

UNITED AUTO GROUP INC

Form 8-K

August 07, 2002

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SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 8-K
CURRENT REPORT

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

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

UNITED AUTO GROUP, INC.

(Exact Name of Registrant as Specified in its Charter)

DELAWARE

(State or Other Jurisdiction of Incorporation)

1-12297

(Commission File Number)

13400 OUTER DRIVE WEST
DETROIT, MI

(Address of Principal Executive Offices)

313-592-7311

(Registrant's Telephone Number, Including Area Code)

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RISK FACTORS

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

- incur additional debt;
- create liens;
- make acquisitions;
- redeem and/or prepay certain debt;
- sell preferred stock of subsidiaries or other assets;
- make certain investments;
- enter new lines of business;
- engage in consolidations, mergers and acquisitions;
- repurchase or redeem capital stock;
- guarantee obligations;
- engage in certain transactions with affiliates; and
- pay dividends and make other distributions.

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

Requirements for Transfer of New Notes

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

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

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

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

Risks Relating to the Business

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

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

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

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

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

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

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

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

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

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

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

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

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

incurring significantly higher capital expenditures and operating expenses;

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

entering new markets with which we are not familiar;

incurring undiscovered liabilities at acquired dealerships;

disrupting our ongoing business;

failing to retain key personnel of the acquired dealerships;

impairing relationships with employees, manufacturers and customers; and

incorrectly valuing acquired entities.

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

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

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

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

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

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

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

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

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

Our failure to meet a manufacturer's consumer satisfaction requirements may adversely affect our ability to acquire new dealerships, our ability to obtain incentive payments from manufacturers and our profitability.

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

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

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

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

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

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

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

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

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

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

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

other national or regional affiliated groups of franchised dealerships;

private market buyers and sellers of used vehicles;

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

service center chain stores; and

independent service and repair shops.

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

currency and exchange risks;

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

changes in U.K. governmental regulations;

the impact of local economic and political conditions;

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

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

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

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ITEM 7. FINANCIAL STATEMENTS

MANAGEMENT'S DISCUSSION AND ANALYSIS

OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This Management's Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements that involve risks and uncertainties. Our actual results may differ materially from those discussed in the forward-looking statements as a result of various factors.

General

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

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

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

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

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

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

Critical Accounting Policies

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

Gross Profit.