments to AGR totaling \$2.1 million during the three months ended March 31, 2002, which payments relate to properties we lease from AGR. We believe we will continue to finance certain capital expenditures in this fashion during 2002. As a result, we anticipate that the net cash we will fund for capital expenditures will amount to approximately \$70.0 million. Funding for such capital expenditures is expected to come from cash flow from operations, supplemented by borrowings under our credit agreement.

The Company agreed to make a contingent payment in cash to the extent the 841,476 shares of common stock issued in connection with an acquisition completed in October 2000 are sold subsequent to the fifth anniversary of the transaction and have a market value at the time of sale of less than \$12.00 per share. The Company will be forever released from this guarantee in the event the average daily closing price of the Company's common stock for any 90 day period subsequent to the fifth anniversary of the transaction exceeds \$12.00 per share. The Company has further granted the seller a put option pursuant to which the Company may be required to repurchase no more than 108,333 shares for \$12.00 per share on each of the first five anniversary dates of the transaction.

In connection with an acquisition of dealerships in October 1997, we agreed that if the acquired companies achieved aggregate specified base earnings levels in any of the five years beginning with the year ending December 31, 1999, we would pay to the sellers for each year in which the acquired companies exceeded base earnings an amount equal to \$700 thousand plus defined percentages of the amounts earned in excess of such base earnings for any such year. The total amount of payments to be made pursuant to this agreement is limited to \$7.0 million. To date we have paid \$2.0 million relating to this agreement. The amount of additional payments, if any, will be determined based upon the financial performance of the acquired business in 2002 and 2003. We also have obligations with respect to past transactions totaling \$32.0 million over the next four years.

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As of March 31, 2002, we had approximately \$2.6 million of cash available to fund operations and future acquisitions. In addition, \$394.3 million was available for borrowing under our credit agreement as of August 1, 2002, which availability is subject to a maximum actual borrowing limit of approximately \$330.0 million due to the credit agreement's borrowing base collateral limitation (in general, the borrowing base equals certain of our allowable tangible assets plus \$300.0 million). Borrowings used to finance the cost of acquisitions and capital construction projects will typically increase tangible assets, allowing the Company to access borrowing capacity which is currently not available due to the base collateral limitation.

We are a holding company whose assets consist primarily of the direct or indirect ownership of the capital stock of our operating subsidiaries. Consequently, our ability to pay dividends is dependent upon the earnings of our subsidiaries and their ability to distribute earnings and other advances and payments to us. The minimum working capital requirement under our franchise agreements could in some cases restrict the ability of our subsidiaries to make distributions, although to date we have not faced any such restrictions.

Our principal source of growth has come from acquisitions of automotive dealerships. We believe that our existing capital resources, including the liquidity provided by our credit agreement and floor plan financing, will be sufficient to fund our current operations and commitments for the next twelve months. To the extent we pursue additional significant acquisitions, we may need to raise additional capital either through the public or private issuance of equity or debt securities or through additional bank borrowings. We may not have sufficient availability under our credit agreement to finance significant additional acquisitions. In certain circumstances, a public equity offering could require the prior approval of several automobile manufacturers. There is no assurance that we would be able to access the capital markets or increase our borrowing capabilities on terms acceptable to us, if at all.

## **Joint Ventures**

From time to time we enter into joint venture arrangements in the ordinary course of business, pursuant to which we acquire dealerships together with a minority investor.

In January 1998, we entered into a joint venture agreement with a third party to manage and acquire dealerships in Illinois, Ohio, North Carolina and South Carolina. With respect to any joint venture established pursuant to this agreement, we are required to buy out the other party at the end of the five-year period following the date of the acquisition. Pursuant to this arrangement, in 1998 we entered into a joint venture with respect to the Citrus Chrysler dealership. We are required to buy out our partner in this dealership in May 2003. We expect this payment to be approximately \$3.0 million.

In November 1999 we formed a joint venture to own and operate certain dealerships in Brazil. Our joint venture partners in Brazil are Roger S. Penske, Jr. and Andre Ribeiro Holdings, Ltda. We contributed approximately \$3.6 million for a 90.6% interest in United Auto do Brasil, Ltda. and Mr. Penske, Jr. and Mr. Ribeiro each contributed approximately \$0.4 million for a 4.7% interest.

In October 2000, we purchased the operating assets of certain dealerships in Fairfield, Connecticut for approximately \$26.8 million. We are contractually committed to sell 20% of this venture to Lucio A. Noto and other investors upon receipt of approval for the transfer of ownership by the manufacturers represented at the Fairfield location. The selling price is approximately \$5.4 million, representing 20% of the consideration we paid inclusive of assets acquired. Mr. Noto will pay for this interest with \$1.2 million at closing, with the remaining \$4.2 million to be paid in quarterly payments over twenty years. The payments will be offset from permitted periodic cash distributions to Mr. Noto by the venture, which are expected to fully fund the investors installment payments. The sale of the minority interest to Mr. Noto is subject to approval by the manufacturers.

In December 2000 we formed a joint venture with Roger Penske, Jr. to own and operate certain Mercedes-Benz, Audi and Porsche dealerships. We contributed \$65.1 million for a 90% interest in HBL, LLC and Mr. Penske, Jr. contributed \$7.2 million for the remaining 10% interest.

In July 2001 we invested in the Tulsa Auto Collection, a group of dealerships in Tulsa, Oklahoma. The Tulsa Auto Collection consists of seven dealerships representing the Ford, Lincoln-Mercury, Jaguar and

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Mazda brands. In addition, through the Tulsa Auto Collection, we operate two automotive care service centers and two used vehicle facilities in the Tulsa market. According to the terms of our joint venture arrangement, we have the option to buy out our partner over a period of time.

### **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 similar periods of decline and recession as 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 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, demand for cars and light trucks is generally lower during the winter months than in other seasons, particularly in regions of the United States where dealerships may be subject to harsh winters. Accordingly, we expect our revenues and profitability to be generally lower in our first and fourth quarters as compared to our second and third quarters. The greatest seasonalities exist with the dealerships in the northeast United States, for which the second and third quarters are the strongest with respect to vehicle-related sales. The service and parts business at all dealerships experiences relatively modest seasonal fluctuations.

### **New Accounting Pronouncements**

Statement of Financial Accounting Standards No. 141 *Business Combinations* ( SFAS No. 141 ) was issued in final form in June 2001. The provisions of SFAS No. 141, which require use of the purchase method of accounting and eliminate the use of the pooling-of-interests method of accounting for business combinations, apply to all business combinations completed after June 30, 2001. In addition, SFAS No. 141 includes transition provisions that apply to business combinations accounted for using the purchase method that were completed before July 1, 2001. The Company adopted SFAS No. 141, which was not material to the Company's reported net income, balance sheet and cash flows.

Statement of Financial Accounting Standards No. 142 *Goodwill and Other Intangible Assets* ( SFAS No. 142 ) was also issued in final form in June 2001. The provisions of SFAS No. 142, which address the financial accounting and related reporting for acquired goodwill and other intangible assets, are effective for fiscal years beginning after December 15, 2001. Pursuant to SFAS 142, the Company is required to perform an assessment for impairment of all intangible assets, including goodwill, upon adoption of the standard and at least annually in the future. The impairment assessment required upon adoption of SFAS No. 142 must be initiated before March 31, 2002, and this first step of the goodwill transition impairment test must be completed by June 30, 2002. Impairment charges, if any, that result from the adoption of SFAS No. 142 would be recorded as the cumulative effect of a change in accounting principle in the first quarter of the year ending December 31, 2002. The Company completed the intangible impairment assessment required by SFAS No. 142 and determined that no adjustment to the carrying value of goodwill is required.

In addition, SFAS No. 142 eliminated amortization relating to intangibles with indefinite lives arising from transactions that closed after June 30, 2001, and calls for the cessation of amortization relating to intangibles with indefinite lives arising from transactions that closed before June 30, 2001 effective January 1, 2002. As a result, the Company experienced a \$4.6 million decrease in amortization during the three months ended March 31, 2002 versus the comparable period in 2001. On a comparable accounting basis for goodwill, net income and earnings per share for the three months ended March 31, 2001 would have been \$9.2 and \$.29 per share, respectively.

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Statement of Financial Accounting Standards No. 144 *Accounting for the Impairment or Disposal of Long-Lived Assets* ( SFAS No. 144 ) was issued in August 2001 and is effective for fiscal years beginning after December 15, 2001. SFAS No. 144, which supercedes Statement of Financial Accounting Standards No. 121, *Accounting for the Impairment of Long-Lived Assets and Long-Lived Assets to Be Disposed of*, and Accounting Principles Board Opinion No. 30, *Reporting the Results of Operations - Reporting the Effect of the Disposal of a Segment of a Business and Extraordinary, Unusual and Infrequently Occurring Events and Transactions*, establishes accounting standards for the impairment and disposal of long-lived assets and criteria for determining when a long-lived asset is held for sale. The statement removes the requirement to allocate goodwill to long-lived assets to be tested for impairment, requires that the depreciable life of a long-lived asset to be abandoned be revised in accordance with Accounting Principles Board Opinion No. 20, *Accounting Changes*, provides that one accounting model be used for long-lived assets to be disposed of by sale, and broadens the presentation of discontinued operations to include more disposal transactions. SFAS 144 was immaterial to earnings during the three months ended March 31, 2002.

### **Effects of Inflation**

We believe that the relatively moderate rates of inflation 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, there can be no assurance that 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 the prime rate or LIBOR. Such rates have historically increased during periods of increasing inflation. We do not believe that we would be placed at a competitive disadvantage should interest rates increase due to increased inflation since most other automotive dealerships have similar floating rate borrowing arrangements.

### **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 indebtedness. Outstanding balances under our credit agreement bear interest at a variable rate based on a margin over LIBOR. Based on the amount outstanding as of December 31, 2001, a 100 basis point change in interest rates would result in an approximate \$5.4 million change to our annual interest expense. Similarly, amounts outstanding under floor plan financing arrangements bear interest at a variable rate based on a margin over LIBOR or Prime. Based on the average aggregate outstanding amounts under floor plan financing arrangements during the year ended December 31, 2001, a 100 basis point change in interest rates would result in an approximate \$6.6 million change to our annual floor plan interest expense.

In October 2001, we entered into swap agreements of approximately four years duration pursuant to which a notional \$400.0 million of our floating rate debt was exchanged for fixed rate debt. The fixed rate interest to be paid by us is based on LIBOR and amounts to approximately 4.23%. During 2000, we entered into a swap agreement of five years duration pursuant to which a notional \$200.0 million of our floating rate debt was exchanged for fixed rate debt for five years. The fixed rate interest paid by us is based on LIBOR and amounts to approximately 7.15%. For fixed rate debt including the notes, certain seller financed promissory notes and obligations under certain capital leases, interest rate changes effect the fair market value of such debt, but do not impact our earnings or cash flows.

*Foreign Currency Exchange Rates.* Substantially all of our business is conducted in the United States where our revenues and expenses are transacted in U.S. dollars. As a result, the majority of our results of operations are not subject to foreign exchange rate fluctuations. We do not hedge against foreign exchange rate fluctuations due to the limited financial exposure we face with respect to such risk. In common with other automotive retailers, we purchase certain of our new vehicle inventories from foreign manufacturers. Our business in this regard 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. Our future results could be materially and adversely impacted by changes in these or other factors.

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**Table of Contents****UNITED AUTO GROUP, INC.****CONSOLIDATED CONDENSED BALANCE SHEETS**

	<b>March 31, 2002</b>	<b>December 31, 2001</b>
	(Unaudited)	
	(In thousands)	
<b>ASSETS</b>		
Cash and cash equivalents	\$ 2,620	\$ 5,416
Accounts receivable, net	289,795	258,266
Inventories	832,526	641,400
Other current assets	27,956	16,434
	<hr/>	<hr/>
Total current assets	1,152,897	921,516
Property and equipment, net	215,986	185,452
Intangible assets, net	905,545	784,149
Other assets	59,509	55,459
	<hr/>	<hr/>
Total Assets	\$ 2,333,937	\$ 1,946,576
	<hr/>	<hr/>
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
<b>Liabilities</b>		
Floor plan notes payable	\$ 758,172	\$ 620,014
Accounts payable	115,250	76,550
Accrued expenses	121,898	85,512
Current portion of long-term debt	12,528	4,202
	<hr/>	<hr/>
Total current liabilities	1,007,848	786,278
Long-term debt	572,693	551,840
Other long-term liabilities	94,208	92,775
	<hr/>	<hr/>
Total liabilities	1,674,749	1,430,893
<b>Stockholders Equity</b>		
Series A Preferred Stock, \$0.0001 par value; liquidation preference \$10 per share; 10 shares authorized; 7 issued and outstanding at March 31, 2002; 9 issued and outstanding at December 31, 2001		
Series B Preferred Stock, \$0.0001 par value; liquidation preference \$10 per share; 10 shares authorized; 1 issued and outstanding at March 31, 2002 and December 31, 2001		
Common stock, \$0.0001 par value, 80,000 shares authorized; 33,645 shares issued, including 3,821 treasury shares, at March 31, 2002; 23,540 shares issued, including 3,821 treasury shares, at December 31, 2001	3	2
Non-voting Common Stock, \$0.0001 par value, 7,125 shares authorized; none issued and outstanding at March 31, 2002 and December 31, 2001		
Class C Common Stock, \$0.0001 par value, 20,000 shares authorized; none issued and outstanding at March 31, 2002 and December 31, 2001		
Additional paid-in-capital	572,122	445,311
Retained earnings	91,742	78,750
Accumulated other comprehensive loss	(4,679)	(8,380)
	<hr/>	<hr/>
Total stockholders equity	659,188	515,683
	<hr/>	<hr/>
Total Liabilities and Stockholders Equity	\$ 2,333,937	\$ 1,946,576

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See Notes to Consolidated Condensed Financial Statements

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**Table of Contents****UNITED AUTO GROUP, INC.****CONSOLIDATED CONDENSED STATEMENTS OF INCOME**

	<b>Three Months Ended March 31,</b>	
	<b>2002</b>	<b>2001</b>
	(In thousands, except per share amounts) (Unaudited)	
New vehicle sales	\$ 977,771	\$ 805,853
Used vehicle sales	312,039	265,980
Finance and insurance	39,068	33,017
Service and parts	169,419	140,622
Fleet sales	34,325	37,526
Wholesale vehicle sales	100,486	88,617
	<hr/>	<hr/>
Total revenues	1,633,108	1,371,615
Cost of sales	1,396,101	1,179,825
	<hr/>	<hr/>
Gross profit	237,007	191,790
Selling, general and administrative expenses	193,820	157,894
	<hr/>	<hr/>
Operating income	43,187	33,896
Floor plan interest expense	8,614	12,578
Other interest expense	7,872	9,668
	<hr/>	<hr/>
Income before minority interests and income taxes	26,701	11,650
Minority interests	(416)	(14)
Income taxes	(10,574)	(5,066)
	<hr/>	<hr/>
Net income	\$ 15,711	\$ 6,570
	<hr/>	<hr/>
Shares used in computing basic per share data	27,542	22,438
	<hr/>	<hr/>
Shares used in computing diluted per share data	39,196	31,843
	<hr/>	<hr/>
Income available to common stockholders	\$ 14,221	\$ 5,119
	<hr/>	<hr/>
Basic net income per common share	\$ 0.52	\$ 0.23
	<hr/>	<hr/>
Net income per diluted common share	\$ 0.40	\$ 0.21
	<hr/>	<hr/>

See Notes to Consolidated Condensed Financial Statements

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## UNITED AUTO GROUP, INC.

## CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOW

	Three Months Ended March 31,	
	2002	2001
(In thousands) (Unaudited)		
Operating activities:		
Net income	\$ 15,711	\$ 6,570
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	4,553	7,677
Minority interests	416	14
Changes in operating assets and liabilities		
Accounts receivable	9,081	(22,540)
Inventories	(46,050)	28,193
Floor plan notes payable	23,489	(45,119)
Accounts payable and accrued expenses	(4,241)	(9,146)
Other	2,639	5,439
	<u>5,598</u>	<u>(28,912)</u>
Investing activities:		
Purchase of equipment and improvements	(36,367)	(22,283)
Proceeds from sale-leaseback transactions	50,000	
Dealership acquisitions, net	(149,485)	(72,169)
	<u>(135,852)</u>	<u>(94,452)</u>
Financing activities:		
Proceeds from borrowings of long-term debt	478,000	110,051
Payments of long-term debt and capital leases	(477,354)	(7,757)
Proceeds from issuance of common stock	126,812	14,142
	<u>127,458</u>	<u>116,436</u>
Net decrease in cash and cash equivalents	(2,796)	(6,928)
Cash and cash equivalents, beginning of period	5,416	7,413
Cash and cash equivalents, end of period	<u>\$ 2,620</u>	<u>\$ 485</u>

See Notes to Consolidated Condensed Financial Statements

**Table of Contents****UNITED AUTO GROUP, INC.****CONSOLIDATED CONDENSED STATEMENT OF STOCKHOLDERS EQUITY  
AND COMPREHENSIVE INCOME**

	Class A Convertible Preferred Stock		Class B Convertible Preferred Stock		Voting and Non-voting Common Stock		Additional Paid-in Capital	Retained Earnings	Accumulated	Total Stockholders Equity	Comprehensive Income
	Issued Shares	Amount	Issued Shares	Amount	Issued Shares	Amount			Other		
(Dollars in thousands) (Unaudited)											
Balances, January 1, 2002	8,794	\$	649	\$	23,540,231	\$ 2	\$ 445,311	\$ 78,750	\$ (8,380)	\$ 515,683	\$
Issuance of common stock	(1,913)				9,936,812	1	124,184			124,185	
Exercise of options					167,778		2,627			2,627	
Payment of preferred stock dividends								(2,719)		(2,719)	
Fair value of interest rate swap agreement									3,539	3,539	3,539
Foreign currency translation									162	162	162
Net income								15,711		15,711	15,711
Balances, March 31, 2002	6,881	\$	649	\$	33,644,821	\$ 3	\$ 572,122	\$ 91,742	\$ (4,679)	\$ 659,188	\$ 19,412

See Notes to Consolidated Condensed Financial Statements

**Table of Contents****UNITED AUTO GROUP, INC.**

**NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS**  
**(In Thousands, Except Share and Per Share Amounts)**  
**(Unaudited)**

**1. Basis of Presentation**

The information presented as of March 31, 2002 and 2001 and for the three month periods then ended is unaudited, but includes all adjustments (consisting only of normal recurring accruals) which the management of United Auto Group, Inc. (the Company) believes to be necessary for the fair presentation of results for the periods presented. The results for the 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, 2001, included elsewhere herein. In order to maintain consistency and comparability of financial information between periods presented, certain reclassifications have been made to the Company's prior year consolidated condensed financial statements to conform to the current year presentation.

