

UNITED AUTO GROUP INC

Form 8-K

May 09, 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): May __, 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)

Item 5. Financial Statement

**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 December 31, 2001, we owned and operated 127 franchises located primarily in major metropolitan areas in 19 states, Puerto Rico and Brazil. 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 and fleet 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, other dealers and wholesalers. 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 new vehicle sales, used vehicle sales, finance and insurance revenues, and service and parts revenues. 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, cyclicity 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 costs), allowing us to adjust them 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.

Results of Operations

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.

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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 and an increase in comparative average selling prices per vehicle. 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 and an increase in comparative average selling prices per vehicle. 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 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.

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.

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

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

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

Other Interest Expense. Other interest expense increased by \$2.0 million, or 6.1%, from \$32.8 million to \$34.8 million. The increase is due primarily to increased acquisition related indebtedness, offset in part by (1) a decrease in our weighted average borrowing rate during 2001, (2) the effect of refinancing our 11.0% senior subordinated notes due 2007 and certain other indebtedness with lower interest borrowings under our amended and restated credit agreement, dated as of December 22, 2000 and (3) the paydown of indebtedness with proceeds from equity offerings subsequent to December 31, 2000.

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

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

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

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

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

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Retail sales of used vehicles, which exclude wholesale transactions, increased by \$142.3 million, or 18.5%, from \$769.6 million to \$912.0 million. The increase is due primarily to: (1) a \$35.2 million, or 5.1%, increase at dealerships owned prior to January 1, 1999, and (2) acquisitions made subsequent to January 1, 1999, partially offset by a decrease resulting from the divestiture of certain dealerships. The increase at dealerships owned prior to January 1, 1999, is due primarily to a 1.5% increase in used retail unit sales and an increase in comparative average selling prices per vehicle. Aggregate retail unit sales of used vehicles increased by 12.0%, due principally to: (1) the net increase at dealerships owned prior to January 1, 1999, and (2) acquisitions made subsequent to January 1, 1999, partially offset by the decrease due to divested dealerships. We retailed 58,252 used vehicles (34.1% of total retail vehicle sales) during the year ended December 31, 2000, compared with 52,027 used vehicles (35.8% of total retail vehicle sales) during the year ended December 31, 1999. Wholesale revenues increased \$45.2 million, or 16.7%, compared to the comparable prior year period. The increase in wholesale revenues is due primarily to: acquisitions made subsequent to January 1, 1999, offset in part by (1) an \$8.2 million, or 3.5%, decrease at dealerships owned prior to January 1, 1999, and (2) a decrease resulting from the divestiture of some dealerships.

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

Service and parts revenues increased by \$93.0 million, or 23.3%, from \$398.8 million to \$491.8 million. The increase is due primarily to: (1) a \$27.1 million, or 7.9%, increase at dealerships owned prior to January 1, 1999, and (2) acquisitions made subsequent to January 1, 1999, partially offset by a decrease resulting from the divestiture of some dealerships.

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

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

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

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due to an increase in inventory levels compared to 1999 and an increase in our weighted average borrowing rate during 2000.

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

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

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

Quarterly Financial Data

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

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

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

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

Liquidity and Capital Resources

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

securities, including floor plan notes payable, sale-leaseback transactions, the issuance of equity securities and cash flow from operations. At December 31, 2001, we had working capital of \$135.2 million.

We finance the majority of our new and a portion of our used vehicle inventory under revolving floor plan financing arrangements into which our subsidiaries have entered with various lenders. We make monthly interest payments on the amount financed, but are generally not required to make loan principal repayments prior to the sale of the new and used vehicles we have financed. The floor plan agreements grant a security interest in substantially all of the assets of our domestic automotive dealership subsidiaries. Interest rates on the floor plan arrangements are variable and increase or decrease based on movements in the prime rate or LIBOR. As of December 31, 2001, our outstanding borrowings under floor plan arrangements amounted to \$620.0 million.

