GROUP 1 AUTOMOTIVE INC
Form 10-Q
October 31, 2013

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

FORM 10-Q

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

For the quarterly period ended September 30, 2013

or

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

For the transition period from to

Commission File Number: 1-13461

Group 1 Automotive, Inc.

(Exact name of registrant as specified in its charter)

| | |
|---|---|
| Delaware | 76-0506313 |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |

800 Gessner, Suite 500
Houston, Texas 77024
(Address of principal executive offices) (Zip code)
(713) 647-5700
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this Chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ No ¨

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

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

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

As of October 29, 2013, the registrant had 24,371,498 shares of common stock, par value $0.01, outstanding.

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PART I. FINANCIAL INFORMATION
Item 1. Financial Statements
GROUP 1 AUTOMOTIVE, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

| | September 30, 2013 (Unaudited) | December 31, 2012 |
|---|---|---|
| | (In thousands, except per share amounts) | |
| ASSETS | | |
| CURRENT ASSETS: | | |
| Cash and cash equivalents | $26,278 | $4,650 |
| Contracts-in-transit and vehicle receivables, net | 160,554 | 204,396 |
| Accounts and notes receivable, net | 123,376 | 111,228 |
| Inventories, net | 1,351,719 | 1,194,288 |
| Deferred income taxes | 22,273 | 19,750 |
| Prepaid expenses and other current assets | 23,775 | 31,869 |
| Total current assets | 1,707,975 | 1,566,181 |
| PROPERTY AND EQUIPMENT, net | 716,514 | 667,768 |
| GOODWILL | 689,871 | 582,384 |
| INTANGIBLE FRANCHISE RIGHTS | 279,806 | 196,058 |
| OTHER ASSETS | 15,742 | 10,624 |
| Total assets | $3,409,908 | $3,023,015 |
| LIABILITIES AND STOCKHOLDERS’ EQUITY | | |
| CURRENT LIABILITIES: | | |
| Floorplan notes payable - credit facility and other | $960,871 | $968,959 |
| Offset account related to floorplan notes payable - credit facility | (47,709) | (112,261) |
| Floorplan notes payable - manufacturer affiliates | 308,869 | 211,965 |
| Current maturities of long-term debt and short-term financing | 27,010 | 31,358 |
| Accounts payable | 201,699 | 167,439 |
| Accrued expenses | 133,777 | 128,118 |
| Total current liabilities | 1,584,517 | 1,395,578 |
| LONG-TERM DEBT, net of current maturities | 560,427 | 555,016 |
| DEFERRED INCOME TAXES | 136,664 | 94,130 |
| LIABILITIES FROM INTEREST RATE RISK MANAGEMENT ACTIVITIES | 29,184 | 43,089 |
| OTHER LIABILITIES | 46,200 | 42,413 |
| COMMITMENTS AND CONTINGENCIES (NOTE 11) | | |
| TEMPORARY EQUITY - Redeemable equity portion of the 3.00% Convertible Senior Notes | 29,974 | 32,505 |
| STOCKHOLDERS’ EQUITY: | | |
| Preferred stock, $0.01 par value, 1,000 shares authorized; none issued or outstanding | — | — |
| Common stock, $0.01 par value, 50,000 shares authorized; 25,888 and 25,836 issued, respectively | 259 | 258 |
| Additional paid-in capital | 369,198 | 332,836 |
| Retained earnings | 758,498 | 677,864 |
| Accumulated other comprehensive loss | (46,345) | (33,057) |
| Treasury stock, at cost; 1,514 and 3,110 shares, respectively | (58,668) | (117,617) |
| Total stockholders’ equity | 1,022,942 | 860,284 |
| Total liabilities and stockholders’ equity | $3,409,908 | $3,023,015 |

The accompanying notes are an integral part of these consolidated financial statements.

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GROUP 1 AUTOMOTIVE, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2013 | 2012 | 2013 | 2012 |
| | (Unaudited, in thousands, except per share amounts) | | | |
| REVENUES: | | | | |
| New vehicle retail sales | $1,386,667 | $1,141,286 | $3,873,121 | $3,134,591 |
| Used vehicle retail sales | 529,828 | 462,395 | 1,536,031 | 1,333,603 |
| Used vehicle wholesale sales | 85,800 | 78,424 | 243,667 | 218,415 |
| Parts and service sales | 255,316 | 224,990 | 753,776 | 658,404 |
| Finance, insurance and other, net | 82,536 | 69,477 | 232,494 | 192,130 |
| Total revenues | 2,340,147 | 1,976,572 | 6,639,089 | 5,537,143 |
| COST OF SALES: | | | | |
| New vehicle retail sales | 1,313,372 | 1,074,736 | 3,656,825 | 2,951,379 |
| Used vehicle retail sales | 488,346 | 424,663 | 1,410,768 | 1,220,628 |
| Used vehicle wholesale sales | 87,334 | 79,067 | 242,267 | 216,031 |
| Parts and service sales | 121,633 | 106,875 | 358,004 | 312,106 |
| Total cost of sales | 2,010,685 | 1,685,341 | 5,667,864 | 4,700,144 |
| GROSS PROFIT | 329,462 | 291,231 | 971,225 | 836,999 |
| SELLING, GENERAL AND ADMINISTRATIVE EXPENSES | 246,863 | 216,082 | 731,455 | 629,521 |
| DEPRECIATION AND AMORTIZATION EXPENSE | 9,093 | 8,096 | 26,390 | 23,074 |
| ASSET IMPAIRMENTS | 565 | — | 1,174 | 288 |
| INCOME FROM OPERATIONS | 72,941 | 67,053 | 212,206 | 184,116 |
| OTHER EXPENSE: | | | | |
| Floorplan interest expense | (10,690) | (7,942) | (30,927) | (23,424) |
| Other interest expense, net | (9,971) | (9,619) | (28,783) | (27,849) |
| Other expense, net | — | — | (789) | — |
| INCOME BEFORE INCOME TAXES | 52,280 | 49,492 | 151,707 | 132,843 |
| PROVISION FOR INCOME TAXES | (19,515) | (18,157) | (59,436) | (49,766) |
| NET INCOME | $32,765 | $31,335 | $92,271 | $83,077 |
| BASIC EARNINGS PER SHARE | $1.34 | $1.38 | $3.83 | $3.64 |
| Weighted average common shares outstanding | 23,373 | 21,521 | 22,994 | 21,600 |
| DILUTED EARNINGS PER SHARE | $1.19 | $1.32 | $3.52 | $3.50 |
| Weighted average common shares outstanding | 26,342 | 22,458 | 25,153 | 22,501 |
| CASH DIVIDENDS PER COMMON SHARE | $0.17 | $0.15 | $0.48 | $0.44 |

The accompanying notes are an integral part of these consolidated financial statements.

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GROUP 1 AUTOMOTIVE, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2013 | 2012 | 2013 | 2012 |
| | (Unaudited, in thousands) | | | |
| NET INCOME | $32,765 | $31,335 | $92,271 | $83,077 |
| Other comprehensive income (loss), net of taxes: | | | | |
| Foreign currency translation adjustment | 3,237 | 1,856 | (23,487) | 1,850 |
| Unrealized loss on marketable securities, net of tax benefit of $0, $10, $0 and $5, respectively | — | (16) | — | (8) |
| Net unrealized gain (loss) on interest rate swaps: | | | | |
| Unrealized gain (loss) arising during the period, net of tax benefit (provision) of $1,615, $2,786, ($2,999) and $7,352, respectively | (2,691) | (4,644) | 4,999 | (12,254) |
| Reclassification adjustment for loss included in interest expense, net of tax provision of $1,075, $1,006, $3,120 and $3,216, respectively | 1,791 | 1,676 | 5,200 | 5,360 |
| Net unrealized gain (loss) on interest rate swaps, net of tax | (900) | (2,968) | 10,199 | (6,894) |
| OTHER COMPREHENSIVE INCOME (LOSS) NET OF TAXES | 2,337 | (1,128) | (13,288) | (5,052) |
| COMPREHENSIVE INCOME | $35,102 | $30,207 | $78,983 | $78,025 |

The accompanying notes are an integral part of these consolidated financial statements.

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GROUP 1 AUTOMOTIVE, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

| | Common Stock | | Additional Paid-in | Retained | Accumulated Other Comprehensive | Treasury | |
|---|---|---|---|---|---|---|---|
| | Shares | Amount | Capital | Earnings | Loss | Stock | Total |
| | (Unaudited, in thousands) | | | | | | |
| BALANCE, December 31, 2012 | 25,836 | $258 | $332,836 | $677,864 | $(33,057) | $(117,617) | $860,284 |
| Net income | — | — | — | 92,271 | — | — | 92,271 |
| Other comprehensive loss, net | — | — | — | — | (13,288) | — | (13,288) |
| Treasury stock used in acquisition | — | — | 27,689 | — | — | 52,709 | 80,398 |
| 3.00% Convertible Notes reclassification from temporary equity | — | — | 2,531 | — | — | — | 2,531 |
| Net issuance of treasury shares to employee stock compensation plans | 52 | 1 | (5,705) | — | — | 6,240 | 536 |
| Stock-based compensation | — | — | 10,434 | — | — | — | 10,434 |
| Tax effect from stock-based compensation plans | — | — | 1,413 | — | — | — | 1,413 |
| Cash dividends, net of estimated forfeitures relative to participating securities | — | — | — | (11,637) | — | — | (11,637) |
| BALANCE, September 30, 2013 | 25,888 | $259 | $369,198 | $758,498 | $(46,345) | $(58,668) | $1,022,942 |

The accompanying notes are an integral part of these consolidated financial statements.
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GROUP 1 AUTOMOTIVE, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

| | Nine Months Ended September 30, | |
|---|---|---|
| | 2013 | 2012 |
| | (Unaudited, in thousands) | |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net income | $92,271 | $83,077 |
| Adjustments to reconcile net income to net cash provided by (used in) operating activities: | | |
| Depreciation and amortization | 26,390 | 23,074 |
| Deferred income taxes | 16,601 | 10,755 |
| Asset impairments | 1,174 | 288 |
| Stock-based compensation | 10,473 | 8,943 |
| Amortization of debt discount and issue costs | 10,453 | 9,659 |
| Gain on real estate transactions | — | (2,131) |
| Gain on disposition of assets | (11,093) | — |
| Tax effect from stock-based compensation | (1,413) | (1,015) |
| Other | 2,301 | 1,609 |
| Changes in operating assets and liabilities, net of effects of acquisitions and dispositions: | | |
| Accounts payable and accrued expenses | (9,500) | 19,294 |
| Accounts and notes receivable | 2,815 | 6,680 |
| Inventories | (107,994) | (193,145) |
| Contracts-in-transit and vehicle receivables | 45,284 | 25,135 |
| Prepaid expenses and other assets | 1,046 | 6,575 |
| Floorplan notes payable - manufacturer affiliates | 49,814 | (5,979) |
| Deferred revenues | 344 | (110) |
| Net cash provided by (used in) operating activities | 128,966 | (7,291) |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Cash paid in acquisitions, net of cash received | (106,672) | (116,528) |
| Proceeds from disposition of franchises, property and equipment | 101,821 | 257 |
| Purchases of property and equipment, including real estate | (63,890) | (67,877) |
| Other | 2,155 | 2,814 |
| Net cash used in investing activities | (66,586) | (181,334) |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Borrowings on credit facility - Floorplan Line and other | 4,707,989 | 4,186,871 |
| Repayments on credit facility - Floorplan Line and other | (4,652,495) | (4,014,024) |
| Borrowings on mortgage facility | — | 18,080 |
| Principal payments on mortgage facility | (7,919) | (1,648) |
| Borrowings of other long-term debt | 828 | 36 |
| Principal payments of long-term debt related to real estate loans | (32,792) | (7,297) |
| Borrowings of short-term and long-term debt related to real estate | 21,105 | 54,320 |
| Principal payments of other long-term debt | (65,446) | (3,938) |
| Repurchases of common stock, amounts based on settlement date | — | (11,317) |
| Issuance of common stock to benefit plans | 538 | 1,753 |
| Tax effect from stock-based compensation | 1,413 | 1,015 |
| Dividends paid | (11,676) | (10,029) |
| Net cash (used in) provided by financing activities | (38,455) | 213,822 |

| | | |
|---|---|---|
| EFFECT OF EXCHANGE RATE CHANGES ON CASH | (2,297) | (1,270) |
| NET INCREASE IN CASH AND CASH EQUIVALENTS | 21,628 | 23,927 |
| CASH AND CASH EQUIVALENTS, beginning of period | 4,650 | 14,895 |
| CASH AND CASH EQUIVALENTS, end of period | $26,278 | $38,822 |
| SUPPLEMENTAL CASH FLOW INFORMATION: | | |
| Purchases of property and equipment, including real estate, accrued in accounts payable and accrued expenses | $501 | $3,738 |

The accompanying notes are an integral part of these consolidated financial statements.