**2. Inventories**

Inventories consisted of the following:

	<b>March 31, 2002</b>	<b>December 31, 2001</b>
	<u>          </u>	<u>          </u>
New vehicles	\$ 605,442	\$ 490,445
Used vehicles	180,073	111,253
Parts, accessories and other	47,011	39,702
	<u>          </u>	<u>          </u>
Total inventories	<u>\$ 832,526</u>	<u>\$ 641,400</u>

**3. Business Combinations**

During 2001 and 2000, the Company completed a number of acquisitions. Each of these acquisitions has been accounted for using the purchase method of accounting. As a result, the Company's financial statements include the results of operations of the acquired dealerships only from the date of acquisition.

During the three months ended March 31, 2002, the Company acquired 62 automobile dealership franchises. The aggregate consideration paid in connection with such acquisitions amounted to \$144,832 in cash. The consolidated condensed balance sheets include preliminary allocations of the purchase price relating to these acquisitions, which are subject to final adjustment pending the final implementation by the Company of Statement of Financial Accounting Standards No. 142 *Goodwill and Other Intangibles*. Such allocations resulted in recording approximately \$120,050 of intangibles. Final purchase price allocations are expected to be completed in connection with the implementation of SFAS No. 142.

**Table of Contents****UNITED AUTO GROUP, INC.****NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)*****Pro Forma Results of Operations (Unaudited)***

The following unaudited consolidated pro forma results of operations of the Company for the three month periods ended March 31, 2002 and 2001 give effect to acquisitions consummated subsequent to January 1, 2001 as if they had occurred on January 1, 2001.

	<b>Three Months Ended March 31,</b>	
	<b>2002</b>	<b>2001</b>
Revenues	\$ 1,813,443	\$ 1,694,172
Income before minority interests and income taxes	29,177	18,684
Net income	17,472	10,884
Net income per diluted common share	0.45	0.34

**4. Capital Stock**

In February 2002, affiliates of Penske Corporation exercised warrants to acquire voting and non-voting common stock of the Company. The warrants were issued in connection with such affiliates' investment in the Company in May and August of 1999. As a result, the Company issued 3,915,580 shares of voting common stock and 1,106,113 shares of non-voting common stock in exchange for \$62,520. In March 2002, the Company completed the sale of 3,000,000 shares of voting common stock to the public in an underwritten registered offering at \$22.00 per share. Net proceeds of the two equity transactions totaled approximately \$124,000, which was used to repay indebtedness under the Company's credit agreement.

**5. Intangible Assets**

Effective January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 142 *Goodwill and Other Intangible Assets*. As a result, the Company no longer amortizes goodwill. The following is presented as if the statement were adopted at January 1, 2001:

	<b>Three Months Ended March 31,</b>	
	<b>2002</b>	<b>2001</b>
Net income	\$ 15,711	\$ 6,570
Goodwill amortization, net of tax		2,616
Pro forma net income	\$ 15,711	\$ 9,186
Pro forma basic net income per common share	\$ 0.52	\$ 0.34
Pro forma net income per diluted common share	\$ 0.40	\$ 0.29

**6. Earnings Per Share**

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Income available to common shareholders used in the computation of basic earnings per share data was computed based on net income, adjusted to reflect accrued dividends relating to outstanding preferred stock. Basic earnings per share data was computed based on the weighted average number of common shares outstanding. Diluted earnings per share data was computed based on the weighted average number of common shares outstanding, adjusted for the dilutive effect of stock options, preferred stock and warrants. For the three months ended March 31, 2002 and 2001 150,000 and 2,526,895 shares attributable to outstanding stock options were excluded from the calculation of diluted earnings per share because the effect of such securities was antidilutive. For the three months ended March 31, 2001, 5,000,000 shares attributable to warrants were excluded from the calculation of diluted earnings per share because the effect of such securities

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**Table of Contents****UNITED AUTO GROUP, INC.****NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)**

was antidilutive. A reconciliation of the number of shares used in the calculation of basic and dilutive earnings per share for the three month periods ended March 31, 2002 and 2001 follows:

	Three Months Ended March 31,	
	2002	2001
Weighted average number of common shares outstanding	27,542,000	22,438,000
Effect of stock options	1,347,000	105,000
Effect of preferred stock	9,443,000	9,300,000
Effect of warrants	864,000	
Weighted average number of common shares outstanding, including effect of dilutive securities	39,196,000	31,843,000

**7. Supplemental Cash Flow Information**

The following table presents certain supplementary information to the consolidated condensed statements of cash flows:

	Three Months Ended March 31,	
	2002	2001
Cash paid for interest	\$ 19,067	\$ 23,037
Cash paid for income taxes	220	1,470
Acquisition costs financed with assumed debt	22,448	

**8. Senior Subordinated Notes**

In March 2002, the Company completed the sale of \$300,000 aggregate principal amount of 9.625% Senior Subordinated Notes due 2012. The sale of the notes was exempt from registration pursuant to Rule 144A and Regulation S under the Securities Act, as amended. The notes are unsecured senior subordinated notes and rank behind all existing and future senior debt, including debt under our credit agreement. The notes are guaranteed on a full and unconditional and joint and several basis by substantially all of our domestic subsidiaries on a senior subordinated basis. We can redeem all or some of the notes at our option beginning in 2007 at specified redemption prices. In addition, until 2005 we are allowed to redeem up to 35% of the notes with the net cash proceeds from specified public equity offerings. Upon a change of control each holder of notes will be able to require us to repurchase all or some of the notes at a redemption price of 101% of the principal amount of the notes. The notes also contain customary negative covenants and events of default. Net proceeds from the offering amounted to approximately \$292,200, which was used to repay indebtedness under the Company's credit agreement. We intend to issue \$300,000 of senior subordinated notes pursuant to a registered offering in exchange for the \$300,000 senior subordinated notes issued in March 2002. These New Notes will have identical terms to the notes issued in March.

**9. Sale-Leaseback Transactions**

The Company finances a portion of its dealership expansion program through sale-leaseback transactions with Automotive Group Realty, LLC (AGR), a wholly owned subsidiary of Penske Corporation. Sales of real property are valued at a price that was either independently confirmed by a third party appraiser, or for the price paid by the Company to an independent third party. Improvements are sold for the Company's cost. All sale-leaseback transactions with AGR have been consummated at the Company's net book value, and the



**Table of Contents**

**UNITED AUTO GROUP, INC.**

**NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)**

resulting leases are being accounted for as operating leases. To date during 2002, the Company has entered into sale-leaseback transactions for \$50,000 of properties and related improvements.

**10. Condensed Consolidating Financial Information**

The following tables include condensed consolidating financial information as of March 31, 2002 and for the three months ended March 31, 2002 and 2001 for United Auto Group, Inc. (as the issuer), the wholly-owned subsidiary guarantors, the non-wholly owned subsidiary guarantors, and the non-guarantor subsidiaries (primarily representing foreign entities). The condensed consolidating financial information includes certain allocations of corporate balance sheet, income statement and cash flow items, which are not necessarily indicative of the financial position, results of operations and cash flows that these entities would have realized on a stand alone basis.

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**Table of Contents****UNITED AUTO GROUP, INC.****CONDENSED CONSOLIDATING STATEMENT OF INCOME**

Three Months Ended March 31, 2002

	<b>Total Company</b>	<b>Eliminations</b>	<b>United Auto Group, Inc.</b>	<b>Guarantor Subsidiaries</b>	<b>Non-Wholly Owned Guarantor Subsidiaries</b>	<b>Non- Guarantor Subsidiaries</b>
(Dollars in thousands)						
Total Revenues	\$ 1,633,108	\$	\$	\$ 1,400,174	\$ 50,696	\$ 182,238
Cost of Sales	1,396,101			1,195,182	43,049	157,870
Gross Profit	237,007			204,992	7,647	24,368
Selling, general, and administrative expenses	193,820		1,719	168,264	5,422	18,415
Operating income	43,187		(1,719)	36,728	2,225	5,953
Floor plan interest expense	8,614			7,966	126	522
Other interest expense	7,872			4,528	725	2,619
Equity in earnings of subsidiaries		(16,717)	16,717			
Income before minority interests and income tax provision	26,701	(16,717)	14,998	24,234	1,374	2,812
Minority interests	(416)				(210)	(206)
Income tax provision	(10,574)		713	(10,120)		(1,167)
Net income (loss)	\$ 15,711	\$ (16,717)	\$ 15,711	\$ 14,114	\$ 1,164	\$ 1,439

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**Table of Contents****UNITED AUTO GROUP, INC.****CONDENSED CONSOLIDATING BALANCE SHEET**

March 31, 2002

	<u>Total Company</u>	<u>Eliminations</u>	<u>United Auto Group, Inc.</u>	<u>Guarantor Subsidiaries</u>	<u>Non-Wholly Owned Guarantor Subsidiaries</u>	<u>Non- Guarantor Subsidiaries</u>
(Dollars in thousands)						
Cash and cash equivalents	\$ 2,620	\$	\$	\$	\$	\$ 2,620
Accounts receivable, net	289,795			220,108	9,098	60,589
Inventories	832,526			633,267	20,947	178,312
Other current assets	27,956		3,185	16,145	392	8,234
<b>Total current assets</b>	<b>1,152,897</b>		<b>3,185</b>	<b>869,520</b>	<b>30,437</b>	<b>249,755</b>
Property and equipment, net	215,986		1,545	150,610	2,072	61,759
Intangible assets, net	905,545			705,495	63,030	137,020
Other assets	59,509	(434,591)	463,970	25,940	868	3,322
<b>Total assets</b>	<b>\$ 2,333,937</b>	<b>\$ (434,591)</b>	<b>\$ 468,700</b>	<b>\$ 1,751,565</b>	<b>\$ 96,407</b>	<b>\$ 451,856</b>
Floorplan notes payable	\$ 758,172	\$	\$	\$ 587,141	\$ 18,961	\$ 152,070
Accounts payable	115,250		1,411	61,161	2,947	49,731
Accrued expenses	121,898		3,993	77,538	6,503	33,864
Current portion of long-term debt	12,528			4,256		8,272
<b>Total current liabilities</b>	<b>1,007,848</b>		<b>5,404</b>	<b>730,096</b>	<b>28,411</b>	<b>243,937</b>
Long-term debt	572,693			329,055	71,392	172,246
Other long-term liabilities	94,208			91,788	1,319	1,101
<b>Total liabilities</b>	<b>1,674,749</b>		<b>5,404</b>	<b>1,150,939</b>	<b>101,122</b>	<b>417,284</b>
<b>Total stockholders' equity</b>	<b>659,188</b>	<b>(434,591)</b>	<b>463,296</b>	<b>600,626</b>	<b>(4,715)</b>	<b>34,572</b>
<b>Total liabilities and stockholders' equity</b>	<b>\$ 2,333,937</b>	<b>\$ (434,591)</b>	<b>\$ 468,700</b>	<b>\$ 1,751,565</b>	<b>\$ 96,407</b>	<b>\$ 451,856</b>

**Table of Contents****UNITED AUTO GROUP, INC.****CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS**

Three Months Ended March 31, 2002

	Total Company	Eliminations	United Auto Group, Inc.	Guarantor Subsidiaries	Non-Wholly Owned Guarantor Subsidiaries	Non- Guarantor Subsidiaries
(Dollars in thousands)						
Net cash provided by (used in) operating activities	\$ 5,598	\$	\$ (159)	\$ 5,322	\$ 1,985	\$ (1,550)
Investing Activities:						
Purchase of equipment and improvements	(36,367)		(257)	(32,930)	(1,360)	(1,820)
Proceeds from sale-leaseback transactions	50,000			50,000		
Dealership acquisitions, net of cash acquired	(149,485)			(149,485)		
Net cash used in investing activities	(135,852)		(257)	(132,415)	(1,360)	(1,820)
Financing Activities:						
Proceeds from borrowings of long-term debt	478,000			478,000		
Payments of long-term debt and capital leases	(477,354)			(477,354)		
Proceeds from issuance of common stock	126,812			126,812		
Distributions to (from) Parent				(3,675)	(625)	4,300
Net cash provided by (used in) financing activities	127,458			123,783	(625)	4,300
Net increase (decrease) in cash and cash equivalents	(2,796)		(416)	(3,310)		930
Cash and cash equivalents, beginning of period	5,416		416	3,310		1,690
Cash and cash equivalents, end of period	\$ 2,620	\$	\$	\$	\$	\$ 2,620

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**Table of Contents****UNITED AUTO GROUP, INC.****CONDENSED CONSOLIDATING STATEMENT OF INCOME**

Three Months Ended March 31, 2001

	<b>Total Company</b>	<b>Eliminations</b>	<b>United Auto Group, Inc.</b>	<b>Guarantor Subsidiaries</b>	<b>Non-Wholly Owned Guarantor Subsidiaries</b>	<b>Non- Guarantor Subsidiaries</b>
<b>(Dollars in thousands)</b>						
Total Revenues	\$ 1,371,615	\$	\$	\$ 1,274,159	\$ 18,282	\$ 79,174
Cost of Sales	1,179,825			1,095,460	15,474	68,891
Gross Profit	191,790			178,699	2,808	10,283
Selling, general, and administrative expenses	157,894		1,640	144,750	2,049	9,455
Operating income	33,896		(1,640)	33,949	759	828
Floor plan interest expense	12,578			11,876	79	623
Other interest expense	9,668			8,874	327	467
Equity in earnings of subsidiaries		(7,530)	7,530			
Income before minority interests and income tax provision	11,650	(7,530)	5,890	13,199	353	(262)
Minority interests	(14)					(14)
Income tax provision	(5,066)		680	(5,668)	(192)	114
Net income (loss)	\$ 6,570	\$ (7,530)	\$ 6,570	\$ 7,531	\$ 161	\$ (162)

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**Table of Contents****UNITED AUTO GROUP, INC.****CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS**

Three Months Ended March 31, 2001

	<b>Total Company</b>	<b>Eliminations</b>	<b>United Auto Group, Inc.</b>	<b>Guarantor Subsidiaries</b>	<b>Non-Wholly Owned Guarantor Subsidiaries</b>	<b>Non- Guarantor Subsidiaries</b>
(Dollars in thousands)						
Net cash provided by (used in) operating activities	\$ (28,912)	\$	\$ 1,090	\$ (22,035)	\$ (3,500)	\$ (4,467)
Investing Activities:						
Purchase of equipment and improvements	(22,283)		(77)	(16,216)	(11)	(5,979)
Dealership acquisitions, net of cash acquired	(72,169)			(72,900)	731	
Net cash provided by (used in) investing activities	(94,452)		(77)	(89,116)	720	(5,979)
Financing Activities:						
Proceeds from borrowings of long-term debt	110,051			110,051		
Payments of long-term debt and capital leases	(7,757)			(22,109)	3,906	10,446
Proceeds from issuance of common stock	14,142			14,142		
Net cash provided by financing activities	116,436			102,084	3,906	10,446
Net increase (decrease) in cash and cash equivalents	(6,928)		1,013	(9,067)	1,126	
Cash and cash equivalents, beginning of period	7,413		124	7,289		
Cash and cash equivalents, end of period	\$ 485	\$	\$ 1,137	\$ (1,778)	\$ 1,126	\$

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**INDEPENDENT AUDITORS REPORT**

To the Board of Directors and Stockholders of United Auto Group, Inc.

Detroit, Michigan

We have audited the accompanying consolidated balance sheets of United Auto Group, Inc. (the Company) and subsidiaries as of December 31, 2001 and 2000, and the related consolidated statements of income, stockholders' equity and comprehensive income (loss), and cash flows for each of the three years in the period ended December 31, 2001. Our audits included the financial statement schedule listed in the accompanying index. These financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on the financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of the Company and subsidiaries at December 31, 2001 and 2000, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2001 in conformity with accounting principles generally accepted in the United States of America.

/s/ DELOITTE & TOUCHE LLP

New York, New York

February 4, 2002 (May 15, 2002 as to Notes  
15 and 16 and August 1,  
2002 as to Note 2  
and the financial  
statement schedule)

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## UNITED AUTO GROUP, INC.

