PENSKE AUTOMOTIVE GROUP, INC.
Form 10-Q
October 26, 2018
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

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

For the quarterly period ended September 30, 2018

or

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

For the transition period from to

Commission file number 1-12297

Penske Automotive Group, Inc.

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	22-3086739 (I.R.S. Employer Identification No.)
2555 Telegraph Road Bloomfield Hills, Michigan (Address of principal executive offices)	48302-0954 (Zip Code)

Registrant's telephone number, including area code:

(248) 648-2500

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

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

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

As of October 22, 2018, there were 84,861,435 shares of voting common stock outstanding.

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PART I — FINANCIAL INFORMATION

Item 1. Financial Statements

PENSKE AUTOMOTIVE GROUP, INC.

CONSOLIDATED CONDENSED BALANCE SHEETS

	September 30, 2018	December 31, 2017
	(Unaudited)	
	(In millions, except share and per share amounts)	
ASSETS		
Cash and cash equivalents	$ 37.6	$ 45.7
Accounts receivable, net of allowance for doubtful accounts of $5.3 and $5.5	953.4	954.9
Inventories	3,783.4	3,944.1
Other current assets	91.8	81.8
Total current assets	4,866.2	5,026.5
Property and equipment, net	2,178.2	2,108.6
Goodwill	1,692.6	1,660.5
Other indefinite-lived intangible assets	471.9	474.0
Equity method investments	1,299.7	1,256.6
Other long-term assets	18.3	14.4
Total assets	$ 10,526.9	$ 10,540.6
LIABILITIES AND EQUITY		
Floor plan notes payable	$ 2,169.5	$ 2,343.2
Floor plan notes payable — non-trade	1,359.0	1,418.6
Accounts payable	633.8	641.6
Accrued expenses	570.2	523.5
Current portion of long-term debt	92.7	72.8
Liabilities held for sale	0.7	0.7
Total current liabilities	4,825.9	5,000.4
Long-term debt	1,993.3	2,090.4
Deferred tax liabilities	547.9	481.5
Other long-term liabilities	547.8	540.3
Total liabilities	7,914.9	8,112.6
Commitments and contingent liabilities (Note 9)		
Equity		
Penske Automotive Group stockholders' equity:		
Preferred Stock, $0.0001 par value; 100,000 shares authorized; none issued and outstanding	—	—
Common Stock, $0.0001 par value, 240,000,000 shares authorized; 84,863,169 shares issued and outstanding at September 30, 2018; 85,787,507 shares issued and outstanding at December 31, 2017	—	—

Non-voting Common Stock, $0.0001 par value; 7,125,000 shares authorized; none issued and outstanding	—	—
Class C Common Stock, $0.0001 par value; 20,000,000 shares authorized; none issued and outstanding	—	—
Additional paid-in capital	487.9	532.3
Retained earnings	2,299.2	2,009.4
Accumulated other comprehensive income (loss)	(203.8)	(146.5)
Total Penske Automotive Group stockholders' equity	2,583.3	2,395.2
Non-controlling interest	28.7	32.8
Total equity	2,612.0	2,428.0
Total liabilities and equity	$ 10,526.9	$ 10,540.6

See Notes to Consolidated Condensed Financial Statements

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PENSKE AUTOMOTIVE GROUP, INC.

CONSOLIDATED CONDENSED STATEMENTS OF INCOME

	Three Months Ended September 30, 2018	Three Months Ended September 30, 2017	Nine Months Ended September 30, 2018	Nine Months Ended September 30, 2017
	(Unaudited) (In millions, except per share amounts)			
Revenue:				
Retail automotive dealership	$ 5,148.5	$ 5,085.4	$ 15,900.0	$ 14,882.5
Retail commercial truck dealership	385.3	299.6	1,016.5	739.8
Commercial vehicle distribution and other	124.8	139.4	429.3	366.6
Total revenues	5,658.6	5,524.4	17,345.8	15,988.9
Cost of sales:				
Retail automotive dealership	4,386.3	4,341.2	13,561.5	12,684.0
Retail commercial truck dealership	327.5	255.3	859.7	619.1
Commercial vehicle distribution and other	92.2	105.3	317.8	271.6
Total cost of sales	4,806.0	4,701.8	14,739.0	13,574.7
Gross profit	852.6	822.6	2,606.8	2,414.2
Selling, general and administrative expenses	662.8	646.1	2,001.3	1,869.8
Depreciation	25.9	24.3	77.2	70.0
Operating income	163.9	152.2	528.3	474.4
Floor plan interest expense	(20.2)	(16.4)	(59.0)	(45.6)
Other interest expense	(28.3)	(27.8)	(86.7)	(79.2)
Equity in earnings of affiliates	41.7	30.9	95.0	70.9
Income from continuing operations before income taxes	157.1	138.9	477.6	420.5
Income taxes	(27.1)	(44.7)	(104.7)	(136.0)
Income from continuing operations	130.0	94.2	372.9	284.5
Income (loss) from discontinued operations, net of tax	0.1	0.1	0.2	(0.3)
Net income	130.1	94.3	373.1	284.2
Less: (Loss) income attributable to non-controlling interests	(0.1)	(0.1)	0.2	1.0
Net income attributable to Penske Automotive Group common stockholders	$ 130.2	$ 94.4	$ 372.9	$ 283.2
Basic earnings per share attributable to Penske Automotive Group common stockholders:				
Continuing operations	$ 1.53	$ 1.10	$ 4.37	$ 3.30
Discontinued operations	0.00	0.00	0.00	0.00
Net income attributable to Penske Automotive Group common stockholders	$ 1.53	$ 1.10	$ 4.37	$ 3.30
Shares used in determining basic earnings per share	84.9	85.9	85.2	85.9
Diluted earnings per share attributable to Penske Automotive Group common stockholders:				
Continuing operations	$ 1.53	$ 1.10	$ 4.37	$ 3.30
Discontinued operations	0.00	0.00	0.00	0.00