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GROUP 1 AUTOMOTIVE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. INTERIM FINANCIAL INFORMATION
Business and Organization
Group 1 Automotive, Inc., a Delaware corporation, through its regions, is a leading operator in the automotive retailing industry with operations in 15 states in the United States of America ("U.S."), 13 towns in the United Kingdom ("U.K.") and two states in Brazil. Group 1 Automotive, Inc. and its subsidiaries are collectively referred to as the "Company" in these Notes to Consolidated Financial Statements. The Company, through its regions, sells new and used cars and light trucks; arranges related vehicle financing; sells service and insurance contracts; provides automotive maintenance and repair services; and sells vehicle parts.
As of September 30, 2013, the Company's U.S. retail network consisted of the following two regions (with the number of dealerships they comprised): (a) the East (44 dealerships in Alabama, Florida, Georgia, Louisiana, Maryland, Massachusetts, Mississippi, New Hampshire, New Jersey, New York and South Carolina), and (b) the West (65 dealerships in California, Kansas, Louisiana, Oklahoma, and Texas). Each U.S. region is managed by a regional vice president who reports directly to the Company's Chief Executive Officer and is responsible for the overall performance of their regions. The financial matters of each U.S. region are managed by a regional chief financial officer who reports directly to the Company's Chief Financial Officer. The Company's two international regions consist of 14 dealerships in the U.K. and 18 dealerships in Brazil, which are also managed locally with direct reporting responsibilities to the Company's corporate management team.
The Company's operating results are generally subject to changes in the economic environment as well as seasonal variations. Generally there are higher volumes of vehicles sales and service in the second and third calendar quarters of each year in the U.S., in the first and third quarters in the U.K. and during the third and fourth quarters in Brazil. This seasonality is generally attributable to consumer buying trends and the timing of manufacturer new vehicle model introductions. In addition, in some regions of the U.S., vehicle purchases decline during the winter months due to inclement weather. As a result, revenues and operating income are typically lower in the first and fourth quarters and higher in the second and third quarters. Other factors unrelated to seasonality, such as changes in economic condition, manufacturer incentive programs, or shifts in governmental taxes or regulations may exaggerate seasonal or cause counter-seasonal fluctuations in our revenues and operating income.
Basis of Presentation
The accompanying unaudited condensed Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the U.S. for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the U.S. for complete financial statements. In the opinion of management, all adjustments of a normal and recurring nature considered necessary for a fair presentation have been included in the accompanying unaudited condensed Consolidated Financial Statements. Due to seasonality and other factors, the results of operations for the interim period are not necessarily indicative of the results that will be realized for the entire fiscal year. For further information, refer to the Consolidated Financial Statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2012 ("2012 Form 10-K").
All business acquisitions completed during the periods presented have been accounted for using the purchase method of accounting, and their results of operations are included from the effective dates of the closings of the acquisitions. The allocations of purchase price to the assets acquired and liabilities assumed are assigned and recorded based on estimates of fair value. All intercompany balances and transactions have been eliminated in consolidation.
Business Segment Information
The Company, through its regions, conducts business in the automotive retailing industry. All of the segments sell new and used cars and light trucks, arrange related vehicle financing, service and insurance contracts, provide automotive maintenance and repair services and sell vehicle parts. Effective with the acquisition of UAB Motors Participações S.A. ("UAB Motors") on February 28, 2013, the Company is aligned into four geographic regions: the East and West Regions in the U.S., the U.K. Region, and the Brazil Region. Also, in conjunction with the acquisition

of UAB Motors and consistent with how the Company's chief operating decision maker evaluates performance and allocates resources, the Company reaffirmed that each region represents an operating segment. As part of this determination, the Company concluded, as it has historically, that the East and West Regions of the U.S. are economically similar in that they deliver the same products and services to a common customer group, their customers are generally individuals, they follow the same procedures and methods in managing their operations, and they operate in similar regulatory environments; therefore, the Company aggregates these two regions into one reportable segment. As such, the Company's three reportable segments are the U.S., which includes the activities of the Company's corporate office, the U.K. and Brazil.

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Variable Interest Entity

In 2013, the Company entered into arrangements to provide a fixed-interest-rate working capital loan and various administrative services to a related-party entity that owns and operates retail automotive dealerships for a variable fee, both of which constitute variable interests in the entity. The Company's exposure to loss as a result of its involvement in the entity includes the balance outstanding under the loan arrangement. The Company holds no equity ownership interest in the entity, and has determined that the entity meets the criteria of a variable interest entity ("VIE"). The terms of the loan and services agreements provide the Company with the right to control the activities of the VIE that most significantly impact the VIE's economic performance, the obligation to absorb potentially significant losses of the VIE and the right to receive potentially significant benefits from the VIE. Accordingly, the Company qualified as the VIE's primary beneficiary and consolidated 100% of the assets and liabilities of the VIE as of September 30, 2013, as well as 100% of the results of operations of the VIE beginning on the effective date of the variable interests arrangements to September 30, 2013. The floorplan notes payable liability of the VIE is securitized by the new and used vehicle inventory of the VIE, as well as the associated receivable balances from the sale of such inventory to the extent necessary. The preliminary carrying amounts and classification of assets and liabilities (for which creditors do not have recourse to the general credit of the Company) are included within amounts from the Company's purchase price allocations. As discussed in Note 2, "Acquisitions and Dispositions," the allocations are based on estimates and assumptions that are subject to change within the purchase price allocation period. The assets and liabilities included in the Company's consolidated statements of financial position for the consolidated VIE are as follows (in thousands):

| | September 30, 2013 |
|---|---|
| Current Assets | $26,918 |
| Non-current Assets | 75,786 |
| Total Assets | $102,704 |
| Current Liabilities | $24,352 |
| Non-current Liabilities | 26,764 |
| Total Liabilities | $51,116 |

Recent Accounting Pronouncements

In February 2013, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2013-2, Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income ("ASU 2013-02"), which requires an entity to provide information about the amounts reclassified out of accumulated other comprehensive income by component. In addition, an entity is required to present, either on the face of the statement where net income is presented or in the notes, significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income but only if the amount reclassified is required under GAAP to be reclassified to net income in its entirety in the same reporting period. For other amounts that are not required under GAAP to be reclassified in their entirety to net income, an entity is required to cross-reference to other disclosures required under GAAP that provide additional detail about those amounts. The Company's adoption of ASU No. 2013-2 as of March 31, 2013 did not have a material impact on the Company's consolidated financial statements.

2. ACQUISITIONS AND DISPOSITIONS

In February 2013, the Company purchased all of the outstanding stock of UAB Motors. At the time of acquisition, UAB Motors consisted of 18 dealerships and 22 franchises in Brazil, as well as five collision centers. As discussed in Note 1, "Interim Financial Information," in connection with this acquisition, the Company entered into arrangements that are variable interests in a VIE. The Company qualifies as the primary beneficiary of the VIE. The consolidation of the VIE into the financial statements of the Company was accounted for as a business combination. In addition, during the nine months ended September 30, 2013, the Company acquired certain assets of four dealerships in the U.K. and two dealerships in the U.S. In conjunction with these acquisitions, the Company incurred $6.5 million of costs, primarily related to professional services associated with the Brazil transaction. The Company included these costs in selling, general and administrative expenses ("SG&A") in the Consolidated Statement of Operations for the nine months ended September 30, 2013.

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Aggregate consideration paid for these acquisitions totaled $190.4 million, including $106.7 million of cash and 1.39 million shares of the Company's common stock. The Company also assumed debt in conjunction with the acquisitions, of which $65.1 million was contemporaneously extinguished. In conjunction with the extinguishment, the Company recognized a loss of $0.8 million that is included in Other Expense, net on the Consolidated Statement of Operations for the nine months ended September 30, 2013. The purchase price has been allocated as set forth below based upon the consideration paid and the estimated fair values of the assets acquired and liabilities assumed at the acquisition date. The allocation of the purchase price is preliminary and based on estimates and assumptions that are subject to change within the purchase price allocation period (generally one year from the acquisition date). Goodwill was assigned to the U.S., U.K. and Brazil reportable segments in the amounts of $13.6 million, $1.6 million and $112.1 million, respectively.

| | As of Acquisition Date<br>(In thousands) |
|---|---|
| Current Assets | $32,370 |
| Inventory | 105,455 |
| Property and Equipment | 32,043 |
| Goodwill & Intangible Franchise Rights | 226,631 |
| Other assets | 1,869 |
| Total Assets | $398,368 |
| Current Liabilities | $116,993 |
| Deferred Income Taxes | 22,290 |
| Long-term Debt | 68,639 |
| Total Liabilities | $207,922 |

The intangible franchise rights are expected to continue for an indefinite period, therefore these rights are not amortized. These intangible assets will be evaluated on an annual basis in accordance with ASC 350. Goodwill represents the excess of consideration paid compared to net assets received in the acquisition. The goodwill relative to the Brazil reportable segment is not currently deductible for tax purposes.

Our supplemental pro forma revenue and net income had the acquisition date for each of the Company's 2013 acquisitions been January 1, 2012, are as follows:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| Supplemental Pro forma: | 2013 | 2012 | 2013 | 2012 |
| | (In thousands) | | | |
| Revenue | $2,354,595 | $2,234,107 | $6,849,938 | $6,331,163 |
| Net income | $32,260 | $36,149 | $100,243 | $95,867 |

The supplemental pro forma revenue and net income are presented for informational purposes only and may not necessarily reflect the future results of operations of the Company or what the results of operations would have been had the Company owned and operated these businesses as of January 1, 2012.

During the three months ended September 30, 2013, the Company sold two dealerships in the U.S. During the nine months ended September 30, 2013, the Company sold six dealerships and one franchise in the U.S. As a result of the dispositions, a net gain of $1.4 million and $10.4 million was recognized for the three and nine months ended September 30, 2013, respectively.

During the nine months ended September 30, 2012, the Company acquired seven dealerships in the U.S. and six dealerships in the U.K. Consideration paid for these dealerships totaled $116.5 million.

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3. DERIVATIVE INSTRUMENTS AND RISK MANAGEMENT ACTIVITIES

The periodic interest rates of the Revolving Credit Facility (as defined in Note 8, “Credit Facilities”), the Mortgage Facility (as defined in Note 9, “Long-Term Debt”) and certain variable-rate real estate related borrowings are indexed to the one-month London Inter Bank Offered Rate (“LIBOR”) plus an associated company credit risk rate. In order to minimize the earnings variability related to fluctuations in these rates, the Company employs an interest rate hedging strategy, whereby it enters into arrangements with various financial institutional counterparties with investment grade credit ratings, swapping its variable interest rate exposure for a fixed interest rate over terms not to exceed the related variable-rate debt.

The Company presents the fair value of all derivatives on its Consolidated Balance Sheets. The Company measures the fair value of its interest rate derivative instruments utilizing an income approach valuation technique, converting future amounts of cash flows to a single present value in order to obtain a transfer exit price within the bid and ask spread that is most representative of the fair value of its derivative instruments. In measuring fair value, the Company utilizes the option-pricing Black-Scholes present value technique for all of its derivative instruments. This option-pricing technique utilizes a one-month LIBOR forward yield curve, obtained from an independent external service provider, matched to the identical maturity term of the instrument being measured. Observable inputs utilized in the income approach valuation technique incorporate identical contractual notional amounts, fixed coupon rates, periodic terms for interest payments and contract maturity. The fair value estimate of the interest rate derivative instruments also considers the credit risk of the Company for instruments in a liability position or the counterparty for instruments in an asset position. The credit risk is calculated by using the spread between the one-month LIBOR yield curve and the relevant average 10 and 20-year rate according to Standard and Poor’s. The Company has determined the valuation measurement inputs of these derivative instruments to maximize the use of observable inputs that market participants would use in pricing similar or identical instruments and market data obtained from independent sources, which is readily observable or can be corroborated by observable market data for substantially the full term of the derivative instrument. Further, the valuation measurement inputs minimize the use of unobservable inputs. Accordingly, the Company has classified the derivatives within Level 2 of the hierarchy framework as described by the Fair Value Measurements and Disclosures Topic of the FASB Accounting Standards Codification.

The related gains or losses on these interest rate derivatives are deferred in stockholders’ equity as a component of accumulated other comprehensive loss. These deferred gains and losses are recognized in income in the period in which the related items being hedged are recognized in expense. However, to the extent that the change in value of a derivative contract does not perfectly offset the change in the value of the items being hedged, that ineffective portion is immediately recognized in other income or expense. Monthly contractual settlements of these swap positions are recognized as floorplan or other interest expense in the Company’s accompanying Consolidated Statements of Operations. All of the Company’s interest rate hedges are designated as cash flow hedges.