## CONSOLIDATED BALANCE SHEETS

	December 31,	
	2001	2000
(In thousands, except per share amounts)		
<b>ASSETS</b>		
Cash and cash equivalents	\$ 5,416	\$ 7,413
Accounts receivable, net	258,266	190,792
Inventories	641,400	737,942
Other current assets	16,434	15,469
	<hr/>	<hr/>
Total current assets	921,516	951,616
Property and equipment, net	185,452	107,085
Intangible assets, net	784,149	664,510
Other assets	55,459	39,484
	<hr/>	<hr/>
Total Assets	\$ 1,946,576	\$ 1,762,695
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
Floor plan notes payable	\$ 620,014	\$ 689,687
Accounts payable	76,550	55,344
Accrued expenses	85,512	72,075
Current portion of long-term debt	4,202	41,456
	<hr/>	<hr/>
Total current liabilities	786,278	858,562
Long-term debt	551,840	377,721
Other long-term liabilities	92,775	64,742
	<hr/>	<hr/>
Total Liabilities	1,430,893	1,301,025
Commitments and contingent liabilities		
Stockholders Equity		
Series A Preferred Stock, \$0.0001 par value; liquidation preference \$10 per share; 10 shares authorized; 9 issued and outstanding at December 31, 2001; 8 issued and outstanding at December 31, 2000		
Series B Preferred Stock, \$0.0001 par value; liquidation preference \$10 per share; 10 shares authorized; 1 issued and outstanding at December 31, 2001 and 2000		
Common Stock, \$0.0001 par value, 80,000 shares authorized; 23,540 shares issued, including 3,821 treasury shares, at December 31, 2001; 21,990 shares issued, including 3,434 treasury shares, at December 31, 2000	2	2
Non-voting Common Stock, \$0.0001 par value, 7,125 shares authorized; none issued and outstanding at December 31, 2001 and 2000		
Class C Common Stock, \$0.0001 par value, 20,000 shares authorized; none issued and outstanding at December 31, 2001 and 2000		
Additional paid-in-capital	445,311	420,166

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Retained earnings	78,750	41,502
Accumulated other comprehensive (loss)	(8,380)	
	<hr/>	<hr/>
Total Stockholders Equity	515,683	461,670
	<hr/>	<hr/>
Total Liabilities and Stockholders Equity	\$ 1,946,576	\$ 1,762,695
	<hr/>	<hr/>

See Notes to Consolidated Financial Statements.

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**Table of Contents****UNITED AUTO GROUP, INC.****CONSOLIDATED STATEMENTS OF INCOME**

	Year Ended December 31,		
	2001	2000	1999
	(In thousands, except per share amounts)		
New vehicle sales	\$ 3,866,699	\$ 2,971,468	\$ 2,417,906
Used vehicle sales	1,488,070	1,227,597	1,040,026
Finance and insurance	253,737	193,121	165,751
Service and parts	612,157	491,803	398,834
<b>Total revenues</b>	<b>6,220,663</b>	<b>4,883,989</b>	<b>4,022,517</b>
Cost of sales	5,369,505	4,206,032	3,473,080
<b>Gross profit</b>	<b>851,158</b>	<b>677,957</b>	<b>549,437</b>
Selling, general and administrative expenses	693,303	539,704	445,142
<b>Operating income</b>	<b>157,855</b>	<b>138,253</b>	<b>104,295</b>
Floor plan interest expense	(42,430)	(44,406)	(28,676)
Other interest expense	(34,790)	(32,777)	(29,344)
Other income (expense), net			2,617
<b>Income before minority interests, income tax provision and extraordinary item</b>	<b>80,635</b>	<b>61,070</b>	<b>48,892</b>
Minority interests	(815)	(512)	(722)
Income tax provision	(35,075)	(26,558)	(21,414)
<b>Income before extraordinary item</b>	<b>44,745</b>	<b>34,000</b>	<b>26,756</b>
Extraordinary item, net of income taxes		(3,969)	732
<b>Net income</b>	<b>\$ 44,745</b>	<b>\$ 30,031</b>	<b>\$ 27,488</b>
Shares used in computing basic per share data	23,147	20,207	21,950
Shares used in computing diluted per share data	34,196	29,415	26,526
<b>Income available to common stockholders</b>	<b>\$ 36,455</b>	<b>\$ 29,529</b>	<b>\$ 24,145</b>
<b>Basic income before extraordinary item per common share</b>	<b>\$ 1.57</b>	<b>\$ 1.46</b>	<b>\$ 1.10</b>
<b>Basic net income per common share</b>	<b>\$ 1.57</b>	<b>\$ 1.26</b>	<b>\$ 1.14</b>
<b>Income before extraordinary item per diluted common share</b>	<b>\$ 1.31</b>	<b>\$ 1.16</b>	<b>\$ 1.01</b>
<b>Net income per diluted common share</b>	<b>\$ 1.31</b>	<b>\$ 1.02</b>	<b>\$ 1.04</b>

See Notes to Consolidated Financial Statements.



**Table of Contents****UNITED AUTO GROUP, INC.****CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY AND****COMPREHENSIVE INCOME (LOSS)**

	Class A Convertible Preferred Stock		Class B Convertible Preferred Stock		Voting and Non-voting Common Stock		Additional Paid-in Capital	Retained Earnings (Deficit)	Accumulated Other Comprehensive Income (Loss)	Total Stockholders Equity	Comprehensive Income (Loss)
	Issued Shares	Amount	Issued Shares	Amount	Issued Shares	Amount					
(Dollars in thousands)											
Balances, December 31, 1998					20,738,384	\$ 2	\$ 352,591	\$ (10,943)	\$	\$ 341,650	\$
Issuance of stock for acquisitions					1,261,327		(13,960)			(13,960)	
Repurchase of common stock					(118,000)		(992)			(992)	
Issuance of preferred stock and warrants	7,904		397				76,679			76,679	
Net income								27,488		27,488	
Balances, December 31, 1999	7,904		397		21,881,711	2	414,318	16,545		430,865	
Issuance of common stock					2,981,011		26,950			26,950	
Repurchase of common stock					(2,872,856)		(26,176)			(26,176)	
Payment in kind dividends	438		124				5,074	(5,074)			
Net income								30,031		30,031	
Balances, December 31, 2000	8,342		521		21,989,866	2	420,166	41,502		461,670	
Issuance of common stock					1,593,869		19,041			19,041	
Exercise of options					343,588		4,781			4,781	
Repurchase of common stock					(387,092)		(5,790)			(5,790)	
Payment in kind dividends	452		128				7,113	(7,113)			
Payment of preferred stock dividends								(384)		(384)	
Fair value of interest rate swap agreement									(7,205)	(7,205)	(7,205)
Foreign currency translation									(1,175)	(1,175)	(1,175)
Net income								44,745		44,745	44,745
Balances, December 31, 2001	8,794		649		23,540,231	\$ 2	\$ 445,311	\$ 78,750	\$ (8,380)	\$ 515,683	\$ 36,365



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## UNITED AUTO GROUP, INC.

## CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended December 31,		
	2001	2000	1999
	(Dollars in thousands)		
Operating Activities:			
Net income	\$ 44,745	\$ 30,031	\$ 27,488
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	33,625	24,174	19,131
Deferred income taxes	12,546	10,897	10,007
Minority interests	815	512	722
Extraordinary item		5,613	
Non-cash compensation expense			2,250
Changes in operating assets and liabilities:			
Accounts receivable	(56,420)	(33,144)	(11,090)
Inventories	158,164	(67,942)	(73,687)
Floor plan notes payable	(124,777)	69,186	59,371
Accounts payable and accrued expenses	18,079	24,478	2,690
Other	(14,338)	(11,969)	13,526
Net cash provided by operating activities	72,439	51,836	50,408
Investing Activities:			
Purchase of equipment and improvements	(83,394)	(37,384)	(22,161)
Dealership acquisitions, net of cash acquired	(138,389)	(197,148)	(28,251)
Net cash used in investing activities	(221,783)	(234,532)	(50,412)
Financing Activities:			
Proceeds from borrowings of long-term debt	289,407	339,449	65,000
Payments of long-term debt and capital leases	(155,092)	(159,863)	(159,147)
Proceeds from issuance of common stock, preferred stock and warrants	18,822	16,852	76,679
Repurchase of common stock	(5,790)	(26,176)	(992)
Deferred financing costs			(227)
Net cash provided by (used in) financing activities	147,347	170,262	(18,687)
Net decrease in cash and cash equivalents	(1,997)	(12,434)	(18,691)
Cash and cash equivalents, beginning of year	7,413	19,847	38,538
Cash and cash equivalents, end of year	\$ 5,416	\$ 7,413	\$ 19,847

See Notes to Consolidated Financial Statements.



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**UNITED AUTO GROUP, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**(Dollars in thousands, Except Per Share Amounts)**

**1. Organization and Summary of Significant Accounting Policies**

United Auto Group, Inc. ( UAG or the Company ) is engaged in the sale of new and used motor vehicles and related products and services, including vehicle service, parts and collision repair, finance and insurance products and other aftermarket products. The Company operates dealerships under franchise agreements with a number of automotive manufacturers. In accordance with the individual franchise agreements, each dealership is subject to certain rights and restrictions typical of the industry. The ability of the manufacturers to influence the operations of the dealerships, or the loss of a franchise agreement, could have a negative impact on the Company's operating results.

***Principles of Consolidation***

The consolidated financial statements include all majority-owned subsidiaries. All intercompany accounts and transactions among the consolidated subsidiaries have been eliminated.

***Cash and Cash Equivalents***

Cash and cash equivalents include all highly-liquid investments that have an original maturity of three months or less at the date of purchase.

***Fair Value of Financial Instruments***

Financial instruments consist of cash and cash equivalents, accounts receivable, accounts payable, debt, including floor plan notes payable, and interest rate swaps used to hedge future cash flows. The carrying amount of all significant financial instruments, except the interest rate swaps, approximates fair value due either to length of maturity or the existence of variable interest rates that approximate prevailing market rates. The net fair value of the interest rate swaps, based on discounted cash flows, is approximately \$12,752.

***Revenue Recognition***

The Company records revenue when vehicles are delivered and title has passed to the customer, when vehicle service work is performed and when parts are delivered. The Company also arranges financing for customers through various financial institutions and receives a commission from the lender equal to the difference between the interest rates charged to customers over the predetermined interest rates set by the financing institution. The Company also receives commissions from the sale of various insurance products to customers, including credit, life and health insurance policies and extended warranty contracts. The Company receives fee income from the placement of these contracts at the time the customers enter into the agreements. The Company is not the obligor under any of these contracts. In the case of finance contracts, a customer may prepay or fail to pay, thereby terminating the agreement. Customers may also terminate extended warranty contracts with the underlying warranty provider, which are fully paid at purchase, and become eligible for refunds of unused premiums. In the event that the consumer terminates a retail finance contract or cancels an extended warranty or other insurance product prior to scheduled maturity, a portion of these fees may be charged back to us based on the relevant terms of the contracts. The revenue we record relating to these fees is net of an estimate of the ultimate amount of chargebacks we will be required to pay. Such estimate of ultimate chargeback exposure is based on our historical chargeback expense, including the impact of refinance and default notes on retail finance contracts and cancellation rates on extended warranty contracts and other insurance products, arising from similar contracts.

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**UNITED AUTO GROUP, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

***Inventory Valuation***

Inventories are stated at the lower of cost or market. Cost for new and used vehicle inventories is determined using the specific identification method. Cost for parts, accessories and other inventories is based on factory list prices.

***Property and Equipment***

Property and equipment are recorded at cost and depreciated over estimated useful lives, primarily using the straight-line method. Useful lives for purposes of computing depreciation for assets, other than equipment under capital lease and leasehold improvements, are between 5 and 10 years. Leasehold improvements and equipment under capital lease are depreciated over the shorter of the term of the lease or the estimated useful life of the asset.

Expenditures relating to recurring repair and maintenance are expensed as incurred. Expenditures that increase the useful life or substantially increase the serviceability of an existing asset are capitalized. When equipment is sold or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts, and any resulting gain or loss is reflected in income.

***Income Taxes***

Income taxes are provided in accordance with Statement of Financial Accounting Standards No. 109, Accounting for Income Taxes ( SFAS 109 ). Deferred tax assets or liabilities are computed based upon the difference between financial reporting and tax bases of assets and liabilities using enacted tax rates. A valuation allowance is provided when it is more likely than not that taxable income will not be sufficient to fully realize deferred tax assets.

***Intangible Assets***

Intangible assets of \$784,149, consisting primarily of excess of cost over the fair value of net assets acquired in purchase business combinations, are being amortized on a straight-line basis over periods not exceeding 40 years. Accumulated amortization at December 31, 2001 amounted to \$68,780. Amortization expense for the years ended December 31, 2001, 2000 and 1999 was \$19,705, \$15,408 and \$12,996, respectively.

***Impairment of Long-Lived Assets***

The carrying value of long-lived assets, including intangibles, is reviewed if the facts and circumstances, such as significant declines in revenues, earnings or cash flows or material adverse changes in the business climate, indicate that they may be impaired. The Company performs its review by comparing the carrying amounts of long-lived assets to the estimated undiscounted cash flows relating to such assets. If any impairment in the value of the long-lived assets is indicated, the carrying value of the long-lived assets is adjusted to reflect such impairment based on the discounted cash flows or the fair value of the impaired assets.

***Defined Contribution Plans***

The Company sponsors a number of defined contribution plans covering a significant majority of the Company's employees. Company contributions to such plans are discretionary and are typically based on the level of compensation and contributions by plan participants. The Company incurred expense of \$1,575, \$1,389 and \$1,315 relating to such plans during the years ended December 31, 2001, 2000 and 1999, respectively.

**Table of Contents****UNITED AUTO GROUP, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)*****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.

***Advertising***

Advertising costs are expensed as incurred. The Company incurred total advertising costs of \$60,952, \$51,248 and \$43,165 during the years ended December 31, 2001, 2000 and 1999, respectively. Qualified advertising expenditures reimbursed by manufacturers were \$6,654, \$3,646 and \$2,859 during the years ended December 31, 2001, 2002 and 1999, respectively.

***Manufacturer Incentives***

The Company is the recipient of incentives from the manufacturers at each of its dealerships. These incentives are variable, the receipt of which are based, among other things, upon the number of new vehicles purchased by the dealership, the attainment of specified new vehicle retail unit sales, the attainment of certain customer satisfaction levels as measured by the manufacturer, and reimbursements for qualified advertising expenditures by the dealerships. All such incentive payments are treated as a reduction of cost of goods sold when earned, other than reimbursements of qualified advertising expenditures which are treated as a reduction of selling, general and administrative expense.

***Net Income Per Common Share***

Income available to common stockholders used in the computation of basic earnings per share data was computed based on net income, as adjusted to reflect dividends accrued relating to outstanding preferred stock. Basic earnings per share data was computed based on the weighted average number of common shares outstanding. Diluted earnings per share data was computed based on the weighted average number of common shares outstanding, adjusted for the dilutive effect of stock options, preferred stock and warrants. For the years ended December 31, 2001, 2000 and 1999, 932, 2,529 and 1,068 shares attributable to outstanding stock options were excluded from the calculation of diluted earnings per share because the effect of such securities was antidilutive. For the years ended December 31, 2000 and 1999, 5,000 shares attributable to warrants were excluded from the calculation of diluted earnings per share because the effect of such securities was antidilutive. A reconciliation of the number of shares used in the calculation of basic and diluted earnings per share for the years ended December 31, 2001, 2000 and 1999 follows:

	Year Ended December 31,		
	2001	2000	1999
Weighted average number of common shares outstanding	23,147	20,207	21,950
Effect of stock options	820	54	114
Effect of preferred stock	9,334	9,154	4,462
Effect of warrants	895		
Weighted average number of common shares outstanding, including effect of dilutive securities	34,196	29,415	26,526

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**UNITED AUTO GROUP, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

***Preferred Stock Dividends***

The Company records dividends on outstanding preferred stock when declared. Payments of in kind dividends are based on the fair market value of the Company's common stock on the date of the dividend. All dividends are recorded as a reduction to retained earnings. The payment of in kind dividends also result in a corresponding increase to additional paid-in-capital.

***Segment Reporting***

The Company follows the provisions of Statement of Financial Accounting Standards No. 131, Disclosures About Segments of an Enterprise and Related Information, which establishes standards for reporting information about a Company's operating segments. The Company operates in one reportable segment.

***Derivative Instruments***

Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities, as amended and interpreted ( SFAS No. 133 ) establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. Under SFAS 133, all derivatives, whether designated in hedging relationships or not, are required to be recorded on the balance sheet at fair value. SFAS 133 defines requirements for designation and documentation of hedging relationships, as well as ongoing effectiveness assessments, which must be met in order to qualify for hedge accounting. For a derivative that does not qualify as a hedge, changes in fair value would be recorded in earnings immediately. If the derivative is designated in a fair-value hedge, the changes in the fair value of the derivative and the hedged item are recorded in earnings. If the derivative is designated in a cash-flow hedge, effective changes in the fair value of the derivative are recorded in other comprehensive income and recorded in the income statement when the hedged item affects earnings. Changes in the fair value of the derivative attributable to hedge ineffectiveness are recorded in earnings immediately. The Company adopted SFAS 133 on January 1, 2001 and recorded \$10,187 as a cumulative transition adjustment (reducing other comprehensive income) relating to an interest rate swap (cash-flow hedge) the Company entered into prior to the adoption of SFAS 133. Pursuant to SFAS 133, the cumulative transition adjustment will be amortized and reflected as floorplan interest expense over the remaining life of the interest rate swap.

***Reclassification***

In order to maintain consistency and comparability of financial information between periods presented, certain reclassifications have been made to the prior year financial statements to conform to the current year presentation.