Net income attributable to Penske Automotive Group common stockholders	$ 1.53	$ 1.10	$ 4.37	$ 3.30
Shares used in determining diluted earnings per share	84.9	86.0	85.3	85.9
Amounts attributable to Penske Automotive Group common stockholders:				
Income from continuing operations	$ 130.0	$ 94.2	$ 372.9	$ 284.5
Less: (Loss) income attributable to non-controlling interests	(0.1)	(0.1)	0.2	1.0
Income from continuing operations, net of tax	130.1	94.3	372.7	283.5
Income (loss) from discontinued operations, net of tax	0.1	0.1	0.2	(0.3)
Net income attributable to Penske Automotive Group common stockholders	$ 130.2	$ 94.4	$ 372.9	$ 283.2
Cash dividends per share	$ 0.36	$ 0.32	$ 1.05	$ 0.93

See Notes to Consolidated Condensed Financial Statements

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PENSKE AUTOMOTIVE GROUP, INC.

CONSOLIDATED CONDENSED STATEMENTS OF COMPREHENSIVE INCOME

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
	(Unaudited) (In millions)			
Net income	$ 130.1	$ 94.3	$ 373.1	$ 284.2
Other comprehensive income:				
Foreign currency translation adjustment	(19.6)	31.7	(57.2)	94.1
Other adjustments to comprehensive income, net	2.1	3.6	(1.3)	7.8
Other comprehensive (loss) income, net of tax	(17.5)	35.3	(58.5)	101.9
Comprehensive income	112.6	129.6	314.6	386.1
Less: Comprehensive (loss) income attributable to non-controlling interests	(0.2)	0.6	(1.0)	3.8
Comprehensive income attributable to Penske Automotive Group common stockholders	$ 112.8	$ 129.0	$ 315.6	$ 382.3

See Notes to Consolidated Condensed Financial Statements

PENSKE AUTOMOTIVE GROUP, INC.

CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS

	Nine Months Ended September 30,	
	2018	2017
	(Unaudited) (In millions)	
Operating Activities:		
Net income	$ 373.1	$ 284.2
Adjustments to reconcile net income to net cash from continuing operating activities:		
Depreciation	77.2	70.0
Earnings of equity method investments	(69.5)	(53.1)
(Income) loss from discontinued operations, net of tax	(0.2)	0.3
Deferred income taxes	64.3	204.9
Changes in operating assets and liabilities:		
Accounts receivable	6.1	(48.7)
Inventories	205.2	(226.7)
Floor plan notes payable	(165.2)	137.8
Accounts payable and accrued expenses	26.2	98.4
Other	18.7	(0.3)
Net cash provided by continuing operating activities	535.9	466.8
Investing Activities:		
Purchase of equipment and improvements	(188.5)	(180.1)
Proceeds from sale of dealerships	58.4	9.0
Proceeds from sale-leaseback transactions	10.7	—
Acquisition of additional ownership interest in Penske Truck Leasing	—	(239.1)
Acquisitions net, including repayment of sellers' floor plan notes payable of $25.8 and $101.6, respectively	(168.6)	(449.7)
Other	(3.5)	4.3
Net cash used in continuing investing activities	(291.5)	(855.6)
Financing Activities:		
Proceeds from borrowings under U.S. credit agreement revolving credit line	1,163.0	1,621.0
Repayments under U.S. credit agreement revolving credit line	(1,335.0)	(1,645.0)
Issuance of 3.75% senior subordinated notes	—	300.0
Net borrowings of other long-term debt	131.0	74.3
Net (repayments) borrowings of floor plan notes payable — non-trade	(59.6)	155.2
Payment of debt issuance costs	—	(4.0)
Repurchases of common stock	(55.8)	(18.5)
Dividends	(89.7)	(80.1)
Other	(6.2)	(5.8)
Net cash (used in) provided by continuing financing activities	(252.3)	397.1
Discontinued operations:		
Net cash provided by discontinued operating activities	0.3	0.5

Net cash provided by discontinued investing activities	—	2.4
Net cash used in discontinued financing activities	—	(0.2)
Net cash provided by discontinued operations	0.3	2.7
Effect of exchange rate changes on cash and cash equivalents	(0.5)	2.2
Net change in cash and cash equivalents	(8.1)	13.2
Cash and cash equivalents, beginning of period	45.7	24.0
Cash and cash equivalents, end of period	$ 37.6	$ 37.2
Supplemental disclosures of cash flow information:		
Cash paid for:		
Interest	$ 127.4	$ 102.2
Income taxes	36.5	21.3
Seller financed/assumed debt	—	3.8
Non cash activities:		
Deferred consideration	$ 6.8	$ —
Consideration transferred through common stock issuance	—	32.4
Contingent consideration	—	20.0

See Notes to Consolidated Condensed Financial Statements

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PENSKE AUTOMOTIVE GROUP, INC.

CONSOLIDATED CONDENSED STATEMENT OF EQUITY

	Common Stock Issued Shares	Amount	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Penske Automotive Group Stockholders' Equity	Non-controlling Interest	Total Equity
	(Unaudited) (Dollars in millions)							
Balance, December 31, 2017	85,787,507	$ —	$ 532.3	$ 2,009.4	$ (146.5)	$ 2,395.2	$ 32.8	$ 2,428.0
Adoption of ASC 606 (Note 1)	—	—	—	6.6	—	6.6	—	6.6
Equity compensation	328,286	—	13.0		—	13.0	—	13.0
Repurchases of common stock	(1,252,624)	—	(55.8)	—	—	(55.8)	—	(55.8)
Dividends	—	—	—	(89.7)	—	(89.7)	—	(89.7)
Purchase of subsidiary shares from non-controlling interest	—	—	(1.4)	—	—	(1.4)	(3.1)	(4.5)
Distributions to non-controlling interest	—	—	—	—	—	—	(0.8)	(0.8)
Foreign currency translation	—	—	—	—	(56.0)	(56.0)	(1.2)	(57.2)
Other	—	—	(0.2)	—	(1.3)	(1.5)	0.8	(0.7)
Net income	—	—	—	372.9	—	372.9	0.2	373.1
Balance, September 30, 2018	84,863,169	$ —	$ 487.9	$ 2,299.2	$ (203.8)	$ 2,583.3	$ 28.7	$ 2,612.0