The Company held interest rate swaps in effect as of September 30, 2013 of $450.0 million in notional value that fixed its underlying one-month LIBOR at a weighted average rate of 2.6%. The Company records the majority of the impact of the periodic settlements of these swaps as a component of floorplan interest expense. For the three and nine months ended September 30, 2013, the impact of the Company’s interest rate hedges in effect increased floorplan interest expense by $2.5 million and $7.4 million, respectively; for the three and nine months ended September 30, 2012, the impact of the Company's interest rate hedges in effect increased floorplan interest expense by $2.4 million and $7.7 million, respectively. Total floorplan interest expense was $10.7 million and $7.9 million for the three months ended September 30, 2013 and 2012, respectively, and $30.9 million and $23.4 million for the nine months ended September 30, 2013 and 2012, respectively.

In addition to the $450.0 million of swaps in effect as of September 30, 2013, the Company held ten additional interest rate swaps with forward start dates between December 2014 and December 2016 and expiration dates between December 2017 and December 2019. As of September 30, 2013, the aggregate notional value of these ten forward-starting swaps was $525.0 million, and the weighted average interest rate was 2.7%. The combination of the interest rate swaps currently in effect and these forward-starting swaps is structured such that the notional value in effect at any given time through December 2019 does not exceed $600.0 million, which is less than the Company's expectation for variable rate debt outstanding during such period.

As of September 30, 2013 and December 31, 2012, the Company reflected liabilities from interest rate risk management activities of $29.2 million and $43.1 million, respectively, in its Consolidated Balance Sheets. In addition, as of September 30, 2013, the Company reflected $2.4 million of assets from interest rate risk management activities included in Other Assets in its Consolidated Balance Sheets. Included in Accumulated Other Comprehensive Loss at September 30, 2013 and 2012 were accumulated unrealized losses, net of income taxes, totaling $16.7 million and $28.2 million, respectively, related to these interest rate swaps.

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At September 30, 2013, all of the Company’s derivative contracts that were in effect were determined to be effective. The Company had no gains or losses related to ineffectiveness or amounts excluded from effectiveness testing recognized in the Consolidated Statements of Operations for either the three months ended September 30, 2013 or 2012, respectively. The following table presents the impact during the current and comparative prior year period for the Company's derivative financial instruments on its Consolidated Statements of Operations and Consolidated Balance Sheets.

| Derivatives in Cash Flow Hedging Relationship | Amount of Unrealized Gain (Loss), Net of Tax, Recognized in Other Comprehensive Income (Loss) Nine Months Ended September 30, 2013 | 2012 |
|---|---|---|
| | (In thousands) | |
| Interest rate swap contracts | $4,999 | $(12,254) |

| Location of Loss Reclassified from Other Comprehensive Loss into Statements of Operations | Amount of Loss Reclassified from Other Comprehensive Income (Loss) into Statements of Operations Nine Months Ended September 30, 2013 | 2012 |
|---|---|---|
| | (In thousands) | |
| Floorplan interest expense | $(7,390) | $(7,720) |
| Other interest expense | $(930) | $(856) |

The amount expected to be reclassified out of other comprehensive income (loss) into earnings (through floorplan interest expense or other interest expense) in the next twelve months is $10.6 million.

## 4. STOCK-BASED COMPENSATION PLANS

The Company provides stock-based compensation benefits to employees and non-employee directors pursuant to its 2007 Long Term Incentive Plan, as amended (the "Incentive Plan"), as well as to employees pursuant to its Employee Stock Purchase Plan (the "Purchase Plan"), as amended.

### 2007 Long Term Incentive Plan

The Incentive Plan provides for the issuance up to 7.5 million shares for grants to non-employee directors, officers and other employees of the Company and its subsidiaries of: (a) options (including options qualified as incentive stock options under the Internal Revenue Code of 1986 and options that are non-qualified), the exercise price of which may not be less than the fair market value of the common stock on the date of the grant; and (b) stock appreciation rights, restricted stock, performance awards, and bonus stock, each granted at the market price of the Company’s common stock at the date of grant. The Incentive Plan expires on March 8, 2017. The terms of the awards (including vesting schedules) are established by the Compensation Committee of the Company’s Board of Directors. As of September 30, 2013, there were 804,024 shares available for issuance under the Incentive Plan.

In 2005, the Company began granting to non-employee directors and certain employees, at no cost to the recipient, restricted stock awards or, at their election, restricted stock units pursuant to the Incentive Plan. Restricted stock awards qualify as participating securities as each contain non-forfeitable rights to dividends. As such, the two-class method is required for the computation of earnings per share. See Note 5, “Earnings Per Share,” for further details. Restricted stock awards are considered outstanding at the date of grant but are subject to vesting periods ranging from six months to five years. Vested restricted stock units, which are not considered outstanding at the grant date, will settle in shares of common stock upon the termination of the grantees’ employment or directorship. In the event an employee or non-employee director terminates his or her employment or directorship with the Company prior to the lapse of the restrictions, the shares, in most cases, will be forfeited to the Company. Compensation expense for these awards is calculated based on the market price of the Company’s common stock at the date of grant and recognized over the requisite service period. Forfeitures are estimated at the time of valuation and reduce expense ratably over the vesting period. This estimate is adjusted annually based on the extent to which actual or expected forfeitures differ from the previous estimate.

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A summary of these awards as of September 30, 2013, along with the changes during the nine months then ended follows:

| | Awards | Weighted Average Grant Date Fair Value |
|---|---|---|
| Nonvested at December 31, 2012 | 1,023,350 | $38.19 |
| Granted | 286,536 | 60.64 |
| Vested | (179,856) | 35.84 |
| Forfeited | (54,520) | 41.68 |
| Nonvested at September 30, 2013 | 1,075,510 | $44.41 |

Employee Stock Purchase Plan

In 1997, the Company adopted the Purchase Plan. The Purchase Plan authorizes the issuance of up to 3.5 million shares of common stock and provides that no options to purchase shares may be granted under the Purchase Plan after March 6, 2016. The Purchase Plan is available to all employees of the Company and its participating subsidiaries and is a qualified plan as defined by Section 423 of the Internal Revenue Code. At the end of each fiscal quarter (the “Option Period”) during the term of the Purchase Plan, employees can acquire shares of common stock from the Company at 85% of the fair market value of the common stock on the first or the last day of the Option Period, whichever is lower. As of September 30, 2013, there were 640,561 shares available for issuance under the Purchase Plan. During the nine months ended September 30, 2013 and 2012, the Company issued 83,698 and 85,081 shares, respectively, of common stock to employees participating in the Purchase Plan.

The weighted average fair value of employee stock purchase rights issued pursuant to the Purchase Plan was $13.65 and $11.23 during the nine months ended September 30, 2013 and 2012, respectively. The fair value of stock purchase rights is calculated using the grant date stock price, the value of the embedded call option and the value of the embedded put option.

Stock-Based Compensation

Total stock-based compensation cost was $3.5 million and $3.0 million for the three months ended September 30, 2013 and 2012, respectively, and $10.5 million and $8.9 million for the nine months ended September 30, 2013 and 2012, respectively. Cash received from Purchase Plan purchases was $4.4 million for the nine months ended September 30, 2013. Cash received from both option exercises and Purchase Plan purchases was $4.2 million for the nine months ended September 30, 2012. The tax benefit realized for the tax deductions from the vesting of restricted shares, which increased additional paid in capital, totaled $1.4 million for the nine months ended September 30, 2013; in addition, the tax benefit realized for the tax deductions from both options exercised and vesting of restricted shares, which increased additional paid in capital, totaled $2.4 million for the nine months ended September 30, 2012.

The Company issues new shares or treasury shares, if available, when restricted stock vests. With respect to shares issued under the Purchase Plan, the Company’s Board of Directors has authorized specific share repurchases to fund the shares issuable under the Purchase Plan.

5. EARNINGS PER SHARE

The two-class method is utilized for the computation of Earnings Per Share (“EPS”). The two-class method requires a portion of net income to be allocated to participating securities, which are unvested awards of share-based payments with non-forfeitable rights to receive dividends or dividend equivalents. The Company’s restricted stock awards qualify as participating securities as each contain non-forfeitable rights to dividends. Income allocated to these participating securities is excluded from net earnings available to common shares, as shown in the table below. Basic EPS is computed by dividing net income available to basic common shares by the weighted average number of basic common shares outstanding during the period. Diluted EPS is computed by dividing net income available to diluted common shares by the weighted average number of dilutive common shares outstanding during the period.

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The following table sets forth the calculation of EPS for the three and nine months ended September 30, 2013 and 2012.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2013 | 2012 | 2013 | 2012 |
| | (In thousands, except per share amounts) | | | |
| Weighted average basic common shares outstanding | 23,373 | 21,521 | 22,994 | 21,600 |
| Dilutive effect of contingently convertible notes and warrants | 2,962 | 926 | 2,153 | 890 |
| Dilutive effect of stock options, net of assumed repurchase of treasury stock | — | 3 | — | 4 |
| Dilutive effect of employee stock purchases, net of assumed repurchase of treasury stock | 7 | 8 | 6 | 7 |
| Weighted average dilutive common shares outstanding | 26,342 | 22,458 | 25,153 | 22,501 |
| Basic: | | | | |
| Net Income | $32,765 | $31,335 | $92,271 | $83,077 |
| Less: Earnings allocated to participating securities | 1,460 | 1,702 | 4,144 | 4,525 |
| Earnings available to basic common shares | $31,305 | $29,633 | $88,127 | $78,552 |
| Basic earnings per common share | $1.34 | $1.38 | $3.83 | $3.64 |
| Diluted: | | | | |
| Net Income | $32,765 | $31,335 | $92,271 | $83,077 |
| Less: Earnings allocated to participating securities | 1,320 | 1,641 | 3,843 | 4,373 |
| Earnings available to diluted common shares | $31,445 | $29,694 | $88,428 | $78,704 |
| Diluted earnings per common share | $1.19 | $1.32 | $3.52 | $3.50 |

The weighted average number of stock-based awards not included in the calculation of the dilutive effect of stock-based awards was immaterial for the three and nine months ended September 30, 2013 and 2012.

As discussed in Note 9, “Long-Term Debt” below, the Company is required to include the dilutive effect, if applicable, of the net shares issuable under the 2.25% Notes (as defined in Note 9) and the 2.25% Warrants sold in connection with the 2.25% Notes (“2.25% Warrants”) in its diluted common shares outstanding for the diluted earnings calculation. As a result, the number of shares included in the Company's diluted shares outstanding each period varies based upon the Company's average adjusted closing common stock price during the applicable period. Although the ten-year call options that the Company purchased on its common stock in connection with the issuance of the 2.25% Notes (“2.25% Purchased Options”) have the economic benefit of decreasing the dilutive effect of the 2.25% Notes, the Company cannot factor this benefit into the diluted common shares outstanding for the diluted earnings calculation since the impact would be anti-dilutive. The average adjusted closing price of the Company's common stock for the three months ended March 31, June 30, and September 30, 2013, was more than the conversion price then in effect at the end of those periods. Therefore, the respective dilutive effect of the 2.25% Notes was included in the computation of diluted EPS for the three months ended March 31, June 30, and September 30, 2013. Since the average price of the Company’s common stock for the three months ended March 31, June 30, and September 30, 2012 was less than the conversion price then in effect at the end of those respective periods, no net shares were included in the computation of diluted EPS for the three and nine months ended September 30, 2012, as the impact would have been anti-dilutive. Refer to Note 9, "Long-Term Debt" for a description of the change to the conversion price of the 2.25% Notes, which occurred during the three months ended September 30, 2013 as a result of the Company’s decision to pay a cash dividend in excess of $0.14.

In addition, the Company is required to include the dilutive effect, if applicable, of the net shares issuable under the 3.00% Notes (as defined in Note 9, "Long-Term Debt" ) and the 3.00% Warrants sold in connection with the 3.00% Notes (“3.00% Warrants”). As a result, the number of shares included in the Company's diluted shares outstanding each period varies based upon the Company's average adjusted closing common stock price during the applicable period. Although the ten-year call options that the Company purchased on its common stock in connection with the issuance of the 3.00% Notes ("3.00% Purchased Options") have the economic benefit of decreasing the dilutive effect of the 3.00% Notes, the Company cannot factor this benefit into the diluted common shares outstanding for the diluted earnings calculation since the impact would be anti-dilutive. Since the average price of the Company's common stock for the three months ended March 31, June 30, and September 30, of 2013 and 2012, was more than the conversion price then in effect at the end of those periods, the respective

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dilutive effect of the 3.00% Notes was included in the computation of diluted earnings per share for the three months ended March 31, June 30, and September 30, 2013 and 2012. The dilutive effect of the 3.00% Warrants was also included in the computation for the three and nine months ended September 30, 2013. Refer to Note 9, "Long-Term Debt" for a description of the change to the conversion price of the 3.00% Notes, which occurred during the three months ended September 30, 2013 as a result of the Company's decision to pay a cash dividend.