**Table of Contents****UNITED AUTO GROUP, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****2. Intangible Assets**

Effective January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 142 *Goodwill and Other Intangible Assets*. As a result, the Company no longer amortizes goodwill. The following is presented as if the statement were adopted at January 1, 1999:

	December 31,		
	2001	2000	1999
Income before extraordinary items	\$ 44,745	\$ 34,000	\$ 26,756
Net income	\$ 44,745	\$ 30,031	\$ 27,488
Goodwill amortization, net of tax	\$ 11,133	\$ 8,706	\$ 7,304
Pro forma income before extraordinary items	\$ 55,878	\$ 42,706	\$ 34,060
Pro forma net income	\$ 55,878	\$ 38,737	\$ 34,792
Pro forma basic income before extraordinary items per common share	\$ 2.05	\$ 1.89	\$ 1.43
Pro forma income before extraordinary items per diluted common share	\$ 1.63	\$ 1.45	\$ 1.28
Pro forma basic net income per common share	\$ 2.05	\$ 1.69	\$ 1.47
Pro forma net income per diluted common share	\$ 1.63	\$ 1.32	\$ 1.31

**3. Business Combinations**

During 2001 and 2000, the Company completed a number of acquisitions. Each of these acquisitions has been accounted for using the purchase method of accounting. As a result, the Company's financial statements include the results of operations of the acquired dealerships from the date of acquisition.

During 2001, the Company acquired 13 automobile dealership franchises. The aggregate consideration paid in connection with such acquisitions amounted to \$138,900, consisting of approximately \$128,350 in cash, the issuance of 289,243 shares of the Company's \$0.0001 par value voting common stock ( Common Stock ) and \$5,550 of seller financed promissory notes. The consolidated balance sheets include preliminary allocations of the purchase price relating to acquisitions completed subsequent to June 30, 2001, which are subject to final adjustment pending the final implementation by the Company of Statement of Financial Accounting Standards No. 142 *Goodwill and Other Intangibles*. Such allocations resulted in recording approximately \$134,383 of intangibles. Final purchase price allocations are expected to be completed in connection with the implementation of SFAS No. 142. In addition, the Company made an equity investment in a dealership group for approximately \$8,000 in cash. During 2000, the Company acquired 35 automobile dealership franchises. The aggregate consideration paid in connection with such acquisitions amounted to \$225,623, consisting of approximately \$204,975 in cash, the issuance of 841,476 shares of Common Stock and \$10,550 of seller financed promissory notes.

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The Company agreed to make a contingent payment in cash to the extent 841,476 shares of common stock issued in connection with an acquisition completed in October 2000 are sold subsequent to the fifth anniversary of the transaction and have a market value of less than \$12.00 per share. The Company will be forever released from this guarantee in the event the average daily closing price of the Company's common stock for any 90 day period subsequent to the fifth anniversary of the transaction exceeds \$12.00 per share. The Company has further granted the seller a put option pursuant to which the Company may be required to repurchase no more than 108,333 shares for \$12.00 per share on each of the first five anniversary dates of the

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**Table of Contents****UNITED AUTO GROUP, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

transaction. The Company also has obligations with respect to past acquisitions totaling approximately \$32,000 over the next four years.

During 2000, the Company paid \$6,147 in cash in final settlement of its obligation with respect to a guarantee relating to 375,404 shares of Common Stock issued in connection with an acquisition that took place prior to 1998.

**Pro Forma Results of Operations (Unaudited)**

The following unaudited consolidated pro forma results of operations of the Company for the years ended December 31, 2001 and 2000 give effect to acquisitions consummated during 2001 and 2000 as if they had occurred on January 1, 2000.

	December 31,	
	2001	2000
Revenues	\$ 6,359,384	\$ 5,790,858
Income before minority interests and income taxes	87,618	75,922
Net income	48,691	42,187
Net income per diluted common share	1.41	1.39

**4. Inventories**

Inventories consisted of the following:

	December 31,	
	2001	2000
New vehicles	\$ 490,445	\$ 564,159
Used vehicles	111,253	136,980
Parts, accessories and other	39,702	36,803
Total Inventories	<u>\$ 641,400</u>	<u>\$ 737,942</u>

**5. Property and Equipment**

Property and equipment consisted of the following:

	December 31,	
	2001	2000
Furniture, fixtures and equipment	\$ 77,006	\$ 58,069
Equipment under capital lease	823	3,806
Buildings and leasehold improvements	142,698	69,357

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Total	220,527	131,232
Less: Accumulated depreciation and amortization	35,075	24,147
	<u>          </u>	<u>          </u>
Property and equipment, net	\$ 185,452	\$ 107,085
	<u>          </u>	<u>          </u>

Depreciation and amortization expense for the years ended December 31, 2001, 2000 and 1999 was \$13,920, \$8,766 and \$6,135, respectively. Accumulated amortization at December 31, 2001 and 2000 on equipment under capital lease, included in accumulated depreciation and amortization above, amounted to \$347 and \$1,629, respectively.

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## UNITED AUTO GROUP, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

**6. Floor Plan Notes Payable**

The Company finances the majority of its new and a portion of its used vehicle inventory under revolving floor plan financing arrangements with various lenders. The Company makes monthly interest payments on the amount financed, but is not required to make loan principal repayments prior to the sale of new and used vehicles. Outstanding borrowings under floor plan financing arrangements amounted to \$620,014 and \$689,687 as of December 31, 2001 and 2000, respectively. The floor plan agreements grant a security interest in substantially all of the assets of the Company's dealership subsidiaries, and require repayment after a vehicle's sale. Interest rates on the floor plan agreements are variable and increase or decrease based on movements in prime or LIBOR borrowing rates. Floor plan interest expense for the years ended December 31, 2001, 2000 and 1999 was \$42,430, \$44,406 and \$28,676, respectively. The weighted average interest rate on floor plan borrowings was 5.60%, 7.92% and 7.33% for the years ended December 31, 2001, 2000 and 1999, respectively. The Company receives non-refundable credits from its vehicle manufacturers, which are treated as a reduction of cost of goods sold. Floor plan assistance was \$31,913, \$31,307 and \$25,772 during the years ended December 31, 2001, 2000 and 1999, respectively.

**7. Long-Term Debt**

Long-term debt consisted of the following:

	December 31,	
	2001	2000
Credit Agreement Revolving Loans, weighted average interest 6.25% and 8.39% at December 31, 2001 and 2000, respectively	\$ 380,500	\$ 204,595
Credit Agreement Term Loans, weighted average interest 7.25% and 9.20% at December 31, 2001 and 2000, respectively	161,000	186,000
Seller financed promissory notes payable through 2002, weighted average interest 7.63% and 6.60% at December 31, 2001 and 2000, respectively	6,634	15,492
Term loans, weighted average interest 6.12% and 6.95% at December 31, 2001 and 2000, respectively	3,435	5,433
11% Series A and B Senior Subordinated Notes due 2007	3,650	3,650
Capitalized lease obligations	823	4,007
	<hr/>	<hr/>
Total long-term debt	556,042	419,177
Less: Current portion	4,202	41,456
	<hr/>	<hr/>
Net long-term debt	\$ 551,840	\$ 377,721
	<hr/>	<hr/>

Scheduled maturities of long-term debt for each of the next five years and thereafter are as follows:

2002	\$ 4,202
2003	26,753
2004	1,404
2005	25,995
2006	791
2007 and thereafter	496,897
	<hr/>
Total long-term debt	\$ 556,042

The Company's Credit Agreement, dated as of August 3, 1999, as amended and restated (the Credit Agreement), provides for up to \$770,000 in revolving loans to be used for acquisitions, working capital, the

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**UNITED AUTO GROUP, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

repurchase of common stock and general corporate purposes, as well as a \$50,000 standby letter of credit facility. In addition, the Credit Agreement provided for up to \$186,000 to be used to repurchase the Company's 11% Senior Subordinated Notes due 2007 (the "New Notes"). Pursuant to the terms of the Credit Agreement, the Company repaid \$25,000 in 2001, resulting in a permanent reduction in the term loans under the Credit Agreement relating to the refinancing of the New Notes. Loans under the Credit Agreement bear interest between LIBOR plus 2.00% and LIBOR plus 3.00%. Outstanding letters of credit under the Credit Agreement as of December 31, 2001 amounted to \$27,824. The Credit Agreement replaced the Company's previous bank borrowing facility, which was terminated upon the effective date of the Credit Agreement. The Company incurred an extraordinary charge during 1999 of \$494 (\$0.02 per diluted share), net of income taxes of \$396, resulting from the write-off of unamortized deferred financing costs relating to the Company's previous bank borrowing facility.

The Credit Agreement is fully and unconditionally guaranteed on a joint and several basis by the Company's domestic automotive dealership subsidiaries and contains a number of significant covenants that, among other things, restrict the ability of the Company to 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 Company is required to comply with specified ratios and tests, including debt to equity and minimum working capital covenants. The Credit Agreement also contains typical events of default including change of control and non-payment of obligations. Substantially all of the Company's assets are subject to security interests granted to lenders under the Credit Agreement.

In October 2001, we entered into swap agreements of approximately four years duration pursuant to which a notional \$400,000 of our floating rate debt was exchanged for fixed rate debt. The fixed rate interest to be paid by us is based on LIBOR and amounts to approximately 4.23%. During 2000, we entered into a swap agreement of five years duration pursuant to which a notional \$200,000 of our floating rate debt was exchanged for fixed rate debt for five years. The fixed rate interest to be paid by us is based on LIBOR and amounts to approximately 7.15%. The swaps have been designated as cash flow hedges of future interest payments of the Company's LIBOR based borrowings. The swaps have been designated as hedges of the Company's floor plan borrowings and Credit Agreement.

During 1997, the Company issued \$200,000 aggregate principal amount of New Notes. The indentures governing the New Notes require the Company to comply with specified debt service coverage ratio levels in order to incur incremental indebtedness. Such indentures also limit the Company's ability to pay dividends based on a formula which takes into account, among other things, the Company's consolidated net income, and contain other covenants which restrict the Company's ability to purchase capital stock, incur liens, sell assets and enter into other transactions. The indentures governing the New Notes further require the Company to offer to purchase all of the then outstanding New Notes at a purchase price in cash equal to 101% of their principal amount in the event of a change in control, as defined. During 2000, the beneficial interest of Penske Capital Partners and certain affiliated entities exceeded 40%, which, pursuant to the indentures, was deemed to be a change in control. As a result, the Company made an offer to purchase the outstanding New Notes. The tender resulted in the repurchase and retirement of \$147,350 face value of New Notes. The Company recorded a \$3,969 loss (\$0.14 per diluted share), net of \$3,118 of tax, relating to the redemption premium paid for the New Notes and the write-off of unamortized deferred financing costs. During 1999, the Company repurchased and retired \$49,000 of the New Notes. As a result, the Company recorded an extraordinary gain of \$1,226 (\$0.04 per diluted share), net of \$1,001 of tax. The New Notes are fully and unconditionally guaranteed on a joint and several basis by the Company's auto dealership subsidiaries.

As noted, the Credit Agreement and the New Notes are fully and unconditionally guaranteed on a joint and several basis by the Company's domestic automotive dealership subsidiaries (the "Note Guarantors"). Separate financial information of the Note Guarantors has been omitted because the Company is a holding company with no independent operations.

**Table of Contents****UNITED AUTO GROUP, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****8. Operating Lease Obligations**

The Company leases its dealership facilities and corporate offices under non-cancelable operating lease agreements with expiration dates through 2026, including all option periods available to the Company. The Company's lease arrangements typically allow for a base term with options for extension in the Company's favor and include escalation clauses tied to the Consumer Price Index.

Minimum future rental payments required under non-cancelable operating leases in effect as of December 31, 2001 follow:

2002	\$ 59,323
2003	58,328
2004	58,048
2005	56,570
2006	54,656
2007 and thereafter	465,574
	<hr/>
	\$ 752,499
	<hr/>

Rent expense for the years ended December 31, 2001, 2000 and 1999 amounted to \$47,693, \$35,113 and \$29,493, respectively. A number of the dealership leases are with former owners who continue to operate the dealerships as employees of the Company or with other affiliated entities. Of the total rental payments, \$12,954, \$5,575 and \$8,466, respectively, were made to related parties during 2001, 2000, and 1999, respectively.

**9. Related Party Transactions**

As discussed in Note 7, the Company is the tenant under a number of non-cancelable lease agreements with employees of the Company and certain other affiliated entities. The terms of the leases with the former owners were negotiated prior to acquisition and the Company believes all such leases are on terms no less favorable to the Company than would be obtained through arm's-length negotiations with unaffiliated third parties. The Company is also a tenant under a number of non-cancelable lease agreements with Automotive Group Realty, LLC (AGR). AGR is a wholly-owned subsidiary of Penske Corporation. The Company paid AGR \$5,753 and \$1,260 under such lease agreements during the years ended December 31, 2001 and 2000, respectively. In addition, the Company sold AGR real property and improvements for \$20,870 and \$23,365 during 2001 and 2000, respectively, which were subsequently leased by AGR to the Company. Sales of real property are valued at a price which was either independently confirmed by a third party appraiser, or at the price paid by the Company to an independent third party. Improvements are sold for the Company's cost. All sale-leaseback transactions with AGR have been consummated at the Company's net book-value, and the resulting leases are being accounted for as operating leases. The Company believes that the terms of these transactions are no less favorable than the terms available from unaffiliated third parties negotiated on an arm's length basis.

The Company is party to operating agreements with Roger S. Penske, Jr., the son of Roger S. Penske, the Company's Chairman and Chief Executive Officer, reflecting (a) the ownership by Mr. Penske, Jr. of 10% of HBL, LLC and the ownership by the Company of the remaining 90% of HBL, LLC and (b) the ownership by Mr. Penske, Jr. of 4.7% of United Auto do Brasil, Ltda. and by the Company of 90.6% of United Auto do Brasil, Ltda. In 2000, the Company contributed approximately \$3,571 for its 90.6% interest in United Auto do Brasil, Ltda. and Mr. Penske, Jr. contributed approximately \$185 for his 4.7% interest in United Auto do Brasil, Ltda. In 2001, Mr. Penske, Jr. contributed approximately \$7,229 for his 10% interest in HBL, LLC and the Company contributed \$65,064 for its 90% interest in HBL, LLC. Prior to December 31, 2001,

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**UNITED AUTO GROUP, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

Mr. Penske, Jr. owned 20% of UAG Cerritos, LLC. On December 31, 2001, the Company purchased Mr. Penske Jr.'s 20% interest in UAG Cerritos, LLC for \$1,838. From time to time, the Company provides these subsidiaries with working capital and other debt financing at costs that are comparable to the costs charged by the Company to its other subsidiaries.

In prior years, the Company entered into management agreements at certain dealerships for which the closing of the acquisition of such dealerships awaited final manufacturer approval. Pursuant to such management agreements, the Company was paid a monthly fee for managing all aspects of the dealerships' operations. Aggregate income relating to such management fees of \$2,571 for the year ended December 31, 1999 has been included in other income (expense), net in the accompanying consolidated statement of operations.

From time to time, the Company pays and/or receives fees from Penske Corporation and its affiliates for services rendered in the normal course of business, including rents paid to AGR. These transactions reflect the provider's cost or an amount mutually agreed upon by both parties. It is the Company's belief that the payments relating to these transactions are on terms at least as favorable as those which could be obtained from an unrelated third party. Aggregate payments relating to such transactions amounted to \$9,798, \$3,721 and \$311 for the years ended December 31, 2001, 2000 and 1999, respectively.

From time to time, the Company paid and/or received fees from Trace International Holdings, Inc. and its affiliates for services rendered in the normal course of business. The Company no longer engages in such transactions. These transactions reflected the provider's cost or an amount mutually agreed upon by both parties. It is the Company's belief that the payments relating to these transactions were on terms at least as favorable as those which would have been obtained from an unrelated third party. Aggregate payments relating to such transactions amounted to \$131 for the year ended December 31, 1999.

The Company has previously agreed to enter into an operating agreement with Lucio A. Noto, a director of the Company, which provides that an entity in which Mr. Noto has an interest will own 20% of UAG Connecticut, LLC. The Company will own the remaining 80% of UAG Connecticut, LLC. The Company purchased the operating assets (excluding real property) of UAG Connecticut, LLC in October 2000 for approximately \$26,789. Mr. Noto's entity will pay approximately \$5,358 for its 20% interest in UAG Connecticut, LLC, which represents 20% of the consideration paid by the Company inclusive of assets acquired and goodwill paid. The payment will be made as follows: \$1,184 upon closing and the remaining \$4,174 in quarterly payments over twenty years at an interest rate equal to LIBOR plus 2.25%. The payments due will be offset from permitted periodic cash distributions to Mr. Noto's entity by UAG Connecticut, LLC. The transaction is subject to approval by the manufacturers.

