

SONIC AUTOMOTIVE INC

Form 10-K

February 24, 2011

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

Form 10-K

- ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the fiscal year ended December 31, 2010
- OR**
- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from to

Commission file number 1-13395
SONIC AUTOMOTIVE, INC.
(Exact Name of Registrant as Specified in its Charter)

DELAWARE
*(State or Other Jurisdiction of
Incorporation or Organization)*

56-2010790
*(I.R.S. Employer
Identification No.)*

6415 IDLEWILD ROAD, SUITE 109
CHARLOTTE, NORTH CAROLINA
(Address of Principal Executive Offices)

28212
(Zip Code)

(704) 566-2400
(Registrant's telephone number, including area code)

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

Title of Each Class	Name of Each Exchange on Which Registered
Class A Common Stock, \$.01 Par Value	New York Stock Exchange

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT:

(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted 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 and post such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company
(Do not check if a smaller reporting company)

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

The aggregate market value of the voting common stock held by non-affiliates of the registrant was approximately \$213,038,584 based upon the closing sales price of the registrant's Class A common stock on June 30, 2010 of \$8.56 per share. As of February 18, 2011 there were 40,760,973 shares of Class A common stock, par value \$0.01 per share, and 12,029,375 shares of Class B common stock, par value \$0.01 per share, outstanding.

Documents incorporated by reference. Portions of the registrant's Proxy Statement for the Annual Meeting of Stockholders to be held April 21, 2011 are incorporated by reference into Part III of this Form 10-K.

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This Annual Report on Form 10-K contains numerous forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements address our future objectives, plans and goals, as well as our intent, beliefs and current expectations regarding future operating performance, and can commonly be identified by words such as may, will, should, believe, expect, anticipate, intend, plan, similar words or phrases. Specific events addressed by these forward-looking statements include, but are not limited to:

vehicle sales rates and same store sales growth;

future liquidity trends or needs;

our business and growth strategies;

future covenant compliance;

our financing plans and our ability to repay or refinance existing debt when due;

future acquisitions or dispositions;

level of fuel prices;

industry trends; and

general economic trends, including employment rates and consumer confidence levels.

These forward-looking statements are based on our current estimates and assumptions and involve various risks and uncertainties. As a result, you are cautioned that these forward-looking statements are not guarantees of future performance, and that actual results could differ materially from those projected in these forward-looking statements. Factors which may cause actual results to differ materially from our projections include those risks described in Item 1A of this Form 10-K and elsewhere in this report, as well as:

the number of new and used cars sold in the United States generally, and as compared to our expectations and the expectations of the market;

our ability to generate sufficient cash flows or obtain additional financing to fund acquisitions, capital expenditures, our share repurchase program, dividends on our Common Stock, and general operating activities;

the reputation and financial condition of vehicle manufacturers whose brands we represent, the financial incentives vehicle manufacturers offer and their ability to design, manufacture, deliver and market their vehicles successfully;

our relationships with manufacturers, which may affect our ability to complete additional acquisitions;

changes in laws and regulations governing the operation of automobile franchises, accounting standards, taxation requirements, and environmental laws;

adverse resolutions of one or more significant legal proceedings against us or our dealerships;

general economic conditions in the markets in which we operate, including fluctuations in interest rates, employment levels, the level of consumer spending and consumer credit availability;

the terms of any refinancing of our existing indebtedness;

high competition in the automotive retailing industry, which not only creates pricing pressures on the products and services we offer, but also on businesses we seek to acquire;

our ability to successfully integrate potential future acquisitions; and

the rate and timing of overall economic recovery or decline.

Table of Contents**PART I****Item 1. Business.**

Sonic Automotive, Inc. was incorporated in Delaware in 1997. We are one of the largest automotive retailers in the United States. As of December 31, 2010, we operated 135 dealership franchises at 118 dealership locations, representing 29 different brands of cars and light trucks, and 25 collision repair centers in 15 states. Our dealerships provide comprehensive services including (1) sales of both new and used cars and light trucks; (2) sales of replacement parts and performance of vehicle maintenance, warranty, paint and repair services (collectively, Fixed Operations); and (3) arrangement of extended service contracts, financing and insurance and other aftermarket products (collectively, F&I) for our customers.

The following charts depict the multiple sources of continuing operations revenue and gross profit for the year ended December 31, 2010:

Revenue**Gross Profit**

As of December 31, 2010, we operated dealerships in the following markets:

Market	Number of Dealerships	Number of Franchises	Percent of 2010 Total Revenue
Houston	21	25	21.7%
Alabama/Tennessee	16	22	10.4%
North/South Carolina/Georgia	13	16	10.4%
South Bay (San Francisco)	6	6	7.5%
Los Angeles North	11	13	7.4%
Los Angeles South	4	4	7.3%
Florida	10	10	6.5%
Mid-Atlantic	5	6	6.3%
North Bay (San Francisco)	10	9	6.0%
Dallas	4	4	5.0%
Oklahoma	5	5	2.9%
Ohio	4	6	2.7%
Colorado	2	2	2.1%
Michigan	4	4	1.9%
Las Vegas	3	3	1.9%
Total	118	135	100.0%

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In the future, we plan to purchase franchises that enrich our franchise portfolio and divest franchises that we believe will not yield acceptable returns over the long-term. Currently, we are not pursuing any significant acquisition opportunities. Although we believe growth through acquisitions will be a significant source of growth for us in the future, we do not see this being a significant source of growth in the near-term. See Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources for a discussion of our plans for the use of capital generated through operations. Our ability to complete acquisitions in the future will depend on many factors, including the availability of financing and the existence of any contractual provisions that may restrict our acquisition activity.

The automotive retailing industry remains highly fragmented, and we believe that further consolidation may occur over the long-term. We believe that attractive acquisition opportunities continue to exist for dealership groups with the capital and experience to identify, acquire and professionally manage dealerships.

Business Strategy

Maximize Asset Returns Through Process Execution. We have developed standardized operating processes which are documented in operating playbooks for our dealerships. Through the continued implementation of these operating playbooks, we believe organic growth opportunities exist. Through the implementation of our standard operating practices at all of our dealerships, we believe we are able to offer a more favorable buying experience to our customers and create efficiencies in our business processes. We believe the development, refinement and implementation of these operating processes will enhance the customer experience, make us more competitive in the marketplace and drive revenue growth across each of our revenue streams.

Invest in Dealership Properties. Historically, we have operated our dealerships primarily on property financed through long-term operating leases. As these leases mature or as we have an opportunity to purchase the underlying real estate prior to renewal, we have begun to purchase and own more of our dealership properties. We remain opportunistic in purchasing existing properties or relocating dealership operations to owned real estate where the returns are favorable. We believe owning our properties will, over the long-term, strengthen our balance sheet and reduce our overall cost of operating and financing our dealership facilities.

Reduce Leverage. As we generate cash through operations and have the ability to repay or repurchase outstanding indebtedness, we will continue to reduce our non-mortgage related leverage.

Diverse Revenue Streams. We have multiple revenue streams. In addition to new vehicle sales, our revenue sources include used vehicle sales, which we believe are less sensitive to economic cycles and seasonal influences that exist with new vehicle sales. Our fixed operations sales carry a higher gross margin and, in the past, have not been as economically sensitive as vehicle sales. We also offer customers assistance in obtaining financing and a range of automobile related insurance products.

Portfolio Management. Although we are not currently pursuing any significant acquisition opportunities, our long-term growth strategy is focused on large metropolitan markets, predominantly in the Southeast, Southwest, Midwest and California. A majority of our dealerships are either luxury or mid-line import brands. For the year ended December 31, 2010, 85.1% of our total revenue was generated by mid-line import and luxury dealerships, which usually have higher operating margins, more stable fixed operations departments, lower associate turnover and lower inventory levels.

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The following table depicts the breakdown of our new vehicle revenues by brand:

	Percentage of New Vehicle Revenue		
	Year Ended December 31,		
Brand(1)	2008	2009	2010
BMW	18.6%	17.2%	17.4%
Honda	15.0%	15.2%	13.9%
Toyota	11.7%	11.7%	11.1%
Mercedes	10.5%	9.7%	9.8%
Ford	5.0%	9.6%	8.8%
General Motors(2)	10.5%	6.5%	6.7%
Lexus	5.9%	6.2%	6.0%
Cadillac	5.6%	4.6%	5.5%
Other(3)	3.6%	3.8%	3.3%
Audi	1.8%	2.6%	3.1%
Volkswagen	1.8%	2.1%	2.3%
Land Rover	1.3%	1.7%	2.0%
Hyundai	1.4%	1.8%	2.0%
Porsche	1.4%	1.5%	1.8%
Infiniti	1.2%	1.2%	1.4%
Nissan	0.9%	1.1%	1.3%
Volvo	1.2%	1.4%	1.2%
Other Luxury(4)	1.1%	1.0%	1.1%
Acura	1.1%	0.8%	1.0%
Chrysler(5)	0.4%	0.3%	0.3%
Total	100.0%	100.0%	100.0%

(1) In accordance with the provisions of Presentation of Financial Statements in the Accounting Standards Codification (the ASC), prior years income statement data reflect reclassifications to (i) exclude franchises sold, identified for sale, or terminated subsequent to December 31, 2009 which had not been previously included in discontinued operations or (ii) include franchises previously held for sale which subsequently were reclassified to held and used. See Notes 1 and 2 to our accompanying Consolidated Financial Statements which discuss these and other factors that affect the comparability of the information for the periods presented.

(2) Includes Buick, Chevrolet and GMC.

(3) Includes Isuzu, Kia, Mini, Scion and Subaru.

(4) Includes Hummer, Jaguar and Saab.

(5) Includes Chrysler, Dodge and Jeep.

Expand our eCommerce Capabilities. Automotive customers have become increasingly more comfortable using technology to research their vehicle buying alternatives and communicate with dealership personnel. The internet presents a unique marketing, advertising and automotive sales channel which we will exploit nationally to drive demand creation and demand maximization for our dealerships. Our technology platforms have given us the ability to leverage technology to more efficiently integrate systems, customize our dealership websites and use our data to improve the effectiveness of our advertising and interaction with our customers. This also allows us to market all of our products and services to a national audience and, at the same time, support the market penetration of our individual dealerships.

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Achieve High Levels of Customer Satisfaction. We focus on maintaining high levels of customer satisfaction. Our personalized sales process is designed to satisfy customers by providing high-quality vehicles in a positive, consumer friendly buying environment. Several manufacturers offer specific financial incentives on a per vehicle basis if certain Customer Satisfaction Index (CSI) levels (which vary by manufacturer) are achieved by a dealership. In addition, all manufacturers consider CSI scores in approving acquisitions. In order to keep dealership management focused on customer satisfaction, we include CSI results as a component of our incentive-based compensation programs.

Train, Develop and Retain Associates. We believe our associates are the cornerstone of our business and crucial to our financial success. Our goal is to develop our associates and foster an environment where our associates can contribute and grow with the company. Associate satisfaction is very important to us and we believe a high level of associate satisfaction reduces turnover and enhances our customers' experience at our stores by pairing our customers with well-trained, seasoned associates. We believe that our comprehensive training of all employees provides us with a competitive advantage over other dealership groups.

Increase Sales of Higher Margin Products and Services. We continue to pursue opportunities to increase our sales of higher-margin products and services by expanding the following:

Finance, Insurance and Other Aftermarket Products (F&I): Each sale of a new or used vehicle gives us an opportunity to provide our customer with financing and insurance options and earn financing fees and insurance commissions. We also offer our customers the opportunity to purchase extended service contracts and other aftermarket products. We currently offer a wide range of non-recourse financing, leasing, other aftermarket products, service contracts and insurance products to our customers. We emphasize menu-selling techniques and other best practices to increase our sales of F&I products at both newly acquired and existing dealerships.

Parts, Service & Repair: Each of our dealerships offers a fully integrated service and parts department. Manufacturers permit warranty work to be performed only at franchised dealerships such as ours. As a result, our franchised dealerships are uniquely qualified and positioned to perform work covered by manufacturer warranties on increasingly complex vehicles. We believe we can continue to grow our profitable parts and service business over the long-term by increasing service capacity, investing in sophisticated equipment and well-trained technicians, using variable rate pricing structures, focusing on customer service and efficiently managing our parts inventory. In addition, we believe our emphasis on selling extended service contracts associated with new and used vehicle retail sales will drive further service and parts business in our dealerships as we increase the potential to retain current customers beyond the term of the standard manufacturer warranty period.

Certified Pre-Owned Vehicles: Various manufacturers provide franchised dealers the opportunity to sell certified pre-owned (CPO) vehicles. This certification process extends the standard manufacturer warranty on the CPO vehicle. We typically earn higher revenues and gross profits on CPO vehicles compared to non-certified pre-owned vehicles. We also believe the extended manufacturer warranty increases our potential to retain the pre-owned purchaser as a future parts and service customer. Since CPO warranty work can only be performed at franchised dealerships, we believe CPO warranty work will increase our fixed operations business.

Value Used Vehicle: We believe the market for value vehicles (used vehicles with retail prices below \$10,000) is broad and not as sensitive to market fluctuations as higher priced used vehicles. Our strategy in retailing these vehicles includes the use of technology and market data to determine optimal pricing and placement of these vehicles at our stores.

Relationships with Manufacturers

Each of our dealerships operates under a separate franchise or dealer agreement that governs the relationship between the dealership and the manufacturer. Each franchise or dealer agreement specifies the location of the dealership for the sale of vehicles and for the performance of certain approved services in a specified market area. The designation of such areas generally does not guarantee exclusivity within a specified territory. In addition, most manufacturers allocate vehicles on a "turn and earn" basis that rewards high sales volume. A franchise or dealer

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agreement requires the dealer to meet specified standards regarding showrooms, facilities and equipment for servicing vehicles, inventories, minimum net working capital, personnel training and other aspects of the business. Each franchise or dealer agreement also gives the related manufacturer the right to approve the dealer operator and any material change in management or ownership of the dealership. Each manufacturer may terminate a franchise or dealer agreement under certain circumstances, such as a change in control of the dealership without manufacturer approval, the impairment of the reputation or financial condition of the dealership, the death, removal or withdrawal of the dealer operator, the conviction of the dealership or the dealership's owner or dealer operator of certain crimes, the failure to adequately operate the dealership or maintain new vehicle financing arrangements, insolvency or bankruptcy of the dealership or a material breach of other provisions of the applicable franchise or dealer agreement.

Many automobile manufacturers have developed policies regarding public ownership of dealerships. Policies implemented by manufacturers include the following restrictions:

the ability to force the sale of their respective franchises upon a change in control of our company or a material change in the composition of our Board of Directors;

the ability to force the sale of their respective franchises if an automobile manufacturer or distributor acquires more than 5% of the voting power of our securities; and

the ability to force the sale of their respective franchises if an individual or entity (other than an automobile manufacturer or distributor) acquires more than 20% of the voting power of our securities, and the manufacturer disapproves of such individual's or entity's ownership interest.

To the extent that new or amended manufacturer policies restrict the number of dealerships which may be owned by a dealership group or the transferability of our common stock, such policies could have a material adverse effect on us. We believe that we will be able to renew at expiration all of our existing franchise and dealer agreements.

Many states have placed limitations upon manufacturers' and distributors' ability to sell new motor vehicles directly to customers in their respective states in an effort to protect dealers from practices they believe constitute unfair competition. In general, these statutes make it unlawful for a manufacturer or distributor to compete with a new motor vehicle dealer in the same brand operating under an agreement or franchise from the manufacturer or distributor in the relevant market area. Certain states, such as Florida, Georgia, Oklahoma, South Carolina, North Carolina and Virginia, limit the amount of time that a manufacturer may temporarily operate a dealership.

In addition, all of the states in which our dealerships currently do business require manufacturers to show good cause for terminating or failing to renew a dealer's franchise agreement. Further, each of the states provides some method for dealers to challenge manufacturer attempts to establish dealerships of the same brand in their relevant market area.

Competition

The retail automotive industry is highly competitive. Depending on the geographic market, we compete both with dealers offering the same brands and product lines as ours and dealers offering other manufacturers' vehicles. We also compete for vehicle sales with auto brokers, leasing companies and services offered on the internet that provide customer referrals to other dealerships or who broker vehicle sales between customers and other dealerships. We compete with small, local dealerships and with large multi-franchise auto dealerships.

We believe that the principal competitive factors in vehicle sales are the location of dealerships, the marketing campaigns conducted by manufacturers, the ability of dealerships to offer an attractive selection of the most popular vehicles, pricing (including manufacturer rebates and other special offers) and the quality of customer service. Other

competitive factors include customer preference for makes of automobiles and manufacturer warranties.

In addition to competition for vehicle sales, we also compete with other auto dealers, service stores, auto parts retailers and independent mechanics in providing parts and service. We believe that the principal competitive factors in parts and service sales are price, the use of factory-approved replacement parts, factory-trained

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technicians, the familiarity with a dealer's makes and models and the quality of customer service. A number of regional and national chains offer selected parts and services at prices that may be lower than our prices.

In arranging or providing financing for our customers' vehicle purchases, we compete with a broad range of financial institutions. In addition, financial institutions are now offering F&I products through the internet, which may reduce our profits on these items. We believe the principal competitive factors in providing financing are convenience, interest rates and contract terms.

Our success depends, in part, on national and regional automobile-buying trends, local and regional economic factors and other regional competitive pressures. Conditions and competitive pressures affecting the markets in which we operate, such as price-cutting by dealers in these areas, or in any new markets we enter, could adversely affect us, even though the retail automobile industry as a whole might not be affected.

Governmental Regulations and Environmental Matters

Numerous federal and state regulations govern our business of marketing, selling, financing and servicing automobiles. We are also subject to laws and regulations relating to business corporations.

Under the laws of the states in which we currently operate as well as the laws of other states into which we may expand, we must obtain a license in order to establish, operate or relocate a dealership or operate an automotive repair service. These laws also regulate our conduct of business, including our sales, operating, advertising, financing and employment practices, including federal and state wage-hour, anti-discrimination and other employment practices laws.

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

Federal, state and local environmental regulations, including regulations governing air and water quality, the clean-up of contaminated property and the use, storage, handling, recycling and disposal of gasoline, oil and other materials, also apply to us and our dealership properties.

We believe that we comply in all material respects with the laws affecting our business. However, claims arising out of actual or alleged violations of laws may be asserted against us or our dealerships by individuals or governmental entities, and may expose us to significant damages or other penalties, including possible suspension or revocation of our licenses to conduct dealership operations and fines.

As with automobile 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 or toxic substances or wastes and other environmentally sensitive materials. Our business also involves the past and current operation and/or removal of above ground and underground storage tanks containing such substances or wastes. Accordingly, we are subject to regulation by federal, state and local authorities that establish health and environmental quality standards, provide for liability related to those standards, and in certain circumstances provide penalties for violations of those standards. We are also subject to laws, ordinances and regulations governing remediation of contamination at facilities we own or operate or to which we send hazardous or toxic substances or wastes for treatment, recycling or disposal.

We do not have any known material environmental liabilities, and we believe that compliance with environmental laws and regulations will not, individually or in the aggregate, have a material adverse effect on our results of

operations, financial condition and cash flows. However, soil and groundwater contamination is known to exist at certain properties owned and used by us. Further, environmental laws and regulations are complex and subject to frequent 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. We cannot assure you that 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 will not require additional expenditures by us, or that such expenditures will not be material.

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Our executive officers as of the date of this Form 10-K, are as follows:

Name	Age	Position(s) with Sonic
O. Bruton Smith	84	Chairman, Chief Executive Officer and Director
B. Scott Smith	43	President, Chief Strategic Officer and Director
Jeff Dyke	43	Executive Vice President of Operations
David P. Cospers	56	Vice Chairman and Chief Financial Officer
David B. Smith	36	Executive Vice President and Director

O. Bruton Smith, 84, is our Founder, Chairman, Chief Executive Officer and a director and has served as such since our formation in January 1997, and he currently is a director and executive officer of many of our subsidiaries. Mr. Smith has worked in the retail automobile industry since 1966. Mr. Smith is also the Chairman and Chief Executive Officer, a director and controlling stockholder of Speedway Motorsports, Inc. (SMI). SMI is a public company traded on the New York Stock Exchange (the NYSE). Among other things, SMI owns and operates the following NASCAR racetracks: Atlanta Motor Speedway, Bristol Motor Speedway, Charlotte Motor Speedway, Infineon Raceway, Las Vegas Motor Speedway, New Hampshire Motor Speedway, Texas Motor Speedway, and Kentucky Speedway. He is also an executive officer or a director of most of SMI s operating subsidiaries.

B. Scott Smith, 43, is our Co-Founder, President, Chief Strategic Officer and a director. Prior to his appointment as President in March 2007, Mr. Smith served as our Vice Chairman and Chief Strategic Officer since October 2002. He held the position of President and Chief Operating Officer from April 1997 to October 2002. Mr. Smith has been a director of our company since our organization was formed in January 1997. Mr. Smith also serves as a director and executive officer of many of our subsidiaries. Mr. Smith, who is the son of O. Bruton Smith and brother of David B. Smith, has been an executive officer of Town & Country Ford since 1993, and was a minority owner of both Town & Country Ford and Fort Mill Ford before our acquisition of these dealerships in 1997. Mr. Smith became the General Manager of Town & Country Ford in November 1992 where he remained until his appointment as President and Chief Operating Officer in April 1997. Mr. Smith has over twenty years experience in the automobile dealership industry.