## 6. INCOME TAXES

The Company is subject to U.S. federal income taxes and income taxes in numerous U.S. states. In addition, the Company is subject to income tax in the U.K. and Brazil relative to its foreign subsidiaries. The effective income tax rate of 37.3% of pretax income for the three months ended September 30, 2013 differed from the federal statutory rate of 35.0% due primarily to taxes provided for the taxable state and foreign jurisdictions in which the Company operates, and the dispositions of certain dealerships with non-deductible goodwill.

For the nine months ended September 30, 2013, the Company's effective tax rate increased to 39.2% from 37.5% for the same period in 2012. The change was primarily due to the mix of pretax income from the taxable state jurisdictions in which the Company operates, the tax effect of acquisition costs, and the dispositions of certain dealerships with non-deductible goodwill.

As of September 30, 2013 and December 31, 2012, the Company had no unrecognized tax benefits with respect to uncertain tax positions and did not incur any interest and penalties nor did it accrue any interest for the nine months ended September 30, 2013. When applicable, consistent with prior practice, the Company recognizes interest and penalties related to uncertain tax positions in income tax expense.

Taxable years 2008 and subsequent remain open for examination by the Company's major taxing jurisdictions.

## 7. DETAIL OF CERTAIN BALANCE SHEET ACCOUNTS

Accounts and notes receivable consisted of the following:

| | September 30, 2013 (unaudited) | December 31, 2012 |
|---|---|---|
| | (In thousands) | |
| Amounts due from manufacturers | $68,591 | $64,039 |
| Parts and service receivables | 31,943 | 17,879 |
| Finance and insurance receivables | 16,545 | 16,060 |
| Other | 9,282 | 14,895 |
| Total accounts and notes receivable | 126,361 | 112,873 |
| Less allowance for doubtful accounts | 2,985 | 1,645 |
| Accounts and notes receivable, net | $123,376 | $111,228 |

Inventories consisted of the following:

| | September 30, 2013 (unaudited) | December 31, 2012 |
|---|---|---|
| | (In thousands) | |
| New vehicles | $988,174 | $895,484 |
| Used vehicles | 230,743 | 184,775 |
| Rental vehicles | 79,459 | 68,014 |
| Parts, accessories and other | 59,054 | 50,370 |
| Total inventories | 1,357,430 | 1,198,643 |
| Less lower of cost or market reserves | 5,711 | 4,355 |
| Inventories, net | $1,351,719 | $1,194,288 |

New and used vehicles are valued at the lower of specific cost or market and are removed from inventory using the specific identification method. Parts and accessories are valued at lower of cost or market determined on either a first-in, first-out basis or on an average cost basis.

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GROUP 1 AUTOMOTIVE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Property and equipment consisted of the following:

| | Estimated Useful Lives in Years (unaudited) | September 30, 2013 | December 31, 2012 |
|---|---|---|---|
| | | (dollars in thousands) | |
| Land | — | $237,084 | $232,944 |
| Buildings | 30 to 40 | 366,788 | 331,526 |
| Leasehold improvements | varies | 111,461 | 97,651 |
| Machinery and equipment | 7 to 20 | 75,761 | 69,630 |
| Furniture and fixtures | 3 to 10 | 69,533 | 61,627 |
| Company vehicles | 3 to 5 | 8,445 | 9,239 |
| Construction in progress | — | 18,974 | 28,188 |
| Total | | 888,046 | 830,805 |
| Less accumulated depreciation | | 171,532 | 163,037 |
| Property and equipment, net | | $716,514 | $667,768 |

During the nine months ended September 30, 2013, the Company incurred $45.8 million of capital expenditures for the construction of new or expanded facilities and the purchase of equipment and other fixed assets in the maintenance of the Company's dealerships and facilities. In addition, the Company purchased real estate during the nine months ended September 30, 2013 associated with existing dealership operations totaling $12.5 million. And, in conjunction with the Company's acquisition of 24 separate dealerships and five collision centers during the nine months ended September 30, 2013, the Company acquired $32.0 million of real estate and other property and equipment.

## 8. CREDIT FACILITIES

In the U.S., the Company has a $1.7 billion revolving syndicated credit arrangement with 25 financial institutions including six manufacturer-affiliated finance companies ("Revolving Credit Facility"). The Company also has a $200.0 million floorplan financing arrangement with Ford Motor Credit Company ("FMCC Facility") for financing of Ford new vehicles in the U.S. and with several other automobile manufacturers for financing of a portion of its rental vehicle inventory. In the U.K., the Company has financing arrangements with BMW Financial Services, Volkswagen Finance and Ford Motor Credit Company ("FMCC") for financing of its new and used vehicles. In Brazil, the Company has financing arrangements for new, used, and rental vehicles with several financial institutions, most of which are manufacturer affiliated. Within the Company's Consolidated Balance Sheets, Floorplan notes payable - credit facility and other primarily reflects amounts payable for the purchase of specific new, used and rental vehicle inventory (with the exception of new and rental vehicle purchases financed through lenders affiliated with the respective manufacturer) whereby financing is provided by the Revolving Credit Facility. Floorplan notes payable - manufacturer affiliates reflects amounts payable for the purchase of vehicles whereby financing is provided by the FMCC Facility, the financing of rental vehicles in the U.S., as well as the financing of new, used, and rental vehicles in both the U.K. and Brazil. Payments on the floorplan notes payable are generally due as the vehicles are sold. As a result, these obligations are reflected in the accompanying Consolidated Balance Sheets as current liabilities.

### Revolving Credit Facility

On June 20, 2013, the Company amended its Revolving Credit Facility principally to increase the total borrowing capacity from $1.35 billion to $1.7 billion and to extend the term from an expiration date on June 1, 2016 to June 20, 2018. The Revolving Credit Facility consists of two tranches, providing a maximum of $1.6 billion for U.S. vehicle inventory floorplan financing ("Floorplan Line"), as well as a maximum of $320.0 million and a minimum of $100.0 million for working capital and general corporate purposes, including acquisitions ("Acquisition Line"). The capacity under these two tranches can be re-designated within the overall $1.7 billion commitment, subject to the aforementioned limits. Up to $125.0 million of the Acquisition Line can be borrowed in either euros or pound sterling. The Revolving Credit Facility can be expanded to a maximum commitment of $1.95 billion, subject to participating lender approval. The Floorplan Line bears interest at rates equal to the one-month LIBOR plus 125 basis points for new vehicle inventory and the one-month LIBOR plus 150 basis points for used vehicle inventory. The Acquisition Line bears interest at the one-month LIBOR plus 150 basis points plus a margin that ranges from zero to 100 basis points for borrowings in U.S. dollars and 150 to 250 basis points on borrowings in euros or pound sterling, depending on the Company’s total adjusted leverage ratio. The Floorplan Line also requires a commitment fee of

0.20% per annum on the unused portion. The Acquisition Line requires a commitment fee ranging from 0.25% to 0.45% per annum, depending on the Company's total adjusted leverage ratio, based on a minimum commitment of $100.0 million less outstanding borrowings. In conjunction with the Revolving Credit Facility, the Company has $7.2 million of related unamortized costs as of September 30, 2013 that are being amortized over the term of the facility. After considering the outstanding balance of $908.2 million at September 30, 2013, the Company had $471.8 million of available floorplan borrowing capacity under the Floorplan Line. Included in the $471.8 million available borrowings under the Floorplan Line was $47.7 million of immediately available funds. The weighted average interest rate on the Floorplan Line was 1.4% as of September 30, 2013 and 1.7% as of December 31, 2012, under the Revolving Credit Facility, excluding the impact of the Company's interest rate swaps. Amounts borrowed by the Company under the Floorplan Line for specific vehicle inventory are to be repaid upon the sale of the vehicle financed, and in no case is a borrowing for a vehicle to remain outstanding for greater than one year. With regards to the Acquisition Line, no borrowings were outstanding as of September 30, 2013 or December 31, 2012, under the Revolving Credit Facility. After considering $27.0 million of outstanding letters of credit and other factors included in the Company's available borrowing base calculation, there was $227.7 million of available borrowing capacity under the Acquisition Line as of September 30, 2013. The amount of available borrowing capacity under the Acquisition Line is limited from time to time based upon certain debt covenants.

All of the Company's domestic dealership-owning subsidiaries are co-borrowers under the Revolving Credit Facility. The Company's obligations under the Revolving Credit Facility are secured by essentially all of the Company's domestic personal property (other than equity interests in dealership-owning subsidiaries), including all motor vehicle inventory and proceeds from the disposition of dealership-owning subsidiaries. The Revolving Credit Facility contains a number of significant covenants that, among other things, restrict the Company's ability to make disbursements outside of the ordinary course of business, dispose of assets, incur additional indebtedness, create liens on assets, make investments and engage in mergers or consolidations. The Company is also required to comply with specified financial tests and ratios defined in the Revolving Credit Facility, such as fixed charge coverage, total adjusted leverage, and senior secured adjusted leverage. Further, the Revolving Credit Facility restricts the Company's ability to make certain payments, such as dividends or other distributions of assets, properties, cash, rights, obligations or securities ("Restricted Payments"). The Restricted Payments cannot exceed the sum of $125.0 million plus (or minus if negative) (a) one-half of the aggregate consolidated net income of the Company for the period beginning on January 1, 2013 and ending on the date of determination and (b) the amount of net cash proceeds received from the sale of capital stock on or after January 1, 2013 and ending on the date of determination less (c) cash dividends and share repurchases ("Restricted Payment Basket"). For purposes of the calculation of the Restricted Payment Basket, net income represents such amounts per the consolidated financial statements adjusted to exclude the Company's foreign operations, non-cash interest expense, non-cash asset impairment charges, and non-cash stock-based compensation. As of September 30, 2013, the Restricted Payment Basket totaled $158.8 million. As of September 30, 2013, the Company was in compliance with all applicable covenants and ratios under the Revolving Credit Facility.

Ford Motor Credit Company Facility

The FMCC Facility provides for the financing of, and is collateralized by, the Company's U.S. Ford new vehicle inventory, including affiliated brands. This arrangement provides for $200.0 million of floorplan financing and is an evergreen arrangement that may be canceled with 30 days notice by either party. As of September 30, 2013, the Company had an outstanding balance of $153.1 million under the FMCC Facility with an available floorplan borrowing capacity of $46.9 million. This facility bears interest at a rate of Prime plus 150 basis points minus certain incentives; however, the prime rate is defined to be a minimum of 3.50%. As of September 30, 2013, the interest rate on the FMCC Facility was 5.00% before considering the applicable incentives.

Other Credit Facilities

The Company has credit facilities with BMW Financial Services, Volkswagen Finance and FMCC for the financing of new, used and rental vehicle inventories related to its U.K. operations. These facilities are denominated in pound sterling and are evergreen arrangements that may be canceled with notice by either party and bear interest at a base rate, plus a surcharge that varies based upon the type of vehicle being financed. Dependent upon the type of inventory financed, the interest rates charged on borrowings outstanding under these facilities ranged from 1.16% to 3.95% as of September 30, 2013.

The Company has credit facilities with financial institutions in Brazil, most of which are affiliated with the manufacturers, for the financing of new, used and rental vehicle inventories related to its Brazil operations. These facilities are denominated in Brazilian real and have renewal terms ranging from one month to twelve months. They may be canceled with notice by either party and bear interest at a benchmark rate, plus a surcharge that varies based upon the type of vehicle being financed. As of September 30, 2013, the interest rates charged on borrowings outstanding under these facilities ranged from 13.28% to 17.32%.

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Excluding rental vehicles financed through the Revolving Credit Facility, financing for U.S. rental vehicles is typically obtained directly from the automobile manufacturers. These financing arrangements generally require small monthly payments and mature in varying amounts over a period of two years. As of September 30, 2013, the interest rate charged on borrowings related to the Company's rental vehicle fleet varied up to 5.00%. Rental vehicles are typically transferred to used vehicle inventory when they are removed from rental service and repayment of the borrowing is required at that time.

9. LONG-TERM DEBT

The Company carries its long-term debt at face value, net of applicable discounts. Long-term debt consisted of the following:

| | September 30, 2013 | December 31, 2012 |
|---|---|---|
| | (dollars in thousands) | |
| 2.25% Convertible Senior Notes | $158,283 | $152,363 |
| 3.00% Convertible Senior Notes | 83,377 | 80,706 |
| Mortgage Facility | 48,757 | 56,677 |
| Other Real Estate Related and Long-Term Debt | 247,988 | 249,710 |
| Capital lease obligations related to real estate, maturing in varying amounts through June 2034 with a weighted average interest rate of 10.6% | 48,216 | 38,232 |
| | 586,621 | 577,688 |
| Less current maturities of mortgage facility and other long-term debt | 26,194 | 22,672 |
| | $560,427 | $555,016 |

Included in current maturities of long-term debt and short-term financing in the Company's Consolidated Balance Sheets as of September 30, 2013 and December 31, 2012 was $0.8 million and $8.7 million, respectively, of short-term financing that is due within one year of the respective balance sheet date.