**Table of Contents****UNITED AUTO GROUP, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****10. Stock Compensation Plans**

The Company's Board of Directors and stockholders adopted a Stock Option Plan pursuant to which all full-time employees of the Company and its subsidiaries and affiliates are eligible to receive stock options. During 2001, the Company granted options to purchase 466,000 shares of Common Stock at the fair market value of the Common Stock on the grant date. Options granted under the Stock Option Plan have a ten year life and typically vest on a pro-rata basis over three or five years. As of December 31, 2001, the aggregate number of shares of Common Stock for which stock options may be granted under the Stock Option Plan is 3,000,838. As of December 31, 2001, 581,080 shares of Common Stock were available for the grant of options under the Stock Option Plan. Presented below is a summary of the status of stock options held by eligible employees during 2001, 2000 and 1999:

Stock Options	2001		2000		1999	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Options outstanding at beginning of year	2,020,147	\$ 13.63	1,431,794	\$ 15.16	1,227,390	\$ 18.06
Granted	466,000	9.78	588,353	9.89	332,790	7.23
Exercised	268,588	11.14				
Forfeited	401,815	18.96			128,386	20.25
Options outstanding at end of year	1,815,744	\$ 11.82	2,020,147	\$ 13.63	1,431,794	\$ 15.16

The following table summarizes the status of stock options outstanding and exercisable at January 1, 2002:

Range of Exercise Prices	Stock Options Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Stock Options Exercisable	Weighted Average Exercise Price
\$7 to \$13	1,243,055	7.97	\$ 9.21	353,154	\$ 9.10
13 to 30	572,689	6.50	17.49	407,587	17.54
	1,815,744			760,741	

The Company has adopted the disclosure only provisions of Financial Accounting Standards Board Statement of Financial Accounting Standards No. 123, *Accounting for Stock Based Compensation* ( SFAS 123 ). Had the Company elected to recognize compensation expense for stock options based on the fair value at the grant dates of awards, income before extraordinary item and income before extraordinary item per diluted common share would have been as follows (unaudited):

Year Ended December 31,		
2001	2000	1999

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Income before extraordinary item	\$ 42,754	\$ 32,032	\$ 24,516
Income before extraordinary item per diluted common share	1.25	1.09	0.92

The weighted average fair value of the Company's stock options was calculated using the Black-Scholes option-pricing model with the following weighted-average assumptions used for grants: no dividend yield; expected volatility of 38.5% in 2001, 40.3% in 2000 and 49.7% in 1999; risk-free interest rate of 5.5% in 2001, 7.75% in 2000 and 8.00% in 1999; and expected lives of five years. The weighted average fair value of options granted during the years ended December 31, 2001, 2000 and 1999 is \$4.15, \$4.67 and \$3.85 per share, respectively.

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**UNITED AUTO GROUP, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

In connection with the Securities Purchase Agreement, the Company issued 800,000 options during 1999 to purchase Common Stock with an exercise price of \$10.00 per share. The Company recorded \$2,250 in compensation expense during 1999 relating to the issuance of such options.

**11. Stockholders Equity**

In September 2001, the Company announced that its Board of Directors authorized the repurchase of up to three million shares of the Company's outstanding stock. Pursuant to such authorization, the Company repurchased 387,092 shares during 2001 through open market purchases and negotiated transactions at an aggregate cost of \$5,790. During 2000 and 1999, the Company completed the repurchase of 2,990,856 shares through open market purchases and negotiated transactions at an aggregate cost of \$27,168.

In February 2001, we issued 1,302,326 shares of voting common stock to Mitsui & Co., Ltd. and Mitsui & Co. (U.S.A.), Inc. in a private placement for \$10.75 per share (the Mitsui Transaction). Aggregate proceeds, amounting to \$14.0 million, were used to reduce debt.

In December 2000, the Company issued 2,139,535 shares of Common Stock to Penske Corporation in a private placement for \$10.75 per share. Aggregate proceeds, amounting to \$23,000, were used to reduce debt. In addition, the Company's Third Restated Certificate of Incorporation was amended to increase the number of authorized shares of Common Stock from 40,000,000 shares to 80,000,000 shares in December 2000.

The shares of Series A preferred stock and Series B preferred stock entitle International Motor Cars Group I, L.L.C. and International Motor Cars Group II, L.L.C. (collectively, the PCP Entities) to dividends at a rate of 6.5% per year. The dividends were payable in kind for the first two years after issuance and are currently payable in cash. The Series A preferred stock is convertible into an aggregate of 8,794,171 shares of common stock and the Series B preferred stock is convertible into an aggregate of 648,588 shares of non-voting common stock (in each case, after giving effect to payable in kind dividends). We are entitled under some circumstances to redeem the preferred stock after May 3, 2002, for an amount per share equal to the liquidation preference. The liquidation preference is currently \$10,000 per share plus accrued and unpaid dividends. Actual cash dividends payable relating to dividends earned during fiscal 2001 in connection with the preferred stock totaled \$3.1 million. Beginning in fiscal 2002, the aggregate annual cash dividends payable by us are expected to total \$6.1 million. Funding for such dividends is expected to come from cash flow from operations and working capital borrowings under our credit agreement.

The warrants, as originally issued to the PCP Entities, were exercisable at a price of \$12.50 per share until February 3, 2002, and \$15.50 per share thereafter until May 2, 2004. Pursuant to the anti-dilution provisions of the warrants and as a result of the sale of equity to Mitsui & Co. in 2001, (a) the number of warrants to purchase common stock was increased from 3,898,665 shares to 3,915,580 shares, (b) the number of warrants to purchase non-voting common stock was increased from 1,101,335 shares to 1,106,113 shares, and (c) the warrant exercise price was lowered from \$12.50 to \$12.45. On February 1, 2002, the PCP Entities exercised the warrants in full and paid us the full exercise price of \$62.5 million. The proceeds of the warrant exercise will be used for general working capital purposes which may include acquisitions. Pending such use, the proceeds will be used to pay down indebtedness.



**Table of Contents****UNITED AUTO GROUP, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****12. Income Taxes**

The income tax provision relating to income from continuing operations consisted of the following:

	<b>Year Ended December 31,</b>		
	<b>2001</b>	<b>2000</b>	<b>1999</b>
<b>Current:</b>			
Federal	\$ 16,990	\$ 11,950	\$ 7,091
State and local	5,535	3,269	3,352
Foreign	4	442	964
<b>Total current</b>	<b>22,529</b>	<b>15,661</b>	<b>11,407</b>
<b>Deferred:</b>			
Federal	10,214	9,397	9,085
State and local	2,080	1,255	517
Foreign	252	245	405
<b>Total deferred</b>	<b>12,546</b>	<b>10,897</b>	<b>10,007</b>
<b>Income tax provision before extraordinary item</b>	<b>\$ 35,075</b>	<b>\$ 26,558</b>	<b>\$ 21,414</b>

The income tax provision varied from the U.S. federal statutory income tax rate due to the following:

	<b>Year Ended December 31,</b>		
	<b>2001</b>	<b>2000</b>	<b>1999</b>
Income tax provision at the federal statutory rate of 35%	\$ 28,222	\$ 21,374	\$ 17,096
State and local income taxes, net of federal benefit	4,950	2,941	2,516
Non-deductible amortization of goodwill	2,393	1,864	1,330
Other	(490)	379	472
<b>Income tax provision relating to continuing operations</b>	<b>\$ 35,075</b>	<b>\$ 26,558</b>	<b>\$ 21,414</b>

The components of deferred tax assets and liabilities at December 31, 2001 and 2000 were as follows:

	<b>2001</b>	<b>2000</b>
<b>Deferred Tax Assets</b>		
Accrued liabilities	\$ 8,056	\$ 7,567
Derivative instruments	5,547	
Net operating loss carryforwards	1,162	2,565

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Capital loss carryforwards	41	3,031
Other	1,491	3,020
	<u>          </u>	<u>          </u>
Total deferred tax assets	16,297	16,183
Valuation allowance		(1,490)
	<u>          </u>	<u>          </u>
Net deferred tax assets	16,297	14,693

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**Table of Contents****UNITED AUTO GROUP, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

	<u>2001</u>	<u>2000</u>
<b>Deferred Tax Liabilities</b>		
Depreciation and amortization	(29,915)	(19,021)
Partnership investments	(16,439)	(17,440)
	<u>(46,354)</u>	<u>(36,461)</u>
Total deferred tax liabilities	(46,354)	(36,461)
	<u>(46,354)</u>	<u>(36,461)</u>
Net deferred tax liabilities	<u>\$ (30,057)</u>	<u>\$ (21,768)</u>

At December 31, 2001, the Company has \$35,691 of state net operating loss carryforwards that expire at various dates through 2021.

**13. Supplemental Cash Flow Information**

The following table presents supplementary cash flow information:

	<u>2001</u>	<u>2000</u>	<u>1999</u>
Cash paid interest	\$ 81,385	\$ 77,560	\$ 57,073
Cash paid income taxes	25,481	14,149	9,587
Non-cash financing and investing activities:			
Dealership acquisition costs financed by issuance of stock	5,000	10,098	
Dealership acquisition cost financed by long-term debt	5,550	10,550	1,500

**14. Summary of Quarterly Financial Data (Unaudited)**

	<u>First Quarter</u>	<u>Second Quarter</u>	<u>Third Quarter</u>	<u>Fourth Quarter</u>
<b>2001</b>				
Total revenues	\$ 1,394,976	\$ 1,615,183	\$ 1,595,783	\$ 1,614,721
Gross profit	191,790	218,996	221,099	219,273
Net income	6,570	13,405	13,488	11,282
Net income per diluted common share	\$ 0.21	\$ 0.40	\$ 0.38	\$ 0.32
<b>2000</b>				
Total revenues	\$ 1,110,767	\$ 1,204,149	\$ 1,331,173	\$ 1,237,900
Gross profit	152,113	166,780	182,613	176,451
Net income	5,640	7,095	11,179	6,117
Net income per diluted common share	\$ 0.19	\$ 0.24	\$ 0.40	\$ 0.21

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(1) As discussed in Note 6, the Company recorded a \$3,969 extraordinary loss in the second quarter of 2000.

The per share amounts are calculated independently for each of the quarters presented. The sum of the quarters may not equal the full year per share amounts.

### **15. Subsequent Event**

In February 2002, the PCP Entities exercised the Warrants for \$62,520. As a result, the Company issued 3,915,580 shares of Common Stock and 1,106,113 shares of Non-Voting Common Stock. In March 2002, the Company completed the sale of 3,000,000 shares of voting common stock to the public for \$22.00 per share and issued \$300.0 million of Senior Subordinated Notes due 2012. The notes bear interest at 9.625% per annum. Net proceeds of \$416.4 million from these transactions was used to repay indebtedness under the Company's credit agreement.

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**UNITED AUTO GROUP, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**16. Condensed Consolidating Financial Information**

The \$300,000 of senior subordinated notes due 2012 were issued pursuant to Rule 144A and Regulation S. The notes are unsecured senior subordinated notes and will rank behind all of our existing and future senior debt, including debt under our credit agreement. The notes are guaranteed on a full and unconditional and joint and several basis by substantially all of our domestic subsidiaries on a senior subordinated basis. We are able to redeem all or some of the notes at our option beginning in 2007 at specified redemption prices. In addition, until 2005 we are allowed to redeem up to 35% of the notes with the net cash proceeds from specified public equity offerings. Upon a change of control each holder of notes is able to require us to repurchase all or some of the notes at a redemption price of 101% of the principal amount of the notes. The notes also contain customary negative covenants and events of default. We intend to issue \$300,000 of senior subordinated notes pursuant to a registered offering in exchange for the \$300,000 senior subordinated notes issued in March 2002. These New Notes will have identical terms to the notes issued in March.

The following tables include condensed consolidating financial information as of December 31, 2001 and 2000 and for the years ended December 31, 2001, 2000 and 1999 for United Auto Group, Inc. (as the issuer), the wholly-owned subsidiary guarantors, the non-wholly owned subsidiary guarantors, and the non-guarantor subsidiaries (primarily representing foreign entities). The condensed consolidating financial information includes certain allocations of corporate balance sheet, income statement and cash flow items, which are not necessarily indicative of the financial position, results of operations and cash flows that these entities would have realized on a stand alone basis.

**Table of Contents****UNITED AUTO GROUP, INC AND SUBSIDIARIES****CONDENSED CONSOLIDATING STATEMENTS OF INCOME**

Year Ended December 31, 2001

	<u>Total Company</u>	<u>Eliminations</u>	<u>United Auto Group, Inc.</u>	<u>Guarantor Subsidiaries</u>	<u>Non-Wholly Owned Guarantor Subsidiaries</u>	<u>Non- Guarantor Subsidiaries</u>
(Dollars in thousands)						
Total revenues	\$ 6,220,663	\$	\$	\$ 5,682,290	\$ 187,211	\$ 351,162
Cost of sales	5,369,505			4,898,824	159,989	310,692
Gross profit	851,158			783,466	27,222	40,470
Selling, general and administrative expenses	693,303		6,973	627,336	20,828	38,166
Operating income	157,855		(6,973)	156,130	6,394	2,304
Floor plan interest expense	(42,430)			(39,958)	(592)	(1,880)
Other interest expense	(34,790)			(28,309)	(3,715)	(2,766)
Equity in earnings of subsidiaries		(48,685)	48,685			
Income before minority interests and income tax provision	80,635	(48,685)	41,712	87,863	2,087	(2,342)
Minority interests	(815)					(815)
Income tax provision	(35,075)		3,033	(37,774)	(1,353)	1,019
Net income (loss)	\$ 44,745	\$ (48,685)	\$ 44,745	\$ 50,089	\$ 734	\$ (2,138)

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**Table of Contents****UNITED AUTO GROUP, INC.****CONDENSED CONSOLIDATING BALANCE SHEET**

December 31, 2001

	<b>Total Company</b>	<b>Eliminations</b>	<b>United Auto Group, Inc.</b>	<b>Guarantor Subsidiaries</b>	<b>Non-Wholly Owned Guarantor Subsidiaries</b>	<b>Non- Guarantor Subsidiaries</b>
(Dollars in thousands)						
Cash and cash equivalents	\$ 5,416	\$	\$ 416	\$ 3,310	\$	\$ 1,690
Accounts receivable, net	258,266			216,154	10,626	31,486
Inventories	641,400			591,227	20,336	29,837
Other current assets	16,434		4,015	10,995	347	1,077
<b>Total current assets</b>	<b>921,516</b>		<b>4,431</b>	<b>821,686</b>	<b>31,309</b>	<b>64,090</b>
Property and equipment, net	185,452		1,493	171,218	753	11,988
Intangible assets, net	784,149			702,649	63,030	18,470
Other assets	55,459	(358,634)	376,999	32,871	868	3,355
<b>Total assets</b>	<b>\$ 1,946,576</b>	<b>\$ (358,634)</b>	<b>\$ 382,923</b>	<b>\$ 1,728,424</b>	<b>\$ 95,960</b>	<b>\$ 97,903</b>
Floor plan notes payable	\$ 620,014	\$	\$	\$ 555,870	\$ 19,022	\$ 45,122
Accounts payable	76,550		1,972	66,105	3,293	5,180
Accrued expenses	85,512		3,337	70,982	6,413	4,780
Current portion of long-term debt	4,202			4,202		
<b>Total current liabilities</b>	<b>786,278</b>		<b>5,309</b>	<b>697,159</b>	<b>28,728</b>	<b>55,082</b>
Long-term debt	551,840			446,266	71,318	34,256
Other long-term liabilities	92,775			91,279	1,095	401
<b>Total liabilities</b>	<b>1,430,893</b>		<b>5,309</b>	<b>1,234,704</b>	<b>101,141</b>	<b>89,739</b>
<b>Total stockholders' equity</b>	<b>515,683</b>	<b>(358,634)</b>	<b>377,614</b>	<b>493,720</b>	<b>(5,181)</b>	<b>8,164</b>
<b>Total liabilities and stockholders' equity</b>	<b>\$ 1,946,576</b>	<b>\$ (358,634)</b>	<b>\$ 382,923</b>	<b>\$ 1,728,424</b>	<b>\$ 95,960</b>	<b>\$ 97,903</b>

**Table of Contents****UNITED AUTO GROUP, INC.****CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS**

Year Ended December 31, 2001

	<u>Total Company</u>	<u>Eliminations</u>	<u>United Auto Group, Inc.</u>	<u>Guarantor Subsidiaries</u>	<u>Non-Wholly Owned Guarantor Subsidiaries</u>	<u>Non- Guarantor Subsidiaries</u>
(Dollars in thousands)						
Net cash provided by (used in) operating activities	\$ 72,439	\$	\$ (4,004)	\$ 73,895	\$ 1,876	\$ 672
Investing activities:						
Purchase of equipment and improvements	(83,394)		(189)	(79,753)	(598)	(2,854)
Dealership acquisitions, net of cash acquired	(138,389)			(137,964)	731	(1,156)
Net cash used in investing activities	(221,783)		(189)	(217,717)	133	(4,010)
Financing activities:						
Proceeds from borrowings of long-term debt	289,407			285,501	3,906	
Payments of long-term debt and capital leases	(155,092)			(161,725)		6,633
Proceeds from issuance of common stock	18,822			18,822		
Distributions to (from) Parent			4,485	3,035	(5,915)	(1,605)
Repurchase of common stock	(5,790)			(5,790)		
Net cash provided by (used in) financing activities	147,347		4,485	139,843	(2,009)	5,028
Net increase (decrease) in cash and cash equivalents	(1,997)		292	(3,979)		1,690
Cash and cash equivalents, beginning of year	7,413		124	7,289		
Cash and cash equivalents, end of year	\$ 5,416	\$	\$ 416	\$ 3,310	\$	\$ 1,690

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**Table of Contents****UNITED AUTO GROUP, INC.****CONDENSED CONSOLIDATING STATEMENT OF INCOME**