Jeff Dyke, 43, is our Executive Vice President of Operations and is responsible for direct oversight for all retail automotive operations of Sonic. From March 2007 to October 2008, Mr. Dyke served as our Division Chief Operating Officer South East Division, where he oversaw retail automotive operations for the states of Alabama, Georgia, Florida, North Carolina, Tennessee, Texas and South Carolina. Mr. Dyke first joined Sonic in October 2005 as its Vice President of Retail Strategy, a position that he held until April 2006, when he was promoted to Division Vice President Eastern Division, a position he held from April 2006 to March 2007. Prior to joining Sonic, Mr. Dyke worked in the automotive retail industry at AutoNation from 1996 to 2005, where he held several positions in divisional, regional and dealership management with that company.

David P. Cospers, 56, is our Vice Chairman and Chief Financial Officer. In March 2007, Mr. Cospers was appointed to Vice Chairman after serving as Executive Vice President since March 2006. He joined Sonic Automotive on March 1, 2006 as an Executive Vice President and became our Chief Financial Officer and Treasurer on March 16, 2006. Mr. Cospers served as Treasurer through the end of 2006 and relinquished the position in February 2007. Prior to joining Sonic, he was Vice Chairman and Chief Financial Officer of Ford Motor Credit Company, a position held since 2003. From 1979, when he joined Ford Motor Company, Mr. Cospers served in a variety of positions in Ford Motor Company and Ford Motor Credit Company, including Vice President and Treasurer of Ford Motor Credit Company and Executive Director of Corporate Finance at Ford Motor Company. In such positions, he was responsible

for worldwide profit analysis and treasury matters, risk management, business planning, and competitive and strategic analysis.

David B. Smith, 36, is our Executive Vice President and a director and has served our organization beginning in October 2000. Prior to being named a director and Executive Vice President of Sonic in October 2008, Mr. Smith, also a son of O. Bruton Smith and brother of B. Scott Smith, served as our Senior Vice President of Corporate Development since March 2007. Prior to that appointment, Mr. Smith served as our Vice President of Corporate Strategy from October 2005 to March 2007, and also served us prior to that time as Dealer Operator of one of our

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Arnold Palmer Cadillac dealerships from January 2004 to October 2005, our Fort Mill Ford dealership from January 2003 to January 2004, and our Town and Country Ford dealership from October 2000 to December 2002.

Employees

As of January 31, 2011, we employed approximately 9,200 associates. We believe that our relationships with our employees are good. Approximately 225 of our employees, primarily service technicians in our Northern California markets, are represented by a labor union. However, due to our dependence on automobile manufacturers, we may be affected by labor strikes, work slowdowns and walkouts at the manufacturers' manufacturing facilities.

Company Information

Our website is located at www.sonicautomotive.com. Our Annual Report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended (the Exchange Act), as well as proxy statements and other information we file with, or furnish to, the Securities and Exchange Commission (SEC) are available free of charge on our website. We make these documents available as soon as reasonably practicable after we electronically file them with, or furnish them to, the SEC. Except as otherwise stated in these documents, the information contained on our website or available by hyperlink from our website is not incorporated into this Annual Report on Form 10-K or other documents we file with, or furnish to, the SEC.

Item 1A: Risk Factors

Risks Related to Our Sources of Financing and Liquidity

Our significant indebtedness could materially adversely affect our financial health, limit our ability to finance future acquisitions and capital expenditures and prevent us from fulfilling our financial obligations.

As of December 31, 2010, our total outstanding indebtedness was approximately \$1.4 billion, including the following:

\$862.0 million under the secured new and used inventory floor plan facilities;

\$208.6 million in 9.0% Senior Subordinated Notes due 2018 (the 9.0% Notes), representing \$210.0 million in aggregate principal amount outstanding less unamortized discount of approximately \$1.4 million;

\$42.7 million in 8.625% Senior Subordinated Notes due 2013 (the 8.625% Notes), representing \$42.9 million in aggregate principal amount outstanding less unamortized net discount of approximately \$0.2 million;

\$147.8 million in 5.0% Convertible Senior Notes due 2029 which are redeemable by us and which may be put to us by the holders after October 1, 2014 under certain circumstances (the 5.0% Convertible Notes), representing \$172.5 million in aggregate principal amount outstanding less unamortized discount of approximately \$24.7 million;

\$132.9 million of mortgage notes, representing \$133.9 million in aggregate principal amount less unamortized net discount of approximately \$1.0 million, due from June 2013 to December 2029, with a weighted average interest rate of 4.91%; and

\$23.5 million of other secured debt, representing \$21.7 million in aggregate principal amount plus unamortized premium of approximately \$1.8 million.

We have \$150.0 million of maximum borrowing availability under a syndicated revolving credit facility (the 2010 Revolving Credit Facility), up to \$321.0 million in maximum borrowing availability for new vehicle inventory floor plan financing and up to \$50.0 million in maximum borrowing availability for used vehicle inventory floor plan financing (the 2010 Floor Plan Facilities). We refer to the 2010 Revolving Credit Facility and 2010 Floor Plan Facilities collectively as our 2010 Credit Facilities . As of December 31, 2010, we had \$97.9 million available for additional borrowings under the 2010 Revolving Credit Facility based on the borrowing

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base calculation, which is affected by numerous factors including eligible asset balances and the market value of certain additional collateral. We are able to borrow under our 2010 Revolving Credit Facility only if, at the time of the borrowing, we have met all representations and warranties and are in compliance with all financial and other covenants contained therein. We also have capacity to finance new and used vehicle inventory purchases under bilateral floor plan agreements with various manufacturer-affiliated finance companies and other lending institutions (the Silo Floor Plan Facilities) as well as our 2010 Floor Plan Facilities. In addition, the indentures relating to our 9.0% Notes, 8.625% Notes, 5.0% Convertible Notes and our other debt instruments allow us to incur additional indebtedness, including secured indebtedness, as long as we comply with the terms thereunder.

In addition, the majority of our dealership properties are leased under long-term operating lease arrangements that commonly have initial terms of fifteen to twenty years with renewal options ranging from five to ten years. These operating leases require compliance with financial and operating covenants similar to those under our 2010 Credit Facilities, and monthly payments of rent that may fluctuate based on interest rates and local consumer price indices. The total future minimum lease payments related to these operating leases and certain equipment leases are significant and are disclosed in the Notes to the accompanying Consolidated Financial Statements under the heading

Commitments and Contingencies in this Annual Report on Form 10-K.

An acceleration of our obligation to repay all or a substantial portion of our outstanding indebtedness or lease obligations would have a material adverse effect on our business, financial condition or results of operations.

Our 2010 Credit Facilities, the indentures governing our 9.0% Notes, 8.625% Notes and many of our facility operating leases contain numerous financial and operating covenants. A breach of any of these covenants could result in a default under the applicable agreement or indenture. If a default were to occur, we may be unable to adequately finance our operations and the value of our common stock would be materially adversely affected because of acceleration and cross default provisions. In addition, a default under one agreement or indenture could result in a default and acceleration of our repayment obligations under the other agreements or indentures, including the indentures governing our outstanding 9.0% Notes, 8.625% Notes, and 5.0% Convertible Notes under the cross default provisions in those agreements or indentures. If a cross default were to occur, we may not be able to pay our debts or borrow sufficient funds to refinance them. Even if new financing were available, it may not be on terms acceptable to us. As a result of this risk, we could be forced to take actions that we otherwise would not take, or not take actions that we otherwise might take, in order to comply with the covenants in these agreements and indentures.

Our ability to make interest and principal payments when due to holders of our debt securities depends upon our future performance.

Our ability to meet our debt obligations and other expenses will depend on our future performance, which will be affected by financial, business, domestic and foreign economic conditions, the regulatory environment and other factors, many of which we are unable to control. If our cash flow is not sufficient to service our debt as it becomes due, we may be required to refinance the debt, sell assets or sell shares of our common stock on terms that we do not find attractive. Further, our failure to comply with the financial and other restrictive covenants relating to the 2010 Credit Facilities and the indentures pertaining to our outstanding notes could result in a default under these agreements that would prevent us from borrowing under the 2010 Revolving Credit Facility, which could adversely affect our business, financial condition and results of operations.

Our ability to make interest and principal payments when due to holders of our debt securities depends upon the receipt of sufficient funds from our subsidiaries.

Substantially all of our consolidated assets are held by our subsidiaries and substantially all of our consolidated cash flow and net income are generated by our subsidiaries. Accordingly, our cash flow and ability to service debt depends

to a substantial degree on the results of operations of our subsidiaries and upon the ability of our subsidiaries to provide us with cash. We may receive cash from our subsidiaries in the form of dividends, loans or distributions. We may use this cash to service our debt obligations or for working capital. Our subsidiaries are separate and distinct legal entities and have no obligation, contingent or otherwise, to distribute cash to us or to make funds available to service debt. In addition, the ability of our subsidiaries to pay dividends or make loans to us

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is subject to minimum net capital requirements under manufacturer franchise agreements and laws of the state in which a subsidiary is organized and depends to a significant degree on the results of operations of our subsidiaries and other business considerations.

The conversion of the 5.0% Convertible Notes, if triggered, may adversely affect our liquidity and financial condition and results of operations.

If the conversion features of the 5.0% Convertible Notes are triggered, holders of those notes will be entitled to convert their notes in accordance with the terms of the indenture governing those notes. We may be required to make cash payments to satisfy our conversion obligations. In the event we have the ability to, and choose to, settle the 5.0% Convertible Notes with cash payments in lieu of settlement with shares of common stock, the amount of these cash payments could have a material adverse effect on our liquidity. In addition, even if the holders of the 5.0% Convertible Notes do not elect to convert their respective notes, we could be required under applicable accounting rules to reclassify all or a portion of the outstanding principal of the notes as a current rather than long-term liability, which could result in a material reduction of our net working capital or could have a material adverse effect on our financial condition and results of operations.

We depend on the performance of sublessees to offset costs related to certain of our lease agreements.

In most cases when we sell a dealership franchise, the buyer of the franchise will sublease the dealership property from us, but we are not released from the underlying lease obligation to the primary landlord. We rely on the sublease income from the buyer to offset the expense incurred related to our obligation to pay the primary landlord. We also rely on the buyer to maintain the property in accordance with the terms of the sublease (which in most cases mirror the terms of the lease we have with the primary landlord). Although we assess the financial condition of a buyer at the time we sell the franchise, and seek to obtain guarantees of the buyer's sublease obligation from the stockholders or affiliates of the buyer, the financial condition of the buyer and/or the sublease guarantors may deteriorate over time. In the event the buyer does not perform under the terms of the sublease agreement (due to the buyer's financial condition or other factors), we may not be able to recover amounts owed to us under the terms of the sublease agreement or the related guarantees. Our operating results, financial condition and cash flows may be materially adversely affected if sublessees do not perform their obligations under the terms of the sublease agreements.

Our use of hedging transactions could limit our gains and result in financial losses.

To reduce our exposure to fluctuations in cash flow due to interest rate fluctuations, we have entered into, and in the future expect to enter into, derivative instruments (or hedging agreements). No hedging activity can completely insulate us from the risks associated with changes in interest rates. As of December 31, 2010, we had interest rate swap agreements to effectively convert a portion of our LIBOR-based variable rate debt to a fixed rate. See *Derivative Instruments and Hedging Activities* under Note 6, Long-Term Debt, to our accompanying Consolidated Financial Statements. We intend to hedge as much of the interest rate risk as management determines is in our best interests given the cost of such hedging transactions.

Our hedging transactions expose us to certain risks and financial losses, including, among other things:

counterparty credit risk;

available interest rate hedging may not correspond directly with the interest rate risk for which we seek protection;

the duration of the amount of the hedge may not match the duration or amount of the related liability;

the value of derivatives used for hedging may be adjusted from time to time in accordance with accounting rules to reflect changes in fair-value. Downward adjustments, or mark-to-market losses, would reduce our stockholders equity; and

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all of our hedging instruments contain terms and conditions with which we are required to meet. In the event those terms and conditions are not met, we may be required to settle the instruments prior to the instruments maturity with cash payments which could significantly affect our liquidity.

A failure on our part to effectively hedge against interest rate changes may adversely affect our financial condition and results of operations.

We may not be able to satisfy our debt obligations upon the occurrence of a change in control or a fundamental change.

Upon the occurrence of a change in control or a fundamental change, as defined in our 9.0% Notes, 8.625% Notes and 5.0% Convertible Notes, holders of these instruments will have the right to require us to purchase all or any part of such holders' notes at a price equal to either 101% (in the case of the 9.0% Notes and 8.625% Notes) or 100% (in the case of the 5.0% Convertible Notes) of principal amount thereof, plus accrued and unpaid interest, if any. The events that constitute a change of control under these indentures may also constitute a default under our 2010 Credit Facility. There can be no assurance that we would have sufficient resources available to satisfy all of our obligations under these debt instruments in the event of a change in control or fundamental change. In the event we were unable to satisfy our obligations under the change in control or fundamental change control provisions, it could have an adverse material impact on us and our Class A and Class B common stock holders. Any future debt instruments that we may incur may contain similar provisions regarding repurchases in the event of a change in control or fundamental change triggering event.

Although O. Bruton Smith, our chairman and chief executive officer, and his affiliates have previously assisted us with obtaining financing, we cannot assure you that he or they will be willing or able to do so in the future.

Our obligations under the 2010 Credit Facilities are secured with a pledge of 5,000,000 shares of Speedway Motorsports, Inc. Common Stock, a publicly traded owner and operator of automobile racing facilities. These shares of Speedway Motorsports, Inc. Common Stock are owned by Sonic Financial Corporation (SFC), an entity controlled by Mr. Smith. Presently, the \$150.0 million borrowing limit of our 2010 Revolving Credit Facility is subject to a borrowing base calculation that is based, in part, on the value of the Speedway Motorsports shares pledged by SFC. Consequently, a withdrawal of this pledge by SFC or a significant decrease in the value of Speedway Motorsports common stock could reduce the amount we can borrow under the 2010 Revolving Credit Facility.

Risks Related to Our Relationships with Vehicle Manufacturers

Our operations may be adversely affected if one or more of our manufacturer franchise agreements is terminated or not renewed.

Each of our dealerships operates under a franchise agreement with the applicable automobile manufacturer or distributor. Without a franchise agreement, we cannot obtain new vehicles from a manufacturer or advertise as an authorized factory service center. As a result, we are significantly dependent on our relationships with the manufacturers.

Manufacturers exercise a great degree of control over the operations of our dealerships through the franchise agreements. The franchise agreements govern, among other things, our ability to purchase vehicles from the manufacturer and to sell vehicles to customers. Each of our franchise agreements provides for termination or non-renewal for a variety of causes, including certain changes in the financial condition of the dealerships and any unapproved change of ownership or management. Manufacturers may also have a right of first refusal if we seek to

sell dealerships.

Actions taken by manufacturers to exploit their superior bargaining position in negotiating the terms of franchise agreements or renewals of these agreements or otherwise could also have a material adverse effect on our results of operations, financial condition and cash flows. We cannot guarantee that any of our existing franchise agreements will be renewed or that the terms and conditions of such renewals will be favorable to us.

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Our failure to meet a manufacturer's customer satisfaction, financial and sales performance and facility requirements may adversely affect our profitability and our ability to acquire new dealerships.

Many manufacturers attempt to measure customers' satisfaction with their sales and warranty service experiences through manufacturer-determined CSI scores. The components of CSI vary from manufacturer to manufacturer and are modified periodically. Franchise agreements also may impose financial and sales performance standards. Under our agreements with certain manufacturers, a dealership's CSI scores, sales and financial performance may be considered a factor in evaluating applications for additional dealership acquisitions. From time to time, some of our dealerships have had difficulty meeting various manufacturers' CSI requirements or performance standards. We cannot assure you that our dealerships will be able to comply with these requirements in the future. A manufacturer may refuse to consent to an acquisition of one of its franchises if it determines our dealerships do not comply with its CSI requirements or performance standards, which could impair the execution of our acquisition strategy. In addition, we receive incentive payments from the manufacturers based, in part, on CSI scores, which could be materially adversely affected if our CSI scores decline.

In addition, a manufacturer may condition its allotment of vehicles, participation in bonus programs, or acquisition of additional franchises upon our compliance with its facility standards. This may put us in a competitive disadvantage with other competing dealerships and may ultimately result in our decision to sell a franchise when we believe it may be difficult to recover the cost of the required investment to reach the manufacturer's facility standards.

If state dealer laws are repealed or weakened, our 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 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, these laws restrict the ability of automobile manufacturers to directly enter the retail market in the future. However, the ability of a manufacturer to grant additional franchises is based on several factors which are not within our control. If manufacturers grant new franchises in areas near or within our existing markets, this could significantly impact our revenues and/or profitability. Further, if manufacturers obtain the ability to directly retail vehicles and do so in our markets, such competition could have a material adverse effect on us.

Our sales volume and profit margin on each sale may be materially adversely affected if manufacturers discontinue or change their incentive programs.

Our dealerships depend on the manufacturers for certain sales incentives, warranties and other programs that are intended to promote and support dealership new vehicle sales. Manufacturers routinely modify their incentive programs in response to changing market conditions. Some of the key incentive programs include:

customer rebates or below market financing on new and used vehicles;

employee pricing;

dealer incentives on new vehicles;

manufacturer floor plan interest and advertising assistance;

warranties on new and used vehicles; and

sponsorship of used vehicle sales by authorized new vehicle dealers.

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Manufacturers frequently offer incentives to potential customers. A reduction or discontinuation of a manufacturer's incentive programs may materially adversely impact vehicle demand and affect our profitability.

Our sales volume may be materially adversely affected if manufacturer captives change their customer financing programs or are unable to provide floor plan financing.

One of the primary finance sources used by consumers in connection with the purchase of a new or used vehicle is the manufacturer captive finance companies. These captive finance companies rely, to a certain extent, on the public debt markets to provide the capital necessary to support their financing programs. In addition, the captive finance companies will occasionally change their loan underwriting criteria to alter the risk profile of their loan portfolio. A limitation or reduction of available consumer financing for these or other reasons could affect consumers' ability to purchase a vehicle, and thus, could have a material adverse effect on our sales volume.

Our parts and service sales volume and profitability are dependent on manufacturer warranty programs.

Franchised automotive retailers perform factory authorized service work and sell original replacement parts on vehicles covered by warranties issued by the automotive manufacturer. Dealerships which perform work covered by a manufacturer warranty are reimbursed at rates established by the manufacturer. For the year ended December 31, 2010, approximately 17.4% of our parts and service revenue was for work covered by manufacturer warranties. To the extent a manufacturer reduces the labor rates or markup of replacement parts for such warranty work, our fixed operations sales volume and profitability could be adversely affected.

Adverse conditions affecting one or more key manufacturers may negatively impact our profitability.

During the year ended December 31, 2010, approximately 82.7% of our new vehicle revenue was derived from the sale of new vehicles manufactured by BMW, Honda (including Acura), Toyota (including Lexus), Mercedes, General Motors (including Cadillac) and Ford. Our success depends to a great extent on these manufacturers' :

financial condition;

marketing;

vehicle design;

publicity concerning a particular manufacturer or vehicle model;

production capabilities;

management;

reputation; and

labor relations.

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 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 limit sales of those vehicles during those periods. This

has been experienced at some of our dealerships from time to time. Adverse conditions affecting these and other important aspects of manufacturers' operations and public relations may adversely affect our ability to sell their automobiles and, as a result, significantly and detrimentally affect our profitability.

Manufacturer stock ownership restrictions may impair our ability to maintain or renew franchise agreements or issue additional equity.

Some of our franchise agreements prohibit transfers of any ownership interests of a dealership and, in some cases, its parent, without prior approval of the applicable manufacturer. A number of manufacturers impose restrictions on the transferability of our Class A common stock and our ability to maintain franchises if a person acquires a significant percentage of the voting power of our common stock. Our existing franchise agreements could

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be terminated if a person or entity acquires a substantial ownership interest in us or acquires voting power above certain levels without the applicable manufacturer's approval. Violations of these levels by an investor are generally outside of our control and may result in the termination or non-renewal of existing franchise agreements or impair our ability to negotiate new franchise agreements for dealerships we acquire in the future. In addition, if we cannot obtain any requisite approvals on a timely basis, we may not be able to issue additional equity or otherwise raise capital on terms acceptable to us. These restrictions may also prevent or deter a prospective acquirer from acquiring control of us.

The current holders of our Class B common stock maintain voting control over us. However, we are unable to prevent our stockholders from transferring shares of our common stock, including transfers by holders of the Class B common stock. If such transfer results in a change in control, it could result in the termination or non-renewal of one or more of our existing franchise agreements, the triggering of provisions in our agreements with certain manufacturers requiring us to sell our dealerships franchised with such manufacturers and/or a default under our credit arrangements.

We depend on manufacturers to supply us with sufficient numbers of popular and profitable new models.