Fair Value of Long-Term Debt

The Company's outstanding 2.25% Convertible Senior Notes due 2036 ("2.25% Notes") had a fair value of $240.8 million and $214.6 million as of September 30, 2013 and December 31, 2012, respectively. The Company's outstanding 3.00% Convertible Senior Notes due 2020 ("3.00% Notes") had a fair value of $247.2 million and $203.5 million as of September 30, 2013 and December 31, 2012, respectively. The fair value estimates are based on Level 2 inputs of the fair value hierarchy available as of September 30, 2013 and December 31, 2012. The Company determined the estimated fair value of its long-term debt using available market information and commonly accepted valuation methodologies. Considerable judgment is required in interpreting market data to develop the estimates of fair value. Accordingly, these estimates are not necessarily indicative of the amounts that the Company, or holders of the instruments, could realize in a current market exchange. The use of different assumptions and/or estimation methodologies could have a material effect on estimated fair values. These amounts have not been revalued since those dates, and current estimates of fair value could differ significantly from the amounts presented. The carrying value of the Company's variable rate debt approximates fair value due to the short-term nature of the interest rates.

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2.25% Convertible Senior Notes

As of September 30, 2013 and December 31, 2012, the carrying value of the 2.25% Notes, related discount and equity component consisted of the following:

| | September 30, 2013 | December 31, 2012 |
|---|---|---|
| | (In thousands) | |
| Carrying amount of equity component | $65,270 | $65,270 |
| Allocated underwriter fees, net of taxes | (1,475) | (1,475) |
| Allocated debt issuance cost, net of taxes | (58) | (58) |
| Total net equity component | $63,737 | $63,737 |
| Deferred income tax component | $8,750 | $10,846 |
| Principal amount of 2.25% Notes | $182,753 | $182,753 |
| Unamortized discount | (23,547) | (29,244) |
| Unamortized underwriter fees | (923) | (1,146) |
| Net carrying amount of liability component | $158,283 | $152,363 |
| Unamortized debt issuance cost | $37 | $45 |

For the nine months ended September 30, 2013 and 2012, the contractual interest expense and the discount amortization, which is recorded as other interest expense in the accompanying Consolidated Statements of Operations, were as follows:

| | Nine Months Ended September 30, | |
|---|---|---|
| | 2013 | 2012 |
| | (dollars in thousands) | |
| Year-to-date contractual interest expense | $3,084 | $3,084 |
| Year-to-date discount amortization (1) | $5,590 | $5,158 |
| Effective interest rate of liability component | 7.7% | 7.7% |

(1) Represents the incremental impact of the accounting for convertible debt as primarily codified in ASC 470, Debt.

The Company determined the discount using the estimated effective interest rate for similar debt with no convertible features. The original effective interest rate of 7.50% was estimated by comparing debt issuances from companies with similar credit ratings during the same annual period as the Company. The effective interest rate differs from the 7.50% due to the impact of underwriter fees associated with this issuance that were capitalized as an additional discount and are being amortized to interest expense through 2016. The effective interest rate may change in the future as a result of future repurchases of the 2.25% Notes. The Company utilized a ten-year term for the assessment of the fair value of its 2.25% Notes.

The 2.25% Notes are convertible into cash and, if applicable, common stock based on the then-applicable conversion rate under the following circumstances: (a) during any calendar quarter (and only during such calendar quarter) , if the closing price of the Company’s common stock for at least 20 trading days in the period of 30 consecutive trading days ending on the last trading day of the immediately preceding fiscal quarter is equal to or more than 130% of the applicable conversion price per share (or $77.15 as of September 30, 2013); (b) during the five business day period after any ten consecutive trading day period in which the trading price per $1,000 principal amount for each day of the ten day trading period was less than 98% of the product of the last reported sale/bid price of the Company’s common stock and the conversion rate on that day; and (c) upon the occurrence of specified corporate transactions set forth in the indenture governing the 2.25% Notes (the "2.25% Notes Indenture"). Upon conversion, a holder will receive an amount in cash and, if applicable, shares of the Company’s common stock, determined in the manner set forth in the 2.25% Notes Indenture. The if-converted value of the 2.25% Notes exceeded the principal amount of the 2.25% Notes by $56.5 million at September 30, 2013.

The Company may redeem all or part of the 2.25% Notes if the last reported sale price of the Company's common stock is greater than or equal to 130% of the conversion price then in effect for at least 20 trading days within a period of 30 consecutive trading days ending on the trading day prior to the date on which the Company mails the redemption notice. Subsequent to September 30, 2013, the 2.25% Notes qualified to be redeemed by the Company. However, the Company has not elected to redeem the 2.25% Notes.

As of September 30, 2013, the conversion rate was 16.8503 shares of common stock per $1,000 principal amount of 2.25% Notes, with a conversion price of $59.35 per share, which was reduced during the third quarter of 2013 as the result of the Company's decision to pay a cash dividend in excess of $0.14 per share. As of September 30, 2013, the exercise price of the 2.25% Warrants, which are related to the issuance of the 2.25% Notes, was reduced to $80.20 due to the Company's decision to pay a cash dividend in excess of $0.14 per share during the third quarter of 2013. If any cash dividend or distribution is made to all, or substantially all, holders of the Company's common stock in excess of $0.14 per share in the future, the conversion rate will be further adjusted based on the formula defined in the 2.25% Notes Indenture.

Under the terms of the 2.25% Purchased Options, which become exercisable upon conversion of the 2.25% Notes, the Company has the right to receive a total of 3.1 million shares of its common stock at the conversion price then in effect. The exercise price of the 2.25% Purchased Options is subject to certain adjustments that mirror the adjustments to the conversion price of the 2.25% Notes (including payments of cash dividends in excess of $0.14 per share).

3.00% Convertible Senior Notes

As of September 30, 2013 and December 31, 2012, the carrying value of the 3.00% Notes, related discount and equity component consisted of the following:

| | September 30, 2013 | December 31, 2012 |
|---|---|---|
| | (In thousands) | |
| Carrying amount of equity component (including temporary equity) | $25,359 | $25,359 |
| Allocated underwriter fees, net of taxes | (760) | (760) |
| Allocated debt issuance cost, net of taxes | (112) | (112) |
| Total net equity component | $24,487 | $24,487 |
| Deferred income tax component | $10,940 | $11,844 |
| Principal amount of 3.00% Notes | $115,000 | $115,000 |
| Unamortized discount | (29,974) | (32,505) |
| Unamortized underwriter fees | (1,649) | (1,789) |
| Net carrying amount of liability component | $83,377 | $80,706 |
| Unamortized debt issuance costs | $243 | $264 |

For the nine months ended September 30, 2013 and 2012, the contractual interest expense and the discount amortization, which is recorded as interest expense in the accompanying Consolidated Statements of Operations, were as follows:

| | Nine Months Ended September 30, | |
|---|---|---|
| | 2013 | 2012 |
| | (dollars in thousands) | |
| Year-to-date contractual interest expense | $2,588 | $2,588 |
| Year-to-date discount amortization (1) | $2,410 | $2,199 |
| Effective interest rate of liability component | 8.6% | 8.6% |

(1) Represents the incremental impact of the accounting for convertible debt as primarily codified in ASC 470, Debt.

The Company determined the discount using the estimated effective interest rate for similar debt with no convertible features. The original effective interest rate of 8.25% was estimated by receiving a range of quotes from the underwriters for the estimated rate that the Company could reasonably expect to issue non-convertible debt for the same tenure. The effective interest rate differs from the 8.25% due to the impact of underwriter fees associated with this issuance that were capitalized as an additional discount and are being amortized to interest expense through 2020. The effective interest rate may change in the future as a result of future repurchases of the 3.00% Notes. The Company utilized a ten-year term for the assessment of the fair value of its 3.00% Notes.

The 3.00% Notes are convertible into cash and, if applicable, common stock based on the then-applicable conversion rate under the following circumstances: (a) during any fiscal quarter (and only during such fiscal quarter), if the last reported sale price of the Company's common stock for at least 20 trading days in the period of 30 consecutive trading days ending on the last trading day of the immediately preceding fiscal quarter is equal to or more than 130% of the applicable conversion price per share (or $48.61 as of September 30, 2013) (the “3.00% Stock Price Trigger”); (b) during the five business day period after any ten consecutive trading day period in which the trading price per $1,000 principal amount for each day of the ten day trading period was less than 98% of the product of the last reported sale/bid price of the Company’s common stock and the conversion rate on that day; and (c) upon the occurrence of specified corporate transactions set forth in the indenture governing the 3.00%

Notes (the "3.00% Notes Indenture"). Upon conversion, a holder will receive an amount in cash and, if applicable, shares of the Company's common stock, determined in the manner set forth in the 3.00% Notes Indenture.

As a result of the 3.00% Stock Price Trigger on September 30, 2013, the 3.00% Notes are convertible at the option of the holders during the three months ending December 31, 2013. As such, the Company reclassified the redeemable equity portion of the 3.00% Notes to temporary equity from the additional paid-in capital component of permanent equity on the Consolidated Balance Sheet as of September 30, 2013. The debt portion of the 3.00% Notes continued to be classified as a long-term liability as of September 30, 2013, since the Company has the intent and ability to refinance any conversion of the 3.00% Notes with another long-term debt instrument. The combination of the debt portion and temporary equity portion represents the aggregate principal obligation of the 3.00% Notes redeemable at the option of the holders as of September 30, 2013. The if-converted value of the 3.00% Notes exceeded the principal amount of the 3.00% Notes by $123.9 million at September 30, 2013.

As of September 30, 2013, the conversion rate was 26.7419 shares of common stock per $1,000 principal amount of 3.00% Notes, with a conversion price of $37.39 per share, which was reduced during the third quarter of 2013 as the result of the Company's decision to pay a cash dividend. As of September 30, 2013, the exercise price of the 3.00% Warrants, which are related to the issuance of the 3.00% Notes, was reduced to $54.95 due to the Company's decision to pay a cash dividend during the third quarter of 2013. If any cash dividend or distribution is made to all, or substantially all, holders of the Company's common stock in the future, the conversion rate will be further adjusted based on the formula defined in the 3.00% Notes Indenture.

Under the terms of the 3.00% Purchased Options, which become exercisable upon conversion of the 3.00% Notes, the Company has the right to receive a total of 3.1 million shares of its common stock at the conversion price then in effect. The exercise price of the 3.00% Purchased Options is subject to certain adjustments that mirror the adjustments to the conversion price of the 3.00% Notes (including payments of cash dividends).

Real Estate Credit Facility

Group 1 Realty, Inc., a wholly-owned subsidiary of the Company, entered into a real estate credit facility with Bank of America, N.A. and Comerica Bank (as amended and restated, the "Mortgage Facility") providing the right for up to $83.4 million of term loans, of which $60.7 million had been used as of September 30, 2013. The term loans can be expanded provided that (a) no default or event of default exists under the Mortgage Facility; (b) the Company obtains commitments from the lenders who would qualify as assignees for such increased amounts; and (c) certain other agreed upon terms and conditions have been satisfied. This facility is guaranteed by the Company and substantially all of the domestic subsidiaries of the Company and is secured by the real property owned by the Company that is mortgaged under the Mortgage Facility. The Company capitalized debt issuance costs related to the Mortgage Facility that are being amortized over the term of the facility, $0.4 million of which were still unamortized as of September 30, 2013.

The interest rate is equal to (a) the per annum rate equal to one-month LIBOR plus 2.50% per annum, determined on the first day of each month; or (b) 1.45% per annum in excess of the higher of (i) the Bank of America prime rate (adjusted daily on the day specified in the public announcement of such price rate), (ii) the Federal Funds Rate adjusted daily, plus 0.5% or (iii) the per annum rate equal to the one-month LIBOR plus 1.05% per annum. The Federal Funds Rate is the weighted average of the rates on overnight Federal funds transactions with members of the Federal Reserve System arranged by Federal funds brokers on such day, as published by the Federal Reserve Bank of New York on the business day succeeding such day.

The Company is required to make quarterly principal payments equal to 1.25% of the principal amount outstanding and is required to repay the aggregate amount outstanding on the maturity dates of the individual property borrowings, ranging, from December 29, 2015 through February 27, 2017. For the nine months ended September 30, 2013, the Company made no additional borrowings and principal payments of $7.9 million on outstanding borrowings from the Mortgage Facility. As of September 30, 2013, borrowings outstanding under the Mortgage Facility totaled $48.8 million, with $2.7 million recorded as a current maturity of long-term debt in the accompanying Consolidated Balance Sheets.