Year Ended December 31, 2000

	<b>Total Company</b>	<b>Eliminations</b>	<b>United Auto Group, Inc.</b>	<b>Guarantor Subsidiaries</b>	<b>Non-Wholly Owned Guarantor Subsidiaries</b>	<b>Non- Guarantor Subsidiaries</b>
(Dollars in thousands)						
Total Revenues	\$ 4,883,989	\$	\$	\$ 4,594,388	\$	\$ 289,601
Cost of Sales	4,206,032			3,954,638		251,394
Gross Profit	677,957			639,750		38,207
Selling, general, and administrative expenses	539,704		5,657	500,942		33,105
Operating income	138,253		(5,657)	138,808		5,102
Floor plan interest expense	(44,406)			(41,731)		(2,675)
Other interest expense	(32,777)			(30,340)		(2,437)
Equity in earnings of subsidiaries		(33,227)	33,227			
Income before minority interests, income tax provision and extraordinary item	61,070	(33,227)	27,570	66,737		(10)
Minority interests	(512)					(512)
Income tax provision	(26,558)		2,461	(29,023)		4
Income before extraordinary item	34,000	(33,227)	30,031	37,714		(518)
Extraordinary item, net of income taxes	(3,969)			(3,969)		
Net income (loss)	\$ 30,031	\$ (33,227)	\$ 30,031	\$ 33,745	\$	\$ (518)

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**Table of Contents****UNITED AUTO GROUP, INC.****CONDENSED CONSOLIDATING BALANCE SHEET**

December 31, 2000

	<u>Total Company</u>	<u>Eliminations</u>	<u>United Auto Group, Inc.</u>	<u>Guarantor Subsidiaries</u>	<u>Non-Wholly Owned Guarantor Subsidiaries</u>	<u>Non- Guarantor Subsidiaries</u>
(Dollars in thousands)						
Cash and cash equivalents	\$ 7,413	\$	\$ 124	\$ 7,289	\$	\$
Accounts receivable, net	190,792			167,248		23,544
Inventories	737,942			694,273		43,669
Other current assets	15,469		1,109	13,039		1,321
<b>Total current assets</b>	<b>951,616</b>		<b>1,233</b>	<b>881,849</b>		<b>68,534</b>
Property and equipment, net	107,085		2,065	97,571		7,449
Intangible assets, net	664,510			646,721		17,789
Other assets	39,484	(278,455)	296,041	21,896		2
<b>Total assets</b>	<b>\$ 1,762,695</b>	<b>\$ (278,455)</b>	<b>\$ 299,339</b>	<b>\$ 1,648,037</b>	<b>\$</b>	<b>\$ 93,774</b>
Floor plan notes payable	\$ 689,687	\$	\$	\$ 637,902	\$	\$ 51,785
Accounts payable	55,344		1,989	48,443		4,912
Accrued expenses	72,075		1,238	66,098		4,739
Current portion of long-term debt	41,456			41,456		
<b>Total current liabilities</b>	<b>858,562</b>		<b>3,227</b>	<b>793,899</b>		<b>61,436</b>
Long-term debt	377,721			350,098		27,623
Other long-term liabilities	64,742			64,531		211
<b>Total liabilities</b>	<b>1,301,025</b>		<b>3,227</b>	<b>1,208,528</b>		<b>89,270</b>
<b>Total stockholders' equity</b>	<b>461,670</b>	<b>(278,455)</b>	<b>296,112</b>	<b>439,509</b>		<b>4,504</b>
<b>Total liabilities and stockholders' equity</b>	<b>\$ 1,762,695</b>	<b>\$ (278,455)</b>	<b>\$ 299,339</b>	<b>\$ 1,648,037</b>	<b>\$</b>	<b>\$ 93,774</b>

**Table of Contents****UNITED AUTO GROUP, INC.****CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS**

Year Ended December 31, 2000

	<u>Total Company</u>	<u>Eliminations</u>	<u>United Auto Group, Inc.</u>	<u>Guarantor Subsidiaries</u>	<u>Non-Wholly Owned Guarantor Subsidiaries</u>	<u>Non- Guarantor Subsidiaries</u>
(Dollars in thousands)						
Net cash provided by (used in) operating activities	\$ 51,836	\$	\$ (1,917)	\$ 53,421	\$	\$ 332
Investing Activities:						
Purchase of equipment and improvements	(37,384)		(846)	(32,900)		(3,638)
Dealership acquisitions, net of cash acquired	(197,148)			(195,013)		(2,135)
Net cash used in investing activities	(234,532)		(846)	(227,913)		(5,773)
Financing Activities:						
Proceeds from borrowings of long-term debt	339,449			339,449		
Payments of long-term debt and capital leases	(159,863)			(166,909)		7,046
Proceeds from issuance of common stock	16,852			16,852		
Distributions to (from) Parent			(8,631)	10,236		(1,605)
Repurchase of common stock	(26,176)			(26,176)		
Net cash provided by (used in) financing activities	170,262		(8,631)	173,452		5,441
Net decrease in cash and cash equivalents	(12,434)		(11,394)	(1,040)		
Cash and cash equivalents, beginning of year	19,847		11,518	8,329		
Cash and cash equivalents, end of year	\$ 7,413	\$	\$ 124	\$ 7,289	\$	\$

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**Table of Contents****UNITED AUTO GROUP INC AND SUBSIDIARIES****CONDENSED CONSOLIDATING STATEMENT OF INCOME**

Year Ended December 31, 1999

	<b>Total Company</b>	<b>Eliminations</b>	<b>United Auto Group, Inc.</b>	<b>Guarantor Subsidiaries</b>	<b>Non-Wholly Owned Guarantor Subsidiaries</b>	<b>Non- Guarantor Subsidiaries</b>
(Dollars in thousands)						
Total Revenues	\$ 4,022,517	\$	\$	\$ 3,788,660	\$	\$ 233,857
Cost of Sales	3,473,080			3,272,666		200,414
Gross Profit	549,437			515,994		33,443
Selling, general, and administrative expenses	445,142		3,418	414,204		27,520
Operating income	104,295		(3,418)	101,790		5,923
Floor plan interest expense	(28,676)			(26,942)		(1,734)
Other interest expense	(29,344)			(27,040)		(2,304)
Other income (expense), net	2,617			2,617		
Equity in earnings of subsidiaries		(29,419)	29,419			
Income before minority interests, income tax provision and extraordinary item	48,892	(29,419)	26,001	50,425		1,885
Minority interests	(722)					(722)
Income tax provision	(21,414)		1,487	(22,081)		(820)
Income before extraordinary item	26,756	(29,419)	27,488	28,344		343
Extraordinary item, net of income taxes	732			732		
Net income (loss)	\$ 27,488	\$ (29,419)	\$ 27,488	\$ 29,076	\$	\$ 343

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**Table of Contents****UNITED AUTO GROUP, INC.****CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS**

Year Ended December 31, 1999

	<u>Total Company</u>	<u>Eliminations</u>	<u>United Auto Group, Inc.</u>	<u>Guarantor Subsidiaries</u>	<u>Non-Wholly Owned Guarantor Subsidiaries</u>	<u>Non- Guarantor Subsidiaries</u>
(Dollars in thousands)						
Net cash provided by (used in) operating activities	\$ 50,408	\$	\$ 193	\$ 51,090	\$	\$ (875)
Investing Activities:						
Purchase of equipment and improvements	(22,161)		(367)	(20,372)		(1,422)
Dealership acquisitions, net of cash acquired	(28,251)			(28,174)		(77)
Net cash used in investing activities	(50,412)		(367)	(48,546)		(1,499)
Financing Activities:						
Proceeds from borrowings of long-term debt	65,000			65,000		
Payments of long-term debt and capital leases	(159,147)			(162,594)		3,447
Proceeds from issuance of common stock, preferred stock and warrants	76,679			76,679		
Distributions to (from) Parent			(9,922)	11,527		(1,605)
Repurchase of common stock	(992)			(992)		
Deferred financing costs	(227)			(227)		
Net cash provided by (used in) financing activities	(18,687)		(9,922)	(10,607)		1,842
Net decrease in cash and cash equivalents	(18,691)		(10,096)	(8,063)		532
Cash and cash equivalents, beginning of year	38,538		21,614	16,392		532
Cash and cash equivalents, end of year	\$ 19,847	\$	\$ 11,518	\$ 8,329	\$	\$

**Table of Contents****HBL, LLC****BALANCE SHEETS**

	<b>March 31, 2002</b>	<b>December 31, 2001</b>
	<b>(unaudited)</b>	
	<b>(In thousands)</b>	
<b>ASSETS</b>		
Cash and cash equivalents	\$	\$
Accounts receivable, net	9,098	10,626
Inventories	20,947	20,336
Other current assets	392	347
	<u>          </u>	<u>          </u>
Total current assets	30,437	31,309
Property and equipment, net	2,072	753
Intangible assets, net	63,030	63,030
Due from Parent	866	866
Other assets	2	2
	<u>          </u>	<u>          </u>
<b>Total Assets</b>	<b>\$ 96,407</b>	<b>\$ 95,960</b>
	<u>          </u>	<u>          </u>
<b>LIABILITIES AND MEMBERS CAPITAL</b>		
Floor plan notes payable	\$ 18,961	\$ 19,022
Accounts payable	2,947	3,293
Accrued expenses	6,294	6,413
	<u>          </u>	<u>          </u>
Total current liabilities	28,202	28,728
Long-term debt	71,392	71,318
Other long-term liabilities	1,319	1,095
	<u>          </u>	<u>          </u>
<b>Total Liabilities</b>	<b>100,913</b>	<b>101,141</b>
	<u>          </u>	<u>          </u>
Commitments and contingent liabilities		
Members Capital		
Members Capital	(4,506)	(5,181)
	<u>          </u>	<u>          </u>
<b>Total Members Capital</b>	<b>(4,506)</b>	<b>(5,181)</b>
	<u>          </u>	<u>          </u>
<b>Total Liabilities and Members Capital</b>	<b>\$ 96,407</b>	<b>\$ 95,960</b>
	<u>          </u>	<u>          </u>

See Notes to Financial Statements.

Table of Contents**HBL, LLC****STATEMENTS OF OPERATIONS**

	<b>Three Months Ended March 31, 2002</b>	<b>Month Ended March 31, 2001</b>
	<b>(unaudited)</b>	
	<b>(In thousands)</b>	
New vehicle sales	\$ 28,385	\$ 10,188
Used vehicle sales	15,144	5,200
Finance and insurance	967	855
Service and parts	6,200	2,039
	<hr/>	<hr/>
Total revenues	50,696	18,282
Cost of sales	43,049	15,474
	<hr/>	<hr/>
Gross profit	7,647	2,808
Selling, general and administrative expenses	5,422	2,049
	<hr/>	<hr/>
Operating income	2,225	759
Floor plan interest expense	126	79
Other interest expense	725	327
	<hr/>	<hr/>
Income before income tax provision	1,374	353
Income tax provision		192
	<hr/>	<hr/>
Net income	\$ 1,374	\$ 161
	<hr/>	<hr/>

See Notes to Financial Statements.

Table of Contents**HBL, INC.****STATEMENT OF OPERATIONS**

	<b>Two Months Ended February 28, 2001</b>
	<b>(In thousands)</b>
Sales	\$ 31,756
Subrental income	
Interest income	22
Other income	(5)
	<hr/>
Total revenues	31,773
	<hr/>
Cost of sales	26,921
Selling, general and administrative	3,683
Interest	168
Depreciation	72
	<hr/>
Total costs and expenses	30,844
	<hr/>
Income before bonuses and taxes	929
Bonuses	4,099
	<hr/>
Loss before income taxes	(3,170)
Income tax provision (benefit)	(1,173)
	<hr/>
Net loss	\$ (1,997)
	<hr/>

See Notes to Financial Statements.

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Table of Contents**HBL, LLC****STATEMENTS OF CASH FLOWS**

	<b>Three Months Ended March 31, 2002</b>	<b>Month Ended March 31, 2001</b>
	<b>(unaudited) (In thousands)</b>	
<b>Operating Activities:</b>		
Net income	\$ 1,374	\$ 161
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	41	181
Changes in operating assets and liabilities:		
Accounts receivable	1,528	1,275
Inventories	(611)	(3,297)
Floor plan notes payable	(61)	2,277
Accounts payable and accrued expenses	(255)	(3,704)
Other	(31)	(393)
	<u>1,985</u>	<u>(3,500)</u>
<b>Investing Activities:</b>		
Purchase of equipment and improvements	(1,360)	(11)
Cash received as part of the acquisition		731
	<u>(1,360)</u>	<u>720</u>
<b>Financing Activities:</b>		
Distributions to Members	(699)	
Additional borrowings	74	3,906
	<u>(625)</u>	<u>3,906</u>
Net increase in cash and cash equivalents		1,126
Cash and cash equivalents, beginning of period		
	<u>\$</u>	<u>\$</u>
Cash and cash equivalents, end of period	<u>\$</u>	<u>\$ 1,126</u>

See Notes to Financial Statements

Table of Contents**HBL, INC.****STATEMENT OF CASH FLOWS**

	<b>Two Months Ended February 28, 2001</b>
	<b>(In thousands)</b>
<b>Operating Activities:</b>	
Net loss	\$ (1,997)
Adjustments to reconcile net loss to net cash provided by operating activities:	
Depreciation	72
Deferred income taxes	(1,484)
Loss on disposal of property and equipment	9
Changes in operating assets and liabilities:	
Accounts receivable, net	1,381
Inventories	(4)
Accounts payable and accrued expenses	3,643
Other	(4)
	<hr/>
Net cash provided by operating activities	1,616
	<hr/>
<b>Investing Activities:</b>	
Purchases of property and equipment	(13)
Decrease in finance receivables	134
Increase in advances to/from affiliates	(99)
	<hr/>
Net cash provided by investing activities	22
	<hr/>
<b>Financing Activities:</b>	
Net decrease in floor plan notes payable	(1,540)
	<hr/>
Net cash used in financing activities	(1,540)
	<hr/>
Net increase in cash and cash equivalents	98
Cash and cash equivalents, beginning of period	633
	<hr/>
Cash and cash equivalents, end of period	\$ 731
	<hr/>

See Notes to Financial Statements

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**Table of Contents**

**HBL, LLC**

**STATEMENT OF MEMBERS CAPITAL**

	<b>Members Capital</b>
	<b>(unaudited) (In thousands)</b>
Balances, January 1, 2002	\$ (5,181)
Distributions to Members	(699)
Net income	1,374
	<hr/>
Balances, March 31, 2002	\$ (4,506)
	<hr/>

See Notes to Financial Statements.

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**Table of Contents****HBL, LLC****NOTES TO FINANCIAL STATEMENTS****(Dollars in Thousands)****(Unaudited)****1. Organization and Summary of Significant Accounting Policies**

HBL, LLC, formerly known as HBL, Inc. ( HBL or the Company ), is engaged in the sale of new and used motor vehicles and related products and services, including vehicle service and parts, finance and insurance products and other aftermarket products. The Company operates the dealership under franchise agreements with 4 automotive manufacturers, including Mercedes-Benz, Audi, Porsche and Land Rover (See Note 3). In accordance with the individual franchise agreements, the dealership is subject to certain rights and restrictions typical of the industry. The ability of the manufacturers to influence the operations of the dealership, or the loss of a franchise agreement, could have a negative impact on the Company's operating results.

HBL, a Delaware limited liability company, is a majority owned subsidiary of HBL Holdings, Inc. ( Holdings ), a Delaware corporation that is a wholly owned subsidiary of Lantzsch-Andreas Enterprises, Inc. ( LAE ). LAE is a wholly owned subsidiary of United Auto Group, Inc. ( UAG ), which UAG acquired on March 1, 2001 for \$67.4 million (the Acquisition ). During the period from March 1, 2001 through December 30, 2001, the operations of the franchises currently owned and operated by HBL were owned and operated by Holdings, which had no assets and liabilities other than those relating to the automobile franchises. On December 31, 2001, Holdings formed HBL, LLC and contributed all of its assets and liabilities to HBL, LLC. Concurrent with the contribution of assets and liabilities to HBL, LLC, Holdings sold a 10% member interest in HBL, LLC to Roger Penske Jr. for \$7.2 million. HBL is operated pursuant to an operating agreement dated as of December 31, 2001 (the Operating Agreement ) between UAG and Roger Penske Jr.

***Basis of Presentation***

The information presented as of March 31, 2002 and for the three month period ended March 31, 2002 and the month ended March 31, 2001 is unaudited, but includes all adjustments (consisting only of normal recurring accruals) which the management of HBL believes to be necessary for the fair presentation of results for the periods presented. The results for the interim periods are not necessarily indicative of results to be expected for the year. These condensed financial statements should be read in conjunction with HBL's audited financial statements included elsewhere herein.

As discussed above, UAG acquired HBL on March 1, 2001. Operating results, financial position and cash flows for the period prior to the formation of HBL reflect the operating results, financial position and cash flows of Holdings. In accordance with Securities & Exchange Commission Staff Accounting Bulletin No. 54 ( SAB No. 54 ), UAG has pushed down HBL's purchase price in revaluing the assets and liabilities of HBL. According to the provisions of SAB No. 54, purchase transactions that result in an entity becoming wholly-owned require a new basis of accounting for the purchased assets and liabilities. As a result of the purchase, HBL recorded the following purchase price adjustments as of March 1, 2001:

	<b>Increase/ (Decrease)</b>
Current assets	\$ 2,219
Property and equipment	(1,935)
Intangible assets	64,417
Accrued liabilities	237
Other long-term liabilities	(242)
Long-term debt	67,407
Stockholders' equity	(2,701)

**Table of Contents****HBL, LLC****NOTES TO FINANCIAL STATEMENTS (Continued)****(Dollars in Thousands)  
(Unaudited)**

The financial statements of HBL for the two-month period ended February 28, 2001 reflect the accounting basis used by HBL prior to its acquisition by UAG. The financial statements of HBL subsequent to March 1, 2001 reflect the accounting basis for the acquired assets and liabilities, including intangibles, utilized by HBL subsequent to its acquisition by UAG. The basis of accounting used by HBL after the acquisition by UAG is not comparable to the basis of accounting used by HBL prior to the purchase by UAG.