Manufacturers typically allocate their vehicles among dealerships based on the sales history of each dealership. Supplies of popular new vehicles may be limited by the applicable manufacturer's production capabilities. Popular new vehicles that are in limited supply typically produce the highest profit margins. We depend on manufacturers to provide us with a desirable mix of popular new vehicles. Our operating results may be materially adversely affected if we do not obtain a sufficient supply of these vehicles.

A decline in the quality of vehicles we sell, or consumers' perception of the quality of those vehicles may adversely affect our business.

Our business is highly dependent on consumer demand and preferences. Events such as manufacturer recalls, negative publicity or legal proceedings related to these events may have a negative impact on the products we sell. If such events are significant, the profitability of our franchises related to those manufacturers could be adversely affected and we could experience a material adverse affect on our overall results of operations, financial position and cash flows.

Risks Related to Our Growth Strategy

Pursuant to the terms of the 2010 Credit Facilities, our ability to make acquisitions is restricted.

Pursuant to the 2010 Credit Facilities, we are restricted from making dealership franchise acquisitions in any fiscal year if the aggregate cost of all such acquisitions occurring in any fiscal year is in excess of \$25.0 million, without the written consent of the Required Lenders (as that term is defined in the 2010 Credit Facilities). With this restriction on our ability to make acquisitions, our growth strategy may be limited. In addition, we may have to forfeit the opportunity to acquire profitable dealerships at attractive valuations.

We may not be able to capitalize on real estate and dealership franchise acquisition opportunities because our ability to obtain capital to fund these acquisitions is limited.

We intend to finance our real estate and dealership franchise acquisitions with cash generated from operations, through issuances of our stock or debt securities and through borrowings under credit arrangements. We may not be able to obtain additional financing by issuing stock or debt securities due to the market price of our Class A common stock, overall market conditions, and covenants under our 2010 Credit Facilities which restrict our ability to issue additional indebtedness, or the need for manufacturer consent to the issuance of equity securities. Using cash to complete acquisitions could substantially limit our operating or financial flexibility.

In addition, we are dependent to a significant extent on our ability to finance our new vehicle inventory with floor plan financing. Floor plan financing arrangements allow us to borrow money to buy a particular vehicle from the manufacturer and pay off the loan when we sell that particular vehicle. We must obtain new floor plan financing or obtain consents to assume existing floor plan financing in connection with our acquisition of dealerships.

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Substantially all the assets of our dealerships are pledged to secure the indebtedness under our Silo Floor Plan Facilities and the 2010 Credit Facilities. These pledges may impede our ability to borrow from other sources. Moreover, because the identified manufacturer-affiliated finance subsidiaries are either owned or affiliated with BMW, Mercedes, Ford and Toyota, respectively, any deterioration of our relationship with the particular manufacturer-affiliated finance subsidiary could adversely affect our relationship with the affiliated manufacturer, and vice-versa.

Manufacturers' restrictions on acquisitions could limit our future growth.

We are required to obtain the approval of the applicable manufacturer before we can acquire an additional dealership franchise of that manufacturer. In determining whether to approve an acquisition, manufacturers may consider many factors such as our financial condition and CSI scores. Obtaining manufacturer approval of acquisitions also takes a significant amount of time, typically three to five months. We cannot assure you that manufacturers will approve future acquisitions or do so on a timely basis, which could impair the execution of our acquisition strategy.

Certain manufacturers also limit the number of its dealerships that we may own, our national market share of that manufacturer's products or the number of dealerships we may own in a particular geographic area. In addition, under an applicable franchise agreement or under state law, a manufacturer may have a right of first refusal to acquire a dealership that we seek to acquire.

A manufacturer may condition approval of an acquisition on the implementation of material changes in our operations or extraordinary corporate transactions, facilities improvements or other capital expenditures. If we are unable or unwilling to comply with these conditions, we may be required to sell the assets of that manufacturer's dealerships or terminate our franchise agreement.

Failure to effectively integrate acquired dealerships with our existing operations could adversely affect our future operating results.

Our future operating results depend on our ability to integrate the operations of acquired dealerships with our existing operations. In particular, we need to integrate our management information systems, procedures and organizational structures, which can be difficult. Our growth strategy has focused on the pursuit of strategic acquisitions that either expand or complement our business.

We cannot assure you that we will effectively and profitably integrate the operations of these dealerships without substantial costs, delays or operational or financial problems, due to:

- the difficulties of managing operations located in geographic areas where we have not previously operated;
- the management time and attention required to integrate and manage newly acquired dealerships;
- the difficulties of assimilating and retaining employees;
- the challenges of keeping customers; and
- the challenge of retaining or attracting appropriate dealership management personnel.

These factors could have a material adverse effect on our financial condition and results of operations.

We may not adequately anticipate all of the demands that growth through acquisitions will impose.

In pursuing a strategy of acquiring other dealerships, we face risks commonly encountered with growth through acquisitions. These risks include, but are not limited to:

incurring significantly higher capital expenditures and operating expenses;

failing to assimilate the operations and personnel of acquired dealerships;

entering new markets with which we are unfamiliar;

potential undiscovered liabilities and operational difficulties at acquired dealerships;

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disrupting our ongoing business;

diverting our management resources;

failing to maintain uniform standards, controls and policies;

impairing relationships with employees, manufacturers and customers as a result of changes in management;

increased expenses for accounting and computer systems, as well as integration difficulties;

failure to obtain a manufacturer's consent to the acquisition of one or more of its dealership franchises or renew the franchise agreement on terms acceptable to us; and

incorrectly valuing entities to be acquired.

We may not adequately anticipate all of the demands that growth will impose on our systems, procedures and structures.

We may not be able to reinstitute our acquisition strategy without the costs of future acquisitions escalating.

We have grown our business primarily through acquisitions. We may not be able to consummate any future acquisitions at acceptable prices and terms or identify suitable candidates. In addition, increased competition for acquisition candidates could result in fewer acquisition opportunities for us and higher acquisition prices. The magnitude, timing, pricing and nature of future acquisitions will depend upon various factors, including:

the availability of suitable acquisition candidates;

competition with other dealer groups for suitable acquisitions;

the negotiation of acceptable terms with the seller and with the manufacturer;

our financial capabilities and ability to obtain financing on acceptable terms;

our stock price; and

the availability of skilled employees to manage the acquired companies.

We may not be able to determine the actual financial condition of dealerships we acquire until after we complete the acquisition and take control of the dealerships.

The operating and financial condition of acquired businesses cannot be determined accurately until we assume control. Although we conduct what we believe to be a prudent level of investigation regarding the operating and financial condition of the businesses we purchase, in light of the circumstances of each transaction, an unavoidable level of risk remains regarding the actual operating condition of these businesses. Similarly, many of the dealerships we acquire, including some of our largest acquisitions, do not have financial statements audited or prepared in accordance with generally accepted accounting principles. We may not have an accurate understanding of the historical financial condition and performance of our acquired entities. Until we actually assume control of business assets and their operations, we may not be able to ascertain the actual value or understand the potential liabilities of

the acquired entities and their operations.

Risks Related to the Automotive Retail Industry

Increasing competition among automotive retailers reduces our profit margins on vehicle sales and related businesses. Further, the use of the internet in the vehicle purchasing process could materially adversely affect us.

Automobile retailing is a highly competitive business. Our competitors include publicly and privately owned dealerships, some of which are larger and have greater financial and marketing resources than we do. Many of our competitors sell the same or similar makes of new and used vehicles that we offer in our markets at competitive prices. We do not have any cost advantage in purchasing new vehicles from manufacturers due to economies of

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scale or otherwise. We typically rely on advertising, merchandising, sales expertise, service reputation and dealership location to sell new vehicles. Our revenues and profitability could be materially adversely affected if manufacturers decide to enter the retail market directly.

Our F&I business and other related businesses, which have higher margins than sales of new and used vehicles, are subject to strong competition from various financial institutions and other third parties.

The internet has become a significant part of the sales process in our industry. Customers are using the internet to compare pricing for vehicles and related F&I services, which may further reduce margins for new and used vehicles and profits for related F&I services. If internet new vehicle sales are allowed to be conducted without the involvement of franchised dealers, our business could be materially adversely affected. In addition, other franchise groups have aligned themselves with services offered on the internet or are investing heavily in the development of their own internet capabilities, which could materially adversely affect our business.

Our franchise agreements do not grant us the exclusive right to sell a manufacturer's product within a given geographic area. Our revenues or profitability could be materially adversely affected if any of our manufacturers award franchises to others in the same markets where we operate or if existing franchised dealers increase their market share in our markets.

We may face increasingly significant competition as we strive to gain market share through acquisitions or otherwise. Our operating margins may decline over time as we expand into markets where we do not have a leading position.

Our dealers depend upon new vehicle sales and, therefore, their success depends in large part upon customer demand for the particular vehicles they carry.

The success of our dealerships depends in large part on the overall success of the vehicle lines they carry. New vehicle sales generate the majority of our total revenue and lead to sales of higher-margin products and services such as finance, insurance, vehicle protection products and other aftermarket products, and parts and service operations. Although we have sought to limit our dependence on any one vehicle brand, and our parts and service operations and used vehicle sales may serve to offset some of this risk, we have focused our new vehicle sales operations in mid-line import and luxury brands.

Our business will be harmed if overall consumer demand suffers from a severe or sustained downturn.

Our business is heavily dependent on consumer demand and preferences. Retail vehicle sales are cyclical and historically have experienced periodic downturns characterized by oversupply and weak demand. These cycles are often dependent on economic conditions, consumer confidence, the level of discretionary personal income and credit availability. Deterioration in any of these conditions may have a material adverse effect on our retail business, particularly sales of new and used automobiles.

In addition, severe or sustained increases in gasoline prices may lead to a reduction in automobile purchases or a shift in buying patterns from luxury and sport utility vehicle models (which typically provide high margins to retailers) to smaller, more economical vehicles (which typically have lower margins).

A decline of available financing in the lending market may adversely affect our vehicle sales volume.

A significant portion of vehicle buyers, particularly in the used car market, finance their purchases of automobiles. Sub-prime lenders have historically provided financing for consumers who, for a variety of reasons including poor credit histories and lack of down payment, do not have access to more traditional finance sources. In the event lenders

further tighten their credit standards or there is a further decline in the availability of credit in the lending market, the ability of these consumers to purchase vehicles could be limited which could have a material adverse effect on our business, revenues and profitability.

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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, parts or vehicles composed of parts that are manufactured outside the United States. As a result, our operations are subject to customary risks of importing merchandise, including fluctuations in the relative values of currencies, import duties, exchange controls, trade restrictions, work stoppages and general political and socio-economic conditions in other 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, which may affect our operations and our ability to purchase imported vehicles and/or parts at reasonable prices.

Natural disasters and adverse weather events can disrupt our business.

Our stores are concentrated in states and regions in the United States, including primarily Florida, Texas, and California, in which actual or threatened natural disasters and severe weather events (such as hurricanes, earthquakes, fires, landslides, and hail storms) may disrupt our store operations, which may adversely impact our business, results of operations, financial condition, and cash flows. In addition to business interruption, the automotive retailing business is subject to substantial risk of property loss due to the significant concentration of property values at store locations. Although we have, subject to certain deductibles, limitations, and exclusions, substantial insurance, we cannot assure you that we will not be exposed to uninsured or underinsured losses that could have a material adverse effect on our business, financial condition, results of operations, or cash flows.

The seasonality of our business may adversely affect our operating results.

Our business is subject to seasonal variations in revenues. In our experience, demand for automobiles is lowest during the first quarter of each year. We therefore receive a disproportionate amount of revenues in the second, third and fourth quarters and expect our revenues and operating results to be lower in the first quarter. Consequently, if conditions surface during the second, third and fourth quarters that impair vehicle sales, such as higher fuel costs, depressed economic conditions or similar adverse conditions, our revenues for the year could be adversely affected.

General Risks Related to Investing in Our Securities

Concentration of voting power and anti-takeover provisions of our charter, bylaws, Delaware law and our dealer agreements may reduce the likelihood of any potential change of control.

Our common stock is divided into two classes with different voting rights. This dual class stock ownership allows the present holders of the Class B common stock to control us. Holders of Class A common stock have one vote per share on all matters. Holders of Class B common stock have 10 votes per share on all matters, except that they have only one vote per share on any transaction proposed or approved by the Board of Directors or a Class B common stockholder or otherwise benefiting the Class B common stockholders constituting a:

going private transaction;

disposition of substantially all of our assets;

transfer resulting in a change in the nature of our business; or

merger or consolidation in which current holders of common stock would own less than 50% of the common stock following such transaction.

The holders of Class B common stock currently hold less than a majority of our outstanding common stock, but a majority of our voting power (which include O. Bruton Smith, Sonic's Chairman, Chief Executive Officer and Director, his family members and entities they control). This may prevent or discourage a change of control of us even if the action was favored by holders of Class A common stock.

Our charter and bylaws make it more difficult for our stockholders to take corporate actions at stockholders' meetings. In addition, stock options, restricted stock and restricted stock units granted under our 1997 Stock Option Plan and 2004 Stock Incentive Plan become immediately exercisable or automatically vest upon a change in

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control. Delaware law also makes it difficult for stockholders who have recently acquired a large interest in a company to consummate a business combination transaction with the company against its directors' wishes. Finally, restrictions imposed by our dealer agreements may impede or prevent any potential takeover bid. Our franchise agreements allow the manufacturers the right to terminate the agreements upon a change of control of our company and impose restrictions upon the transferability of any significant percentage of our stock to any one person or entity who may be unqualified, as defined by the manufacturer, to own one of its dealerships. The inability of a person or entity to qualify with one or more of our manufacturers may prevent or seriously impede a potential takeover bid. In addition, provisions of our lending arrangements create an event of default on a change in control. These agreements, corporate governance documents and laws may have the effect of delaying or preventing a change in control or preventing stockholders from realizing a premium on the sale of their shares if we were acquired.

The outcome of legal and administrative proceedings we are or may become involved in could have a material adverse effect on our future business, results of operations, financial condition and cash flows.

We are involved, and expect to continue to be involved, in numerous legal and administrative proceedings arising out of the conduct of our business, including regulatory investigations and private civil actions brought by plaintiffs purporting to represent a potential class or for which a class has been certified. Although we vigorously defend ourselves in all legal and administrative proceedings, the outcomes of pending and future proceedings arising out of the conduct of our business, including litigation with customers, employment related lawsuits, contractual disputes, class actions, purported class actions and actions brought by governmental authorities, cannot be predicted with certainty. An unfavorable resolution of one or more of these matters could have a material adverse effect on our business, financial condition, results of operations, cash flows or prospects.

We are a defendant in the matter of Galura, et al. v. Sonic Automotive, Inc., a private civil action filed in the Circuit Court of Hillsborough County, Florida. In this action, originally filed on December 30, 2002, the plaintiffs allege that we and our Florida dealerships sold an antitheft protection product in a deceptive or otherwise illegal manner, and further sought representation on behalf of any customer of any of our Florida dealerships who purchased the antitheft protection product since December 30, 1998. The plaintiffs are seeking monetary damages and injunctive relief on behalf of this class of customers. In June 2005, the court granted the plaintiffs' motion for certification of the requested class of customers, but the court has made no finding to date regarding actual liability in this lawsuit. We subsequently filed a notice of appeal of the court's class certification ruling with the Florida Court of Appeals. In April 2007, the Florida Court of Appeals affirmed a portion of the trial court's class certification, and overruled a portion of the trial court's class certification. The Florida trial court granted Summary Judgment in our favor against Plaintiff Enrique Galura, and his claim has been dismissed. Virginia Galura's claim is still pending. We currently intend to continue our vigorous appeal and defense of this lawsuit and to assert available defenses. However, an adverse resolution of this lawsuit could result in the payment of significant costs and damages, which could have a material adverse effect on our future results of operations, financial condition and cash flows. At a mediation held February 4, 2011, our company reached an agreement in principle with the plaintiffs to settle this class action lawsuit. This agreement in principle remains conditioned upon execution of a definitive settlement agreement and subsequent approval by the Florida state court. In the event that a definitive settlement of this lawsuit is finalized upon terms and conditions consistent with the agreement in principle, such a settlement would not have a material adverse effect on our future results of operations, financial condition and cash flows.

Several private civil actions have been filed against Sonic Automotive, Inc. and several of our dealership subsidiaries that purport to represent classes of customers as potential plaintiffs and made allegations that certain products sold in the finance and insurance departments were done so in a deceptive or otherwise illegal manner. One of these private civil actions was filed on November 15, 2004 in South Carolina state court, York County Court of Common Pleas, against Sonic Automotive, Inc. and 10 of our South Carolina subsidiaries. The plaintiffs in that lawsuit were Misty J. Owens, James B. Wright, Vincent J. Astey and Joseph Lee Williams, on behalf of themselves and all other persons

similarly situated, with plaintiffs seeking monetary damages and injunctive relief on behalf of the purported class. The group of plaintiffs attorneys representing the plaintiffs in the South Carolina lawsuit also filed another private civil class action lawsuit against Sonic Automotive, Inc. and 3 of our subsidiaries on February 14, 2005 in state court in North Carolina, Lincoln County Superior Court, which similarly sought

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certification of a multi-state class of plaintiffs and alleged that certain products sold in the finance and insurance departments were done so in a deceptive or otherwise illegal manner. The plaintiffs in this North Carolina lawsuit were Robert Price, Carolyn Price, Marcus Cappeletti and Kathy Cappeletti, on behalf of themselves and all other persons similarly situated, with plaintiffs seeking monetary damages and injunctive relief on behalf of the purported class. The South Carolina state court action and the North Carolina state court action have since been consolidated into a single proceeding in private arbitration before the American Arbitration Association. On November 12, 2008, claimants in the consolidated arbitration filed a Motion for Class Certification as a national class action including all of the states in which we operate dealerships. Claimants are seeking monetary damages and injunctive relief on behalf of this class of customers. The parties have briefed and argued the issue of class certification.

On July 19, 2010, the Arbitrator issued a Partial Final Award on Class Certification, certifying a class which includes all customers who, on or after November 15, 2000, purchased or leased from a Sonic dealership a vehicle with the Etch product as part of the transaction, but not including customers who purchased or leased such vehicles from a Sonic dealership in Florida. The Partial Final Award on Class Certification is not a final decision on the merits of the action. The merits of Claimants' assertions and potential damages will still have to be proven through the remainder of the arbitration. The Arbitrator stayed the Arbitration for thirty days to allow either party to petition a court of competent jurisdiction to confirm or vacate the award. Sonic will seek review of the class certification ruling by a court of competent jurisdiction and will continue to press its argument that this action is not suitable for a class-based arbitration. On July 22, 2010, the plaintiffs in this consolidated arbitration filed a Motion to Confirm the Arbitrator's Partial Final Award on Class Certification in state court in North Carolina, Lincoln County Superior Court. On August 17, 2010, Sonic filed to remove this North Carolina state court action to federal court, and simultaneously filed a Petition to Vacate the Arbitrator's Partial Final Award on Class Certification, with both filings made in the United States District Court for the Western District of North Carolina.

We intend to continue our vigorous defense of this arbitration and to assert all available defenses. However, an adverse resolution of this arbitration could result in the payment of significant costs and damages, which could have a material adverse effect on our future results of operations, financial condition and cash flows. Currently, we are unable to estimate a range of potential loss related to this matter.

Our business may be adversely affected by claims alleging violations of laws and regulations in our advertising, sales and finance and insurance activities.

Our business is highly regulated. In the past several years, private plaintiffs and state attorney generals have increased their scrutiny of advertising, sales, and finance and insurance activities in the sale and leasing of motor vehicles. The conduct of our business is subject to numerous federal, state and local laws and regulations regarding unfair, deceptive and/or fraudulent trade practices (including advertising, marketing, sales, insurance, repair and promotion practices), truth-in-lending, consumer leasing, fair credit practices, equal credit opportunity, privacy, insurance, motor vehicle finance, installment finance, closed-end credit, usury and other installment sales. Claims arising out of actual or alleged violations of law may be asserted against us or any of our dealers by individuals, either individually or through class actions, or by governmental entities in civil or criminal investigations and proceedings. Such actions may expose us to substantial monetary damages and legal defense costs, injunctive relief and criminal and civil fines and penalties, including suspension or revocation of our licenses and franchises to conduct dealership operations.

Our business may be adversely affected by unfavorable conditions in our local markets, even if those conditions are not prominent nationally.

Our performance is subject to local economic, competitive, weather and other conditions prevailing in geographic areas where we operate. We may not be able to expand geographically and any geographic expansion may not adequately insulate us from the adverse effects of local or regional economic conditions. In addition, due to the

provisions and terms contained in our operating lease agreements, we may not be able to relocate a dealership operation to a more favorable location without incurring significant costs or penalties.

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The loss of key personnel and limited management and personnel resources could adversely affect our operations and growth.

Our success depends to a significant degree upon the continued contributions of our management team, particularly our senior management, and service and sales personnel. Additionally, manufacturer franchise agreements may require the prior approval of the applicable manufacturer before any change is made in franchise general managers. We do not have employment agreements with certain members of our senior management team, our dealership managers and other key dealership personnel. Consequently, the loss of the services of one or more of these key employees could have a material adverse effect on our results of operations.