The Mortgage Facility also contains usual and customary provisions limiting the Company's ability to engage in certain transactions, including limitations on the Company's ability to incur additional debt, additional liens, make investments, and pay distributions to its stockholders. In addition, the Mortgage Facility requires certain financial covenants that are identical to those contained in the Company's Revolving Credit Facility. As of September 30, 2013, the Company was in compliance with all applicable covenants and ratios under the Mortgage Facility.

Real Estate Related Debt

The Company, as well as certain of its wholly-owned subsidiaries, has entered into separate term mortgage loans in the U.S. with four of its manufacturer-affiliated finance partners – Toyota Motor Credit Corporation ("TMCC"), Mercedes-Benz Financial Services USA, LLC ("MBFS"), BMW Financial Services NA, LLC ("BMWFS"), FMCC and several third-party financial institutions (collectively, “Real Estate Notes”). The Real Estate Notes are on specific buildings and/or properties and are guaranteed by the Company. Each loan was made in connection with, and is secured by mortgage liens on, the real property owned by the Company that is mortgaged under the Real Estate Notes. The Real Estate Notes bear interest at fixed rates between 3.67% and 9.00%, and at variable indexed rates plus a spread between 2.25% and 3.35% per annum. The Company capitalized debt issuance costs related to the Real Estate Notes that are being amortized over the terms of the notes, $0.8 million of which were still unamortized as of September 30, 2013.

The loan agreements with TMCC consist of eight term loans. As of September 30, 2013, $52.0 million was outstanding under the TMCC term loans, with $7.0 million classified as a current maturity of long-term debt in the accompanying Consolidated Balance Sheets. The maturity dates vary from three to seven years and provide for monthly payments based on a 20-year amortization schedule. These eight loans are cross-collateralized and cross-defaulted with each other and are cross-defaulted with the Revolving Credit Facility.

The loan agreements with MBFS consist of three term loans. As of September 30, 2013, $45.9 million was outstanding under the MBFS term loans, with $1.7 million classified as a current maturity of long-term debt in the accompanying Consolidated Balance Sheets. The agreements provide for monthly payments based on a 20-year amortization schedule and have a maturity date of five years. These three loans are cross-collateralized and cross-defaulted with each other and are also cross-defaulted with the Revolving Credit Facility.

The loan agreements with BMWFS consist of 14 term loans. As of September 30, 2013, $71.1 million was outstanding under the BMWFS term loans, with $4.1 million classified as a current maturity of long-term debt in the accompanying Consolidated Balance Sheets. The agreements provide for monthly payments based on a 15-year amortization schedule and have a maturity date of 7 years. In the case of three properties owned by subsidiaries, the applicable loan is also guaranteed by the subsidiary real property owner. These 14 loans are cross-collateralized with each other. In addition, they are cross-defaulted with each other, the Revolving Credit Facility, and certain dealership franchising agreements with BMW of North America, LLC.

In addition, agreements with third-party financial institutions consist of 11 term loans for an aggregate principal amount of $59.4 million, to finance real estate associated with the Company’s dealerships. These loans are inclusive of the Company's one term loan with FMCC with $5.4 million outstanding and $0.2 million classified as a current maturity of long-term debt. The loans are being repaid in monthly installments that will mature by November 2022. As of September 30, 2013, borrowings under these notes totaled $52.4 million, with $3.0 million classified as a current maturity of long-term debt in the accompanying Consolidated Balance Sheets. Nine of these loans are cross-defaulted with the Revolving Credit Facility. The other two loans, including the FMCC loan, are subject to separate restrictions and covenants. The Company was in compliance with all applicable covenants and ratios under the agreements.

The Company has also entered into separate term mortgage loans in the U.K. with another third-party financial institution which are secured by the Company’s U.K. properties. These mortgage loans (collectively, “Foreign Notes”) are being repaid in monthly installments that mature August 2027. As of September 30, 2013, borrowings under the Foreign Notes totaled $21.9 million, with $2.8 million classified as a current maturity of long-term debt in the accompanying Consolidated Balance Sheets.

## 10. FAIR VALUE MEASUREMENTS

Accounting Standards Codification (“ASC”) 820 defines fair value as the price that would be received in the sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date; requires disclosure of the extent to which fair value is used to measure financial and non-financial assets and liabilities, the inputs utilized in calculating valuation measurements, and the effect of the measurement of significant unobservable inputs on earnings, or changes in net assets, as of the measurement date; establishes a three-level valuation hierarchy based upon the transparency of inputs utilized in the measurement and valuation of financial assets or liabilities as of the measurement date:

- Level 1 — unadjusted, quoted prices for identical assets or liabilities in active markets;

•Level 2 — quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, and inputs other than quoted market prices that are observable or that can be corroborated by observable market data by correlation; and

•Level 3 — unobservable inputs based upon the reporting entity’s internally developed assumptions that market participants would use in pricing the asset or liability.

The Company’s financial instruments consist primarily of cash and cash equivalents, contracts-in-transit and vehicle receivables, accounts and notes receivable, investments in debt and equity securities, accounts payable, credit facilities, long-term debt and interest rate swaps. The fair values of cash and cash equivalents, contracts-in-transit and vehicle receivables, accounts and notes receivable, accounts payable, and credit facilities approximate their carrying values due to the short-term nature of these instruments or the existence of variable interest rates.

The Company periodically invests in unsecured, corporate demand obligations with manufacturer-affiliated finance companies, which bear interest at a variable rate and are redeemable on demand by the Company. Therefore, the Company has classified these demand obligations as cash and cash equivalents in the accompanying Consolidated Balance Sheets. The Company determined that the valuation measurement inputs of these instruments include inputs other than quoted market prices, that are observable or that can be corroborated by observable data by correlation. Accordingly, the Company has classified these instruments within Level 2 of the hierarchy framework.

The Company's derivative financial instruments are recorded at fair market value. See Note 3, "Derivative Instruments and Risk Management Activities" for further details regarding the Company's derivative financial instruments.

The Company evaluated its assets and liabilities for those that met the criteria of the disclosure requirements and fair value framework of ASC 820 and identified investments in marketable securities, debt instruments, and interest rate derivative financial instruments as having met such criteria. The respective fair values measured on a recurring basis as of September 30, 2013 and December 31, 2012, respectively, were as follows:

| | As of September 30, 2013 | | |
|---|---|---|---|
| | Level 1 | Level 2 | Total |
| | (In thousands) | | |
| Assets: | | | |
| Interest rate derivative financial instruments | $— | $2,413 | $2,413 |
| Debt securities: | | | |
| Demand obligations | — | 65 | 65 |
| Total | $— | $2,478 | $2,478 |
| Liabilities: | | | |
| Interest rate derivative financial instruments | $— | $29,184 | $29,184 |
| Total | $— | $29,184 | $29,184 |

| | As of December 31, 2012 | | |
|---|---|---|---|
| | Level 1 | Level 2 | Total |
| | (In thousands) | | |
| Assets: | | | |
| Debt securities: | | | |
| Demand obligations | $— | $616 | $616 |
| Total | $— | $616 | $616 |
| Liabilities: | | | |
| Interest rate derivative financial instruments | $— | $43,089 | $43,089 |
| Total | $— | $43,089 | $43,089 |

## 11. COMMITMENTS AND CONTINGENCIES

From time to time, the Company’s dealerships are named in various types of litigation involving customer claims, employment matters, class action claims, purported class action claims, as well as claims involving the manufacturer of automobiles, contractual disputes and other matters arising in the ordinary course of business. Due to the nature of the automotive retailing business, the Company may be involved in legal proceedings or suffer losses that could have a material adverse effect on the Company’s business. In the normal course of business, the Company is required to respond to customer, employee and other third-party complaints. Amounts that have been accrued or paid related to the settlement of litigation are included in SG&A expenses in the Company’s Consolidated Statements of Operations. In addition, the manufacturers of the vehicles that the Company sells and services have audit rights allowing them to review the validity of amounts claimed for incentive, rebate or warranty-related items and charge the Company back for amounts determined to be invalid payments under the manufacturers’ programs, subject to the Company’s right to appeal any such decision. Amounts that have been accrued or paid related to the settlement of manufacturer chargebacks of recognized incentives and rebates are included in cost of sales in the Company’s Consolidated Statements of Operations, while such amounts for manufacturer chargebacks of recognized warranty-related items are included as a reduction of revenues in the Company’s Consolidated Statements of Operations.

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GROUP 1 AUTOMOTIVE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Legal Proceedings

Currently, the Company is not party to any legal proceedings that, individually or in the aggregate, are reasonably expected to have a material adverse effect on the Company's results of operations, financial condition, or cash flows, including class action lawsuits. However, the results of current, or future, matters cannot be predicted with certainty, and an unfavorable resolution of one or more of such matters could have a material adverse effect on the Company's results of operations, financial condition, or cash flows.

In December 2011, an adverse jury verdict was rendered against the Company in the San Diego County Superior Court, awarding $7.5 million to the plaintiff who sought reimbursement for medical expenses, lost wages and pain and suffering arising from an accident involving one of the Company's customer shuttle vans and the plaintiff's motorcycle. The Company's insurance covered any loss in excess of its $1.0 million self-insured retention relative to this matter. The Company fully accrued the amount of the award and the related insurance charge as a current account receivable and a current accrued expense, respectively, in the Consolidated Balance Sheet as of December 31, 2011. During the three months ended September 30, 2013, the insurance company settled this matter with the plaintiff, the Company paid its self-insured retention and the full amount of the current account receivable and current accrued expense was settled as originally anticipated.

Other Matters

The Company, acting through its subsidiaries, is the lessee under many real estate leases that provide for the use by the Company's subsidiaries of their respective dealership premises. Pursuant to these leases, the Company's subsidiaries generally agree to indemnify the lessor and other parties from certain liabilities arising as a result of the use of the leased premises, including environmental liabilities, or a breach of the lease by the lessee. Additionally, from time to time, the Company enters into agreements in connection with the sale of assets or businesses in which it agrees to indemnify the purchaser, or other parties, from certain liabilities or costs arising in connection with the assets or business. Also, in the ordinary course of business in connection with purchases or sales of goods and services, the Company enters into agreements that may contain indemnification provisions. In the event that an indemnification claim is asserted, liability would be limited by the terms of the applicable agreement.

From time to time, primarily in connection with dealership dispositions, the Company's subsidiaries assign or sublet to the dealership purchaser the subsidiaries' interests in any real property leases associated with such dealerships. In general, the Company's subsidiaries retain responsibility for the performance of certain obligations under such leases to the extent that the assignee or sublessee does not perform, whether such performance is required prior to or following the assignment or subletting of the lease. Additionally, the Company and its subsidiaries generally remain subject to the terms of any guarantees made by the Company and its subsidiaries in connection with such leases. Although the Company generally has indemnification rights against the assignee or sublessee in the event of non-performance under these leases, as well as certain defenses, and the Company presently has no reason to believe that it or its subsidiaries will be called on to perform under any such assigned leases or subleases, the Company estimates that lessee rental payment obligations during the remaining terms of these leases were $27.2 million as of September 30, 2013. The Company's exposure under these leases is difficult to estimate and there can be no assurance that any performance of the Company or its subsidiaries required under these leases would not have a material adverse effect on the Company's business, financial condition, or cash flows. The Company and its subsidiaries also may be called on to perform other obligations under these leases, such as environmental remediation of the leased premises or repair of the leased premises upon termination of the lease. However, the Company does not have any known material environmental commitments or contingencies and presently has no reason to believe that it or its subsidiaries will be called on to so perform.

In the ordinary course of business, the Company is subject to numerous laws and regulations, including automotive, environmental, health and safety, and other laws and regulations. The Company does not anticipate that the costs of such compliance will have a material adverse effect on its business, consolidated results of operations, financial condition, or cash flows, although such outcome is possible given the nature of its operations and the extensive legal and regulatory framework applicable to its business. The Dodd-Frank Wall Street Reform and Consumer Protection

Act, which was signed into law on July 21, 2010, established a new consumer financial protection agency with broad regulatory powers. Although automotive dealers are generally excluded, the Dodd-Frank Act could lead to additional, indirect regulation of automotive dealers through its regulation of automotive finance companies and other financial institutions. In addition, the Patient Protection and Affordable Care Act, which was signed into law on March 23, 2010, has the potential to increase the Company’s future annual employee health care costs. Further, new laws and regulations, particularly at the federal level, may be enacted, which could also have a materially adverse impact on its business.