**2. Inventories**

Inventories consisted of the following:

	<b>March 31, 2002</b>	<b>December 31, 2001</b>
New vehicles	\$ 14,426	\$ 14,460
Used vehicles	5,313	4,399
Parts, accessories and other	1,208	1,477
	<hr/>	<hr/>
Total Inventories	\$ 20,947	\$ 20,336

**3. Sale of Land Rover Franchise**

On February 22, 2002, HBL sold substantially all of the assets of its Land Rover operation, including the franchise rights to the Land Rover product line, to an unaffiliated third party for \$1.4 million in cash. The sale did not have a material effect on HBL's results of operations. Aggregate cash flows generated by the Land Rover franchise are expected to be replaced through expansion of the remaining franchises and as a result, conditions for reporting discontinued operations would not be met.

**4. Supplemental Cash Flow Information**

Cash paid interest for the three months ended March 31, 2002, the month ended March 31, 2001 and the two months ended February 28, 2001 was \$126, \$79 and \$68, respectively.

**5. Income Taxes**

For the three months ended March 31, 2002 there is no tax provision as HBL is not a tax paying entity.

**6. Intangible Assets**

Effective January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 142 *Goodwill and Other Intangible Assets*. As a result, the Company no longer amortizes goodwill. The following is presented as if the statement were adopted at January 1, 2001:

<b>Three Months Ended</b>	<b>Month Ended</b>	<b>Two Months Ended</b>
<b>March 31, 2002</b>	<b>March 31, 2001</b>	<b>February 28, 2001</b>
<hr/>	<hr/>	<hr/>

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Net income (loss)	\$ 1,374	\$ 161	\$ (1,997)
Goodwill amortization, net of tax		139	
	<u>          </u>	<u>          </u>	<u>          </u>
Adjusted net income (loss)	\$ 1,374	\$ 300	\$ 1,997
	<u>          </u>	<u>          </u>	<u>          </u>

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**INDEPENDENT AUDITORS REPORT**

To the Members

HBL, LLC

We have audited the accompanying balance sheet of HBL, LLC (the Company), a majority owned subsidiary of HBL, Inc., as of December 31, 2001, and the related statements of operations, stockholders' equity/ members' capital and cash flows for the ten-month period then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of HBL, LLC as of December 31, 2001, and the results of its operations and its cash flows for the ten-month period then ended in conformity with accounting principles generally accepted in the United States of America.

/s/ CROWE, CHIZEK AND COMPANY LLP

South Bend, Indiana

May 10, 2002

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**INDEPENDENT AUDITORS REPORT**

To the Shareholder

HBL, Inc.

We have audited the accompanying balance sheets of HBL, Inc. (the Company ) as of February 28, 2001 and December 31, 2000, and the related statements of operations, stockholder s equity and cash flows for the two months ended February 28, 2001 and the years ended December 31, 2000 and 1999. These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of HBL, Inc. as of February 28, 2001 and December 31, 2000, and the results of its operations and its cash flows for the two months ended February 28, 2001 and the years ended December 31, 2000 and 1999 in conformity with accounting principles generally accepted in the United States of America.

/s/ KAISER SCHERER & SCHLEGEL, PLLC

Washington, D.C.

April 9, 2001

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**Table of Contents****HBL, LLC****BALANCE SHEET**

	<b>December 31, 2001</b>
	<b>(In thousands)</b>
<b>ASSETS</b>	
Cash and cash equivalents	\$
Accounts receivable, net	10,626
Inventories	20,336
Other current assets	347
	<hr/>
Total current assets	31,309
Property and equipment, net	753
Intangible assets, net	63,030
Due from Parent	866
Other assets	2
	<hr/>
Total Assets	\$ 95,960
	<hr/>
<b>LIABILITIES AND MEMBERS' CAPITAL</b>	
Floor plan notes payable	\$ 19,022
Accounts payable	3,293
Accrued expenses	6,413
	<hr/>
Total current liabilities	28,728
Long-term debt	71,318
Other long-term liabilities	1,095
	<hr/>
Total Liabilities	101,141
	<hr/>
Commitments and contingent liabilities	
Members' Capital	
Members' Capital	(5,181)
	<hr/>
Total Members' Capital	(5,181)
	<hr/>
Total Liabilities and Members' Capital	\$ 95,960
	<hr/>

See Notes to Financial Statements.

**Table of Contents****HBL, INC.****BALANCE SHEETS**

	<b>February 28, 2001</b>	<b>December 31, 2000</b>
	<u>                    </u>	<u>                    </u>
	(In thousands, except share data)	
<b>ASSETS</b>		
Cash and cash equivalents	\$ 731	\$ 633
Accounts receivable, net	5,662	7,043
Inventories	15,175	15,170
Other current assets	314	295
	<u>                    </u>	<u>                    </u>
Total current assets	21,882	23,141
Due from affiliates companies		969
Property and equipment, net	2,131	2,198
Finance receivables	100	233
Deferred tax assets	2,278	796
	<u>                    </u>	<u>                    </u>
Total Assets	\$ 26,391	\$ 27,337
	<u>                    </u>	<u>                    </u>
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
Floor plan notes payable	\$ 13,529	\$ 15,069
Accounts payable and accrued expenses	7,261	3,930
Income taxes payable	637	325
Capital lease obligations, current portion	53	52
Deferred service contract earnings, current portion	524	525
Customer deposits	349	324
	<u>                    </u>	<u>                    </u>
Total current liabilities	22,353	20,225
Deferred service contract earnings, non-current portion	1,183	1,183
Capital lease obligations, non-current portion	154	163
	<u>                    </u>	<u>                    </u>
Total Liabilities	23,690	21,571
	<u>                    </u>	<u>                    </u>
Commitments and contingent liabilities		
Stockholders Equity		
Common Stock, \$1 par value, 50,000 shares authorized, issued and outstanding	50	50
Paid-in-capital	603	603
Retained earnings	2,048	5,113
	<u>                    </u>	<u>                    </u>
Total Stockholders Equity	2,701	5,766
	<u>                    </u>	<u>                    </u>
Total Liabilities and Stockholders Equity	\$ 26,391	\$ 27,337
	<u>                    </u>	<u>                    </u>

See Notes to Financial Statements.

Table of Contents**HBL, LLC****STATEMENT OF OPERATIONS**

	<b>Ten Months Ended December 31, 2001</b>
	<b>(In thousands)</b>
New vehicle sales	\$ 106,036
Used vehicle sales	53,174
Finance and insurance	7,291
Service and parts	20,710
	<hr/>
Total revenues	187,211
Cost of sales	159,989
	<hr/>
Gross profit	27,222
Selling, general and administrative expenses	20,828
	<hr/>
Operating income	6,394
Floor plan interest expense	592
Other interest expense	3,715
	<hr/>
Income before income tax provision	2,087
Income tax provision	1,353
	<hr/>
Net income	\$ 734
	<hr/> <hr/>

See Notes to Financial Statements.

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**Table of Contents****HBL, INC.****STATEMENTS OF OPERATIONS**

	Two Months Ended February 28, 2001	Year Ended December 31, 2000	Year Ended December 31, 1999
		(In thousands)	
Sales	\$ 31,756	\$ 213,271	\$ 186,155
Subrental income		267	267
Interest income	22	107	65
Other income	(5)	234	101
	<u>31,773</u>	<u>213,879</u>	<u>186,588</u>
Total revenues	31,773	213,879	186,588
Cost of sales	26,921	181,611	160,299
Selling, general and administrative	3,683	21,716	18,446
Bonuses	4,099	5,051	3,800
Interest	168	1,113	898
Depreciation	72	430	488
	<u>34,943</u>	<u>209,921</u>	<u>183,931</u>
Total costs and expenses	34,943	209,921	183,931
Income (loss) before income taxes	(3,170)	3,958	2,657
Income tax provision (benefit)	(1,173)	1,621	1,070
	<u>(1,997)</u>	<u>2,337</u>	<u>1,587</u>
Net income (loss)	\$ (1,997)	\$ 2,337	\$ 1,587

See Notes to Financial Statements.

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**Table of Contents****HBL, LLC****STATEMENT OF STOCKHOLDERS EQUITY/MEMBERS CAPITAL**

	<u>Voting Common Stock</u>		<u>Paid-in Capital</u>	<u>Retained Earnings</u>	<u>Members Capital</u>	<u>Total Stockholders Equity/ Members Capital</u>
	<u>Issued Shares</u>	<u>Amount</u>				
	(In thousands, except share data)					
Balances, March 1, 2001	50,000	\$ 50	\$ 603	\$ 2,048	\$	\$ 2,701
Effect of pushdown and purchase accounting at acquisition date		(50)	(603)	(2,048)		(2,701)
Adjusted balances, March 1, 2001	50,000					
Distributions to Parent				(5,915)		(5,915)
Net income				734		734
Formation of HBL, LLC	(50,000)			5,181	(5,181)	
Balances, December 31, 2001		\$	\$	\$	\$ (5,181)	\$ (5,181)

See Notes to Financial Statements.

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**Table of Contents****HBL, INC.****STATEMENTS OF STOCKHOLDERS EQUITY**

	Voting Common Stock		Paid-in Capital	Retained Earnings	Total Stockholders Equity
	Issued Shares	Amount			
(In thousands, except share data)					
Balances, January 1, 1999	50,000	\$ 50	\$ 603	\$ 2,117	\$ 2,770
Net income				1,587	1,587
Balances, December 31, 1999	50,000	50	603	3,704	4,357
Dividends				(928)	(928)
Net income				2,337	2,337
Balances, December 31, 2000	50,000	50	603	5,113	5,766
Dividends				(1,068)	(1,068)
Net loss				(1,997)	(1,997)
Balances, February 28, 2001	50,000	\$ 50	\$ 603	\$ 2,048	\$ 2,701

See Notes to Financial Statements.

Table of Contents**HBL, LLC****STATEMENT OF CASH FLOWS**

	<b>Ten Months Ended December 31, 2001</b>
	<b>(In thousands)</b>
<b>Operating Activities:</b>	
Net income	\$ 734
Adjustments to reconcile net income to net cash provided by operating activities:	
Depreciation and amortization	1,429
Deferred income taxes	1,328
Changes in operating assets and liabilities:	
Accounts receivable	(4,864)
Inventories	(2,859)
Floor plan notes payable	5,493
Accounts payable and accrued expenses	644
Other	(29)
	<hr/>
Net cash provided by operating activities	1,876
	<hr/>
<b>Investing Activities:</b>	
Purchase of equipment and improvements	(598)
Cash received as part of the acquisition	731
	<hr/>
Net cash provided by investing activities	133
	<hr/>
<b>Financing Activities:</b>	
Distributions to Parent	(5,915)
Additional borrowings	3,906
	<hr/>
Net cash used in financing activities	(2,009)
	<hr/>
Net change in cash and cash equivalents	
Cash and cash equivalents, beginning of period	<hr/>
Cash and cash equivalents, end of period	\$ <hr/>

See Notes to Financial Statements

**Table of Contents****HBL, INC.****STATEMENTS OF CASH FLOWS**

	<b>Two Months Ended February 28, 2001</b>	<b>Year Ended December 31, 2000</b>	<b>Year Ended December 31, 1999</b>
	<b>(In thousands)</b>		
<b>Operating Activities:</b>			
Net income (loss)	\$ (1,997)	\$ 2,337	\$ 1,587
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:			
Depreciation	72	430	489
Deferred income taxes	(1,484)	(112)	(118)
(Gain) loss on disposal of property and equipment	9	(18)	48
Increase in LIFO reserve		145	434
Changes in operating assets and liabilities:			
Accounts receivable, net	1,381	798	(4,192)
Inventories	(4)	(3,199)	(2,799)
Accounts payable and accrued expenses	3,643	251	1,033
Deferred service contract earnings		172	266
Other	(4)	63	(15)
Net cash provided by (used in) operating activities	<u>1,616</u>	<u>867</u>	<u>(3,267)</u>
<b>Investing Activities:</b>			
Purchases of property and equipment	(13)	(229)	(116)
Proceeds from disposal of property and equipment		218	
Increase (decrease) in finance receivables	134	83	(151)
Increase in advances to/from affiliates	(99)	(364)	(269)
Net cash provided by (used in) investing activities	<u>22</u>	<u>(292)</u>	<u>(536)</u>
<b>Financing Activities:</b>			
Net increase (decrease) in floor plan notes	(1,540)	361	4,222
Decrease in officer loan		(250)	(250)
Deferred financing costs		(53)	(169)
Net cash provided by (used in) financing activities	<u>(1,540)</u>	<u>58</u>	<u>3,803</u>
Net increase in cash and cash equivalents	98	633	
Cash and cash equivalents, beginning of period	633		
Cash and cash equivalents, end of period	<u>\$ 731</u>	<u>\$ 633</u>	<u>\$</u>

See Notes to Financial Statements



**Table of Contents****HBL, LLC****NOTES TO FINANCIAL STATEMENTS  
(Dollars in thousands, Except Share Data)****1. Organization and Summary of Significant Accounting Policies**

HBL, LLC, formerly known as HBL, Inc. ( HBL or the Company ), is engaged in the sale of new and used motor vehicles and related products and services, including vehicle service and parts, finance and insurance products and other aftermarket products. The Company operates the dealership under franchise agreements with 4 automotive manufacturers, including Mercedes-Benz, Audi, Porsche and Land Rover. In accordance with the individual franchise agreements, the dealership is subject to certain rights and restrictions typical of the industry. The ability of the manufacturers to influence the operations of the dealership, or the loss of a franchise agreement, could have a negative impact on the Company's operating results.

HBL, a Delaware limited liability company, is a majority owned subsidiary of HBL Holdings, Inc. ( Holdings ), a Delaware corporation that is a wholly owned subsidiary of Lantzsch-Andreas Enterprises, Inc. ( LAE ). LAE is a wholly owned subsidiary of United Auto Group, Inc. ( UAG ), which UAG acquired on March 1, 2001 for \$67.4 million (the Acquisition ). During the period from March 1, 2001 through December 30, 2001, the operations of the franchises currently owned and operated by HBL were owned and operated by Holdings, which had no assets and liabilities other than those relating to the four automobile franchises. On December 31, 2001, Holdings formed HBL, LLC and contributed all of its assets and liabilities to HBL, LLC. Concurrent with the contribution of assets and liabilities to HBL, LLC, Holdings sold a 10% member interest in HBL, LLC to Roger Penske Jr. for \$7.2 million. HBL is operated pursuant to an operating agreement dated as of December 31, 2001 (the Operating Agreement ) between UAG and Roger Penske Jr.

***Basis of Presentation***

As discussed above, UAG acquired HBL on March 1, 2001. Operating results, financial position and cash flows for the period prior to the formation of HBL reflect the operating results, financial position and cash flows of Holdings. In accordance with Securities & Exchange Commission Staff Accounting Bulletin No. 54 ( SAB No. 54 ), UAG has pushed down HBL's purchase price in revaluing the assets and liabilities of HBL. According to the provisions of SAB No. 54, purchase transactions that result in an entity becoming wholly-owned require a new basis of accounting for the purchased assets and liabilities. As a result of the purchase, HBL recorded the following purchase price adjustments as of March 1, 2001:

	<b>Increase/ (Decrease)</b>
Current assets	\$ 2,219
Property and equipment	(1,935)
Intangible assets	64,417
Accrued liabilities	237
Other long-term liabilities	(242)
Long-term debt	67,407
Stockholders' equity	(2,701)

The financial statements of HBL as of February 28, 2001 and December 31, 2000, for the two-month period ended February 28, 2001 and for each of the years ended December 31, 2000 and 1999 reflect the accounting basis used by HBL prior to its acquisition by UAG. The financial statements of HBL subsequent to March 1, 2001 reflect the accounting basis for the acquired assets and liabilities, including intangibles, utilized by HBL subsequent to its acquisition by UAG. The basis of accounting used by HBL after the acquisition by UAG is not comparable to the basis of accounting used by HBL prior to the purchase by UAG.

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**HBL, LLC**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

***Cash and Cash Equivalents***

Cash and cash equivalents include all highly-liquid investments that have an original maturity of three months or less at the date of purchase.

***Fair Value of Financial Instruments***

Financial instruments consist of cash and cash equivalents, accounts receivable, accounts payable and debt, including floor plan notes payable. The carrying amount of all significant financial instruments approximates fair value due either to length of maturity or the existence of variable interest rates that approximate prevailing market rates.

***Revenue Recognition***

The Company records revenue when vehicles are delivered to customers, when vehicle service work is performed and when parts are delivered.

The Company arranges financing for customers through various financial institutions and receives a commission from the lender equal to the difference between the interest rates charged to customers over the predetermined interest rates set by the financing institution. The Company also receives commissions from the sale of various insurance contracts to customers. The Company may be assessed a chargeback fee in the event of early cancellation of a loan or insurance contract by the customer. Finance and insurance commission revenue is recorded net of estimated chargebacks at the time the related contract is placed with the financial institution.

The Company also receives commissions from the sale of non-recourse third party extended service contracts to customers. Under these contracts the applicable manufacturer or third party warranty company is directly liable for all warranties provided within the contract. Commission revenue from the sale of these third party extended service contracts is recorded net of estimated chargebacks at the time of sale. Prior to the Acquisition, the Company was the warrantor with respect to certain extended warranty insurance products it sold to customers. Commission revenue from the sale of such contracts was amortized over the warranty period using the straight-line method.