In addition, as we expand we may need to hire additional managers. The market for qualified employees in the industry and in the regions in which we operate, particularly for general managers and sales and service personnel, is highly competitive and may subject us to increased labor costs during periods of low unemployment. The loss of the services of key employees or the inability to attract additional qualified managers could have a material adverse effect on our results of operations. In addition, the lack of qualified management or employees employed by potential acquisition candidates may limit our ability to consummate future acquisitions.

Governmental regulation and environmental regulation compliance costs may adversely affect our profitability.

We are subject to a wide range of federal, state and local laws and regulations, such as local licensing requirements, retail financing and consumer protection laws and regulations, and wage-hour, anti-discrimination and other employment practices laws and regulations. Our facilities and operations are also subject to federal, state and local laws and regulations relating to environmental protection and human health and safety, including those governing wastewater discharges, air emissions, the operation and removal of underground and aboveground storage tanks, the use, storage, treatment, transportation, release, recycling and disposal of solid and hazardous materials and wastes and the cleanup of contaminated property or water. The violation of these laws and regulations can result in administrative, civil or criminal penalties against us or in a cease and desist order against our operations that are not in compliance. Our future acquisitions may also be subject to regulation, including antitrust reviews. We believe that we comply in all material respects with all laws and regulations applicable to our business, but future regulations may be more stringent and require us to incur significant additional compliance costs.

Our past and present business operations are subject to environmental laws and regulations. We may be required by these laws to pay the full amount of the costs of investigation and/or remediation of contaminated properties, even if we are not at fault for disposal of the materials or if such disposal was legal at the time. Like many of our competitors, we have incurred, and will continue to incur, capital and operating expenditures and other costs in complying with these laws and regulations. In addition, soil and groundwater contamination exists at certain of our properties. We cannot assure you that our other properties have not been or will not become similarly contaminated. In addition, we could become subject to potentially material new or unforeseen environmental costs or liabilities because of our acquisitions.

Climate change legislation or regulations restricting emission of greenhouse gases could result in increased operating costs and reduced demand for the vehicles we sell.

On December 15, 2009, the U.S. Environmental Protection Agency (EPA) published its findings that emissions of carbon dioxide, methane and other greenhouse gases present an endangerment to public health and the environment because emissions of such gases are, according to the EPA, contributing to warming of the earth's atmosphere and other climatic changes. These findings allow the EPA to adopt and implement regulations that would restrict emissions of greenhouse gases under existing provisions of the federal Clean Air Act. Accordingly, the EPA has proposed regulations that would require a reduction in emissions of greenhouse gases from motor vehicles and could

trigger permit review for greenhouse gas emissions from certain stationary sources. In addition, on October 30, 2009, the EPA published a final rule requiring the reporting of greenhouse gas emissions from specified large greenhouse gas emission sources in the United States, including facilities that emit more than 25,000 tons of greenhouse gases on an annual basis, beginning in 2011 for emissions occurring in 2010. At the state level, more than one-third of the states, either individually or through multi-state regional initiatives, already have begun

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implementing legal measures to reduce emissions of greenhouse gases. The adoption and implementation of any regulations imposing reporting obligations on, or limiting emissions of greenhouse gases from, our equipment and operations or from the vehicles that we sell could adversely affect demand for those vehicles and require us to incur costs to reduce emissions of greenhouse gases associated with our operations.

Potential conflicts of interest between us and our officers or directors could adversely affect our future performance.

O. Bruton Smith serves as the chairman and chief executive officer of Speedway Motorsports. Accordingly, we compete with Speedway Motorsports for the management time of Mr. Smith.

We have in the past and will likely in the future enter into transactions with Mr. Smith, entities controlled by Mr. Smith or our other affiliates. We believe that all of our existing arrangements with affiliates are as favorable to us as if the arrangements were negotiated between unaffiliated parties, although the majority of these transactions have neither been verified by third parties in that regard nor are likely to be so verified in the future. Potential conflicts of interest could arise in the future between us and our officers or directors in the enforcement, amendment or termination of arrangements existing between them.

We may be subject to substantial withdrawal liability assessments in the future related to a multi-employer pension plan to which certain of our dealerships make contributions pursuant to collective bargaining agreements.

Six of our dealership subsidiaries in Northern California currently make fixed-dollar contributions to the Automotive Industries Pension Plan (the AI Pension Plan) pursuant to collective bargaining agreements between our subsidiaries and the International Association of Machinists (the IAM). The AI Pension Plan is a multi-employer pension plan as defined under the Employee Retirement Income Security Act of 1974, as amended, and our six dealership subsidiaries are among approximately 100 automobile dealerships that make contributions to the AI Pension Plan pursuant to collective bargaining agreements with the IAM. In June 2006, we received information that the AI Pension Plan was substantially underfunded as of December 31, 2005. In July 2007, we received updated information that the AI Pension Plan continued to be substantially underfunded as of December 31, 2006, with the amount of such underfunding increasing versus year end 2005. In March 2008, the Board of Trustees of the AI Pension Plan notified participants, participating employers and local unions that the Plan's actuary, in accordance with the requirements of the federal Pension Protection Act of 2006, had issued a certification that the AI Pension Plan is in Critical Status effective with the plan year commencing January 1, 2008. In conjunction with this finding, the Board of Trustees of the AI Pension Plan adopted a Rehabilitation Plan that implements reductions or eliminations of certain adjustable benefits that were previously available under the Plan (including some forms of early retirement benefits, and disability and death benefits), and also implements a requirement on all participating employers to increase employer contributions to the Plan for a seven year period commencing in 2013. Under applicable federal law, any employer contributing to a multi-employer pension plan that completely ceases participating in the plan while the plan is underfunded is subject to payment of such employer's assessed share of the aggregate unfunded vested benefits of the plan. In certain circumstances, an employer can be assessed withdrawal liability for a partial withdrawal from a multi-employer pension plan. In addition, if the financial condition of the AI Pension Plan were to continue to deteriorate to the point that the Plan is forced to terminate and be assumed by the Pension Benefit Guaranty Corporation, the participating employers could be subject to assessments by the PBGC to cover the participating employers' assessed share of the unfunded vested benefits. If any of these adverse events were to occur in the future, it could result in a substantial withdrawal liability assessment that could have a material adverse effect on our business, financial condition, results of operations or cash flows.

A change in historical experience and/or assumptions used to estimate reserves could have a material impact on our earnings.

As described in Item 7 under the heading Management's Discussion and Analysis of Financial Condition and Results of Operations Use of Estimates and Critical Accounting Policies management relies on estimates in various areas of accounting and financial reporting. For example, our estimates for finance, insurance and service

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contracts and insurance reserves are based on historical experience. Differences between actual results and our historical experiences and/or our assumptions could have a material impact on our earnings in the period of the change and in periods subsequent to the change.

Impairment of our goodwill could have a material adverse impact on our earnings.

Pursuant to applicable accounting pronouncements, we evaluate goodwill for impairment annually or more frequently if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. We describe the process for testing goodwill more thoroughly in Item 7 under the heading Management's Discussion and Analysis of Financial Condition and Results of Operations Use of Estimates and Critical Accounting Policies. If we determine that the amount of our goodwill is impaired at any point in time, we are required to reduce goodwill on our balance sheet. If goodwill of our single reporting unit is impaired based on a future impairment test, we will be required to record a significant non-cash impairment charge that may also have a material adverse effect on our results of operations for the period in which the impairment of goodwill occurs. As of December 31, 2010, our balance sheet reflected a carrying amount of approximately \$468.5 million in goodwill.

Item 1B: *Unresolved Staff Comments*

None.

Item 2: *Properties.*

Our principal executive offices are located at 6415 Idlewild Road, Suite 109, Charlotte, North Carolina 28212, and our telephone number is (704) 566-2400. We lease these offices from a related party. See Note 8, Related Parties, to our accompanying Consolidated Financial Statements.

Our dealerships are generally located along major U.S. or interstate highways. One of the principal factors we consider in evaluating an acquisition candidate is its location. We prefer to acquire dealerships or build dealership facilities located along major thoroughfares, which can be easily visited by prospective customers.

We lease the majority of the properties utilized by our dealership operations from affiliates of Capital Automotive REIT (CARS) and other individuals and entities. The properties utilized by our dealership operations that are owned by us or one of our subsidiaries are pledged as security for our 2010 Credit Facilities or under mortgages. We believe that our facilities are adequate for our current needs.

Under the terms of our franchise agreements, each of our dealerships must maintain an appropriate appearance and design of its dealership facility and is restricted in its ability to relocate.

Item 3: *Legal Proceedings.*

We are a defendant in the matter of Galura, et al. v. Sonic Automotive, Inc., a private civil action filed in the Circuit Court of Hillsborough County, Florida. In this action, originally filed on December 30, 2002, the plaintiffs allege that we and our Florida dealerships sold an antitheft protection product in a deceptive or otherwise illegal manner, and further sought representation on behalf of any customer of any of our Florida dealerships who purchased the antitheft protection product since December 30, 1998. The plaintiffs are seeking monetary damages and injunctive relief on behalf of this class of customers. In June 2005, the court granted the plaintiffs' motion for certification of the requested class of customers, but the court has made no finding to date regarding actual liability in this lawsuit. We subsequently filed a notice of appeal of the court's class certification ruling with the Florida Court of Appeals. In April 2007, the Florida Court of Appeals affirmed a portion of the trial court's class certification, and overruled a portion of the trial

court's class certification. In November 2009, the Florida trial court granted Summary Judgment in our favor against Plaintiff Enrique Galura, and his claim has been dismissed. Marisa Hazelton's claim is still pending. We currently intend to continue our vigorous appeal and defense of this lawsuit and to assert available defenses. However, an adverse resolution of this lawsuit could result in the payment of significant costs and damages, which could have a material adverse effect on our future results of operations, financial condition and cash flows. At a mediation held February 4, 2011, our company reached an agreement in

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principle with the plaintiffs to settle this class action lawsuit. This agreement in principle remains conditioned upon execution of a definitive settlement agreement and subsequent approval by the Florida state court. In the event that a definitive settlement of this lawsuit is finalized upon terms and conditions consistent with the agreement in principle, such a settlement would not have a material adverse affect on our future results of operations, financial condition and cash flows.

Several private civil actions have been filed against Sonic Automotive, Inc. and several of our dealership subsidiaries that purport to represent classes of customers as potential plaintiffs and made allegations that certain products sold in the finance and insurance departments were done so in a deceptive or otherwise illegal manner. One of these private civil actions was filed on November 15, 2004 in South Carolina state court, York County Court of Common Pleas, against Sonic Automotive, Inc. and 10 of our South Carolina subsidiaries. The plaintiffs in that lawsuit were Misty J. Owens, James B. Wright, Vincent J. Astey and Joseph Lee Williams, on behalf of themselves and all other persons similarly situated, with plaintiffs seeking monetary damages and injunctive relief on behalf of the purported class. The group of plaintiffs attorneys representing the plaintiffs in the South Carolina lawsuit also filed another private civil class action lawsuit against Sonic Automotive, Inc. and 3 of our subsidiaries on February 14, 2005 in state court in North Carolina, Lincoln County Superior Court, which similarly sought certification of a multi-state class of plaintiffs and alleged that certain products sold in the finance and insurance departments were done so in a deceptive or otherwise illegal manner. The plaintiffs in this North Carolina lawsuit were Robert Price, Carolyn Price, Marcus Cappelletti and Kathy Cappelletti, on behalf of themselves and all other persons similarly situated, with plaintiffs seeking monetary damages and injunctive relief on behalf of the purported class. The South Carolina state court action and the North Carolina state court action have since been consolidated into a single proceeding in private arbitration before the American Arbitration Association. On November 12, 2008, claimants in the consolidated arbitration filed a Motion for Class Certification as a national class action including all of the states in which we operate dealerships. Claimants are seeking monetary damages and injunctive relief on behalf of this class of customers. The parties have briefed and argued the issue of class certification.

On July 19, 2010, the Arbitrator issued a Partial Final Award on Class Certification, certifying a class which includes all customers who, on or after November 15, 2000, purchased or leased from a Sonic dealership a vehicle with the Etch product as part of the transaction, but not including customers who purchased or leased such vehicles from a Sonic dealership in Florida. The Partial Final Award on Class Certification is not a final decision on the merits of the action. The merits of Claimants assertions and potential damages will still have to be proven through the remainder of the arbitration. The Arbitrator stayed the Arbitration for thirty days to allow either party to petition a court of competent jurisdiction to confirm or vacate the award. Sonic will seek review of the class certification ruling by a court of competent jurisdiction and will continue to press its argument that this action is not suitable for a class-based arbitration. On July 22, 2010, the plaintiffs in this consolidated arbitration filed a Motion to Confirm the Arbitrator s Partial Final Award on Class Certification in state court in North Carolina, Lincoln County Superior Court. On August 17, 2010, Sonic filed to remove this North Carolina state court action to federal court, and simultaneously filed a Petition to Vacate the Arbitrator s Partial Final Award on Class Certification, with both filings made in the United Stated District Court for the Western District of North Carolina. We intend to continue our vigorous defense of this arbitration and to assert all available defenses. However, an adverse resolution of this arbitration could result in the payment of significant costs and damages, which could have a material adverse effect on our future results of operations, financial condition and cash flows. Currently, we are unable to estimate a range of potential loss related to this matter.

We are involved, and expect to continue to be involved, in numerous legal and administrative proceedings arising out of the conduct of our business, including regulatory investigations and private civil actions brought by plaintiffs purporting to represent a potential class or for which a class has been certified. Although we vigorously defend ourselves in all legal and administrative proceedings, the outcomes of pending and future proceedings arising out of the conduct of our business, including litigation with customers, employment related lawsuits, contractual disputes,

class actions, purported class actions and actions brought by governmental authorities, cannot be predicted with certainty. An unfavorable resolution of one or more of these matters could have a material adverse effect on our business, financial condition, results of operations, cash flows or prospects.

Table of Contents**Item 4:** *[Removed and Reserved]***PART II****Item 5:** *Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.*

Our Class A common stock is currently traded on the NYSE under the symbol SAH. Our Class B Common Stock is not traded on a public market.

As of February 18, 2011, there were 40,760,973 shares of Sonic's Class A common stock and 12,029,375 shares of Sonic's Class B common stock outstanding. As of February 18, 2011, there were 95 record holders of the Class A common stock and three record holders of the Class B common stock. As of February 18, 2011, the closing stock price for the Class A common stock was \$14.80.

Our Board of Directors approved four quarterly cash dividends on all outstanding shares of common stock totaling \$0.48 per share during 2008. No dividends were declared during 2009, but in the fourth quarter of 2010 our Board of Directors approved a cash dividend on all outstanding shares of common stock of \$0.025 per share. Subsequent to December 31, 2010, our Board of Directors approved a cash dividend on all outstanding shares of common stock of \$0.025 per share for shareholders of record on March 15, 2011 to be paid on April 15, 2011. There is no guarantee that additional dividends will be declared and paid at any time in the future. See Note 6, Long-Term Debt, to the accompanying Consolidated Financial Statements and Item 7: *Management's Discussion and Analysis of Financial Condition and Results of Operations* for additional discussion of dividends and for a description of restrictions on the payment of dividends.

The following table sets forth the high and low closing sales prices for Sonic's Class A common stock for each calendar quarter during the periods indicated as reported by the NYSE Composite Tape and the dividends declared during such periods.

	Market Price		Cash Dividend Declared
	High	Low	
2010			
First Quarter	\$ 12.51	\$ 9.05	\$
Second Quarter	13.18	8.45	
Third Quarter	10.23	8.39	
Fourth Quarter	13.64	9.50	0.025
2009			
First Quarter	\$ 4.16	\$ 0.95	\$
Second Quarter	11.03	1.06	
Third Quarter	14.77	8.35	
Fourth Quarter	13.04	8.54	

Table of Contents**Issuer Purchases of Equity Securities**

The following table sets forth information about the shares of Class A Common Stock we repurchased during the quarter ended December 31, 2010.

	Total Number of Shares Purchased(1)(2)	Average Price Paid per Share (In thousands, except per share data)	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs(2)(3)	Approximate Dollar Value of Shares That May Yet Be Purchased Under the Plans or Programs
October 2010	1	\$ 10.53	1	\$ 43,547
November 2010				43,547
December 2010	2	13.23	2	43,511
Total	3	\$ 12.92	3	\$ 43,511

(1) All shares repurchased were part of publicly announced share repurchase programs

(2) Shares purchased represent the required tax withholding upon issuance of restricted stock.

(3) Our publicly announced Class A Common Stock repurchase authorizations occurred as follows:

	(Amounts in thousands)
November 1999	\$ 25,000
February 2000	25,000
December 2000	25,000
May 2001	25,000
August 2002	25,000
February 2003	20,000
December 2003	20,000
July 2004	20,000
July 2007	30,000
October 2007	40,000
April 2008	40,000
Total	\$ 295,000

Table of Contents**Item 6: Selected Financial Data.**

This selected consolidated financial data should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations and the Consolidated Financial Statements and related notes included elsewhere in this Annual Report on Form 10-K.

We have accounted for all of our dealership acquisitions using the purchase method of accounting and, as a result, we do not include in our Consolidated Financial Statements the results of operations of these dealerships prior to the date we acquired them. Our selected consolidated financial data reflect the results of operations and financial positions of each of our dealerships acquired prior to December 31, 2010. As a result of the effects of our acquisitions and other potential factors in the future, the historical consolidated financial information described in selected consolidated financial data is not necessarily indicative of the results of our operations and financial position in the future or the results of operations and financial position that would have resulted had such acquisitions occurred at the beginning of the periods presented in the selected consolidated financial data.

	Year Ended December 31,				
	2006	2007	2008	2009	2010
	(In millions, except per share data)				
Income Statement Data(1)(2):					
Total revenues	\$ 7,376.9	\$ 7,767.0	\$ 6,900.2	\$ 6,055.3	\$ 6,880.8
Impairment charges	\$ 4.7	\$ 0.9	\$ 812.0	\$ 23.5	\$ 0.2
Income (loss) from continuing operations before income taxes	\$ 139.1	\$ 172.1	\$ (756.1)	\$ 27.9	\$ 78.4
Income (loss) from continuing operations	\$ 82.9	\$ 104.6	\$ (633.8)	\$ 57.2	\$ 95.9
Basic earnings (loss) per share from continuing operations	\$ 1.95	\$ 2.44	\$ (15.70)	\$ 1.29	\$ 1.82
Diluted earnings (loss) per share from continuing operations	\$ 1.91	\$ 2.36	\$ (15.70)	\$ 1.07	\$ 1.58
Consolidated Balance Sheet Data(2):					
Total assets	\$ 3,124.8	\$ 3,282.7	\$ 2,405.5	\$ 2,068.9	\$ 2,250.8
Current maturities of long-term debt	\$ 2.7	\$ 4.2	\$ 738.4	\$ 24.0	\$ 9.1
Total long-term debt	\$ 567.8	\$ 678.4	\$ 738.4	\$ 576.1	\$ 555.5
Total long-term liabilities (including long-term debt)	\$ 768.2	\$ 915.8	\$ 809.6	\$ 717.2	\$ 689.5
Cash dividends declared per common share	\$ 0.48	\$ 0.48	\$ 0.48	\$	\$ 0.025

(1) In accordance with the provisions of Presentation of Financial Statements in the ASC, prior years' income statement data reflect reclassifications to (i) exclude franchises sold, identified for sale, or terminated subsequent to December 31, 2009 which had not been previously included in discontinued operations or (ii) include franchises previously held for sale which subsequently were reclassified to held and used. See Notes 1 and 2 to our accompanying Consolidated Financial Statements which discuss these and other factors that affect the comparability of the information for the periods presented.

(2) As mentioned in Management's Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources and Notes 2, 5 and 6 to our accompanying Consolidated Financial Statements, impairment charges, business combinations and dispositions and debt refinancings have had a material impact on

our reported financial information.

Item 7: *Management's Discussion and Analysis of Financial Condition and Results of Operations.*

2010 Events

In January 2010, we replaced our 2006 Credit Facility, which was scheduled to mature in February 2010, with a new revolving credit and vehicle floor plan facility (the 2010 Credit Facilities), which matures in August 2012, and additional manufacturer-affiliated finance company floor plan agreements (the Silo Floor Plan Facilities).

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In March 2010, we issued \$210.0 million in aggregate principal amount of 9.0% Senior Subordinated Notes (the 9.0% Notes) which mature on March 15, 2018. In April 2010, we used net proceeds from this issuance together with cash on hand to redeem \$200.0 million in aggregate principal amount of our 8.625% Senior Subordinated Notes due 2013 (the 8.625% Notes). During the second and third quarters of 2010, we repurchased an additional \$32.1 million in aggregate principal amount of the 8.625% Notes, resulting in \$42.9 million in remaining aggregate principal amount outstanding at December 31, 2010.

In November 2010, we redeemed \$16.0 million in remaining aggregate principal amount outstanding of the 4.25% Convertible Senior Subordinated Notes (the 4.25% Convertible Notes), completely extinguishing our obligations under the 4.25% Convertible Notes.