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GROUP 1 AUTOMOTIVE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

## 12. INTANGIBLE FRANCHISE RIGHTS AND GOODWILL

The following is a roll-forward of the Company's intangible franchise rights and goodwill accounts:

| | Intangible Franchise Rights | Goodwill | |
|---|---|---|---|
| | (In thousands) | | |
| BALANCE, December 31, 2012 | $196,058 | $582,384 | (1) |
| Additions through acquisitions | 99,965 | 125,466 | |
| Disposals | (5,826) | (6,333) | |
| Currency Translation | (10,391) | (11,546) | |
| Tax adjustments | — | (100) | |
| BALANCE, September 30, 2013 | 279,806 | 689,871 | (1) |

(1) Net of accumulated impairment of $40.3 million

The increase in the Company's goodwill and intangible franchise rights was primarily related to the purchase of franchises in the U.K. and Brazil.

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GROUP 1 AUTOMOTIVE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

## 13. ACCUMULATED OTHER COMPREHENSIVE LOSS

Changes in the balances of each component of accumulated other comprehensive loss for the nine months ended September 30, 2013 and 2012 were as follows:

| | Nine Months Ended September 30, 2013 | | | |
|---|---|---|---|---|
| | Accumulated foreign currency translation loss | Accumulated gain (loss) on marketable securities | Accumulated (loss) gain on interest rate swaps | Total |
| | (In thousands) | | | |
| Balance, December 31, 2012 | $(6,126) | $— | $(26,931) | $(33,057) |
| Other comprehensive income (loss) before reclassifications: | | | | — |
| Pre-tax | (23,487) | — | 7,998 | (15,489) |
| Tax effect | — | — | (2,999) | (2,999) |
| Amounts reclassified from accumulated other comprehensive income to: | | | | |
| Floorplan interest expense | — | — | 7,390 | 7,390 |
| Other interest expense | — | — | 930 | 930 |
| Tax effect | — | — | (3,120) | (3,120) |
| Net current period other comprehensive (loss) income | (23,487) | — | 10,199 | (13,288) |
| Balance, September 30, 2013 | $(29,613) | $— | $(16,732) | $(46,345) |

| | Nine Months Ended September 30, 2012 | | | |
|---|---|---|---|---|
| | Accumulated foreign currency translation gain (loss) | Accumulated gain (loss) on marketable securities | Accumulated (loss) gain on interest rate swaps | Total |
| | (In thousands) | | | |
| Balance, December 31, 2011 | $(7,969) | $8 | $(21,275) | $(29,236) |
| Other comprehensive income (loss) before reclassifications: | | | | |
| Pre-tax | 1,850 | (13) | (19,606) | (17,769) |
| Tax effect | — | 5 | 7,352 | 7,357 |
| Amounts reclassified from accumulated other comprehensive income to: | | | | |
| Floorplan interest expense | — | — | 7,720 | 7,720 |
| Other interest expense | — | — | 856 | 856 |
| Tax effect | — | — | (3,216) | (3,216) |
| Net current period other comprehensive (loss) income | 1,850 | (8) | (6,894) | (5,052) |
| Balance, September 30, 2012 | $(6,119) | $— | $(28,169) | $(34,288) |

## 14. SEGMENT INFORMATION

As of September 30, 2013, the Company had three reportable segments: (1) the U.S., (2) the U.K., and (3) Brazil. Each of the reportable segments is comprised of retail automotive franchises, which sell new vehicles, used vehicles, parts and automotive services, finance and insurance products, and collision centers. The vast majority of the Company's corporate activities are associated with the operations of the U.S. operating segments and therefore the corporate financial results are included within the U.S. reportable segment.

GROUP 1 AUTOMOTIVE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The reportable segments identified above are the business activities of the Company for which discrete financial information is available and for which operating results are regularly reviewed by our chief operating decision maker to allocate resources and assess performance. Our chief operating decision maker is our Chief Executive Officer. Reportable segment revenue, gross profit, SG&A, floorplan interest expense, net income and capital expenditures were as follows for the three and nine months ended September 30, 2013 and 2012:

| | Three Months Ended September 30, 2013 | | | | Nine Months Ended September 30, 2013 | | | |
|---|---|---|---|---|---|---|---|---|
| | U.S. | U.K. | Brazil | Total | U.S. | U.K. | Brazil (1) | Total |
| | (In thousands) | | | | (In thousands) | | | |
| Revenues | $1,889,378 | $234,914 | $215,855 | $2,340,147 | $5,492,819 | $613,428 | $532,842 | $6,639,089 |
| Gross profit | 280,265 | 25,513 | 23,684 | 329,462 | 843,683 | 68,428 | 59,114 | 971,225 |
| Selling, general and administrative expense (2) | 206,635 | 19,656 | 20,572 | 246,863 | 626,939 | 54,262 | 50,254 | 731,455 |
| Floorplan interest expense | 8,087 | 425 | 2,178 | 10,690 | 25,027 | 1,152 | 4,748 | 30,927 |
| Other interest expense (income), net | 9,649 | 293 | 29 | 9,971 | 27,990 | 800 | (7) | 28,783 |
| Net income | 28,963 | 3,607 | 195 | 32,765 | 82,637 | 8,095 | 1,539 | 92,271 |
| Capital expenditures | 12,502 | 311 | 623 | 13,436 | 43,197 | 1,071 | 1,551 | 45,819 |

(1) Represents financial data from date of acquisition in February 2013.

(2) Includes a net gain on the disposition of dealerships of $1.4 million and $10.4 million for the three and nine months ended September 30, 2013, respectively, in the U.S. segment. Also, includes losses due to catastrophic events of $0.3 million and $12.2 million for the three and nine months ended September 30, 2013, respectively, in the U.S. segment. For the nine months ended September 30, 2013, includes acquisition costs of $5.2 million, $0.1 million and $1.2 million in the U.S., U.K. and Brazil segments, respectively. Also includes severance cost of $0.3 million each in the U.S. and Brazil segments, as well as lease termination charges of $0.2 million in the U.S. segment for the nine months ended September 30, 2013.

| | Three Months Ended September 30, 2012 | | | | Nine Months Ended September 30, 2012 | | | |
|---|---|---|---|---|---|---|---|---|
| | U.S. | U.K. | Brazil | Total | U.S. | U.K. | Brazil | Total |
| | (In thousands) | | | | (In thousands) | | | |
| Revenues | $1,814,186 | $162,386 | $— | $1,976,572 | $5,158,039 | $379,104 | $— | $5,537,143 |
| Gross profit | 271,562 | 19,669 | — | 291,231 | 792,046 | 44,953 | — | 836,999 |
| Selling, general and administrative expense (1) | 200,980 | 15,102 | — | 216,082 | 593,874 | 35,647 | — | 629,521 |
| Floorplan interest expense | 7,613 | 329 | — | 7,942 | 22,640 | 784 | — | 23,424 |
| Other interest expense, net | 9,416 | 203 | — | 9,619 | 27,406 | 443 | — | 27,849 |
| Net income | 28,633 | 2,702 | — | 31,335 | 78,110 | 4,967 | — | 83,077 |
| Capital expenditures | 13,423 | 99 | — | 13,522 | 39,422 | 259 | — | 39,681 |

(1) Includes a loss due to catastrophic events of $2.7 million, as well as a net gain on real estate transactions of $1.1 million for the nine months ended September 30, 2012, in the U.S. segment.

Reportable segment goodwill and intangible franchise rights and total assets by segment were as follows:

| | As of September 30, 2013 | | | |
|---|---|---|---|---|
| | U.S. | U.K. | Brazil | Total |
| | (In thousands) | | | |
| Goodwill and Intangible Franchise Rights | $762,380 | $27,663 | $179,634 | $969,677 |
| Total assets | 2,845,727 | 228,192 | 335,989 | 3,409,908 |

| | As of December 31, 2012 | | | |
|---|---|---|---|---|
| | U.S. | U.K. | Brazil | Total |
| | (In thousands) | | | |
| Goodwill and Intangible Franchise Rights | $752,372 | $26,070 | $— | $778,442 |
| Total assets | 2,860,771 | 162,244 | — | 3,023,015 |

CAUTIONARY STATEMENT ABOUT FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q (this “Form 10-Q”) includes certain “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933, as amended (“Securities Act”), and Section 21E of the Securities Exchange Act of 1934, as amended (“Exchange Act”). This information includes statements regarding our plans, goals or current expectations with respect to, among other things:

•our future operating performance;
•our ability to maintain or improve our margins;
•operating cash flows and availability of capital;
•the completion of future acquisitions;
•the future revenues of acquired dealerships;
•future stock repurchases, refinancing of convertible notes and dividends;
•future capital expenditures;
•changes in sales volumes and availability of credit for customer financing in new and used vehicles and sales volumes in the parts and service markets;
•business trends in the retail automotive industry, including the level of manufacturer incentives, new and used vehicle retail sales volume, customer demand, interest rates and changes in industry-wide inventory levels; and
•availability of financing for inventory, working capital, real estate and capital expenditures.

Although we believe that the expectations reflected in these forward-looking statements are reasonable when and as made, we cannot assure that these expectations will prove to be correct. When used in this Form 10-Q, the words “anticipate,” “believe,” “estimate,” “expect,” "intend," “may” and similar expressions, as they relate to our company and management, are intended to identify forward-looking statements. Our forward-looking statements are not assurances of future performance and involve risks and uncertainties. Actual results may differ materially from anticipated results in the forward-looking statements for a number of reasons, including:

•depressed consumer confidence, raised unemployment and limited availability of consumer credit, may cause a marked decline in demand for new and used vehicles;
•future deterioration in the economic environment, including consumer confidence, interest rates, the price of gasoline, the level of manufacturer incentives and the availability of consumer credit may affect the demand for new and used vehicles, replacement parts, maintenance and repair services and finance and insurance products;
•adverse domestic and international developments such as war, terrorism, political conflicts or other hostilities may adversely affect the demand for our products and services;
•the existing and future regulatory environment, including legislation related to the Dodd-Frank Wall Street Reform and Consumer Protection Act, climate control changes legislation, and unexpected litigation or adverse legislation, including changes in state franchise laws, may impose additional costs on us or otherwise adversely affect us;
•a concentration of risk associated with our principal automobile manufacturers, especially Toyota, Nissan, Honda, BMW, Ford, Daimler, General Motors, Chrysler, and Volkswagen, because of financial distress, bankruptcy, natural disasters that disrupt production or other reasons, may not continue to produce or make available to us vehicles that are in high demand by our customers or provide financing, insurance, advertising or other assistance to us;
•restructuring by one or more of our principal manufacturers, up to and including bankruptcy may cause us to suffer financial loss in the form of uncollectible receivables, devalued inventory or loss of franchises;
•requirements imposed on us by our manufacturers may require dispositions, limit our acquisitions or increases in the level of capital expenditures related to our dealership facilities;
•our existing and/or new dealership operations may not perform at expected levels or achieve expected improvements;
•our failure to achieve expected future cost savings or future costs may be higher than we expect;

- manufacturer quality issues may negatively impact vehicle sales and brand reputation;
- available capital resources, increases in cost of financing (such as higher interest rates) and our various debt agreements may limit our ability to complete acquisitions, complete construction of new or expanded facilities, repurchase shares or pay dividends;
- our ability to refinance or obtain financing in the future may be limited and the cost of financing could increase significantly;
- foreign exchange controls and currency fluctuations;
- new accounting standards could materially impact our reported earnings per share;
- our ability to acquire new dealerships and successfully integrate those dealerships into our business;
- the impairment of our goodwill, our indefinite-lived intangibles and our other long-lived assets;
- natural disasters and adverse weather events;
- our foreign operations and sales in the U.K. and Brazil, which pose additional risks;
- the inability to adjust our cost structure to offset any reduction in the demand for our products and services;
- our loss of key personnel;
- competition in our industry may impact our operations or our ability to complete additional acquisitions;
- the failure to achieve expected sales volumes from our new franchises;
- insurance costs could increase significantly and all of our losses may not be covered by insurance; and
- our inability to obtain inventory of new and used vehicles and parts, including imported inventory, at the cost, or in the volume, we expect.

For additional information regarding known material factors that could cause our actual results to differ from our projected results, please see (a) Part II, “Item 1A. Risk Factors” in this Form 10-Q and (b) Part I, “Item 1A. Risk Factors” in our 2012 Form 10-K.

Readers are cautioned not to place undue reliance on forward-looking statements, which speak only as of the date hereof. We undertake no responsibility to publicly release the result of any revision of our forward-looking statements after the date they are made.

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## Item 2. 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 because of various factors. See “Cautionary Statement about Forward-Looking Statements.”