Our credit agreement with DaimlerChrysler Services North America LLC and Toyota Motor Credit Corporation provides for revolving loans to be used for acquisitions, working capital, the repurchase of common stock and general corporate purposes. Upon completion of the offering for the Original Notes on March 18, 2002, our borrowing capacity under the revolving portion of the credit agreement was \$700.0 million and, in addition, we have use of a standby letter of credit facility in the amount of \$50.0 million. Our credit agreement also provides for a term loan of \$161.0 million, all of which was used during 1999 and 2000 to repurchase our senior subordinated notes. Loans under the credit agreement bear interest between LIBOR plus 2.00% and LIBOR plus 3.00%. The credit agreement is fully and unconditionally guaranteed on a joint and several basis by our domestic automotive dealership subsidiaries (and will be guaranteed by domestic automotive dealership subsidiaries acquired or established by us in the future) and contains a number of significant covenants that, among other things, restrict our ability to dispose of assets, incur additional indebtedness, repay other indebtedness, create liens on assets, make investments or acquisitions and engage in mergers or consolidations. In addition, we are required to comply with specified ratios and tests, including debt to equity, debt to EBITDA (as defined) and minimum working capital covenants. Our credit agreement also contains typical events of default including change of control and non-payment of obligations. Substantially all of our assets are subject to security interests granted to lenders under the credit agreement. The availability under the revolving portion of the credit agreement is subject to a collateral-based borrowing limitation which is determined based on certain of our allowable tangible assets (which does not include foreign assets). Revolving loans mature on August 3, 2005. With respect to the \$161.0 million of term loans, \$25.0 million must be repaid on December 23, 2003, \$25.0 million must be repaid on December 23, 2005, and the remainder must be repaid on December 23, 2007. As of December 31, 2001, our outstanding borrowings under the credit agreement amounted to \$541.5 million, \$161.0 million of which was incurred in connection with the repurchase of notes. As of March 12, 2002, our outstanding borrowings under the credit agreement amounted to \$604.5 million, which includes debt repayments subsequent to December 31, 2001 of \$62.5 million (proceeds of warrants) and \$50.0 million (sale-leaseback proceeds), and borrowings of \$135.0 million placed in escrow to pay for Sytner.

In October 2001, we entered into swap agreements of approximately four years duration pursuant to which a notional \$400.0 million of our floating rate debt was exchanged for fixed rate debt. The fixed rate interest to be paid by us is based on LIBOR and amounts to approximately 4.23%. During 2000, we entered into a swap agreement of five years duration pursuant to which a notional \$200.0 million of our floating rate debt was exchanged for fixed rate debt for five years. The fixed rate interest to be paid by us is based on LIBOR and amounts to approximately 7.1%.

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

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automotive dealership subsidiaries. As of December 31, 2001, \$3.7 million of subordinated notes remain outstanding. The notes become redeemable at our option, with the payment of a premium, on July 15, 2002.

On March 18, 2002, we issued \$300.0 million of senior subordinated notes pursuant to an offering memorandum pursuant to Rule 144A and Regulation S. These notes mature in 2012. The notes are unsecured senior subordinated notes and rank behind all of our existing and future senior debt, including debt under our credit agreement. The notes are guaranteed by substantially all of our domestic subsidiaries on a senior subordinated basis. We are able to redeem all or some of the notes at our option beginning in 2007 at specified redemption prices. In addition, until 2005 we are allowed to redeem up to 35% of the notes with the net cash proceeds from specified public equity offerings. Upon a change of control each holder of notes is able to require us to repurchase all or some of the notes at a redemption price of 101% of the principal amount of the notes. The notes also contain customary negative covenants and events of default. We are required to file a registration statement with the SEC and offer to exchange publicly-traded notes with the notes being privately issued. We are required to pay penalty interest on the notes to the extent we do not comply with these registration requirements.

Concurrently with the offering of the notes on March 18, 2002, we offered 6,000,000 shares of our common stock pursuant to an underwritten registered offering, of which we offered 3,000,000 shares and selling stockholders offered 3,000,000 shares.

We intend to issue \$300.0 million of senior subordinated notes pursuant to this prospectus in exchange for the \$300.0 million senior subordinated notes issued March 18, 2002. These New Notes will mature in 2012. The New Notes will be unsecured senior subordinated notes and will rank behind all of our existing and future senior debt, including debt under our credit agreement. The New Notes will be guaranteed by substantially all of our domestic subsidiaries on a senior subordinated basis. We will be able to redeem all or some of the New Notes at our option beginning in 2007 at specified redemption prices. In addition, until 2005 we will be allowed to redeem up to 35% of the New Notes with the net cash proceeds from specified public equity offerings. Upon a change of control each holder of New Notes we will be able to require us to repurchase all or some of the New Notes at a redemption price of 101% of the principal amount of the New Notes. The New Notes will also contain customary negative covenants and events of default.