As a result of these refinancing activities, other than principal payments due on mortgage notes and certain term notes, we do not have another significant debt maturity until the 2010 Credit Facilities expire in 2012 or when the remaining aggregate principal amount outstanding of the 8.625% Notes matures in 2013.

In 2009, General Motors offered financial assistance with winding down the operations of the franchises for which we executed termination agreements in conjunction with the restructuring of General Motors. Assistance to be received from General Motors totaled \$3.3 million, all of which had been collected by December 31, 2010. As of December 31, 2010, we operated 23 General Motors franchises (under the Cadillac, Chevrolet, GMC, Saab and Buick brands) at 18 dealership locations.

During 2010, Toyota Motor Corporation issued recalls affecting certain of its most popular models in certain model years. Toyota Motor Corporation had instructed its dealerships to stop selling vehicles affected by the recall until it developed a solution to the problem and provided the necessary parts and instructions to fix it. During the period of time when affected vehicles could not be sold, Toyota Motor Corporation offered its dealers floor plan assistance to help reduce dealers' cost of carrying vehicles which dealers could not sell due to the recall, which reduced our floor plan interest expense. As of December 31, 2010, we operated 11 Toyota franchises. During the year ended December 31, 2010, we experienced a benefit to our fixed operations business as a result of work performed on vehicles affected by the recall which was paid for by the manufacturer and provided free of charge to the customer. We cannot estimate how this recall will affect consumer preferences over the long-term.

The following discussion and analysis of the results of operations and financial condition should be read in conjunction with the Sonic Automotive, Inc. and Subsidiaries Consolidated Financial Statements and the related notes thereto appearing elsewhere in this Annual Report on Form 10-K. The financial and statistical data contained in the following discussion for all periods presented reflects our December 31, 2010 classification of franchises between continuing and discontinued operations in accordance with Presentation of Financial Statements in the ASC.

Overview

We are one of the largest automotive retailers in the United States. As of December 31, 2010, we operated 135 dealership franchises, representing 29 different brands of cars and light trucks, at 118 locations and 25 collision repair centers in 15 states. As a result of the way we manage our business, we have a single operating segment for purposes of reporting financial condition and results of operations.

Our dealerships provide comprehensive services including sales of both new and used cars and light trucks, sales of replacement parts, performance of vehicle maintenance, manufacturer warranty repairs, paint and collision repair services, and arrangement of extended service contracts, financing, insurance and other aftermarket products for our customers. Although vehicle sales are cyclical and are affected by many factors, including overall economic conditions, consumer confidence, levels of discretionary personal income, interest rates and available credit, our parts,

service and collision repair services are not closely tied to vehicle sales and are not as dependent upon near-term sales volume.

The automobile industry's total amount of new vehicles sold increased by 11.5% to 11.6 million vehicles in 2010 from 10.4 million vehicles in 2009. From an industry perspective, new vehicle unit sales on a year-over-year basis increased 9.3% for import brands and 13.4% for domestic brands. Average industry expectations for new vehicle sales volume in 2011 are between 12.0 million and 13.0 million vehicles which, if realized, would be an

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increase of 3.4% to 12.1% from the 2010 level. Changes in consumer confidence, availability of consumer financing or changes in the financial stability of the automotive manufacturers could cause 2011 industry results to vary. Many factors such as brand and geographic concentrations have caused our past results to differ from the industry's overall trend.

Use of Estimates and Critical Accounting Policies

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 and 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.

Critical accounting policies are those that are both most important to the portrayal of our financial position and results of operations and require the most subjective and complex judgments. The following is a discussion of what we believe are our critical accounting policies and estimates. See Note 1, Description of Business and Summary of Significant Accounting Policies, in the accompanying Consolidated Financial Statements for additional discussion regarding our accounting policies.

Finance, Insurance and Service Contracts

We arrange financing for customers through various financial institutions and receive a commission from the lender either in a flat fee amount or in an amount equal to the difference between the actual interest rates charged to customers and the predetermined base rates set by the financing institution. We also receive commissions from the sale of various insurance contracts and 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.

In the event a customer terminates a financing, insurance or extended service contract prior to the original termination date, we may be required to return a portion of the commission revenue originally recorded to the third party provider (chargebacks). The commission revenue for the sale of these products and services is recorded net of estimated chargebacks at the time of sale. Our estimate of future chargebacks is established based on our historical chargeback rates, termination provisions of the applicable contracts and industry data. While chargeback rates vary depending on the type of contract sold, a 100 basis point change in the estimated chargeback rates used in determining our estimates of future chargebacks would have changed our estimated reserve for chargebacks at December 31, 2010 by approximately \$1.6 million. Our estimate of chargebacks (\$11.3 million as of December 31, 2010) is influenced by early contract termination events such as vehicle repossessions, refinancings and early pay-offs. If these factors negatively change, the resulting impact would affect our future estimate for chargebacks and could have a negative adverse impact on our operations, financial position and cash flows. Our actual chargeback experience has not been materially different from our recorded estimates.

Goodwill and Franchise Assets

Goodwill is tested for impairment at least annually, or more frequently when events or circumstances indicate that impairment might have occurred. An exception to the annual impairment test is provided by Intangibles Goodwill and Other in the ASC, wherein a detailed determination of the fair value of a reporting unit may be carried forward from one year to the next if the following criteria have been met: (i) the assets and liabilities that make up the reporting unit have not changed significantly since the most recent fair value determination; (ii) the most recent fair value determination resulted in an amount that exceeded the carrying amount of the reporting unit by a substantial margin; and (iii) based on the analysis of events that have occurred and circumstances that have changed since the most recent

fair value determination, the likelihood that a current fair value determination would be less than the current carrying amount of the reporting unit is remote. As of December 31, 2010, we determined that we had met the criteria necessary to carry forward our step one testing from December 31, 2009.

In completing step one of our impairment analyses as of December 31, 2009, we used a discounted cash flow (DCF) model to calculate fair value. We believe a discounted cash flow model is the most reliable valuation

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method to use because the fair value of our business is dependent on our ability to generate cash through sales and service of new and used vehicles. The DCF method is based on forward-looking projections that incorporate current trends and market expectations. We also analyzed our market capitalization along with potential adjustments to market capitalization such as control premium and cost synergies in evaluating our estimate of fair value. The results of our DCF model compared to our adjusted market capitalization determine whether the DCF model provided an accurate measure of fair value for the purpose of the impairment test. Our estimate of fair value was then compared to our book value at December 31, 2009 to determine whether an indicator of impairment existed. At December 31, 2009, the fair value of our reporting unit exceeded the carrying value of the reporting unit by a substantial margin. As a result, we were not required to conduct the second step of the impairment test, and determined that no indicator of impairment existed at December 31, 2009.

The significant assumptions in our DCF model include projected earnings, weighted average cost of capital (and estimates in the weighted average cost of capital inputs) and residual growth rates. To the extent the reporting unit's earnings decline significantly or there are changes in one or more of these assumptions that would result in lower valuation results, it could cause the carrying value of the reporting unit to exceed its fair value and thus require us to conduct the second step of the impairment test described above. In projecting our reporting unit's earnings, we develop many assumptions which include, but are not limited to, new and used vehicle unit sales, internal revenue enhancement initiatives, cost control initiatives, internal investment programs such as training and technology, infrastructure and inventory floor plan borrowing rates. Our expectation of new vehicle unit sales is driven by our expectation of the SAAR of new vehicles. The estimate of the industry SAAR in future periods is the basis of our assumptions related to new vehicle unit sales volumes in our DCF model because we believe the historic and projected level of SAAR is the best indicator of our new vehicle unit sales trends. The level of SAAR assumed in our projection of earnings for 2010 was approximately 11.0 million units with a gradual increase in the level of SAAR to approximately 14.0 million units in 2013, and remaining level thereafter. Actual SAAR in 2010 was approximately 11.6 million units, and average industry expectations for the SAAR in 2011 are between 12.0 million and 13.0 million units, consistent with the expectations used in our DCF model in 2009.

Our DCF model is dependent on the assumptions used and is sensitive to changes in assumptions. For example, assuming all other factors remain the same, a 10% change in projected earnings would change the calculated fair value estimate as of December 31, 2009 by approximately \$136.3 million. In the event the weighted average cost of capital changed 100 basis points, assuming all other factors remain the same, the calculated fair value estimate as of December 31, 2009 would change by approximately \$143.9 million. Finally, if the residual growth estimate changed 100 basis points, assuming all other factors remain the same, the calculated fair value estimate as of December 31, 2009 would change by approximately \$119.9 million. Based on our DCF model estimating the fair value of our reporting unit, none of the items above, if realized, would have resulted in lowering the fair value of the reporting unit below the reporting unit's carrying value.

We continue to face a challenging automotive retail environment. As a result of these conditions, there can be no assurances that a material impairment charge will not occur in a future period. We will continue to monitor events in future periods to determine if additional asset impairment testing should be performed. If we are required to apply the second step of the goodwill impairment test in future periods, we could be required to record an impairment charge to goodwill that would have a material adverse impact on our financial condition.

We test franchise assets for impairment annually or more frequently if events or circumstances indicate possible impairment. We estimate the value of our franchise assets using a discounted cash flow model. The discounted cash flow model used contains inherent uncertainties, including significant estimates and assumptions related to growth rates, projected earnings and cost of capital. We are subject to financial risk to the extent that our franchise assets become impaired due to deterioration of the underlying businesses. The risk of a franchise asset impairment loss may increase to the extent the underlying businesses' earnings or projected earnings decline. As a result of our impairment

testing in 2010, no franchise asset impairments were required. The balance of our franchise assets (related to continuing operations and discontinued operations) totaled \$64.8 million at December 31, 2010.

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Insurance Reserves

We have various high deductible retention and insurance programs which require us to make estimates in determining the ultimate liability we may incur for claims arising under these programs. We accrue for insurance reserves on a pro-rata basis throughout the year based on the expected year-end liability. We estimate the ultimate liability under these programs is between \$20.0 million and \$22.2 million. At December 31, 2010, we had \$21.0 million reserved for such programs. Changes in significant assumptions used in the development of the ultimate liability for these programs could have a material impact on the level of reserves, our operating results, financial position and cash flows. These significant assumptions would include the volume of claims, medical cost trends, claims handling and reporting patterns, historical claims experience, the effect of related court rulings and current or projected changes in state laws. From a sensitivity analysis perspective, it is difficult to quantify the effect of changes in any of these significant assumptions with the exception of the volume of claims. We believe a 10% change in the volume of claims would have a proportional effect on our reserves. We believe our actual loss experience has not been materially different from our recorded estimates.

Lease Exit Accruals

The majority of our dealership properties are leased under long-term operating lease arrangements. When leased properties are no longer utilized in operations, we record lease exit accruals. These situations could include the relocation of an existing facility or the sale of a franchise where the buyer will not be subleasing the property for either the remaining term of the lease or for an amount equal to our obligation under the lease, or in situations where a store is closed as a result of the associated franchise being terminated by the manufacturer and no other operations continue on the leased property. The lease exit accruals represent the present value of the lease payments, net of estimated sublease rentals, for the remaining life of the operating leases and other accruals necessary to satisfy lease commitments to the landlords. At December 31, 2010, we had \$43.5 million accrued for lease exit costs. A significant change in our assumptions regarding the time period necessary to obtain a subtenant or the amount of the anticipated sublease income could have a material effect on our accrual and, as a result, earnings. For example, assuming all other factors remain the same, a 50% decrease in our estimated proceeds from subleases would change our lease exit accruals by approximately \$1.1 million. In addition, based on the terms and conditions negotiated in the sale of franchises in the future, additional accruals may be necessary if the purchaser of the franchise does not assume the lease of the associated franchise, or we are unable to negotiate a sublease with the buyer of the franchise on terms that are identical to or better than those associated with the original lease.

Legal Proceedings

We are involved, and expect to continue to be involved, in numerous legal proceedings arising out of the conduct of our business, including litigation with customers, employment related lawsuits, contractual disputes and actions brought by governmental authorities. As of December 31, 2010, we had accrued \$9.1 million in legal reserves. Although we vigorously defend ourselves in all legal and administrative proceedings, the outcomes of pending and future proceedings arising out of the conduct of our business, including litigation with customers, employment related lawsuits, contractual disputes, class actions, purported class actions and actions brought by governmental authorities, cannot be predicted with certainty. An unfavorable resolution of one or more of these matters that are significant could exceed the amount of our legal reserve and have a material adverse effect on our business, financial condition, results of operations, cash flows or prospects.

Classification of Franchises in Continuing and Discontinued Operations

We classify the results from operations of our continuing and discontinued operations in our Consolidated Statements of Income based on the provisions of Presentation of Financial Statements in the ASC. Many of these provisions

involve judgment in determining whether a franchise will be reported as continuing or discontinued operations. Such judgments include whether a franchise will be sold or terminated, the period required to complete the disposition and the likelihood of changes to a plan for sale. If in future periods we determine that a franchise should be either reclassified from continuing operations to discontinued operations or from discontinued operations to continuing operations, previously reported Consolidated Statements of Income will be reclassified in order to reflect that classification. During the year ended December 31, 2010, we identified one franchise that was held for

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sale and previously included in discontinued operations, which we chose to continue to hold and operate in continuing operations in 2010. At December 31, 2010 there were no dealership franchises classified as held for sale.

Income Taxes

As a matter of course, we are regularly audited by various taxing authorities and from time to time these audits result in proposed assessments where the ultimate resolution may result in us owing additional taxes. We believe that our tax positions comply, in all material respects, with applicable tax law and that we have adequately provided for any reasonably foreseeable outcome related to these matters. Included in other accrued liabilities at December 31, 2010 is \$27.6 million in reserves that we have provided for these matters (including estimates related to possible interest and penalties). From time to time, we engage in transactions in which the tax consequences may be subject to uncertainty. Examples of such transactions include business acquisitions and disposals, including consideration paid or received in connection with such transactions. Significant judgment is required in assessing and estimating the tax consequences of these transactions. We determine whether it is more-likely-than-not that a tax position will be sustained upon examination, including resolution of any related appeals or litigation processes, based on the technical merits of the position. In evaluating whether a tax position has met the more-likely-than-not recognition threshold, we presume that the position will be examined by the appropriate taxing authority that has full knowledge of all relevant information. A tax position that does not meet the more-likely-than-not recognition threshold is measured to determine the amount of benefit to be recognized in the financial statements. The tax position is measured at the largest amount of benefit that is likely of being realized upon ultimate settlement.

We adjust our estimates periodically because of ongoing examinations by and settlements with the various taxing authorities, as well as changes in tax laws, regulations and precedent. The effects on our financial statements of income tax uncertainties are discussed in Note 7, *Income Taxes*, to our Consolidated Financial Statements.

We continually review all deferred tax asset positions (including state net operating loss carryforwards) to determine whether it is more-likely-than-not that the deferred tax assets will be utilized. Certain factors considered in evaluating the potential for realization of deferred tax assets include the time remaining until expiration (related to state net operating loss carryforwards) and various sources of taxable income that may be available under the tax law to realize a tax benefit related to a deferred tax asset. This evaluation requires management to make certain assumptions about future profitability, the execution of tax strategies that may be available to us and the likelihood that these assumptions or execution of tax strategies would occur. This evaluation is highly judgmental. The results of future operations, regulatory framework of these taxing authorities and other related matters cannot be predicted with certainty. Therefore, actual realization of these deferred tax assets may be materially different from management's estimate.

At December 31, 2008, 2009 and 2010, we had a valuation allowance recorded totaling \$116.3 million, \$61.9 million and \$10.9 million, respectively.

During the years ended December 31, 2009 and 2010, we reduced the recorded valuation allowance amount by \$54.4 million and \$51.0 million, respectively. These changes were the result of the use of certain state net operating loss carryforwards as well as a change in estimate that we would be able to ultimately realize the benefits of recorded deferred tax balances. These changes in estimate were primarily driven by the improvement experienced in our operating results, the overall improvement of the automotive retailing industry and the expectation that our results and those of the automotive retailing industry would continue to improve in the future. Notwithstanding these facts, at December 31, 2010, we maintained valuation allowance amounts of \$10.9 million related to certain state net operating loss carryforwards as it was likely that we would not be able to generate sufficient state taxable income in the related entities to utilize the accumulated net operating loss carryforward balances.

We accrue for income taxes on a pro-rata basis throughout the year based on the expected year end liability. These estimates, judgments and assumptions are made quarterly by our management based on available information and take into consideration estimated income taxes based on prior year income tax returns, changes in income tax law, our income tax strategies and other factors. If our management receives information which causes us to change our estimate of the year end liability, the amount of expense or expense reduction required to be recorded in any particular quarter could be material to our operating results, financial position and cash flows.

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The following table summarizes the percentages of total revenues represented by certain items reflected in our Consolidated Statements of Income:

	Percentage of Total Revenue(1) for the Year Ended December 31,		
	2008	2009	2010
Revenues:			
New vehicles	58.1%	53.3%	53.0%
Used vehicles	19.5%	24.0%	25.8%
Wholesale vehicles	3.9%	2.4%	2.2%
Parts, service and collision repair	15.9%	17.7%	16.4%
Finance, insurance and other	2.6%	2.6%	2.6%
Total revenue	100.0%	100.0%	100.0%
Cost of sales(2)	84.0%	82.9%	83.8%
Gross profit	16.0%	17.1%	16.2%
Selling, general and administrative expenses	13.1%	13.7%	13.0%
Impairment charges	11.7%	0.4%	0.0%
Depreciation and amortization	0.5%	0.6%	0.5%
Operating income	(9.3%)	2.4%	2.7%
Interest expense, floor plan	0.6%	0.3%	0.3%
Interest expense, other, net	0.9%	1.3%	1.0%
Interest expense, non-cash, convertible debt	0.2%	0.0%	0.1%
Interest expense, non-cash, cash flow swaps	0.0%	0.2%	0.1%
Other expense, net	0.0%	0.1%	0.1%
Income (loss) from continuing operations before income taxes	(11.0%)	0.5%	1.1%
Income tax expense (benefit)	(1.8%)	(0.4%)	(0.3%)
Income (loss) from continuing operations	(9.2%)	0.9%	1.4%

(1) In accordance with the provisions of Presentation of Financial Statements in the ASC, prior years income statement data reflect reclassifications to (i) exclude franchises sold, identified for sale, or terminated subsequent to December 31, 2009 which had not been previously included in discontinued operations or (ii) include franchises previously held for sale which subsequently were reclassified to held and used. See Notes 1 and 2 to our accompanying Consolidated Financial Statements which discuss these and other factors that affect the comparability of the information for the periods presented.

(2) The cost of sales line item includes the cost of new and used vehicles, vehicle parts and all costs directly linked to servicing customer vehicles.

During the year ended December 31, 2010, we disposed of 13 franchises and, at December 31, 2010, had no other franchises held for sale. The results of operations of these dealerships, including gains or losses on disposition, have been included in discontinued operations on the accompanying Consolidated Statements of Income for all periods presented. In addition to these dispositions, we disposed of 10 and 18 franchises, respectively, in each of the years ended December 31, 2008 and 2009. See additional discussions of franchises held for sale in the Liquidity and Capital Resources discussion.

The following discussions are based on reported figures. Same store amounts do not vary significantly from reported totals since there were no significant dealership franchise acquisitions in the years ended December 31, 2009 and 2010.

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Impairments and Other Charges

We recorded various charges in connection with the decision to exit certain facility leases since the planned use of certain leased properties will not occur. See the table below for the amounts and classification of the charges recorded. Of the \$27.6 million recorded in discontinued operations in the year ending December 31, 2009, \$11.4 million relates to lease exit accruals for our General Motors dealerships which were terminated in the fourth quarter of 2009.

Annually, we review franchise asset and property and equipment valuations. Based on historical and projected operating losses for certain continuing operating dealerships, we determined that certain dealerships would not be able to recover recorded franchise asset and property and equipment asset balances and that we would not complete certain capital projects at these stores. As such, we partially or fully impaired the franchise asset, property and equipment asset values as well as costs for construction in progress for those stores. Further, as a result of lowering the estimates of expected proceeds from the sale of certain dealership franchises held for sale based on market conditions, we recorded franchise asset, property and equipment and other asset impairment charges in discontinued operations. See the table below for the amounts and classification of the charges recorded for the years ended December 31, 2008, 2009 and 2010. In 2010, we recorded \$0.2 million of impairment related to property and equipment and construction in progress in continuing operations.

Goodwill is tested for impairment at least annually, or more frequently when events or circumstances indicate that impairment might have occurred. An exception to the annual impairment test provided by Intangibles Goodwill and Other in the ASC allowed us to carry forward our goodwill impairment analysis from 2009, resulting in no goodwill impairment in 2010. For the year ended December 31, 2009, we recorded goodwill impairment charges of \$1.1 million within continuing operations and \$1.6 million within discontinued operations due to the determination that a portion of the goodwill was not recoverable, based on estimated proceeds, while certain dealership operations were held for sale. For the year ended December 31, 2008, we recorded an impairment of \$797.3 million related to our evaluation of goodwill. We recorded \$795.3 million in continuing operations and \$2.0 million in discontinued operations as a result of step two of our goodwill impairment test and based on the determination that a portion of goodwill was not recoverable from assets held for sale based on estimated proceeds. See additional discussion of goodwill impairment testing in the previous heading Use of Estimates and Critical Accounting Policies Goodwill and Franchise Assets.