***Inventory Valuation***

Inventories are stated at the lower of cost or market. Cost for new and used vehicle inventories is determined using the specific identification method. Cost for parts, accessories and other inventories is based on factory list prices. Prior to the Acquisition, cost for new vehicle inventories was determined using the last-in, first-out ( LIFO ) method, and cost for parts, accessories and other inventories was based on the first-in, first-out ( FIFO ) method.

***Property and Equipment***

Property and equipment are recorded at cost and depreciated over estimated useful lives, primarily using the straight-line method. Useful lives for purposes of computing depreciation for assets, other than equipment under capital lease and leasehold improvements, are between 5 and 10 years. Leasehold improvements and equipment under capital lease are depreciated over the shorter of the term of the lease or the estimated useful life of the asset.

Expenditures relating to recurring repair and maintenance are expensed as incurred. Expenditures that increase the useful life or substantially increase the serviceability of an existing asset are capitalized. When equipment is sold or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts, and any resulting gain or loss is reflected in income.

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**HBL, LLC**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

***Income Taxes***

HBL is not an income tax paying entity. For the period from March 1, 2001 through December 31, 2001, Holdings was included in the consolidated federal and state tax returns of UAG. For the period from January 1, 1999 through February 28, 2001, Holdings was included in the consolidated federal and state tax returns of LAE. The income tax provision (benefit) reflected in the accompanying financial statements reflects taxes relating to HBL computed on a stand-alone basis.

Income taxes for periods through December 30, 2001 are provided in accordance with Statement of Financial Accounting Standards No. 109, Accounting for Income Taxes ( SFAS No. 109 ). Deferred tax assets or liabilities are computed based upon the difference between financial reporting and tax bases of assets and liabilities using enacted tax rates. A valuation allowance is provided when it is more likely than not that taxable income will not be sufficient to fully realize deferred tax assets.

***Intangible Assets***

Intangible assets of \$64,417, consisting primarily of excess of cost over the fair value of net assets acquired in purchase business combinations, are being amortized on a straight-line basis over periods not exceeding 40 years. Accumulated amortization at December 31, 2001 amounted to \$1,387. Amortization expense for the ten months ended December 31, 2001 was \$1,387.

***Impairment of Long-Lived Assets***

The carrying value of long-lived assets, including intangibles, is reviewed if the facts and circumstances, such as significant declines in revenues, earnings or cash flows or material adverse changes in the business climate, indicate that they may be impaired. The Company performs its review by comparing the carrying amounts of long-lived assets to the estimated undiscounted cash flows relating to such assets. If any impairment in the value of the long-lived assets is indicated, the carrying value of the long-lived assets is adjusted to reflect such impairment based on the discounted cash flows or the fair value of the impaired assets.

***Defined Contribution Plans***

LAE sponsors a defined contribution plan covering a significant majority of the Company's employees. Company contributions to such plans are determined on a discretionary basis by LAE's Board of Directors. The Company incurred expense of \$71, \$0, \$25 and \$50 relating to such plans during the ten months ended December 31, 2001, the two months ended February 28, 2001, the year ended December 31, 2000 and the year ended December 31, 1999, respectively.

***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.

***Advertising***

Advertising costs are expensed as incurred. The Company incurred advertising costs of \$1,393, \$242, \$1,634 and \$1,349 during the ten months ended December 31, 2001, the two months ended February 28, 2001, the year ended December 31, 2000 and the year ended December 31, 1999, respectively.

**Table of Contents****HBL, LLC****NOTES TO FINANCIAL STATEMENTS (Continued)*****Derivative Instruments***

Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities, as amended and interpreted ( SFAS No. 133 ) establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. Under SFAS 133, all derivatives, whether designated in hedging relationships or not, are required to be recorded on the balance sheet at fair value. SFAS 133 defines requirements for designation and documentation of hedging relationships, as well as ongoing effectiveness assessments, which must be met in order to qualify for hedge accounting. For a derivative that does not qualify as a hedge, changes in fair value would be recorded in earnings immediately. If the derivative is designated in a fair-value hedge, the changes in the fair value of the derivative and the hedged item are recorded in earnings. If the derivative is designated in a cash-flow hedge, effective changes in the fair value of the derivative are recorded in other comprehensive income and recorded in the income statement when the hedged item affects earnings. Changes in the fair value of the derivative attributable to hedge ineffectiveness are recorded in earnings immediately. The Company adopted SFAS 133 on January 1, 2001, which had no impact on its financial position or results of operations.

**2. Inventories**

Inventories consisted of the following:

	<b>December 31, 2001</b>	<b>February 28, 2001</b>	<b>December 31, 2000</b>
New vehicles	\$ 14,460	\$ 9,643	\$ 10,367
Used vehicles	4,399	4,307	3,569
Parts, accessories and other	1,477	1,225	1,234
<b>Total Inventories</b>	<b>\$ 20,336</b>	<b>\$ 15,175</b>	<b>\$ 15,170</b>

As previously stated, the Company used the LIFO method for valuing new vehicle inventories for all periods presented prior to the Acquisition. Had the FIFO method been used for valuing new vehicle inventories, inventories would have increased by \$2,399 and \$2,389 as of February 28, 2001 and December 31, 2000, respectively, and the Company would have reported net income (loss) of (\$1,991), \$2,525 and \$1,849 for the two months ended February 28, 2001, the year ended December 31, 2000 and the year ended December 31, 1999, respectively.

**3. Property and Equipment**

Property and equipment consisted of the following:

	<b>December 31, 2001</b>	<b>February 28, 2001</b>	<b>December 31, 2000</b>
Furniture, fixtures and equipment	\$ 301	\$ 2,504	\$ 2,512
Leasehold improvements	489	1,941	1,941
<b>Total</b>	<b>790</b>	<b>4,445</b>	<b>4,453</b>
Less: Accumulated depreciation and amortization	37	2,314	2,255
<b>Property and equipment, net</b>	<b>\$ 753</b>	<b>\$ 2,131</b>	<b>\$ 2,198</b>

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Depreciation and amortization expense for the ten months ended December 31, 2001, the two months ended February 28, 2001, the year ended December 31, 2000 and the year ended December 31, 1999 was \$42, \$72, \$430 and \$489, respectively.

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**Table of Contents****HBL, LLC****NOTES TO FINANCIAL STATEMENTS (Continued)****4. Floor Plan Notes Payable**

The Company currently finances the majority of its new and a portion of its used vehicle inventory under revolving floor plan financing arrangements with DaimlerChrysler Services North America LLC. The floor plan financing arrangements with DaimlerChrysler Services North America LLC are guaranteed by UAG. Prior to the Acquisition, the Company financed the majority of its new and a portion of its used vehicle inventory under revolving floor plan financing arrangements with a bank. Under the terms of its floor plan financing agreements, the Company makes monthly interest payments on the amount financed, but is not required to make loan principal repayments prior to the sale of new and used vehicles. Outstanding borrowings under floor plan financing arrangements as of December 31, 2001, February 28, 2001 and December 31, 2000 were \$19,022, \$13,529 and \$15,069, respectively. The floor plan agreements grant a security interest in substantially all of the assets of the Company, and require repayment after a vehicle's sale. Prior to the Acquisition, the Company's floor plan financing agreement was guaranteed by LAE. Interest rates on the floor plan agreements are variable and increase or decrease based on movements in LIBOR or prime borrowing rates. Floor plan interest expense for the ten months ended December 31, 2001, the two months ended February 28, 2001, the year ended December 31, 2000 and the year ended December 31, 1999 was \$592, \$165, \$1,095 and \$841, respectively.

**5. Operating Lease Obligations**

The Company leases its dealership facilities under non-cancelable operating lease agreements with expiration dates through 2026, including all option periods available to the Company.

Minimum future rental payments required under non-cancelable operating leases in effect as of December 31, 2001 follow:

2002	\$ 2,112
2003	2,232
2004	2,256
2005	2,256
2006	2,256
2007 and thereafter	22,936
	<hr/>
	\$ 34,048
	<hr/>

Rent expense for the ten months ended December 31, 2001, the two months ended February 28, 2001, the year ended December 31, 2000 and the year ended December 31, 1999 amounted to \$2,006, \$418, \$2,496 and \$2,329, respectively.

**6. Long-Term Debt**

Long-term debt represents the debt incurred by UAG in connection with the Acquisition. The interest expense included in these financial statements reflects the Parent's weighted average interest rate of 6.25% on this indebtedness during the ten months ended December 31, 2001. UAG borrowed these funds under a credit agreement with DaimlerChrysler Services North America LLC and Toyota Motor Credit Corporation that provides UAG with revolving loans to be used for acquisitions, working capital, the repurchase of common stock and general corporate purposes. UAG's credit agreement is fully and unconditionally guaranteed on a joint and several basis by the majority of its domestic automotive dealership subsidiaries (and will be guaranteed by domestic automotive dealership subsidiaries acquired or established by them in the future), including the Company. Substantially all of our assets are subject to security interests granted to lenders under UAG's credit agreement.

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**HBL, LLC**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

In March 2002, UAG issued \$300.0 million of senior subordinated notes due 2012 pursuant to Rule 144A and Regulation S, and is scheduled to file a registration statement with the SEC and offer to exchange publicly-traded notes for the notes issued in March 2002. The notes are fully and unconditionally guaranteed on a joint and several basis by the majority of UAG's domestic automotive dealership subsidiaries (and will be guaranteed by domestic automotive dealership subsidiaries acquired or established by them in the future), including the Company.

**7. Related Party Transactions**

From time to time, the Company pays and/or receives fees from UAG and its affiliates for services rendered in the normal course of business. These transactions reflect the provider's cost or an amount mutually agreed upon by both parties. It is the Company's belief that the payments relating to these transactions are on terms at least as favorable as those which could be obtained from an unrelated third party. In addition, management fees of \$998 were charged to HBL by the Parent for the ten month period ended December 31, 2001. Aggregate payments relating to such transactions amounted to \$1,443 for the ten months ended December 31, 2001.

Prior to the Acquisition, LAE allocated costs to the Company in the amount of \$0, \$2,398 and \$1,929 during the two months ended February 28, 2001, the year ended December 31, 2000 and the year ended December 31, 1999, respectively. Amounts due to/from LAE on the balance sheets as of December 31, 2000 and December 31, 1999 represent loans and the payment of various miscellaneous expenses by the Company on LAE's behalf.

Prior to the Acquisition, the Company received sub-rental income in the amount of \$0, \$267 and \$267 during the two months ended February 28, 2001, the year ended December 31, 2000 and the year ended December 31, 1999, respectively.

Prior to the Acquisition, the property leased by the Company for its dealership operations was owned by an entity controlled by LAE's principal shareholders. The Company leased the facility under an operating lease agreement which was set to expire in 2008. The terms of this lease were re-negotiated in connection with the Acquisition. In addition, in the two months ended February 28, 2001 and the year ended December 31, 2000 the Company distributed non-interest bearing related party receivables to LAE of \$1,068 and \$928, respectively.

**8. Members Equity/ Stockholders Equity**

Subsequent to the Acquisition, the Company made distributions of \$5,915 in accordance with the Operating Agreement. Prior to the Acquisition, the Company made distributions to LAE of \$1,068 and \$928 during the two months ended February 28, 2001 and the year ended December 31, 2000, respectively.

**Table of Contents****HBL, LLC****NOTES TO FINANCIAL STATEMENTS (Continued)****9. Income Taxes**

The income tax provision (benefit) consisted of the following:

	Ten Months Ended December 31, 2001	Two Months Ended February 28, 2001	Year Ended December 31, 2000	Year Ended December 31, 1999
<b>Current:</b>				
Federal	\$ 21	\$ 252	\$ 1,470	\$ 1,007
State and local	4	45	263	181
	<u>25</u>	<u>297</u>	<u>1,733</u>	<u>1,188</u>
<b>Deferred:</b>				
Federal	1,123	(1,247)	(95)	(100)
State and local	205	(223)	(17)	(18)
	<u>1,328</u>	<u>(1,470)</u>	<u>(112)</u>	<u>(118)</u>
Income tax (benefit) provision	<u>\$ 1,353</u>	<u>\$ (1,173)</u>	<u>\$ 1,621</u>	<u>\$ 1,070</u>

The income tax provision (benefit) varied from the U.S. federal statutory income tax rate due to the following:

	Ten Months Ended December 31, 2001	Two Months Ended February 28, 2001	Year Ended December 31, 2000	Year Ended December 31, 1999
Income tax provision (benefit) at the Federal statutory rate of 35%	\$ 730	\$ (1,110)	\$ 1,385	\$ 930
State and local income taxes, net of federal benefit	136	(118)	148	99
Non-deductible amortization of goodwill	487			
Other		55	88	41
	<u>1,353</u>	<u>(1,173)</u>	<u>1,621</u>	<u>1,070</u>
Income tax provision (benefit)	<u>\$ 1,353</u>	<u>\$ (1,173)</u>	<u>\$ 1,621</u>	<u>\$ 1,070</u>

The components of deferred tax assets and liabilities at February 28, 2001 and December 31, 2000 were as follows:

	February 28, 2001	December 31, 2000
<b>Deferred Tax Assets</b>		
Accrued liabilities	\$ 2,189	\$ 645
Other	89	151



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Total deferred tax assets	2,278	796
Valuation allowance		
Net deferred tax assets	\$ 2,278	\$ 796

**10. Supplemental Cash Flow Information**

Cash paid interest for the ten months ended December 31, 2001, the two months ended February 28, 2001, the year ended December 31, 2000 and the year ended December 31, 1999 was \$592, \$194, \$1,121 and

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**HBL, LLC**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

\$855, respectively. Cash paid income taxes for the ten months ended December 31, 2001, the two months ended February 28, 2001, the year ended December 31, 2000 and the year ended December 31, 1999 was \$621, \$0, \$1,569 and \$837, respectively. Non cash investing and financing activities include the distribution of intercompany receivables of \$1,068 for the two-months ended February 28, 2001 and \$928 in the year ended December 31, 2000, and the acquisition of assets financed with capital leases and other forms of indebtedness totaling \$277 in 1999.

**11. Subsequent Event**

On February 22, 2002, HBL sold substantially all of the assets of its Land Rover operation, including the franchise rights to the Land Rover product line, to an unaffiliated third party for \$1.4 million in cash. Total revenues for the ten months ended December 31, 2001 were \$13,101.

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Schedule II

## UNITED AUTO GROUP, INC.

## VALUATION AND QUALIFYING ACCOUNTS

Description	Balance at Beginning of Year	Additions	Deductions, Recoveries & Other	Balance at End of Year
(In Thousands)				
<b>Year Ended December 31, 2001</b>				
Allowance for doubtful accounts	\$ 2,038	\$ 2,179	\$ (1,196)	\$ 3,021
Allowance for chargebacks	9,440	19,517	(15,908)	13,049
	<u>\$ 11,478</u>	<u>\$ 21,696</u>	<u>\$ (17,104)</u>	<u>\$ 16,070</u>
<b>Year Ended December 31, 2000</b>				
Allowance for doubtful accounts	\$ 1,899	\$ 1,081	\$ (942)	\$ 2,038
Allowance for chargebacks	8,875	13,813	(13,248)	9,440
	<u>\$ 10,774</u>	<u>\$ 14,894</u>	<u>\$ (14,190)</u>	<u>\$ 11,478</u>
<b>Year Ended December 31, 1999</b>				
Allowance for doubtful accounts	\$ 860	\$ 1,815	\$ (776)	\$ 1,899
Allowance for chargebacks	8,465	11,780	(11,370)	8,875
	<u>\$ 9,325</u>	<u>\$ 13,595</u>	<u>\$ (12,146)</u>	<u>\$ 10,774</u>

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**Item 7. (CONT.)**

c. Exhibits

- Exhibit 23.1 Consent of Deloitte & Touche LLP
- Exhibit 23.2 Consent of Crowe, Chizek and Company LLP
- Exhibit 23.3 Consent of Kaiser Scherer & Schlegel, PLLC
- Exhibit 99.1 Certificate pursuant to § 1350 of Chief Executive Officer
- Exhibit 99.2 Certificate pursuant to § 1350 of Chief Financial Officer
- Exhibit 99.3 Statement Under Oath of Chief Executive Officer dated August 7, 2002
- Exhibit 99.4 Statement Under Oath of Chief Financial Officer dated August 7, 2002

**Item 9. Regulation FD Disclosure**

On August 7, 2002, each of the Chief Executive Officer, Roger S. Penske, and Chief Financial Officer, James R. Davidson, of United Auto Group, Inc. submitted to the SEC sworn statements pursuant to Securities and Exchange Commission Order No. 4-460. A copy of each of these statements is attached hereto as an Exhibit (99.3 and 99.4).

**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 hereunto duly authorized.

Dated: August 7, 2002

UNITED AUTO GROUP, INC.

By: /s/ Roger S. Penske

\_\_\_\_\_  
Roger S. Penske

Its: Chief Executive Officer

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Index to Exhibits

<u>Exhibit No.</u>	<u>Description</u>
23.1	Consent of Deloitte & Touche LLP
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99.1	Certification pursuant to § 1350 of Chief Executive Officer
99.2	Certification pursuant to § 1350 of Chief Financial Officer
99.3	Statement Under Oath of Chief Executive Officer dated August 7, 2002
99.4	Statement Under Oath of Chief Financial Officer dated August 7, 2002