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

The shares of Series A preferred stock and Series B preferred stock entitle the PCP Entities to dividends at a rate of 6.5% per year. The dividends were payable in kind for the first two years after issuance and are currently payable in cash. The Series A preferred stock is convertible into an aggregate of 8,794,171 shares of common stock (7,021,304 shares following the proposed equity offering) and the Series B preferred stock is convertible into an aggregate of 648,588 shares of non-voting common stock (in each case, after giving effect to payable in kind dividends). We are entitled under some circumstances to redeem the preferred stock after May 3, 2002, for an amount per share equal to the liquidation preference. The liquidation preference is currently \$10,000 per share plus accrued and unpaid dividends. Actual cash dividends payable relating to dividends earned during fiscal 2001 in connection with the preferred stock totaled \$3.1 million. Beginning in fiscal 2002, the aggregate annual cash dividends payable by us are expected to total \$6.1 million. Funding for such dividends is expected to come from cash flow from operations and working capital borrowings under our credit agreement.

The warrants, as originally issued to the PCP Entities, were exercisable at a price of \$12.50 per share until February 3, 2002, and \$15.50 per share thereafter until May 2, 2004. Pursuant to the anti-dilution provisions of the warrants and as a result of the sale of equity to Mitsui & Co. in 2001, (a) the number of warrants to purchase common stock was increased from 3,898,665 shares to 3,915,580 shares, (b) the number

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of warrants to purchase non-voting common stock was increased from 1,101,335 shares to 1,106,113 shares, and (c) the warrant exercise price was lowered from \$12.50 to \$12.45. On February 1, 2002, the PCP Entities exercised the warrants in full and paid us the full exercise price of \$62.5 million. The proceeds of the warrant exercise were used to pay down indebtedness.

In December 2000, we issued 2,139,535 shares of common stock to Penske Corporation for \$10.75 per share. Aggregate proceeds, amounting to \$23.0 million, were used to reduce debt. In February 2001, we issued 1,302,326 shares of voting common stock to Mitsui & Co., Ltd. and Mitsui & Co. (U.S.A.), Inc. in a private placement for \$10.75 per share (the Mitsui Transaction). Aggregate proceeds, amounting to \$14.0 million, were used to reduce debt.

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

During 2001, net cash provided by operations amounted to \$72.4 million. Net cash used in investing activities during 2001 totaled \$221.8 million, of which \$83.4 million related to capital expenditures and \$138.4 million was for acquisitions. Net cash provided by financing activities during 2001 totaled \$147.3 million, relating to: (1) net borrowings of \$134.3 million for capital expenditures and acquisitions and (2) \$18.8 million relating to the issuance of voting common stock, partially offset by \$5.8 million used to repurchase common stock.

We have a number of capital projects planned or underway relating to the expansion and renovation of our retail automotive operations. Gross cash expenditures during 2002 relating to such projects are estimated to aggregate to \$130.0 million, a portion of which has already been spent. Historically, we have financed such capital expenditures with borrowings under our credit agreement and cash flow from operations. In the past, we have also entered into sale-leaseback transactions with Automotive Group Realty, LLC (AGR), a wholly owned subsidiary of Penske Corporation. We sold certain properties to AGR in 2001 for consideration of \$20.9 million and made lease payments to AGR totaling \$5.8 million during 2001, which payments relate to properties we lease from AGR. We believe we will continue to finance certain capital expenditures in this fashion during 2002. As a result we anticipate that the net cash we will fund for capital expenditures will amount to approximately \$70.0 million.

During 2002, we received \$50.0 million from AGR representing consideration relating to the sale-leaseback of certain properties and related capital expenditures, including capital expenditures at properties previously sold to AGR, which cost us \$29.9 million. The excess of the cash received by us represents a prepayment by AGR to us for future contractually committed construction costs that we anticipate will be incurred by us during the first quarter of 2002 at properties owned by AGR and leased to us.

In addition, we have entered into a number of arrangements to acquire retail automotive franchises from unaffiliated third parties. Funding for the cash element of these acquisitions, expected to approximate \$19.0 million, is expected to come from cash flow from operations and borrowings under our credit agreement. We also have obligations with respect to past acquisitions totaling \$32.0 million over the next four years.

In connection with the acquisition of Sytner, as an alternative to receiving all or any part of the £95.3 million of cash consideration which would otherwise be receivable under the offer, Sytner shareholders (other than certain non-U.K. shareholders) who validly accepted the offer could elect to receive loan notes issued by UAG UK Holdings Limited. For every £1 of cash consideration otherwise receivable under the offer, Sytner shareholders could elect to receive £1 of loan notes.

In connection with one of the acquisitions consummated during 2001, we agreed to make a contingent payment in cash to the extent the 289,243 shares of common stock issued in connection with the acquisition have a market value at the time of sale of less than \$17.29 per share. In addition, we agreed to make a contingent payment in cash to the extent the 841,476 shares of common stock issued in connection with an acquisition completed in 2000 have a market value at the time of sale of less than \$12.00 per share.