For the year ended December 31, 2008, our results of operations were negatively impacted by the effects of Hurricane Ike and hail storms in the Houston and mid-west markets. We estimate the overall impact (physical damage and business interruption) in 2008 lowered pre-tax earnings by approximately \$8.0 million. For the year ended December 31, 2010, our results of operations were negatively impacted by the effects of hail storms in the Mid-Atlantic market. We estimate the overall impact (physical damage and business interruption) in 2010 lowered pre-tax earnings by approximately \$0.6 million.

We have entered into interest rate swap agreements (the Fixed Swaps) to effectively convert a portion of our LIBOR-based variable rate debt to a fixed rate, in order to reduce our exposure to market risks from fluctuations in interest rates. As a result of the refinancing of our 2006 Credit Facility and the new terms of the 2010 Credit Facilities, at December 31, 2009 we determined it was no longer probable that we would incur interest payments that match the terms of certain Fixed Swaps that previously were designated and qualified as cash flow hedges, as we would be borrowing certain amounts under the Silo Floor Plan Facilities rather than under the new 2010 Credit Facilities. Certain of the lenders terms under the Silo Floor Plan Facilities did not match the terms of our Fixed Swaps that previously qualified as cash flow hedges. Of the Fixed Swaps (including the two \$100.0 million notional swaps which were settled in 2009), \$565.0 million of the notional amount had previously been documented as hedges against the variability of cash flows related to interest payments on certain debt obligations. At December 31, 2010, we estimate that under the new 2010 Credit Facilities and other facilities with matching terms, it is probable that the expected debt

balance with interest payments that match the terms of the Fixed Swaps will be \$400.0 million. As a result, non-cash charges were recorded in interest expense, non-cash, cash flow swaps in the accompanying Consolidated Statements of Income related to the Fixed Swaps and amortization of amounts in accumulated other comprehensive income (loss) related to other terminated cash flow swaps. The non-cash charges for the year ended December 31, 2010 were \$4.9 million, and for the year ended December 31, 2009 were

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\$11.8 million. Changes in the fair value of the notional amount of certain cash flow swaps are recognized through earnings. See the heading **Derivative Instruments and Hedging Activities** in Note 1, **Description of Business and Summary of Significant Accounting Policies**, in the notes to the accompanying Consolidated Financial Statements for further discussion.

In the year ended December 31, 2009, we recognized a non-cash benefit of \$11.3 million related to the extinguishment of the derivative liability associated with the redemption of the 6.0% Convertible Notes. In the table below, this amount partially offsets the \$11.8 million non-cash charge related to cash flow swaps discussed above.

In the year ended December 31, 2009, we recorded \$12.0 million of debt restructuring charges. Of the \$12.0 million, \$6.6 million related to the amendment of our 2006 Credit Facility executed March 31, 2009, in which we agreed to the payment of amendment fees and increases in the interest rates for amounts outstanding and the quarterly commitment fees payable by us on the unused portion and \$5.4 million related to the loan cost amortization on our 6.0% Convertible Notes which we repurchased on October 28, 2009.

For the year ended December 31, 2009, other income (expense), net, includes a gain of approximately \$0.4 million on the repurchase of a portion of the 4.25% Convertible Notes at a discount and a gain of approximately \$0.1 million related to the derecognition of liability and equity components of the 4.25% Convertible Notes upon repurchase of a portion of the 4.25% Convertible Notes during the third quarter of 2009. These gains were offset by a loss of approximately \$7.2 million related to the write-off of the unamortized debt discount associated with the redemption of the 6.0% Convertible Notes during the fourth quarter of 2009, resulting in a net loss on debt extinguishment of approximately \$6.7 million. We recorded a loss on extinguishment of debt of approximately \$7.7 million in the year ended December 31, 2010, related to the retirement of \$232.1 million in aggregate principal amount of the 8.625% Notes. See Note 6, **Long-Term Debt**, in the notes to the accompanying Consolidated Financial Statements for further discussion.

At December 31, 2009, we had a total of \$61.9 million of valuation allowances recorded related to our deferred tax asset balances, \$15.9 million related to state net operating loss carryforwards and \$46.0 million related to all other deferred tax asset balances. The change in the recorded valuation allowance balances in the year ended December 31, 2009 was primarily driven by the assumption that state net operating loss carryforwards generated in 2010 would not be realizable, the utilization of net deferred tax assets to reduce income tax payments and changes in assumptions related to the overall realization of net deferred tax asset balances.

At December 31, 2010, we had \$10.9 million of valuation allowances recorded related to our deferred tax asset balances, the total balance of which was related to state net operating loss carryforwards. During the year ended December 31, 2010, we lowered the recorded valuation allowance amount by \$51.0 million. This was the result of the use of certain state net operating loss carryforwards as well as a change in estimate that we will be able to ultimately realize the benefits of recorded deferred tax balances. See the table below for amounts and classification of the charges recorded.

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The amount and location of the pre-tax charges discussed above in the accompanying Consolidated Statements of Income are presented in the following table:

	Continuing Operations for the Year Ended December 31, 2008 2009 2010 (In millions)		
Selling, general & administrative expenses			
Hurricane and hail storm related expenses	8.0		0.6
Lease exit and other accruals	13.5	1.1	
Franchise tax assessment		2.9	
Total selling, general & administrative expenses	21.5	4.0	0.6
Impairment charges			
Property impairment charges	10.0	18.1	0.2
Goodwill impairment charges	795.3	1.1	
Franchise agreement and other asset impairment charges	6.7	4.3	
Total impairment charges	812.0	23.5	0.2
Interest expense			
Cash-flow swap ineffectiveness, mark-to-market and amortization charges		0.5	4.9
Debt restructuring charges		12.0	1.5
Total interest expense		12.5	6.4
Other (income) expense			
Loss on debt extinguishment		6.7	7.7
Income tax related adjustments			
Valuation allowances and other tax adjustment expense (benefit)	111.6	(41.3)	(48.2)
		Discontinued Operations for the Year Ended December 31, 2008 2009 2010 (In millions)	
Gross profit, selling, general & administrative expenses			
Lease exit and other accruals	\$ 12.8	\$ 27.6	\$ 0.9
Impairment charges			
Property impairment charges	14.9	5.0	
Goodwill impairment charges	2.0	1.6	
Franchise agreement and other asset impairment charges	20.5		
Favorable lease asset impairment charges	1.9		
Total impairment charges	39.3	6.6	
Income tax related adjustments			
Valuation allowances and other tax adjustment expense / (benefit)	3.4	(6.1)	

New Vehicles

New vehicle revenues include the sale of new vehicles to retail customers, as well as the sale of fleet vehicles. New vehicle revenues are highly dependent on manufacturer incentives, which vary from cash-back incentives to low interest rate financing. New vehicle revenues are also dependent on manufacturers to provide adequate vehicle allocations to meet customer demands and the availability of consumer credit.

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The automobile manufacturing industry is cyclical and historically has experienced periodic downturns characterized by oversupply and weak demand. As an automotive retailer, we seek to mitigate the effects of this cyclicity by maintaining a diverse brand mix of dealerships. Our brand diversity allows us to offer a broad range of products at a wide range of prices from lower priced, or economy vehicles, to luxury vehicles. For the year ended December 31, 2010, 84.2% of our total new vehicle revenue was generated by import and luxury dealerships compared to 83.7% for 2009.

The automobile retail industry uses the SAAR to measure the amount of new vehicle unit sales activity within the United States market. The SAAR averages below reflect a blended average of all brands marketed or sold in the United States market. The SAAR includes brands we do not sell and markets in which we do not operate.

SAAR	2009	2010	% Change (In millions of vehicles)	2008	2009	% Change
Year Ended December 31,	10.4	11.6	11.5%	13.2	10.4	(21.2%)

Source: Bloomberg Financial Markets, via Stephens Inc.

During 2010 we experienced an increase in customer traffic at our dealerships as compared to 2009. We believe this was caused in part by the improved overall economic conditions in 2010. Despite increases in new vehicle volume in 2010, year-over-year new vehicle sales comparisons are impacted by the government's Car Allowance Rebate System (CARS) program in effect in the third quarter of 2009, which significantly affected new vehicle sales in 2009. Average industry expectations for the 2011 SAAR are currently between 12.0 million and 13.0 million vehicles which, if realized, would be an increase of 3.4% to 12.1% from the 2010 level. Following is information related to our new vehicle sales:

	For the Year-Ended December 31,		Change	Better/(Worse) % Change
	2009	2010		
	(In thousands, except units and per unit data)			
Revenue	\$ 3,229,948	\$ 3,646,200	\$ 416,252	12.9%
Gross profit	\$ 219,158	\$ 237,071	\$ 17,913	8.2%
Unit sales	99,361	107,151	7,790	7.8%
Revenue per unit	\$ 32,507	\$ 34,029	\$ 1,522	4.7%
Gross profit per unit	\$ 2,206	\$ 2,212	\$ 6	0.3%
Gross profit as a % of revenue	6.8%	6.5%	(30)bps	

	For the Year-Ended December 31,		Change	Better/(Worse) % Change
	2008	2009		
	(In thousands, except units and per unit data)			

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Revenue	\$ 4,009,496	\$ 3,229,948	\$ (779,548)	(19.4%)
Gross profit	\$ 264,962	\$ 219,158	\$ (45,804)	(17.3%)
Unit sales	123,356	99,361	(23,995)	(19.5%)
Revenue per unit	\$ 32,503	\$ 32,507	\$ 4	0.0%
Gross profit per unit	\$ 2,148	\$ 2,206	\$ 58	2.7%
Gross profit as a % of revenue	6.6%	6.8%	20bps	

During 2010, our luxury and import dealerships experienced increases in new vehicle volume of 12.1% and 6.4%, respectively. The majority of our luxury and import brands experienced increases in new vehicle volume, with the most notable increases being experienced by our Cadillac, BMW and Mercedes dealerships. These stores experienced increases of 34.1%, 13.2% and 9.3%, respectively. Our domestic brands experienced a new vehicle volume increase in 2010 of 4.4%, led by our General Motors (GM) dealerships (excluding Cadillac), which increased 15.5% compared to the prior year. Our domestic brands new vehicle volume increases were partially offset by declines at our Ford stores of 1.9% compared to 2009. However, excluding fleet, our GM stores increased

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9.3%, while our Ford stores increased 15.3% compared to 2009. The increase in new vehicle gross profit in 2010 compared to 2009 was due primarily to a 7.8% increase in new vehicle sales volume.

Overall, our new vehicle price per unit increased \$1,522, or 4.7%, compared to 2009, with our luxury stores increasing \$1,909, or 4.1%, our domestic stores increasing \$1,554, or 5.5%, and our import stores increasing \$542, or 2.3% in 2010. The increase in our overall new vehicle price per unit in 2010 can be attributed to a larger percentage of our sales being generated by higher priced luxury vehicles.

During 2009, our dealerships experienced a 19.5% decrease in new unit volume, with our luxury stores declining 21.1%, our import stores declining 16.9% and our domestic dealerships declining 22.6% compared to 2008. Our price per unit remained relatively flat in 2009 compared to 2008, which can be attributed to the decrease in new luxury unit volume in 2009 primarily due to a shift in consumer preferences as a result of the CARS program. Our gross profit decreased in 2009 compared to 2008, which can be attributed to the volatile economic conditions and the lack of credit availability to consumers in 2009.

Used Vehicles

Used vehicle revenues are directly affected by a number of factors including the level of manufacturer incentives on new vehicles, the number and quality of trade-ins and lease turn-ins and the availability of consumer credit. In addition, various manufacturers provide franchised dealers the opportunity to certify pre-owned vehicles based on criteria established by the manufacturer. This certification process extends the standard manufacturer warranty. In 2010, we continued to see improvements in our CPO unit volume, which increased 9.6% as compared to 2009. However, our sales of CPO vehicles decreased as a percentage of total used vehicle units to 35.4% from 38.4% in 2009. This percentage decrease was primarily due to an increase in our sales of non-CPO used vehicles of 11,697 units, or 25.1%, during 2010. Following is information related to our used vehicle sales:

	For the Year-Ended December 31,		Better/(Worse) %	
	2009	2010	Change	Change
	(In thousands, except units and per unit data)			
Revenue	\$ 1,451,870	\$ 1,776,581	\$ 324,711	22.4%
Gross profit	\$ 123,993	\$ 139,620	\$ 15,627	12.6%
Unit sales	75,795	90,290	14,495	19.1%
Revenue per unit	\$ 19,155	\$ 19,676	\$ 521	2.7%
Gross profit per unit	\$ 1,636	\$ 1,546	\$ (90)	(5.5%)
Gross profit as a % of revenue	8.5%	7.9%	(60)bps	
CPO revenue	\$ 744,244	\$ 849,323	\$ 105,079	14.1%
CPO unit sales	29,135	31,933	2,798	9.6%

	For the Year-Ended December 31,		Better/(Worse) %	
	2008	2009	Change	Change
	(In thousands, except units and per unit data)			

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Revenue	\$ 1,342,486	\$ 1,451,870	\$ 109,384	8.1%
Gross profit	\$ 119,077	\$ 123,993	\$ 4,916	4.1%
Unit sales	67,237	75,795	8,558	12.7%
Revenue per unit	\$ 19,966	\$ 19,155	\$ (811)	(4.1%)
Gross profit per unit	\$ 1,771	\$ 1,636	\$ (135)	(7.6%)
Gross profit as a % of revenue	8.9%	8.5%	(40)bps	
CPO revenue	\$ 708,663	\$ 744,244	\$ 35,581	5.0%
CPO unit sales	27,951	29,135	1,184	4.2%

During 2010, our used vehicle unit volume increased significantly compared to 2009, primarily due to the continued implementation of our standardized used vehicle merchandising process. This process allows us to price

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our used vehicles more competitively, market them more effectively and physically move certain used vehicles to specific dealerships within a particular region that have shown success in retailing that specific type of used vehicle. Our import dealerships used unit sales volume increased 21.5% compared to 2009. Our domestic and luxury dealerships used unit sales increased by 19.9% and 17.0%, respectively.

In 2010, gross profit per unit from used vehicles declined compared to the prior year due in part to a shift toward purchasing more vehicles from auction as obtaining vehicles through trade did not fulfill our used inventory requirements. However, obtaining more used vehicles from auction allowed us to better implement the standardized used vehicle merchandising process, as buying cars at auction allowed us to optimize the used vehicle inventory mix at each dealership, increasing unit sales and overall gross profit.

In 2009, the overall increase in gross profit when compared to 2008 can be mainly attributed to rebounding consumer confidence levels despite a challenging consumer credit environment. Gross margin rates for used vehicles declined in 2009 compared to 2008 primarily due to sourcing more vehicles through wholesale auctions versus trades and actively managing our vehicle days supply, resulting in more favorable pricing to customers.

Wholesale Vehicles

Wholesale vehicle revenues are highly correlated with new and used vehicle retail sales and the associated trade-in volume. Wholesale revenues are also significantly affected by our corporate inventory management policies, which are designed to optimize our total used vehicle inventory. Following is information related to wholesale vehicles:

	For the Year-Ended December 31,		Better/(Worse) %	
	2009	2010	Change	Change
	(In thousands, except units and per unit data)			
Revenue	\$ 147,002	\$ 149,041	\$ 2,039	1.4%
Gross loss	\$ (5,486)	\$ (5,041)	\$ 445	8.1%
Unit sales	25,271	24,128	(1,143)	(4.5%)
Revenue per unit	\$ 5,817	\$ 6,177	\$ 360	6.2%
Gross loss per unit	\$ (217)	\$ (209)	\$ 8	3.7%
Gross loss as a % of revenue	(3.7%)	(3.4%)	30bps	

	For the Year-Ended December 31,		Better/(Worse) %	
	2008	2009	Change	Change
	(In thousands, except units and per unit data)			
Revenue	\$ 272,172	\$ 147,002	\$ (125,170)	(46.0%)
Gross loss	\$ (6,191)	\$ (5,486)	\$ 705	11.4%
Unit sales	35,802	25,271	(10,531)	(29.4%)
Revenue per unit	\$ 7,602	\$ 5,817	\$ (1,785)	(23.5%)
Gross loss per unit	\$ (173)	\$ (217)	\$ (44)	(25.4%)
Gross loss as a % of revenue	(2.3%)	(3.7%)	(140)bps	

During 2010, there was a decrease in wholesale unit sales, in part due to an increased focus on selling vehicles through our retail channel. Further, consumer demand has increased in 2010 for used vehicles which historically would have been wholesaled. Consequently, pre-owned vehicles are in higher demand and are staying on the lot for less time, resulting in lower wholesale volume. Wholesale vehicle gross loss decreased in 2010 compared to 2009 as a result of the decreased unit sales combined with a lower gross loss per unit.

During 2009, there was a decrease in wholesale gross loss due primarily to decreased wholesale unit sales, offset by a higher gross loss per unit. The decrease in wholesale unit volume and gross margins compared to 2008 can be primarily attributed to our increased focus on retailing used vehicles which historically we would have disposed of through the wholesale market and fewer vehicles received in trades for new and used vehicles.

Table of Contents**Parts, Service and Collision Repair (Fixed Operations)**

Parts and service revenue consists of customer requested repairs (customer pay), warranty repairs, retail parts, wholesale parts and collision repairs. Parts and service revenue is driven by the mix of warranty repairs versus customer pay repairs, available service capacity, vehicle quality, customer loyalty and manufacturer warranty programs.

We believe that over time, vehicle quality will improve, but vehicle complexity will offset any revenue lost from improvement in vehicle quality. We also believe that over the long-term we have the ability to continue to add service capacity and increase revenues. However, based on current market conditions, we do not anticipate a near-term increase in additional service capacity. Manufacturers continue to extend new vehicle warranty periods and have also begun to include regular maintenance items in the warranty coverage. These factors, over the long-term, combined with the extended manufacturer warranties on CPO vehicles (see the discussion in Business Business Strategy Certified Pre-Owned Vehicles above), should facilitate long-term growth in our service and parts business. Barriers to long-term growth may include reductions in the rate paid by manufacturers to dealers for warranty work performed. Following is information related to fixed operations:

	For the Year-Ended December 31,		Better / (Worse) %	
	2009	2010	Change	Change
	(In thousands)			
Revenue				
Parts	\$ 581,056	\$ 599,348	\$ 18,292	3.1%
Service	443,247	479,759	36,512	8.2%
Collision Repair	47,522	48,947	1,425	3.0%
Total	\$ 1,071,825	\$ 1,128,054	\$ 56,229	5.2%
Gross profit				
Parts	\$ 199,193	\$ 199,850	\$ 657	0.3%
Service	314,227	335,377	21,150	6.7%
Collision Repair	26,891	26,833	(58)	(0.2%)
Total	\$ 540,311	\$ 562,060	\$ 21,749	4.0%
Gross profit as a % of revenue				
Parts	34.3%	33.3%	(100)bps	
Service	70.9%	69.9%	(100)bps	
Collision Repair	56.6%	54.8%	(180)bps	
Total	50.4%	49.8%	(60)bps	

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	For the Year-Ended December 31,		Better/(Worse) Change	% Change
	2008	2009 (In thousands)		
Revenue				
Parts	\$ 589,758	\$ 581,056	\$ (8,702)	(1.5%)
Service	454,534	443,247	(11,287)	(2.5%)
Collision Repair	51,482	47,522	(3,960)	(7.7%)
Total	\$ 1,095,774	\$ 1,071,825	\$ (23,949)	(2.2%)
Gross profit				
Parts	\$ 202,973	\$ 199,193	\$ (3,780)	(1.9%)
Service	317,212	314,227	(2,985)	(0.9%)
Collision Repair	28,891	26,891	(2,000)	(6.9%)
Total	\$ 549,076	\$ 540,311	\$ (8,765)	(1.6%)
Gross profit as a % of revenue				
Parts	34.4%	34.3%	(10)bps	
Service	69.8%	70.9%	110bps	
Collision Repair	56.1%	56.6%	50bps	
Total	50.1%	50.4%	30bps	

Our total fixed operations revenues increased in 2010 compared to 2009, led by increases at our Cadillac, BMW, and Toyota dealerships which all experienced significant fixed operations revenue increases in 2010 compared to 2009, accounting for 49.1% of the year-over-year improvement in overall fixed operations revenues. Overall customer pay sales increased \$15.1 million, or 3.0%, during 2010. Internal sales, primarily related to reconditioning work on used vehicles, increased \$20.0 million, or 15.6%, compared to 2009. Warranty sales decreased \$3.5 million, or 1.8%, in 2010 compared to 2009, primarily due to decreases at our BMW dealerships partially offset by an 86.3% increase in warranty sales at our Toyota dealerships due to the 2010 Toyota recalls discussed previously. Our Lexus dealerships experienced a 7.2% decrease in warranty sales in 2010 due to the Lexus recalls that occurred in 2009.