See Notes to Consolidated Condensed Financial Statements

PENSKE AUTOMOTIVE GROUP, INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

(Unaudited)
(In millions, except share and per share amounts)

1. Interim Financial Statements

Business Overview

Unless the context otherwise requires, the use of the terms “PAG,” “we,” “us,” and “our” in these Notes to the Consolidated Condensed Financial Statements refers to Penske Automotive Group, Inc. and its consolidated subsidiaries.

We are a diversified international transportation services company that operates automotive and commercial truck dealerships principally in the United States, Canada, and Western Europe, and distributes commercial vehicles, diesel engines, gas engines, power systems and related parts and services principally in Australia and New Zealand.

Retail Automotive Dealership. We believe we are the second largest automotive retailer headquartered in the U.S. as measured by the $19.8 billion in total retail automotive dealership revenue we generated in 2017. As of September 30, 2018, we operated 342 retail automotive franchises, of which 151 franchises are located in the U.S. and 191 franchises are located outside of the U.S. The franchises outside the U.S. are located primarily in the U.K. In the nine months ended September 30, 2018, we retailed and wholesaled more than 493,000 vehicles. We are diversified geographically, with 54% of our total retail automotive dealership revenues in the nine months ended September 30, 2018 generated in the U.S. and Puerto Rico and 46% generated outside the U.S. We offer over 40 vehicle brands, with 69% of our retail automotive dealership revenue in the nine months ended September 30, 2018 generated from premium brands, such as Audi, BMW, Mercedes-Benz and Porsche. Each of our franchised dealerships offers a wide selection of new and used vehicles for sale. In addition to selling new and used vehicles, we generate higher-margin revenue at each of our dealerships through maintenance and repair services and the sale and placement of third-party finance and insurance products, third-party extended service and maintenance contracts and replacement and aftermarket automotive products. We operate our franchised dealerships under franchise agreements with a number of automotive manufacturers and distributors that are subject to certain rights and restrictions typical of the industry.

We operate fourteen stand-alone used vehicle dealerships in the U.S. and the U.K. We acquired CarSense in the U.S. and CarShop in the U.K. in the first quarter of 2017 and acquired The Car People in the U.K. in January 2018. Our

CarSense operations in the U.S. consist of five locations operating in the Philadelphia and Pittsburgh, Pennsylvania market areas, including southern New Jersey. Our CarShop operations in the U.K. consist of five retail locations and a vehicle preparation center operating principally throughout Southern England. The Car People operations in the U.K. consist of four retail locations operating across Northern England, which complement CarShop's Southern England locations.

During the nine months ended September 30, 2018, we acquired four retail automotive franchises, were awarded one retail automotive franchise, and disposed of six retail automotive franchises. The four retail automotive franchises acquired are located in Italy and represent the Mercedes-Benz and smart brands.

Retail Commercial Truck Dealership. We operate a heavy and medium duty truck dealership group known as Premier Truck Group ("PTG") with locations in Texas, Oklahoma, Tennessee, Georgia, and Canada. As of September 30, 2018, PTG operated twenty-one locations, including fifteen full-service dealerships and six collision centers, offering primarily Freightliner and Western Star branded trucks. One of these locations was acquired in April 2018 in Canada. PTG also offers a full range of used trucks available for sale as well as service and parts departments, providing a full range of maintenance and repair services.

Commercial Vehicle Distribution. We are the exclusive importer and distributor of Western Star heavy-duty trucks (a Daimler brand), MAN heavy and medium duty trucks and buses (a VW Group brand), and Dennis Eagle refuse collection vehicles, together with associated parts, across Australia, New Zealand and portions of the Pacific. This business, known as Penske Commercial Vehicles Australia (“PCV Australia”), distributes commercial vehicles and parts to a network of more than 70 dealership locations, including eight company-owned retail commercial vehicle dealerships.

We are also a leading distributor of diesel and gas engines and power systems, principally representing MTU, Detroit Diesel, Allison Transmission and MTU Onsite Energy. This business, known as Penske Power Systems (“PPS”), offers products across the on- and off-highway markets in Australia, New Zealand and portions of the Pacific and supports full parts and aftersales service through a network of branches, field locations and dealers across the region. The on-highway portion of this business complements our PCV Australia distribution business, including integrated operations at retail locations selling PCV brands.

Penske Truck Leasing. We hold a 28.9% ownership interest in Penske Truck Leasing Co., L.P. (“PTL”), a leading provider of transportation services and supply chain management. PTL is capable of meeting customers’ needs across the supply chain with a broad product offering that includes full-service truck leasing, truck rental and contract maintenance, along with logistic services such as dedicated contract carriage, distribution center management, transportation management and lead logistics provider. On September 7, 2017, we acquired an additional 5.5% ownership interest in PTL from subsidiaries of GE Capital Global Holdings, LLC (collectively, “GE Capital”). Prior to this acquisition, we held a 23.4% ownership interest in PTL. PTL is currently owned 41.1% by Penske Corporation, 28.9% by us, and 30.0% by Mitsui & Co., Ltd. (“Mitsui”). GE Capital no longer owns any ownership interests in PTL. We account for our investment in PTL under the equity method, and we therefore record our share of PTL’s earnings on our statements of income under the caption “Equity in earnings of affiliates,” which also includes the results of our other equity method investments.