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In connection with an acquisition of dealerships in October 1997, we agreed that if the acquired companies achieved aggregate specified base earnings levels in any of the five years beginning with the year ending December 31, 1999, we would pay to the sellers \$0.7 million plus defined percentages of the amounts earned in excess of such base earnings for any such year. The total amount of payments to be made pursuant to this agreement is limited to \$7.0 million. To date we have paid \$2.0 million relating to this agreement.

As of December 31, 2001, we had approximately \$5.4 million of cash available to fund operations and future acquisitions. In addition, a maximum of \$256.5 million was available for borrowing under our credit agreement as of March 12, 2002, which 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). The borrowing base limitations currently limit our ability to access the full availability under our credit agreement. In the past twelve months, the actual availability which we could access under the credit agreement ranged from a high of \$156.5 million as of February 12, 2002 prior to borrowing \$135.0 million for the Sytner acquisition to a low of \$11.5 million as of March 12, 2002. When availability under the credit agreement is low, we rely on cash flow from operations and the availability of floor plan financing to fund our day-to-day cash needs. After completion of both the debt and the equity offerings on March 18, 2002, actual availability under our credit agreement increased by approximately \$351.7 million.

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

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

Joint Ventures

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

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

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

In October 2000, we purchased the operating assets of certain dealerships in Fairfield, Connecticut for approximately \$26.8 million. We intend to sell 20% of this venture to Lucio A. Noto and other investors for approximately \$5.4 million, representing 20% of the consideration we paid inclusive of assets acquired.

Mr. Noto will pay for this interest with \$1.2 million at closing and the remaining \$4.2 million will be paid in quarterly payments over twenty years. The payments will be offset from permitted periodic cash distributions to Mr. Noto by the venture. The sale of the minority interest to Mr. Noto is subject to approval by the manufacturers.

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

In July 2001 we invested in the Tulsa Auto Collection, a group of dealerships in Tulsa, Oklahoma. The Tulsa Auto Collection consists of seven dealerships representing the Ford, Lincoln-Mercury, Jaguar and Mazda brands. In addition, through the Tulsa Auto Collection, we operate two automotive care service centers and two used vehicle facilities in the Tulsa market. According to the terms of our joint venture arrangement, we have the option to buy out our partner over a period of time. Through December 2003, we also may, at our option, cause our partner to purchase our share of the collection or sell our share or the entire collection to a third party.

Cyclicality

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

Seasonality

Our business is modestly seasonal overall. Our operations generally experience higher volumes of vehicle sales in the second and third quarters of each year due in part to consumer buying trends and the introduction of new vehicle models. Also, demand for cars and light trucks is generally lower during the winter months than in other seasons, particularly in regions of the United States where dealerships may be subject to harsh winters. Accordingly, we expect our revenues and profitability to be generally lower in our first and fourth quarters as compared to our second and third quarters. The greatest seasonalities exist with the dealerships in the northeast United States, for which the second and third quarters are the strongest with respect to vehicle-related sales. The service and parts business at all dealerships experiences relatively modest seasonal fluctuations.

New Accounting Pronouncements

Statement of Financial Accounting Standards No. 141, *Business Combinations* (*SFAS No. 141*), and Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets* (*SFAS No. 142*), were issued in final form in June 2001. The provisions of SFAS No. 141, which require use of the purchase method of accounting and eliminate the use of the pooling-of-interests method of accounting for business combinations, apply to all business combinations completed after June 30, 2001. In addition, SFAS No. 141 includes transition provisions that apply to business combinations accounted for using the purchase method which were completed before July 1, 2001.

The provisions of SFAS No. 142, which address the financial accounting and related reporting for acquired goodwill and other intangible assets, are effective for fiscal years beginning after December 15, 2001. SFAS No. 142, which we adopted on January 1, 2002, eliminates goodwill amortization over its estimated useful life. However, goodwill will be subject to at least an annual assessment for impairment by applying a fair-value based test. Additionally, acquired intangible assets should be separately recognized if the benefit of the intangible asset is obtained through contractual or other legal rights, or if the intangible asset can be sold, transferred, licensed, rented, or exchanged, regardless of the acquiror's intent to do so. Intangible assets with definitive lives will need to be amortized over their useful lives.

By March 31, 2002, companies were required to begin to perform an impairment analysis of intangible assets. Furthermore, companies must complete the first step of the goodwill transition impairment test by June 30, 2002. Impairment charges, if any, that result from the application of the above tests would be recorded as the cumulative effect of a change in accounting principle in the first quarter of the year ending December 31, 2002.