Our fixed operations gross profit increased \$21.7 million, or 4.0%, in 2010 compared to 2009. An increase in fixed operations revenue contributed approximately \$28.2 million in gross profit increase, partially offset by a \$6.5 million decrease in gross profit due to a 60 basis point decline in the gross margin rate.

Fixed operations revenues decreased \$23.9 million, or 2.2%, during 2009 compared to 2008, primarily due to an \$11.0 million, or 13.9%, decrease at our Cadillac dealerships and a \$10.7 million, or 7.2%, decrease at our Honda dealerships. Customer pay sales remained flat in 2009 compared to 2008. Warranty sales decreased \$10.6 million, or 5.3%, during 2009 compared to 2008, which was primarily caused by decreases at our BMW and Mercedes dealerships. Our fixed operations gross profit decreased \$8.8 million, or 1.6%, during 2009 compared to 2008, primarily due to a \$10.7 million, or 7.2%, gross profit decrease at our Honda dealerships.

As of December 31, 2010, we operated 25 collision repair centers. Reported collision repair revenues increased \$1.4 million, or 3.0%, during 2010 compared to 2009, primarily due to an increase in sublet revenues of \$0.8 million, or 14.6%. Collision repair revenues decreased \$4.0 million, or 7.7%, during 2009 compared to 2008, primarily due to a decline in customer pay revenues of \$3.0 million, or 8.3%.

Finance, Insurance and Other (F&I)

Finance, insurance and other revenues include commissions for arranging vehicle financing and insurance, sales of third-party extended service contracts for vehicles and other aftermarket products. In connection with vehicle financing, service contracts, other aftermarket products and insurance contracts, we receive commissions from the providers for originating contracts.

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Rate spread is another term for the commission earned by our dealerships for arranging vehicle financing for consumers. The amount of the commission could be zero, a flat fee or an actual spread between the interest rate charged to the consumer and the interest rate provided by the direct financing source (bank, credit union or manufacturers captive finance company). We have established caps on the potential rate spread our dealerships can earn with all finance sources. We believe the rate spread we earn for arranging financing represents value to the consumer in numerous ways, including the following:

Lower cost, below-market financing is often available only from the manufacturers captives and franchised dealers;

Generally easy access to multiple high-quality lending sources;

Lease-financing alternatives are largely available only from manufacturers captives or other indirect lenders;

Customers with substandard credit frequently do not have direct access to potential sources of sub-prime financing; and

Customers with significant negative equity in their current vehicle (i.e., the customer's current vehicle is worth less than the balance of their vehicle loan or lease obligation) frequently are unable to pay off the loan on their current vehicle and finance the purchase or lease of a replacement new or used vehicle without the assistance of a franchised dealer.

F&I revenues are driven by the level of new and used vehicle unit sales, manufacturer financing or leasing incentives and our F&I penetration rate. The F&I penetration rate represents the percentage of vehicle sales on which we are able to originate financing or sell extended service contracts, other aftermarket products or insurance contracts. Our finance penetration rates increased to 67.8% in 2010 from 65.0% in 2009. Our extended service contract penetration rates declined to 26.1% in 2010 from 30.2% in 2009. Further, the aftermarket products penetration rate increased to 87.0% in 2010 from 82.9% in 2009. Penetration rates were positively impacted by a strengthening economy and increasing consumer confidence, combined with an effective roll-out of our F&I best practices during 2010. Following is information related to F&I:

	For the Year-Ended December 31,		Better/(Worse)	
	2009	2010	Change	% Change
	(In thousands, except per unit data)			
Revenue	\$ 154,696	\$ 180,968	\$ 26,272	17.0%
Gross profit per retail unit (excluding fleet)	\$ 929	\$ 957	\$ 28	3.0%

	For the Year-Ended December 31,		Better/(Worse)	
	2008	2009	Change	% Change
	(In thousands, except per unit data)			
Revenue	\$ 180,274	\$ 154,696	\$ (25,578)	(14.2%)
Gross profit per retail unit (excluding fleet)	\$ 1,015	\$ 929	\$ (86)	(8.5%)

F&I revenues increased during 2010 compared to 2009 primarily due to an increase in total new and used retail (excluding fleet) unit volume of 22,651 units, or 13.6%, increased penetration rates and higher profit per unit. Gross profit per retail unit increased 3.0% in 2010 compared to 2009, primarily due to better pricing on finance contracts in 2010 and a 19.2% increase in aftermarket products sold. Finance contracts may be under pressure in the event manufacturers offer attractive financing rates from their captive finance affiliates as we tend to earn lower commissions under these programs.

F&I revenues decreased during 2009 when compared to 2008 primarily due to a decrease in total new and used retail (excluding fleet) unit volume of 11,224 or 6.3%. In addition to the unit decline, F&I gross profit per unit decreased during 2009 when compared to 2008. This decrease in F&I revenue per unit can be attributed to a decrease in finance contract penetration rates to 65.0% in 2009 from 69.4% in 2008 and a decrease in service contract penetration rates to 30.2% in 2009 from 32.8% in 2008.

Table of Contents***Selling, General and Administrative (SG&A) Expenses***

SG&A expenses are comprised of four major groups: compensation expense, advertising expense, rent and rent related expense, and other expense. Compensation expense primarily relates to dealership personnel who are paid a commission or a modest salary plus commission (which typically vary depending on gross profits realized) and support personnel who are paid a fixed salary. Due to the salary component for certain dealership and corporate personnel, gross profits and compensation expense do not change in direct proportion to one another. Advertising expense and other expenses vary based on the level of actual or anticipated business activity and number of dealerships owned. Rent and rent related expense typically varies with the number of dealerships owned, investments made for facility improvements and interest rates. Although not completely correlated, we believe the best way to measure SG&A expenses are as a percentage of gross profit. Following is information related to our SG&A expenses:

	For the Year-Ended December 31,		Better/(Worse) %	
	2009	2010	Change	Change
	(In thousands)			
Compensation	\$ 470,293	\$ 526,577	\$ (56,284)	(12.0%)
Advertising	44,736	46,908	(2,172)	(4.9%)
Rent and Rent Related	131,262	130,739	523	0.4%
Other	182,929	192,473	(9,544)	(5.2%)
Total	\$ 829,220	\$ 896,697	\$ (67,477)	(8.1%)
SG&A as a % of gross				
Compensation	45.5%	47.2%	(170)bps	
Advertising	4.3%	4.2%	10bps	
Rent and Rent Related	12.7%	11.7%	100bps	
Other	17.8%	17.3%	50bps	
Total	80.3%	80.4%	(10)bps	

	For the Year-Ended December 31,		Better/(Worse) %	
	2008	2009	Change	Change
	(In thousands)			
Compensation	\$ 489,922	\$ 470,293	\$ 19,629	4.0%
Advertising	56,837	44,736	12,101	21.3%
Rent and Rent Related	133,278	131,262	2,016	1.5%
Other	226,206	182,929	43,277	19.1%
Total	\$ 906,243	\$ 829,220	\$ 77,023	8.5%

SG&A as a % of gross

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Compensation	44.2%	45.5%	(130)bps
Advertising	5.1%	4.3%	80bps
Rent and Rent Related	12.0%	12.7%	(70)bps
Other	20.6%	17.8%	280bps
Total	81.9%	80.3%	160bps

2010 Compared to 2009

Total SG&A expenses increased both in dollar amount and as a percentage of gross profit in 2010. The increase can be attributed to the increases in revenue and gross profit as well as higher compensation costs.

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In 2010, total compensation expense increased in both dollar amount and as a percentage of gross profit compared to 2009. Compensation costs were higher in the first half of 2010 and improved in the latter half of the year when pay plans were adjusted to compensate for higher than expected retail activity.

Advertising expense increased in dollar amount but improved slightly as a percentage of gross profit. Total advertising costs were higher versus prior year primarily due to the rebound in economic activity in 2010.

In 2010, rent and rent related expenses remained flat as compared to 2009. As a percentage of gross profit, rent and rent related expenses decreased in 2010 compared to 2009, primarily due to increases in gross profit resulting from an improved sales environment.

Other SG&A expenses increased compared to 2009, primarily due to higher insurance related expenses and investments in our employees through training. Other SG&A as a percentage of gross profit decreased due to gross profit increases in an improved economic environment.

2009 Compared to 2008

Total SG&A expenses decreased both in dollar amount and as a percentage of gross profit in 2009 as compared to 2008. The dollar decrease can be attributed to lower sales volume in 2009, while the decrease as a percentage of gross profit is primarily attributable to reductions in other SG&A expenses due to hail and hurricane damage, loss on marketable securities and legal expenses incurred in 2008.

In 2009, total reported compensation expense decreased compared to 2008. However, as a percentage of gross profit, total compensation expense increased. The dollar decrease was the result of overall declines in retail volume due to a slow sales environment which led to lower sales commissions. The unfavorable increase as a percentage of gross profit was primarily the result of sales compensation not being perfectly correlated with changes in gross profit.

Advertising expense decreased both in dollar amount and as a percentage of gross profit in 2009 compared to 2008. Total advertising costs were lower versus prior year due to adjustments in advertising strategies in response to the soft operating environment and an overall effort to reduce costs in 2009. In addition, during 2009 we shifted our advertising strategy away from traditional media and more towards internet and other outlets.

Rent and rent related expenses decreased slightly in 2009 as compared to 2008. Rent and rent related expenses were negatively impacted by lease exit charges recorded in 2008. As a percentage of gross profit, rent and rent related expenses increased slightly in 2009 compared to 2008 due to declines in gross profit in a slower sales environment in 2009.

Other SG&A expenses decreased in 2009 as compared to 2008, primarily due to our efforts to reduce costs in 2009. Further, we incurred \$4.4 million of hail and hurricane damage and loss on marketable securities of \$6.4 million in 2008. In 2009, there were no significant losses from weather events and we recorded a \$3.8 million gain on marketable securities, further contributing to the decrease.

Impairment Charges

Impairment charges decreased \$23.3 million from 2009 to 2010 due to impairment charges recorded in 2009 and no significant charges in 2010 related to goodwill, franchise assets and fixed assets. See the table and discussion included under the previous heading **Impairments and Other Charges** for a detail of other impairment charges recorded during 2009 and 2010.

In 2009, impairment charges decreased \$788.5 million compared to 2008 primarily due to goodwill impairment recorded in 2008. See the table and discussion included under the previous heading Impairments and Other Charges for a detail of impairment charges recorded during 2009 and 2008.

Depreciation and Amortization

Depreciation expense increased \$0.2 million, or 0.7%, in 2010 compared to 2009, and \$2.1 million, or 6.6%, in 2009 compared to 2008. The increases were primarily related to additions to gross property and equipment of

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\$35.0 million in 2010 and \$31.2 million in 2009 related to continuing operations, excluding land and construction in progress. The increases in depreciable property were due in part to our strategic shift to continue to own and hold more dealership properties. Also, the increase in 2010 compared to 2009 was partially due to infrastructure investments in facilities that were completed and transferred out of construction in progress and placed into service in 2010.

Interest Expense, Floor Plan

Interest expense, floor plan for new vehicles increased \$1.1 million, or 6.2%, in 2010 compared to 2009. The average new vehicle floor plan interest rate related to new vehicles incurred by continuing dealerships was 2.69% for the year ended December 31, 2010, compared to 2.50% for the year ended December 31, 2009, which increased interest expense by approximately \$1.4 million. The average floor plan balance for new vehicles decreased by \$11.0 million in 2010, resulting in a decrease in expense of approximately \$0.3 million.

Interest expense, floor plan for used vehicles incurred by continuing operations increased \$0.6 million, or 37.1%, in 2010 compared to 2009. Before considering used vehicle floor plan interest expense allocated to discontinued operations for the year ended December 31, 2009 of \$0.2 million, the weighted average used vehicle floor plan interest rate incurred by both continuing and discontinued operations was 2.88% for the year ended December 31, 2010, compared to 2.31% for the year ended December 31, 2009, which increased interest expense by approximately \$0.4 million. The average used vehicle floor plan notes payable balance from continuing and discontinued dealerships increased \$2.2 million in 2010 compared to 2009, resulting in an increase in used vehicle floor plan interest expense of approximately \$0.1 million.

Interest expense, floor plan for new vehicles decreased \$21.6 million, or 54.2%, in 2009 compared to 2008. The average floor plan interest rate for new vehicles incurred by continuing dealerships was 2.50% for the year ended December 31, 2009, compared to 4.12% for the year ended December 31, 2008, which decreased interest expense by approximately \$11.8 million. During 2009 the average floor plan balance for new vehicles decreased \$237.3 million which resulted in a decrease in expense of approximately \$9.8 million.

Interest expense, floor plan for used vehicles incurred by continuing operations decreased \$2.0 million, or 55.5%, in 2009 compared to 2008. Before considering used vehicle floor plan interest expense allocated to discontinued operations for the year ended December 31, 2009 and December 31, 2008 of \$0.2 million and \$0.6 million, respectively, the weighted average used vehicle floor plan interest rate incurred by both continuing and discontinued operations was 2.31% for the year ended December 31, 2009, compared to 4.37% for the year ended December 31, 2008, which decreased interest expense by approximately \$1.6 million. The average used vehicle floor plan notes payable balance from continuing and discontinued dealerships decreased \$19.0 million in 2009 compared to 2008, resulting in a decrease in used vehicle floor plan interest expense of approximately \$0.7 million.

Table of Contents***Interest Expense, Other, Net***

Interest expense, other, net, was \$59.0 million, \$78.3 million and \$63.4 million in 2008, 2009 and 2010, respectively. Changes in interest expense, other, net, are summarized in the schedule below:

	2009		2010
	Increase (Decrease) in Interest Expense		Increase (Decrease) in Interest Expense (In millions)
Debt balances			
- Increase (decrease) in debt balances	\$ (2.1)	\$	(3.6)
Other factors			
- (Increase) decrease in capitalized interest	0.8		(1.6)
- Incremental interest expense (benefit) related to variable to fixed rate swaps(1)	6.1		(0.9)
- Incremental interest expense (benefit) related to fixed rate to variable swaps(1)	0.8		
- Interest expense (benefit) allocation to discontinued operations	1.1		1.8
- Increase (decrease) in deferred loan cost amortization(2)	11.7		(10.3)
- Increase (decrease) in other expense, net	0.9		(0.3)
	\$ 19.3	\$	(14.9)

(1) Represent difference in cash payments to and from the counterparty.

(2) Includes loan costs related to the issuance of the 6.0% Convertible Notes and amendments to the 2006 Credit Facility.

Interest Expense, Non-Cash, Convertible Debt

Non-cash convertible debt interest expense for the year ended December 31, 2010 is comprised of the amortization of the debt discount and deferred loan costs associated with our 5.0% Convertible Notes and 4.25% Convertible Notes. The initial debt discount was determined based on a valuation of the debt component of these notes and is being amortized monthly to interest expense over the expected life of the notes.

Interest expense of approximately \$10.7 million, \$6.2 million and \$0.5 million in 2008, 2009 and 2010, respectively, represents the non-cash amortization of the debt discount associated with the 5.25% Convertible Notes and 4.25% Convertible Notes. Interest expense of approximately \$1.2 million and \$5.1 million in 2009 and 2010, respectively, was recorded related to amortization of the debt discount on the 5.0% Convertible Notes. Interest expense of approximately \$4.1 million in 2009 represents the non-cash amortization of the debt discount associated with the 6.0% Convertible Notes. We recognized a non-cash benefit of \$11.3 million for the year ended December 31, 2009 due to the extinguishment of the derivative liability associated with the redemption of our 6.0% Convertible Notes during 2009. Deferred loan cost amortization related to the 4.25% Convertible Notes and 5.0% Convertible

Notes was \$1.3 million for the year ended December 31, 2010.

Interest expense, non-cash, convertible debt is summarized in the schedule below:

	Year Ended December 31,		
	2008	2009	2010
	(In millions)		
Amortization of debt discount	\$ 10.7	\$ 11.5	\$ 5.6
Amortization of deferred loan costs		0.5	1.3
Mark-to-market on derivative liability		(11.3)	
	\$ 10.7	\$ 0.7	\$ 6.9

Table of Contents***Interest Expense/Amortization, Non-Cash, Cash Flow Swaps***

We have entered into the Fixed Swaps to effectively convert a portion of our LIBOR-based variable rate debt to a fixed rate, in order to reduce our exposure to market risks from fluctuations in interest rates. As a result of the refinancing of our 2006 Credit Facility and the new terms of the 2010 Credit Facilities, it is no longer probable that we will incur interest payments that match the terms of certain Fixed Swaps that previously were designated and qualified as cash flow hedges, as we would be borrowing certain amounts under the Silo Floor Plan Facilities rather than under the new 2010 Credit Facilities. Certain of the lenders' terms under the Silo Floor Plan Facilities did not match the terms of our Fixed Swaps that previously qualified as cash flow hedges. Of the Fixed Swaps (including the two \$100.0 million notional swaps which were settled in 2009), \$565.0 million of the notional amount had previously been documented as hedges against the variability of cash flows related to interest payments on certain debt obligations. At December 31, 2010, we estimate that under the new 2010 Credit Facilities and other facilities with matching terms, it is probable that the expected debt balance with interest payments that match the terms of the Fixed Swaps will be \$400.0 million. As a result, for the years ended December 31, 2010 and December 31, 2009, non-cash charges of approximately \$4.9 million and \$11.8 million, respectively, related to the Fixed Swaps and amortization of amounts in accumulated other comprehensive income (loss) related to other existing and terminated cash flow swaps were included in interest expense/amortization, non-cash, cash flow swaps in the accompanying Consolidated Statements of Income. Changes in the fair value of notional amounts of certain cash flow swaps are recognized through earnings. See the heading *Derivative Instruments and Hedging Activities* in Note 6 *Long-Term Debt*, in the accompanying notes to the Consolidated Financial Statements for further discussion.

For the Fixed Swaps which qualify as cash flow hedges, the changes in the fair value of these swaps have been recorded in other comprehensive income (loss), net of related income taxes in the Consolidated Statements of Stockholders' Equity. The incremental interest expense (the difference between interest paid and interest received) related to the Fixed Swaps was \$17.6 million in 2010, \$18.5 million in 2009 and \$12.4 million in 2008, and is included in interest expense, other, net, in the accompanying Consolidated Statements of Income. The estimated net expense expected to be reclassified out of other comprehensive income (loss) into results of operations during the year ended December 31, 2011 is approximately \$10.8 million.

Other Income (Expense), Net

We recorded a loss on extinguishment of debt of approximately \$7.7 million in the year ended December 31, 2010, related to the retirement of \$232.1 million in aggregate principal amount of the 8.625% Notes. For the year ended December 31, 2009, other income (expense), net, includes a gain of approximately \$0.4 million on the repurchase of a portion of the 4.25% Convertible Notes at a discount and a gain of approximately \$0.1 million related to the derecognition of liability and equity components of the 4.25% Convertible Notes upon repurchase of a portion of the 4.25% Convertible Notes during the third and fourth quarter of 2009. These gains were offset by a loss of approximately \$7.2 million related to the write-off of the unamortized debt discount associated with the redemption of the 6.0% Convertible Notes during the fourth quarter of 2009. See Note 6, *Long-Term Debt*, in the notes to the accompanying Consolidated Financial Statements for further discussion.

Provision for Income Taxes

The effective tax rate from continuing operations was (22.3%) in 2010, (105.0%) in 2009 and 16.2% in 2008. In 2010 and 2009, a reduction of valuation allowances on deferred tax assets and other tax adjustments of \$48.2 million and \$41.3 million, respectively, resulted in an overall tax benefit from continuing operations. Excluding the effect of these items, the effective tax rate from continuing operations would have been 43.2% and 39.9% for the years ended December 31, 2009 and 2010, respectively. The 2008 effective tax rate for continuing operations was affected by valuation allowance and other account adjustments as well as the effect of non-deductible goodwill. Absent these

items the effective tax rate for the year ended December 31, 2008 would have been 38.5%. Our effective tax rate varies from year to year based on the distribution of taxable income between states in which we operate. We expect the effective tax rate in future periods to fall within a range of 38.0% to 41.0% before the impact, if any, of changes in valuation allowances related to deferred income tax assets.

Table of Contents***Discontinued Operations***

The pre-tax losses from operations and the sale of discontinued franchises were as follows:

	Year Ended December 31,		
	2008	2009	2010
	(In thousands)		
Loss from operations	\$ (20,103)	\$ (12,579)	\$ (6,634)
Gain (loss) on disposal of franchises	(2,325)	(293)	2,629
Lease exit charges	(13,747)	(30,794)	(4,232)
Property impairment charges	(14,912)	(4,992)	
Goodwill impairment charges	(2,025)	(1,586)	
Franchise agreement and other asset impairment charges	(20,500)		
Favorable lease asset impairment charges	(1,903)		
Pre-tax loss	\$ (75,515)	\$ (50,244)	\$ (8,237)
Total revenues	\$ 587,801	\$ 294,390	\$ 55,077

Loss from discontinued operations has declined from 2008 levels due to the disposal of under-performing franchises which incurred significant operating losses in the periods prior to their disposal. For a description of the impairment and other charges taken for the years ended December 31 2010, 2009 and 2008, see the discussion under the previous heading *Impairments and Other Charges*.