Basis of Presentation

The accompanying unaudited consolidated condensed financial statements of PAG have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”). Certain information and disclosures normally included in our annual financial statements prepared in accordance with accounting principles generally accepted in the United States (“U.S. GAAP”) have been condensed or omitted pursuant to the SEC rules and regulations. The information presented as of September 30, 2018 and December 31, 2017 and for the three and nine month periods ended September 30, 2018 and 2017 is unaudited, but includes all adjustments which our management believes to be necessary for the fair presentation of results for the periods presented. Results for interim periods are not necessarily indicative of results to be expected for the year. These consolidated condensed financial statements should be read in conjunction with our audited financial statements for the year ended December 31, 2017, which are included as part of our Annual Report on Form 10-K.

Estimates

The preparation of financial statements in conformity with U.S. GAAP 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.

Fair Value of Financial Instruments

Accounting standards define fair value as the price that would be received from selling an asset, or paid to transfer a liability in the principal, or most advantageous market for the asset or liability, in an orderly transaction between market participants at the measurement date. Accounting standards establish a fair value hierarchy that requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value and also establishes the following three levels of inputs that may be used to measure fair value:

Level 1 Quoted prices in active markets for identical assets or liabilities

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Level 2	Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted market prices in markets that are not active; or model-derived valuations or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities
Level 3	Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities

Our financial instruments consist of cash and cash equivalents, debt, floor plan notes payable, and forward exchange contracts used to hedge future cash flows. Other than our fixed rate debt, the carrying amount of all significant financial instruments approximates fair value due either to length of maturity, the existence of variable interest rates that approximate prevailing market rates, or as a result of mark to market accounting.

Our fixed rate debt consists of amounts outstanding under our senior subordinated notes and mortgage facilities. We estimate the fair value of our senior unsecured notes using quoted prices for the identical liability (Level 2), and we estimate the fair value of our mortgage facilities using a present value technique based on current market interest rates for similar types of financial instruments (Level 2). A summary of our fixed rate debt is as follows:

	September 30, 2018		December 31, 2017	
	Carrying Value	Fair Value	Carrying Value	Fair Value
3.75% senior subordinated notes due 2020	$ 297.5	$ 296.8	$ 296.5	$ 301.7
5.75% senior subordinated notes due 2022	546.6	557.5	545.9	562.3
5.375% senior subordinated notes due 2024	297.5	294.2	297.2	300.2
5.50% senior subordinated notes due 2026	494.9	491.4	494.4	505.0
Mortgage facilities	243.0	238.5	235.5	233.4

Assets Held for Sale and Discontinued Operations

We had no entities newly classified as held for sale during the nine months ended September 30, 2018 or 2017 that met the criteria to be classified as discontinued operations. The financial information for entities that were classified as discontinued operations prior to adoption of Accounting Standards Update No. 2014-08 are included in “Income (loss) from discontinued operations” in the accompanying consolidated condensed statements of income and “Liabilities held for sale” in the accompanying consolidated condensed balance sheets for all periods presented.

Disposals

During the nine months ended September 30, 2018, we disposed of six retail automotive franchises. The results of operations for these businesses are included within continuing operations for the three and nine months ended September 30, 2018 and 2017, as these franchises did not meet the criteria to be classified as held for sale and treated as discontinued operations.

Income Taxes

Tax regulations may require items to be included in our tax returns at different times than the items are reflected in our financial statements. Some of these differences are permanent, such as expenses that are not deductible on our tax return, and some are temporary differences, such as the timing of depreciation expense. Temporary differences create deferred tax assets and liabilities. Deferred tax assets generally represent items that will be used as a tax deduction or credit in our tax returns in future years which we have already recorded in our financial statements. Deferred tax liabilities generally represent deductions taken on our tax returns that have not yet been recognized as expense in our financial statements. We establish valuation allowances for our deferred tax assets if the amount of expected future taxable income is not likely to allow for the use of the deduction or credit.

The U.S. Tax Cuts and Jobs Act (the “Act”) was signed into law on December 22, 2017. The Act modified several provisions of the Internal Revenue Code related to corporations, including a permanent corporate income tax rate

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reduction from 35% to 21%, effective January 1, 2018. The Act also significantly changed international tax laws for tax years beginning after December 31, 2017 and required a one-time mandatory deemed repatriation of all cumulative post-1986 foreign earnings and profits of a U.S. shareholder’s foreign subsidiaries, which we recognized in 2017, the year of enactment.

On December 22, 2017, Staff Accounting Bulletin No. 118 (“SAB 118”) was issued to address the application of U.S. GAAP in situations when a registrant does not have the necessary information available, prepared or analyzed (including computations) in reasonable detail to complete the accounting for certain income tax effects of the Act. SAB 118 provides a measurement period that should not extend beyond one year from the Act enactment date for companies to complete such income tax accounting under ASC 740.

In accordance with SAB 118, we have now obtained, prepared, and analyzed additional information about facts and circumstances that existed as of the enactment date and computed the U.S. tax impact of the Act. Since the enactment of new tax legislation, the Internal Revenue Service (“IRS”) and state tax authorities have issued news releases, notices, instructions and other forms of guidance to assist taxpayers with implementing the Act. We have also considered the impact of any new information provided by the IRS and state tax authorities in reaching our conclusions. We consider our conclusions to be final and complete.

We determined that our final U.S. federal and state tax liability as a result of the transition tax on repatriation resulted in $52.2 million on a deemed repatriation of $946.0 million of foreign earnings and profits. The remeasurement of certain deferred tax assets and liabilities due to the corporate income tax rate reduction provided an income tax benefit of $301.2 million.

Changes made to provisional estimates for the tax year ended December 31, 2017 were primarily related to our foreign earnings and profits, foreign tax credits, and partnership outside basis difference related to our investment in Penske Truck Leasing.