We are in the process of evaluating the impact of SFAS No. 142 on our business. At the present time we cannot determine the ultimate impact of SFAS No. 142. Amortization of goodwill for the year ended December 31, 2001 was \$19.7 million.

Statement of Financial Accounting Standards No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets (SFAS No. 144) was issued in August 2001. This statement supersedes Statement of Financial Accounting Standards No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of, and establishes accounting standards for the impairment and disposal of long-lived assets and criteria for determining when a long-lived asset is held for sale. The statement removes the requirement to allocate goodwill to long-lived assets to be tested for impairment, requires that the depreciable life of a long-lived asset to be abandoned be revised in accordance with Accounting Principals Board Opinion No. 20, Accounting Changes, provides that one accounting model be used for long-lived assets to be disposed of by sale and broadens the presentation of discontinued operations to include more disposal transactions. SFAS No. 144 is effective for fiscal years beginning after December 15, 2001. We are currently evaluating the impact of adopting SFAS No. 144 on our financial statements.

Effects of Inflation

We believe that the relatively moderate rates of inflation over the last few years have not had a significant impact on revenues or profitability. We do not expect inflation to have any near-term material effects on the sale of our products and services. However, there can be no assurance that there will be no such effect in the future.

We finance substantially all of our inventory through various revolving floor plan arrangements with interest rates that vary based on the prime rate or LIBOR. Such rates have historically increased during periods of increasing inflation. We do not believe that we would be placed at a competitive disadvantage should interest rates increase due to increased inflation since most other automotive dealerships have similar floating rate borrowing arrangements.

Quantitative and Qualitative Disclosures About Market Risk

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

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

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

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INDEPENDENT AUDITORS REPORT

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

Detroit, Michigan

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

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

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

/s/ DELOITTE & TOUCHE LLP

New York, New York

February 4, 2002 (except for Note 14,
as to which the date is April 29, 2002)

UNITED AUTO GROUP, INC.

CONSOLIDATED BALANCE SHEETS

	December 31,	
	2001	2000
	(In thousands, except per share amounts)	
ASSETS		
Cash and cash equivalents	\$ 5,416	\$ 7,413
Accounts receivable, net	258,266	190,792
Inventories	641,400	737,942
Other current assets	16,434	15,469
	<hr/>	<hr/>
Total current assets	921,516	951,616
Property and equipment, net	185,452	107,085
Intangible assets, net	784,149	664,510
Other assets	55,459	39,484
	<hr/>	<hr/>
Total Assets	\$ 1,946,576	\$ 1,762,695
	<hr/>	<hr/>
LIABILITIES AND STOCKHOLDERS EQUITY		
Floor plan notes payable	\$ 620,014	\$ 689,687
Accounts payable	76,550	55,344
Accrued expenses	85,512	72,075
Current portion of long-term debt	4,202	41,456
	<hr/>	<hr/>
Total current liabilities	786,278	858,562
Long-term debt	551,840	377,721
Other long-term liabilities	92,775	64,742
	<hr/>	<hr/>
Total Liabilities	1,430,893	1,301,025
	<hr/>	<hr/>
Commitments and contingent liabilities		
Stockholders Equity		
Series A Preferred Stock, \$0.0001 par value; 10 shares authorized; 9 issued and outstanding at December 31, 2001; 8 issued and outstanding at December 31, 2000		
Series B Preferred Stock, \$0.0001 par value; 10 shares authorized; 1 issued and outstanding at December 31, 2001 and 2000		
Common Stock, \$0.0001 par value, 80,000 shares authorized; 23,540 shares issued, including 3,821 treasury shares, at December 31, 2001; 21,990 shares issued, including 3,434 treasury shares, at December 31, 2000	2	2
Non-voting Common Stock, \$0.0001 par value, 7,125 shares authorized; none issued and outstanding at December 31, 2001 and 2000		
Class C Common Stock, \$0.0001 par value, 20,000 shares authorized; none issued and outstanding at December 31, 2001 and 2000		
Additional paid-in-capital	445,311	420,166
Retained earnings	78,750	41,502

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Accumulated other comprehensive (loss)	(8,380)	
	<u> </u>	<u> </u>
Total Stockholders Equity	515,683	461,670
	<u> </u>	<u> </u>
Total Liabilities and Stockholders Equity	\$ 1,946,576	\$ 1,762,695
	<u> </u>	<u> </u>

See Notes to Consolidated Financial Statements.

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UNITED AUTO GROUP, INC.

CONSOLIDATED STATEMENTS OF INCOME

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