Adjusted Results of Operations

Along with the evaluation of our performance presented on a basis consistent with GAAP, we believe there is benefit in evaluating our results of operations exclusive of certain significant items which affect the comparability of results between periods. The *As Adjusted* columns below are not measures of financial performance under GAAP. Accordingly, they should not be considered as substitutes for their *As Reported* GAAP counterparts, which are prepared in accordance with GAAP. Although we find these non-GAAP results useful in evaluating the performance of our business, our reliance on these measures is limited because the adjustments often have a material impact on our financial statements presented in accordance with GAAP. Therefore, we typically use these *As Adjusted* amounts in conjunction with our GAAP results to address these limitations. See the previous discussion in this section under the heading *Impairments and Other Charges* for discussion of the adjustments in

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the table below, which reconciles adjusted results of operations (a non-GAAP measure) to the results of operations presented in the accompanying Consolidated Statements of Income in accordance with GAAP.

	2008		Year Ended December 31, 2009			2010		As Adjusted	
	As Reported	Adjustments	As Adjusted (\$ in millions, shares in thousands, except per share data)	As Reported	Adjustments	As Adjusted	As Reported		Adjustments
Revenues	\$ 6,900.2	\$	\$ 6,900.2	\$ 6,055.3	\$	\$ 6,055.3	\$ 6,880.8	\$	\$ 6,880.8
Operating profit	1,107.2		1,107.2	1,032.7		1,032.7	1,114.7		1,114.7
Expenses, general and administrative									
Depreciation and amortization	(906.3)	21.5	(884.8)	(829.2)	4.0	(825.2)	(896.8)	0.6	(896.2)
Restructuring charges	(812.0)	812.0		(23.5)	23.5		(0.2)	0.2	
Goodwill impairment									
Provision for doubtful accounts	(32.7)		(32.7)	(34.9)		(34.9)	(35.1)		(35.1)
Operating income	(643.8)	833.5	189.7	145.1	27.5	172.6	182.6	0.8	183.4
Other income (expense):									
Restructuring expense, plan	(43.4)		(43.4)	(19.8)		(19.8)	(21.5)		(21.5)
Restructuring expense, net	(59.0)		(59.0)	(78.3)	12.0	(66.3)	(63.3)	1.5	(64.8)
Restructuring expense, cash	(10.7)		(10.7)	(12.5)	0.5	(12.0)	(11.8)	4.9	(7.9)
Restructuring income (expense), net	0.8		0.8	(6.6)	6.7	0.1	(7.6)	7.7	(7.5)
Other expense	(112.3)		(112.3)	(117.2)	19.2	(98.0)	(104.2)	14.1	(90.1)
Income (loss) from continuing operations before income tax benefit (expense)	(756.1)	833.5	77.4	27.9	46.7	74.6	78.4	14.9	93.3
Income tax benefit (expense)	122.3	(146.3)(1)	(24.0)	29.3	(61.5)(3)	(32.2)	17.5	(54.0)(5)	(36.5)
Income (loss) from continuing operations	(633.8)	687.2	53.4	57.2	(14.8)	42.4	95.9	(39.1)	56.8
Income (loss) from discontinued operations	(58.5)	46.9(2)	(11.6)	(25.7)	15.5(4)	(10.2)	(6.0)	0.7(6)	(5.3)
Income (loss)	\$ (692.3)	\$ 734.1	\$ 41.8	\$ 31.5	\$ 0.7	\$ 32.2	\$ 89.9	\$ (38.4)	\$ 51.5

earnings (loss)										
Common share:										
Earnings (loss) per										
from										
Continuing										
operations	\$ (15.70)	\$ 17.01	\$ 1.31	\$ 1.29	\$ (0.33)	\$ 0.96	\$ 1.82	\$ (0.74)	\$	
per share from										
discontinued										
operations	(1.46)	1.17	(0.29)	(0.58)	0.35	(0.23)	(0.12)	0.02	(0.02)	
Earnings (loss) per										
Common share	\$ (17.16)	\$ 18.18	\$ 1.02	\$ 0.71	\$ 0.02	\$ 0.73	\$ 1.70	\$ (0.72)	\$	
Weighted average										
Shares outstanding	40,356		40,356	43,836		43,836	52,214			52,214
Adjusted earnings										
per common										
share										
Earnings (loss) per										
from										
Continuing										
operations	\$ (15.70)	\$ 17.01	\$ 1.31	\$ 1.07	\$ (0.26)	\$ 0.81	\$ 1.58	\$ (0.59)	\$	
per share from										
discontinued										
operations	(1.46)	1.17	(0.29)	(0.45)	0.27	(0.18)	(0.09)	0.01	(0.02)	
Earnings (loss) per										
Common share	\$ (17.16)	\$ 18.18	\$ 1.02	\$ 0.62	\$ 0.01	\$ 0.63	\$ 1.49	\$ (0.58)	\$	
Weighted average										
Shares outstanding	40,356		40,556	55,832		55,832	65,794			65,794

- (1) Tax effect of the pre-tax adjustments above in addition to expense of \$111.6 million related to valuation allowance and other tax adjustments.
- (2) Tax-effected adjustments to discontinued operations in addition to expense of \$3.4 million related to valuation allowance and other tax adjustments.
- (3) Tax effect of the pre-tax adjustments above in addition to a benefit of \$41.3 million related to valuation allowance and other tax adjustments.

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- (4) Tax-effected adjustments to discontinued operations in addition to a benefit of \$6.1 million related to valuation allowance and other tax adjustments.
- (5) Tax effect of the pre-tax adjustments above in addition to a benefit of \$48.2 million related to valuation allowance and other tax adjustments.
- (6) Tax-effected adjustments to discontinued operations.

Liquidity and Capital Resources

We require cash to fund debt service, operating lease obligations, working capital requirements and to finance acquisitions. We rely on cash flows from operations, borrowings under our revolving credit and floor plan borrowing arrangements, real estate mortgage financing, asset sales and offerings of debt and equity securities to meet these requirements. Our liquidity could be negatively affected if we fail to comply with the financial covenants in our existing debt or lease arrangements. Cash flows provided by our dealerships are derived from various sources. The primary sources include individual consumers, automobile manufacturers, automobile manufacturers captive finance subsidiaries and finance companies. Disruptions in these cash flows can have a material and adverse impact on our operations and overall liquidity.

Because the majority of our consolidated assets are held by our dealership subsidiaries, the majority of our cash flows from operations are generated by these subsidiaries. As a result, our cash flows and ability to service our obligations depends to a substantial degree on the cash generated from the operations of these dealership subsidiaries.

In 2010, our overall debt maturity position improved as a result of the refinancing of our credit facilities in January 2010 and the issuance of our 9.0% Notes in March 2010. During 2010, we also redeemed \$232.1 million in aggregate principal amount of our 8.625% Notes and the remaining \$17.0 million in aggregate principal amount of our 4.25% Convertible Notes.

In 2010, our operational performance began to rebound as the economy and the automotive retail industry environment improved coming out of the economic crisis that began in the fourth quarter of 2008. Average industry expectations for new vehicle sales volume in 2011 are between 12.0 million and 13.0 million vehicles which, if realized, would be an increase of 3.4% to 12.1% from the 2010 level. This suggests a steady improvement in automotive retailing in 2011. We believe our current capital structure and the expected results of our operating activities will enable us to continue to service our liquidity requirements.

Long-Term Debt and Credit Facilities

2010 Credit Facilities

Our 2010 Credit Facilities, executed on January 15, 2010, provide a total of up to \$521.0 million in combined revolving credit and floor plan financing.

Under the terms of the 2010 Credit Facilities, up to \$321.0 million is available for new vehicle inventory floor plan financing (the 2010 New Vehicle Floor Plan Sub-Facility), up to \$50.0 million is available for used vehicle inventory floor plan financing (the 2010 Used Vehicle Floor Plan Sub-Facility) and up to \$150.0 million is available for working capital and general corporate purposes (the 2010 Revolving Credit Facility). The 2010 Credit Facilities mature on August 15, 2012. We also have capacity to finance new and used vehicle inventory purchases under bilateral floor plan agreements with various manufacturer-affiliated finance companies and other lending institutions (the Silo Floor

Plan Facilities).

Availability under our 2010 Revolving Credit Facility is calculated as the lesser of \$150.0 million or a borrowing base calculated based on certain eligible assets plus 50% of the fair market value of 5,000,000 shares of common stock of Speedway Motorsports, Inc. that are pledged as collateral (the 2010 Revolving Borrowing Base). The 2010 Revolving Credit Facility may be expanded up to \$215.0 million upon satisfaction of certain conditions. A withdrawal of this pledge by Sonic Financial Corporation (SFC), which holds the 5,000,000 shares of common stock of Speedway Motorsports, Inc., or a significant decline in the value of Speedway Motorsports, Inc. common stock, could reduce the amount we can borrow under the 2010 Revolving Credit Facility.

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The 2010 Revolving Borrowing Base was approximately \$145.6 million at December 31, 2010. The amount available to be borrowed under the 2010 Revolving Credit Facility is calculated by subtracting the sum of (1) any outstanding borrowings plus (2) the cumulative face amount of any outstanding letters of credit from the 2010 Revolving Borrowing Base. At December 31, 2010, we had no outstanding borrowings and \$47.7 million in outstanding letters of credit resulting in total borrowing availability of \$97.9 million.

Under the 2010 Revolving Credit Facility, the amounts outstanding bear interest at a specified percentage above LIBOR, ranging from 2.50% per annum to 4.00% per annum, (but, in any case, not less than 3.50% per annum through the end of the first quarter of 2011) according to a performance-based pricing grid determined by our Consolidated Total Debt to EBITDA Ratio as of the last day of the immediately preceding fiscal quarter (the Performance Grid).

Under the 2010 New Vehicle Floor Plan Sub-Facility, amounts outstanding bear interest at a specified percentage above LIBOR, ranging from 1.50% per annum to 2.25% per annum (but, in any case, not less than 2.00% per annum through the end of the first quarter of 2011), according to the Performance Grid. Under the 2010 Used Vehicle Floor Plan Sub-Facility, amounts outstanding bear interest at a specified percentage above LIBOR, ranging from 1.75% per annum to 2.50% per annum (but, in any case, not less than 2.25% per annum through the end of the first quarter of 2011), according to the Performance Grid.

Availability under our 2010 Used Vehicle Floor Plan Sub-Facility is calculated as the lesser of \$50.0 million or a borrowing base calculated based on certain eligible inventory, net of any liens or reserves (the 2010 Used Vehicle Borrowing Base). At December 31, 2010, the 2010 Used Vehicle Borrowing Base was approximately \$27.9 million and we had \$10.0 million in outstanding borrowings, resulting in total availability of approximately \$17.9 million.

The Silo Floor Plan Facilities provide financing for new and used vehicle inventory and bear interest at variable rates based on prime or LIBOR. Our obligations under the Silo Floor Plan Facilities are guaranteed by us and are secured by liens on substantially all of the assets of our respective dealership franchise subsidiaries that receive financing under these arrangements.

All amounts outstanding (including any outstanding letters of credit) under the 2010 Credit Facilities are secured by a pledge of substantially all of our assets and the assets of substantially all of our dealership franchise subsidiaries, in addition to the pledge of 5,000,000 shares of Speedway Motorsports, Inc. Common Stock owned by SFC. The collateral for the 2010 Credit Facilities also includes the pledge of the stock or equity interests of our dealership franchise subsidiaries, except where such a pledge is prohibited by the applicable vehicle manufacturer.

We agreed under the 2010 Credit Facilities not to pledge any assets to any third party, subject to certain stated exceptions, including floor plan financing arrangements. In addition, the 2010 Credit Facilities contain certain negative covenants, including covenants which could restrict or prohibit indebtedness, liens, the payment of dividends, capital expenditures and material dispositions of assets as well as other customary covenants and default provisions. Specifically, the 2010 Credit Facilities permit cash dividends on our Class A and Class B common stock so long as no event of default (as defined in the 2010 Credit Facilities) has occurred and is continuing and provided that we remain in compliance with all financial covenants under the 2010 Credit Facilities.

The 2010 Credit Facilities contain events of default, including cross-defaults to other material indebtedness, change of control events and events of default customary for syndicated commercial credit facilities. Upon the occurrence of an event of default, we could be required to immediately repay all outstanding amounts under the 2010 Credit Facilities. See Note 6, Long-Term Debt, in the accompanying Consolidated Financial Statements for further discussion of the 2010 Credit Facilities.

9.0% Notes

On March 12, 2010, we issued \$210.0 million in aggregate principal amount of 9.0% Notes which mature on March 15, 2018. On April 12, 2010, we used the net proceeds, together with cash on hand, to redeem \$200.0 million in aggregate principal amount of our 8.625% Notes due 2013. The 9.0% Notes are unsecured senior subordinated obligations and are guaranteed by our domestic operating subsidiaries and rank equal in right of payment to all of our and the subsidiary guarantors' existing and future senior subordinated indebtedness. Interest is payable semi-annually on March 15 and September 15 each year. We may redeem the 9.0% Notes in whole or in part at any time.

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after March 15, 2014 at the redemption prices in the following table, which are expressed as percentages of the principal amount. See Note 6, Long-Term Debt, in the accompanying Consolidated Financial Statements for further discussion of the 9.0% Notes.

	Redemption
Beginning on March 15, 2014	104.50%
Beginning on March 15, 2015	102.25%
Beginning on March 15, 2016 and thereafter	100.00%

8.625% Notes

As discussed above, during 2010 we redeemed \$200.0 million in aggregate principal amount of our 8.625% Notes using proceeds from the issuance of the 9.0% Notes. We also redeemed an additional \$32.1 million in aggregate principal amount of our 8.625% Notes using cash on hand. At December 31, 2010, we had \$42.9 million outstanding under the 8.625% Notes. Our obligations under the 8.625% Notes are guaranteed by our operating domestic subsidiaries. The 8.625% Notes are unsecured obligations that rank equal in right of payment to all of our and the subsidiary guarantors' existing and future senior subordinated indebtedness, mature on August 15, 2013 and are currently redeemable at our option. The redemption premiums for the twelve-month periods beginning August 15 of the years 2010 and 2011 are 101.438% and 100.000%, respectively. See Note 6, Long-Term Debt, in the accompanying Consolidated Financial Statements for further discussion of the 8.625% Notes.

5.0% Convertible Notes

On September 23, 2009, we issued \$172.5 million in principal of 5.0% Convertible Notes and 10,350,000 shares of Class A common stock. Net proceeds from these issuances were used to repurchase \$143.0 million in aggregate principal amount of our 4.25% Convertible Notes, \$85.6 million in aggregate principal amount of our 6.0% Convertible Notes and to repay amounts outstanding under the 2006 Credit Facility.

The 5.0% Convertible Notes bear interest at a rate of 5.0% per year, payable semiannually on April 1 and October 1 of each year and mature on October 1, 2029. We may redeem some or all of the 5.0% Convertible Notes for cash at any time subsequent to October 1, 2014 at a repurchase price equal to 100% of the principal amount of the Notes. Holders have the right to require us to purchase the 5.0% Convertible Notes on each of October 1, 2014, October 1, 2019 and October 1, 2024 or in the event of a change in control for cash at a purchase price equal to 100% of the principal amount of the notes.

Holder of the 5.0% Convertible Notes may convert their notes at their option prior to the close of business on the business day immediately preceding July 1, 2029 only under the following circumstances: (1) during any fiscal quarter commencing after December 31, 2009, if the last reported sale price of the Class A common stock for at least 20 trading days (whether or not consecutive) during a period of 30 consecutive trading days ending on the last trading day of the preceding fiscal quarter is greater than or equal to 130% of the applicable conversion price on each applicable trading day; (2) during the five business day period after any 10 consecutive trading day period (the measurement period) in which the trading price (as defined below) per \$1,000 principal amount of notes for each day of that measurement period was less than 98% of the product of the last reported sale price of our Class A common stock and the applicable conversion rate on each such day; (3) if we call any or all of the notes for redemption, the notes so called for redemption at any time prior to the close of business on the third scheduled trading day prior to the redemption date; or (4) upon the occurrence of specified corporate events. On and after July 1, 2029 to (and including) the close of business on the third scheduled trading day immediately preceding the maturity date, holders may convert

their notes at any time, regardless of the foregoing circumstances. The conversion rate is 74.7245 shares of Class A common stock per \$1,000 principal amount of notes, which is equivalent to a conversion price of approximately \$13.38 per share of Class A common stock. The 5.0% Convertible Notes were not convertible at any time in 2010.

To recognize the equity component of a convertible borrowing instrument, upon issuance of the 5.0% Convertible Notes in September 2009, we recorded a debt discount of \$31.0 million and a corresponding amount (net of taxes of \$12.8 million) to equity. The debt discount will be amortized to interest expense through October 2014, the

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earliest redemption date. See Note 6, *Long-Term Debt*, in the accompanying Consolidated Financial Statements for further discussion of the 5.0% Convertible Notes.

4.25% Convertible Notes

As discussed above, \$143.0 million in aggregate principal amount of the 4.25% Convertible Notes were repurchased in 2009, resulting in a gain of \$0.1 million recorded in other income (expense), net, in the accompanying Consolidated Statements of Income. In addition, the repurchase required the write-off of approximately \$7.1 million of unamortized debt discount, which was offset by a \$4.3 million adjustment to paid-in capital and a \$2.9 million adjustment to deferred income tax assets.

We repurchased approximately \$1.0 million in aggregate principal amount of the 4.25% Convertible Notes during the second quarter of 2010 at amounts close to par. In November 2010, we used cash on hand to extinguish the remaining \$16.0 million in aggregate principal amount of 4.25% Convertible Notes at the applicable redemption price (100.00% of principal redeemed) plus accrued but unpaid interest. The 4.25% Convertible Notes were not convertible at any time in 2010. See Note 6, *Long-Term Debt*, in the accompanying Consolidated Financial Statements for further discussion of the 4.25% Convertible Notes.

Notes Payable to a Finance Company

Three notes payable totaling \$26.6 million in aggregate principal were assumed with the purchase of certain dealerships during the second quarter of 2004 (the *Assumed Notes*). The Assumed Notes mature November 1, 2015 through September 1, 2016 and are collateralized by letters of credit. We recorded the Assumed Notes at fair value using an interest rate of 5.35%. Although the Assumed Notes allow for prepayment, the penalties and fees are disproportionately burdensome relative to the Assumed Notes' principal balance. Therefore, we do not currently intend to prepay the Assumed Notes.

Mortgage Notes

During 2010, we obtained \$21.2 million in mortgage financing related to four of our properties. During 2009, we obtained \$6.3 million in mortgage financing for capital construction projects on our dealership facilities. Since implementing our strategy of owning more of our dealership properties in late 2007, we have added \$142.7 million in mortgage financing to our capital structure on 14 of our dealership properties. These mortgage notes require monthly payments of principal and interest through maturity, are secured by the underlying properties and contain certain cross-default provisions. Maturity dates range between June 2013 and December 2029. At December 31, 2010, the weighted average interest rate was 4.91% and the total outstanding balance of our mortgages was \$133.9 million.

Operating Leases

We lease facilities for the majority of our dealership operations under operating lease arrangements. These facility lease arrangements normally have fifteen to twenty year terms with one or two ten year renewal options and do not contain provisions for contingent rent related to dealership's operations. Many of the leases are subject to the provisions of a guaranty and subordination agreement that contains financial and affirmative covenants. Approximately 20% of these facility leases are based on capitalization rates with payments that vary based on interest rates. We also lease certain equipment for use in dealership operations. These equipment lease arrangements normally have three to five year terms with one or two year renewal options. See the table under the heading *Future Liquidity Outlook* below for our future minimum lease payment obligations, net of sublease proceeds.

Floor Plan Facilities

We finance our new and certain of our used vehicle inventory through standardized floor plan facilities which are due on demand. These floor plan facilities bear interest at variable rates based on LIBOR and prime. The weighted average interest rate for our floor plan facilities for continuing and discontinued operations was 2.54% for 2009 and 2.71% for 2010. We receive floor plan assistance from certain manufacturers. Floor plan assistance received is capitalized in inventory and charged against cost of sales when the associated inventory is sold. We

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received approximately \$30.8 million, \$19.4 million and \$24.6 million in 2008, 2009 and 2010, respectively, and recognized in cost of sales for continuing operations and discontinued operations approximately \$30.1 million, \$22.6 million and \$24.0 million in 2008, 2009 and 2010, respectively, in manufacturer assistance. Interest payments under each of our floor plan facilities are due monthly and we are not required to make principal repayments prior to the sale of the vehicles.

Covenants and Default Provisions

Non-compliance with covenants, including a failure to make any payment when due, under our 2010 Credit Facilities, Silo Floor Plan Facilities, operating lease agreements, mortgage notes, 9.0% Notes, 8.625% Notes and 5.0% Convertible Notes (collectively, our Significant Debt Agreements) could result in a default and an acceleration of our repayment obligation under our 2010 Credit Facilities. A default under our 2010 Credit Facilities would constitute a default under our Silo Floor Plan Facilities and could entitle these lenders to accelerate our repayment obligations under the one or more of the floor plan facilities. Certain defaults under our 2010 Credit Facilities an