The following adjustments to our provisional estimates have been recorded to current tax expense or deferred tax expense, as applicable, in the third quarter of 2018:

(In millions)	
Federal and State Changes Due to Repatriation	$ 12.5
Other Adjustments	(0.9)
Total SAB 118 Benefit	$ 11.6

As a result of the changes made to the provisional estimates mentioned above, the total benefit recorded as a result of the enactment of the Act increased from $243.4 million to $255.0 million, with the corresponding income tax benefit of $11.6 million recorded in the third quarter of 2018.

We have considered and analyzed the applicability of the global intangible low-taxed income ("GILTI") provisions of the Act beginning in 2018 and its effect on our annualized effective tax rate for 2018. The effect of the GILTI inclusions on the 2018 annualized effective tax rate is not material. We have adopted the method of accounting for GILTI inclusions as a period expense and therefore have not accrued any deferred taxes in relation to this provision in the first nine months of 2018 or in the 2017 consolidated financial statements.

Recent Accounting Pronouncements

Revenue Recognition

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09, "Revenue from Contracts with Customers (Topic 606)." The FASB also issued additional ASUs containing various updates to Topic 606 which are to be adopted along with ASU 2014-09 (collectively, "the new revenue recognition standard," "ASC 606"). ASC 606 supersedes the revenue recognition requirements in ASC 605, "Revenue Recognition." In accordance with the new revenue recognition standard, an entity recognizes revenue when it

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transfers promised goods or services to customers using a five-step model that requires entities to exercise judgment when considering the terms of contracts with customers. For public companies, the new revenue recognition standard is effective for financial statements issued for annual periods beginning after December 15, 2017, and interim periods within those annual periods. Entities may adopt the new guidance retrospectively to each prior reporting period presented under a full retrospective approach, or as a cumulative-effect adjustment as of the date of adoption under a modified retrospective approach. We adopted ASC 606 on January 1, 2018 using the modified retrospective approach to contracts not completed as of the date of adoption, with no restatement of comparative periods, and a cumulative-effect adjustment to retained earnings recognized as of the date of adoption.

As part of the adoption of ASC 606, we performed an assessment of the impact the new revenue recognition standard would have on our consolidated financial statements. Our assessment also considered required changes in internal controls resulting from the adoption of the new revenue recognition standard. Although new controls have been implemented as a result of the adoption, such changes were not deemed material. A summary of the impact of the adoption of ASC 606 on our consolidated financial statements is included below.

For our Retail Automotive and Retail Commercial Truck reportable segments, under legacy guidance we recognized revenues at a point in time upon meeting relevant revenue recognition criteria. Under ASC 606, the timing of revenue recognition for our service, parts and collision revenue stream changed, as we concluded that performance obligations for service and collision work are satisfied over time under the new revenue recognition standard. All other revenue streams for these businesses continue to be recognized at a point in time, and our performance obligations and revenue recognition timing and practices are substantially similar to how revenues were recorded under legacy guidance.

For our Other reportable segment consisting primarily of our businesses in Australia and New Zealand, Penske Commercial Vehicles Australia and Penske Power Systems, under legacy guidance we recognized revenues for vehicles, engines, parts, and services at a point in time upon meeting relevant revenue recognition criteria. For our long-term power generation contracts at Penske Power Systems, we recognized revenues using the percentage of completion method in accordance with contract milestones. Under ASC 606, the timing of revenue recognition for the service and parts revenue stream for PCV Australia and PPS changed, as we concluded that performance obligations for service work are satisfied over time under the new revenue recognition standard. For revenues previously recognized using the percentage of completion method, these revenues are recognized as performance obligations are satisfied over time, consistent with the timing of recognition under legacy guidance, but are now recognized using an output method, which measures the value to the customer of the goods or services transferred to date relative to the remaining goods or services promised. All other revenue streams for these businesses continue to be recognized at a point in time, and our performance obligations and revenue recognition timing and practices are substantially similar to how revenues were recorded under legacy guidance.

See Note 2 "Revenues" for additional disclosures in accordance with the new revenue recognition standard.

The adoption of the new revenue recognition standard resulted in a net, after-tax cumulative effect adjustment to retained earnings of approximately $6.6 million as of January 1, 2018. The details of this adjustment are summarized below.

	Balance at December 31, 2017	Adjustments Due to ASC 606	Balance at January 1, 2018
Assets			
Accounts receivable	$ 954.9	$ 22.4	$ 977.3
Inventories	3,944.1	(13.4)	3,930.7
Liabilities and Equity			
Accrued expenses	$ 523.5	$ 0.1	$ 523.6
Deferred tax liabilities	481.5	2.3	483.8
Retained earnings	2,009.4	6.6	2,016.0

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The following tables summarize the impact of the adoption of ASC 606 on our consolidated condensed statement of income and consolidated condensed balance sheet for the three and nine months ended and as of September 30, 2018:

	For the Three Months Ended September 30, 2018		
Statement of Income	As Reported	Without Adoption of ASC 606	Impact of Adoption of ASC 606
Revenue:			
Retail automotive dealership	$ 5,148.5	$ 5,149.4	$ (0.9)
Retail commercial truck dealership	385.3	384.3	1.0
Commercial vehicle distribution and other	124.8	126.2	(1.4)
Cost of sales:			
Retail automotive dealership	4,386.3	4,387.0	(0.7)
Retail commercial truck dealership	327.5	327.0	0.5
Commercial vehicle distribution and other	92.2	92.9	(0.7)
Gross profit	852.6	853.0	(0.4)
Income taxes	(27.1)	(27.2)	(0.1)
Net income	130.1	130.4	(0.3)

	For the Nine Months Ended September 30, 2018		
Statement of Income	As Reported	Without Adoption of ASC 606	Impact of Adoption of ASC 606
Revenue:			
Retail automotive dealership	$ 15,900.0	$ 15,898.2	$ 1.8
Retail commercial truck dealership	1,016.5	1,015.4	1.1
Commercial vehicle distribution and other	429.3	426.9	2.4
Cost of sales:			
Retail automotive dealership	13,561.5	13,560.4	1.1
Retail commercial truck dealership	859.7	859.1	0.6
Commercial vehicle distribution and other	317.8	316.8	1.0
Gross profit	2,606.8	2,604.2	2.6
Income taxes	(104.7)	(103.9)	0.8
Net income	373.1	371.3	1.8

Balance Sheet	September 30, 2018 As Reported	Without Adoption of ASC 606	Impact of ASC 606 Adoption
Assets			
Accounts receivable	$ 953.4	$ 925.7	$ 27.7
Inventories	3,783.4	3,799.2	(15.8)
Liabilities and Equity			
Accrued expenses	$ 570.2	$ 569.8	$ 0.4
Deferred tax liabilities	547.9	544.9	3.0
Retained earnings	2,299.2	2,290.7	8.5

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Accounting for Leases

In February 2016, the FASB issued ASU No. 2016-02, “Leases (Topic 842).” Under this new guidance, a company will now recognize most leases on its balance sheet as lease liabilities with corresponding right-of-use assets. For public companies, this ASU is effective for financial statements issued for annual periods beginning after December 15, 2018, and interim periods within those annual periods, with early adoption permitted. The FASB has since issued further ASUs related to the standard providing additional practical expedients and an optional transition method allowing entities to not recast comparative periods. We intend to adopt this ASU, including all available practical expedients, on January 1, 2019 using the optional transition method. As such, we will recognize the effects of applying the new standard as a cumulative-effect adjustment to retained earnings as of January 1, 2019.

We have a significant amount of leases for property and equipment that are classified as operating leases under current lease accounting guidance. The adoption of this ASU will result in a significant increase to our consolidated balance sheets for lease liabilities and right-of-use assets. We believe our current off-balance sheet leasing commitments are reflected in our credit rating. We are also in the process of evaluating and documenting any changes in controls and procedures that may be necessary as part of our implementation of the new standards; however, we do not expect material changes. We will continue to assess the impact that these new standards will have our on our consolidated financial statements throughout the remainder of 2018.

Classification of Certain Cash Receipts and Cash Payments

In August 2016, the FASB issued ASU No. 2016-15, “Statement of Cash Flows (Topic 230) — Classification of Certain Cash Receipts and Cash Payments.” This ASU provides new guidance on eight specific cash flow issues related to how such cash receipts and cash payments should be presented in a statement of cash flows. For public companies, this ASU is effective for financial statements issued for annual periods beginning after December 15, 2017, and interim periods within those annual periods, with early adoption permitted. The amendments from this update are to be applied retrospectively. We adopted this ASU retrospectively on January 1, 2018. The adoption of this accounting standard update did not have an impact on our consolidated cash flows for the nine months ended September 30, 2018 and September 30, 2017.

Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income

In February 2018, the FASB issued ASU No. 2018-02, “Income Statement — Reporting Comprehensive Income (Topic 220) — Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income.” This ASU allows for a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the enactment of the U.S. Tax Cuts and Jobs Act (“the Act”). The update also requires entities to disclose whether or not they elected to reclassify the tax effects related to the Act as well as their accounting policy for releasing income tax effects from accumulated other comprehensive income. This ASU is effective for financial statements issued for annual periods beginning after December 15, 2018, and interim periods within those annual periods, with early adoption permitted. We do not intend to adopt the optional guidance of this accounting standard update, as the potential impact on our consolidated financial statements is not material.

Fair Value Measurement Disclosure

In August 2018, the FASB issued ASU No. 2018-13, “Fair Value Measurement (Topic 820): Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement.” This ASU eliminates, modifies, and adds certain disclosure requirements on fair value measurements. For public companies, this ASU is effective for financial statements issued for annual periods beginning after December 15, 2019, and interim periods within those annual periods, with early adoption permitted. Entities are permitted to early adopt any eliminated or amended disclosures and delay adoption of the additional disclosure requirements until the effective date. We intend to adopt this ASU on January 1, 2020. We do not expect the adoption of this accounting standard update to have a significant impact on our consolidated financial statements.

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Accounting for Cloud Computing Arrangements

In August 2018, the FASB issued ASU No. 2018-15, "Intangibles—Goodwill and Other—Internal-Use Software - Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract." Under this new guidance, certain implementation costs incurred in a hosted cloud computing service arrangement will be capitalized in accordance with ASC 350-40. For public companies, this ASU is effective for financial statements issued for annual periods beginning after December 15, 2019, and interim periods within those annual periods, with early adoption permitted. The amendments from this update are to be applied retrospectively or prospectively to all implementation costs incurred after adoption. We intend to adopt this ASU on January 1, 2020. We are currently evaluating the impacts the adoption of this accounting standard update will have on our consolidated financial statements.

2. Revenues

Automotive and commercial truck dealerships represent the majority of our revenues. New and used vehicle revenues typically include sales to retail customers, to fleet customers, and to leasing companies providing consumer leasing. We generate finance and insurance revenues from sales of third-party extended service contracts, sales of third-party insurance policies, commissions relating to the sale of finance and lease contracts to third parties, and the sales of certain other products. Service and parts revenues include fees paid by customers for repair, maintenance and collision services, and the sale of replacement parts and other aftermarket accessories, as well as warranty repairs that are reimbursed directly by various OEMs. Revenues are recognized upon satisfaction of our performance obligations under contracts with our customers and are measured at the amount of consideration we expect to be entitled to in exchange for transferring goods or providing services. A discussion of revenue recognition by reportable segment is included below.

Retail Automotive and Retail Commercial Truck Dealership Revenue Recognition

Dealership Vehicle Sales. We record revenue for vehicle sales at a point in time when vehicles are delivered, which is when the transfer of title, risks and rewards of ownership and control are considered passed to the customer. The amount of consideration we receive for vehicle sales is stated within the executed contract with our customer and is reduced by any noncash consideration representing the fair value of trade-in vehicles, if applicable. Payment is typically due and collected within 30 days subsequent to transfer of control of the vehicle.

Dealership Parts and Service Sales. We record revenue for vehicle service and collision work over time as work is completed, and when parts are delivered to our customers. For service and parts revenues recorded over time, we utilize a method that considers total costs incurred to date and the applicable margin in relation to total expected efforts to complete our performance obligation in order to determine the appropriate amount of revenue to recognize over time. Recognition of this revenue over time reflects the amount of consideration we expect to be entitled to for the transfer of goods and services performed to date, representative of the amount for which we have a right to payment. The amount of consideration we receive for parts and service sales, including collision repair work, is based upon labor hours expended and parts utilized to perform and complete the necessary services to our customers. Payment is typically due upon delivery or within a period of time shortly thereafter. We receive payment from our customers upon transfer of control or within a period typically less than 30 days subsequent to the completion of services for the customer. We allow for customer returns of parts sales up to 30 days after the sale; however, parts returns are not material.

Dealership Finance and Insurance Sales. Subsequent to the sale of a vehicle to a customer, we sell installment sale contracts to various financial institutions on a non recourse basis (with specified exceptions) to mitigate the risk of default. We receive a commission from the lender equal to either the difference between the interest rate charged to the customer and the interest rate set by the financing institution or a flat fee. We also receive commissions for facilitating the sale of various products to customers, including guaranteed vehicle protection insurance, vehicle theft protection and extended service contracts. These commissions are recorded as revenue at a point in time when the customer enters into the contract. Payment is typically due and collected within 30 days subsequent to the execution of the contract with the customer. In the case of finance contracts, a customer may prepay or fail to pay their contract, thereby terminating the contract. Customers may also terminate extended service contracts and other insurance products, which are fully paid at purchase, and become eligible for refunds of unused premiums. In these circumstances, a portion of the commissions we

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received may be charged back based on the terms of the contracts. The revenue we record relating to these transactions is net of an estimate of the amount of chargebacks we will be required to pay. Our estimate is based upon our historical experience with similar contracts, including the impact of refinance and default rates on retail finance contracts and cancellation rates on extended service contracts and other insurance products. Aggregate reserves relating to chargeback activity were $25.9 million and $24.9 million as of September 30, 2018 and December 31, 2017, respectively.

Commercial Vehicle Distribution and Other Revenue Recognition

Penske Commercial Vehicles Australia. We record revenue from the distribution of vehicles and other products at a point in time when delivered, which is when the transfer of title, risks and rewards of ownership and control are considered passed to the customer. We record revenue for service or repair work over time as work is completed, and when parts are delivered to our customers. For service and parts revenues recorded over time, we utilize a method that considers total costs incurred to date and the applicable margin in relation to total expected efforts to complete our performance obligation in order to determine the appropriate amount of revenue to recognize over time. Recognition of this revenue over time reflects the amount of consideration we expect to be entitled to for the transfer of goods and services performed to date, representative of the amount for which we have a right to payment.

The amount of consideration we receive for vehicle and product sales is stated within the executed contract with our customer. The amount of consideration we receive for parts and service sales is based upon labor hours expended and parts utilized to perform and complete the necessary services to our customers. Payment is typically due upon delivery, upon invoice, or within a period of time shortly thereafter. We receive payment from our customers upon transfer of control or within a period typically less than 30 days subsequent to transfer of control or invoice.

Penske Power Systems. We record revenue from the distribution of engines and other products at a point in time when delivered, which is when the transfer of title, risks and rewards of ownership and control are considered passed to the customer. We record revenue for service or repair work over time as work is completed, and when parts are delivered to our customers. For service and parts revenues recorded over time, we utilize a method that considers total costs incurred to date and the applicable margin in relation to total expected efforts to complete our performance obligation in order to determine the appropriate amount of revenue to recognize over time. Recognition of revenue over time reflects the amount of consideration we expect to be entitled to for the transfer of goods and services performed to date, representative of the amount for which we have a right to payment.

For our long-term power generation contracts, we record revenue over time as services are provided in accordance with contract milestones, which is considered an output method that requires judgment to determine our progress towards contract completion and the corresponding amount of revenue to recognize. Any revisions to estimates related to revenues or costs to complete contracts are recorded in the period in which the revisions to estimates are identified and the amounts can be reasonably estimated.

The amount of consideration we receive for engine, product, and power generation sales is stated within the executed contract with our customer. The amount of consideration we receive for service sales is based upon labor hours expended and parts utilized to perform and complete the necessary services to our customers. Payment is typically due upon delivery, upon invoice, or within a period of time shortly thereafter. We receive payment from our customers upon transfer of control or within a period typically less than 30 days subsequent to transfer of control or invoice.

Other. Other revenue primarily consists of our non-automotive motorcycle dealership operations. Revenue recognition practices for these operations do not differ materially from those described under “Retail Automotive and Retail Commercial Truck Dealership Revenue Recognition” above.

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Retail Automotive Dealership

The following tables disaggregate our retail automotive reportable segment revenue by product type and geographic location for the three and nine months ended September 30, 2018 and 2017:

	Three Months Ended September 30,		Nine Months Ended September 30,	
Retail Automotive Dealership Revenue	2018	2017	2018	2017
New vehicle	$ 2,350.2	$ 2,480.8	$ 7,325.6	$ 7,189.9
Used vehicle	1,825.2	1,669.5	5,588.9	4,850.6
Finance and insurance, net	158.5	152.0	482.2	436.6
Service and parts	523.8	520.9	1,615.1	1,540.1
Fleet and wholesale	290.8	262.2	888.2	865.3
Total retail automotive dealership revenue	$ 5,148.5	$ 5,085.4	$ 15,900.0	$ 14,882.5

	Three Months Ended September 30,		Nine Months Ended September 30,	
Retail Automotive Dealership Revenue	2018	2017	2018	2017
U.S.	$ 2,891.6	$ 2,953.1	$ 8,596.4	$ 8,625.5
U.K.	1,945.1	1,864.6	6,244.9	5,412.3
Germany and Italy	311.8	267.7	1,058.7	844.7
Total retail automotive dealership revenue	$ 5,148.5	$ 5,085.4	$ 15,900.0	$ 14,882.5

Retail Commercial Truck Dealership

The following table disaggregates our retail commercial truck reportable segment revenue by product type for the three and nine months ended September 30, 2018 and 2017:

	Three Months Ended September 30,		Nine Months Ended September 30,	
Retail Commercial Truck Dealership Revenue	2018	2017	2018	2017
New truck	$ 249.4	$ 184.3	$ 630.5	$ 411.5
Used truck	32.5	25.7	86.3	67.9
Finance and insurance, net	2.9	2.1	9.0	6.6
Service and parts	93.1	83.3	275.7	244.6
Other	7.4	4.2	15.0	9.2

Total retail commercial truck dealership revenue	$ 385.3	$ 299.6	$ 1,016.5	$ 739.8

Commercial Vehicle Distribution and Other

The following table disaggregates our other reportable segment revenue by business for the three and nine months ended September 30, 2018 and 2017:

	Three Months Ended September 30,		Nine Months Ended September 30,	
Commercial Vehicle Distribution and Other	2018	2017	2018	2017
Penske Commercial Vehicles Australia	$ 50.4	$ 70.7	$ 169.6	$ 191.6
Penske Power Systems	73.3	67.6	256.8	171.8
Other	1.1	1.1	2.9	3.2
Total commercial vehicle distribution and other revenue	$ 124.8	$ 139.4	$ 429.3	$ 366.6

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Contract Balances

The following table summarizes our accounts receivable and unearned revenues as of September 30, 2018 and December 31, 2017:

	September 30, 2018	December 31, 2017
Accounts receivable		
Contracts in transit	$ 318.7	$ 356.1
Vehicle receivables	251.9	233.0
Manufacturer receivables	216.8	230.1
Trade receivables	158.9	136.7
Accrued expenses		
Unearned revenues	$ 271.7	$ 302.6

Contracts in transit represent receivables from unaffiliated finance companies relating to the sale of customers' installment sales and lease contracts arising in connection with the sale of a vehicle by us. Vehicle receivables represent receivables for any portion of the vehicle sales price not paid by the finance company. Manufacturer receivables represent amounts due from manufacturers, including incentives, holdbacks, rebates, warranty claims, and other receivables due from the factory. Trade receivables represent receivables due from customers, including amounts due for parts and service sales, as well as receivables due from finance companies and others for the commissions earned on financing and commissions earned on insurance and extended service products provided by third parties. We evaluate collectability of receivables and estimate an allowance for doubtful accounts based on the age of the receivable and historical collection experience, which is recorded within "Accounts receivable" on our consolidated balance sheets with our receivables presented net of the allowance.

Unearned revenues primarily relate to payments received from customers prior to satisfaction of our performance obligations, such as customer deposits and deferred revenues from operating leases. These amounts are presented within "Accrued expenses" on our consolidated balance sheets. Of the amounts recorded as unearned revenues as of December 31, 2017, $220.3 million was recognized as revenue during the nine months ended September 30, 2018.

Additional Revenue Recognition Related Policies

We do not have any material significant payment terms associated with contracts with our customers. Payment is due and collected as previously detailed for each reportable segment. We do not offer material rights of return or service-type warranties.

Taxes collected from customers and remitted to governmental authorities are recorded on a net basis (excluded from revenue). Shipping costs incurred subsequent to transfer of control to our customers are recognized as cost of sales. Sales promotions that we offer to customers are accounted for as a reduction of revenues at the time of sale.

We expense sales commissions as incurred, as the amortization period for such costs would be less than one year. We do not disclose the value of unsatisfied performance obligations for contracts with an original expected length of one year or less nor for contracts that we recognize revenue at the amount to which we have the right to invoice for services performed. The effect of applying these practical expedients is not material.

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3. Inventories

Inventories consisted of the following:

	September 30, 2018	December 31, 2017
Retail automotive dealership new vehicles	$ 2,143.2	$ 2,344.1
Retail automotive dealership used vehicles	1,042.4	993.1
Retail automotive parts, accessories and other	126.3	141.7
Retail commercial truck dealership vehicles and parts	245.9	207.0
Commercial vehicle distribution vehicles, parts and engines	225.6	258.2
Total inventories	$ 3,783.4	$ 3,944.1

We receive credits from certain vehicle manufacturers that reduce cost of sales when the vehicles are sold. Such credits amounted to $15.1 million and $15.7 million during the three months ended September 30, 2018 and 2017, respectively, and $40.7 million and $40.2 million during the nine months ended September 30, 2018 and 2017, respectively.

4. Business Combinations

During the nine months ended September 30, 2018, we acquired The Car People, a stand-alone specialty retailer of used vehicles in the U.K. representing four locations; acquired four retail automotive franchises; and acquired one retail commercial truck dealership. During the nine months ended September 30, 2017, we acquired CarSense, a stand-alone specialty retailer of used vehicles in the U.S. representing five locations, acquired CarShop, a stand-alone specialty retailer of used vehicles in the U.K. representing five retail locations and a vehicle preparation center, and acquired eight retail automotive franchises. Our financial statements include the results of operations of the acquired entities from the date of acquisition. The fair value of the assets acquired and liabilities assumed have been recorded in our consolidated condensed financial statements, and may be subject to adjustment pending completion of final valuation. A summary of the aggregate consideration paid and the aggregate amounts of the assets acquired and liabilities assumed for the nine months ended September 30, 2018 and 2017 follows:

	September 30,	
	2018	2017
Accounts receivable	$ 3.6	$ 11.1
Inventories	62.8	139.9

Other current assets	—	2.9
Property and equipment	52.6	21.8