### Overview

We are a leading operator in the automotive retail industry. Through our operating subsidiaries, we sell new and used cars and light trucks; arrange related vehicle financing; sell service and insurance contracts; provide automotive maintenance and repair services; and sell vehicle parts. Effective with the acquisition of UAB Motors Participações S.A. (“UAB Motors”) on February 28, 2013, we are aligned into four geographic regions: the East and West Regions in the United States ("U.S."), the United Kingdom ("U.K.") Region, and the Brazil Region. Also, in conjunction with the acquisition of UAB Motors and associated changes in how our chief operating decision maker evaluates performance and allocates resources, we reaffirmed that each region represents an operating segment. Each U.S. region is managed by a regional vice president who reports directly to our Chief Executive Officer and is responsible for the overall performance of their region. The financial matters of each U.S. region are managed by a regional chief financial officer who reports directly to our Chief Financial Officer. As part of this determination, we further concluded that the East and West Regions of the U.S. continue to be economically similar in that they deliver the same products and services to a common customer group, their customers are generally individuals, they follow the same procedures and methods in managing their operations, and they operate in similar regulatory environments and, therefore we aggregate these two regions into one reportable segment. As such, our three reportable segments are the U.S., which includes the activities of our corporate office, the U.K. and Brazil.

As of September 30, 2013, we owned and operated 179 franchises, representing 33 brands of automobiles, at 141 dealership locations and 35 collision service centers worldwide. We own 138 franchises at 109 dealerships, and 26 collision centers in the U.S., 19 franchises at 14 dealerships and four collision centers in the U.K. as well as 22 franchises at 18 dealerships and five collision service centers in Brazil. Our operations are primarily located in major metropolitan areas in Alabama, California, Florida, Georgia, Kansas, Louisiana, Maryland, Massachusetts, Mississippi, New Hampshire, New Jersey, New York, Oklahoma, South Carolina and Texas in the U.S., in 13 towns in the U.K. and in key metropolitan markets in the states of Sao Paulo and Parana in Brazil.

### Outlook

During the nine months ended September 30, 2013, consumer demand for new and used vehicles in the U.S. improved over 2012. According to industry experts, the average seasonally adjusted annual rate of sales (“SAAR”) in the U.S. through the nine months ended September 30, 2013 was 15.5 million units, compared to 14.2 million units for the same period in 2012. We believe that the improving economic trends provide opportunities for us to improve our operating results as we: (a) expand our new and used vehicle unit sales and improve our sales efficiency; (b) continue to focus on our higher margin parts and service business, implementing strategic selling methods, and improving operational efficiencies; (c) invest capital where necessary to support our anticipated growth, particularly in our parts and service business; and (d) further leverage our revenue and gross profit growth through continued cost controls.

The U.K. economy represents the sixth largest economy in the world. The U.K. automotive sales market continues to outperform the rest of Europe. Vehicle registrations in the U.K. increased 12.1% and 10.8% through the three and nine months ended September 30, 2013, respectively, when compared to the same period a year ago. The latest industry estimates have new vehicle sales continuing to grow for the remainder of the year.

The Brazilian economy represents the seventh largest in the world and recently has been one of the fastest growing economies in the world. We believe the Brazilian government's decision in 2013 to not implement the planned increases in Industrial Products taxes that were scheduled for April 1, 2013 and to freeze current tax rates indefinitely were positive developments for the market. However, the Brazilian economy is facing many challenges and is not demonstrating significant growth at the moment. Industry sales in Brazil declined 10.0% during the three months ended September 30, 2013 as compared to the same period a year ago and we have seen a rise in inflation and interest rates and a decrease in the value of the Brazilian real compared to the U.S. dollar. We expect industry sales in Brazil to be flat in 2013, but we remain optimistic for growth in the longer run.

Our operations have generated, and we believe that our operations will continue to generate, positive cash flow. As such, we are focused on maximizing the return that we generate from our invested capital and positioning our balance sheet to take advantage of investment opportunities as they arise. We continue to closely scrutinize all planned future capital spending and work closely with our original equipment manufacturer ("OEM") partners in this area to make prudent investment decisions that are expected to generate an adequate return and/or improve the customer experience. We anticipate that our capital spending for the full year of 2013 will be approximately $75.0 million.

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We remain committed to our growth-by-acquisition strategy. We believe that significant opportunities exist to enhance our portfolio with dealerships that meet our stringent investment criteria in the U.S., U.K. and Brazil. During the first nine months of 2013, we completed the acquisition of 24 dealerships in the U.S., U.K. and Brazil. We will continue to pursue dealership investment opportunities that we believe will add value for our stockholders.

Financial and Operational Highlights

Our operating results reflect the combined performance of each of our interrelated business activities, which include the sale of new vehicles, used vehicles, finance and insurance products, and parts, as well as maintenance and collision repair services. Historically, each of these activities has been directly or indirectly impacted by a variety of supply/demand factors, including vehicle inventories, consumer confidence, discretionary spending, availability and affordability of consumer credit, manufacturer incentives, weather patterns, fuel prices and interest rates. For example, during periods of sustained economic downturn or significant supply/demand imbalances, new vehicle sales may be negatively impacted as consumers tend to shift their purchases to used vehicles. Some consumers may even delay their purchasing decisions altogether, electing instead to repair their existing vehicles. In such cases, however, we believe the new vehicle sales impact on our overall business is mitigated by our ability to offer other products and services, such as used vehicles and parts, as well as maintenance and collision repair services. In addition, our ability to reduce our costs in response to lower sales also tempers the impact of lower new vehicle sales volume.

We generally experience higher volumes of vehicle sales and service in the second and third calendar quarters of each year in the U.S., in the first and third quarters in the U.K. and expect higher volumes during the third and fourth quarters in Brazil. This seasonality is generally attributable to consumer buying trends and the timing of manufacturer new vehicle model introductions. In addition, in some regions of the U.S., vehicle purchases decline during the winter months due to inclement weather. As a result, our revenues and operating income are typically lower in the first and fourth quarters and higher in the second and third quarters. Other factors unrelated to seasonality, such as changes in economic condition, manufacturer incentive programs, or shifts in governmental taxes or regulations may exaggerate seasonal or cause counter-seasonal fluctuations in our revenues and operating income.

For the three months ended September 30, 2013, total revenues increased 18.4% from 2012 levels to $2.3 billion and gross profit improved 13.1% to $329.5 million over the prior year period. For the nine months ended September 30, 2013, total revenues increased 19.9% from 2012 levels to $6.6 billion and gross profit improved 16.0% to $971.2 million over the prior year period. Operating income increased from 2012 levels by 8.8% to $72.9 million for the three months ended September 30, 2013 and by 15.3% to $212.2 million for the nine months ended September 30, 2013. Income before income taxes increased to $52.3 million for the third quarter of 2013, which was a 5.6% improvement over the comparable prior year period, and increased to $151.7 million for nine months ended September 30, 2013, which was a 14.2% improvement over 2012. For the three months ended September 30, 2013, we realized a 4.6% improvement in net income to $32.8 million and a 9.8% decrease in diluted income per share to $1.19. For the nine months ended September 30, 2013, we realized an 11.1% increase in net income to $92.3 million and a 0.6% increase in diluted income per share to $3.52. For the three and nine months ended September 30, 2013, our weighted average dilutive common shares outstanding increased 17.3% and 11.8% over prior year periods to 26.3 million and 25.2 million, respectively. These increases were primarily the result of the increases in dilution from the potential conversion of our 3.00% Convertible Senior Notes due 2020 ("3.00% Notes") and 2.25% Convertible Senior Notes due 2036 ("2.25% Notes"), which mirrors the rise in our average stock price during the third quarter of 2013 and from levels during the same periods in 2012. The share dilution calculation does not include the beneficial impact of the call spreads that we have in place. A complete presentation of the dilutive effect of the 3.00% Notes and 2.25% Notes can be found in the Liquidity and Capital Resources section of this Item 2. For the nine months ended September 30, 2013, our adjusted net cash provided by operations was $147.1 million compared to $168.5 million in the same period in 2012. See further explanation of the adjusted cash flow metrics in the Non-GAAP Financial Measures section of this Item 2.

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Key Performance Indicators

Consolidated Statistical Data

The following table highlights certain of the key performance indicators we use to manage our business.

| | Three Months Ended September 30, 2013 | Three Months Ended September 30, 2012 | Nine Months Ended September 30, 2013 | Nine Months Ended September 30, 2012 |
|---|---|---|---|---|
| Unit Sales | | | | |
| Retail Sales | | | | |
| New Vehicle | 42,311 | 34,532 | 116,938 | 95,386 |
| Used Vehicle | 26,059 | 22,433 | 74,931 | 65,186 |
| Total Retail Sales | 68,370 | 56,965 | 191,869 | 160,572 |
| Wholesale Sales | 13,445 | 12,049 | 37,852 | 33,287 |
| Total Vehicle Sales | 81,815 | 69,014 | 229,721 | 193,859 |
| Gross Margin | | | | |
| New Vehicle Retail Sales | 5.3 % | 5.8 % | 5.6 % | 5.8 % |
| Total Used Vehicle Sales | 6.5 % | 6.9 % | 7.1 % | 7.4 % |
| Parts and Service Sales | 52.4 % | 52.5 % | 52.5 % | 52.6 % |
| Total Gross Margin | 14.1 % | 14.7 % | 14.6 % | 15.1 % |
| SG&A[1] as a % of Gross Profit | 74.9 % | 74.2 % | 75.3 % | 75.2 % |
| Operating Margin | 3.1 % | 3.4 % | 3.2 % | 3.3 % |
| Pretax Margin | 2.2 % | 2.5 % | 2.3 % | 2.4 % |
| Finance and Insurance Revenues per Retail Unit Sold | $1,207 | $1,220 | $1,212 | $1,197 |

(1) Selling, general and administrative expenses.

The following discussion briefly highlights certain of the results and trends occurring within our business. Throughout the following discussion, references are made to Same Store results and variances which are discussed in more detail in the “Results of Operations” section that follows.

U.S. SAAR has risen from an average of 14.2 million units for the nine months ended September 30, 2012 to 15.5 million units for the same period in 2013, an increase of 9.2%. Our consolidated new vehicle retail sales revenues increased 21.5% and 23.6% for the three and nine months ended September 30, 2013, respectively, as compared to the same periods in 2012. This growth primarily reflects an increase in new vehicle unit sales of 22.5% and 22.6%, for the three and nine months ended September 30, 2013, respectively, as compared to the same periods in 2012, as a result of dealership acquisition activity, stronger consumer confidence in the U.S., better industry conditions in the U.K., improved inventory levels and the execution of our operating team. New vehicle retail gross margin declined 50 basis points to 5.3% and 20 basis points to 5.6% for the three and nine months ended September 30, 2013, respectively, as compared to the same periods in 2012 as gross profit per retail unit sold decreased. This decline in new vehicle retail gross margin was experienced in most of our brands, primarily reflecting the competitive nature of the U.S. industry.

Our used vehicle results are directly affected by economic conditions, the level of manufacturer incentives on new vehicles and new vehicle financing, the number and quality of trade-ins and lease turn-ins, the availability of consumer credit, and our ability to effectively manage the level and quality of our overall used vehicle inventory. Our used vehicle retail sales revenues increased 14.6% and 15.2%, for the three and nine months ended September 30, 2013, as compared to the same periods in 2012. This growth primarily reflects increases in the used vehicle retail unit sales of 16.2% and 14.9%, as compared to the respective periods in 2012, including the impact of our dealership acquisitions in the U.K. and Brazil. The improving U.S. economic environment that has benefited new vehicle sales also supported improved used vehicle demand. Used vehicle retail gross margin declined 40 and 30 basis points, respectively, for the three and nine months ended September 30, 2013, as compared to the same periods in 2012. Used vehicle margins are generally lower in our U.K. and Brazil segments. The decline in consolidated used vehicle gross margin primarily relates to the mix shift effect, as a result of a larger contribution from these foreign segments.

Our parts and service sales increased 13.5% and 14.5%, for the three and nine months ended September 30, 2013, respectively, as compared to the same periods in 2012. This growth was driven by increases in all aspects of our business: collision, customer-pay, warranty, and wholesale parts. Our parts and service gross margin decreased 10 basis points for the

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three and nine months ended September 30, 2013, as compared to the same periods in 2012, primarily due to a mix shift with the acquisition of our Brazil segment, which generally realizes lower parts and service gross margins particularly within the warranty parts and service business.

Our consolidated finance and insurance revenues per retail unit sold decreased by $13 for the three months ended September 30, 2013, as compared to the same period in 2012, primarily due to the mix effect resulting from our Brazil and U.K. acquisitions. Finance and insurance revenues per retail unit sold increased $15 for the nine months ended September 30, 2013, as compared to the same period in 2012, primarily as a result of higher income per contract and increased penetration rates in the U.S., partially offset by unfavorable country mix.

Our total gross margin decreased 60 basis points for the three months ended September 30, 2013 and 50 basis points for the nine months ended September 30, 2013, as compared to the same periods in 2012, primarily due to the shift in business mix towards lower margin new and used vehicle businesses and growing contribution from our foreign segments.

Our consolidated SG&A expenses increased as a percentage of gross profit by 70 basis points to 74.9% for the three months ended September 30, 2013 and by 10 basis points to 75.3% for the nine months ended September 30, 2013, as compared to the same periods in 2012, as a result of largely variable expenses, such as personnel and advertising, that grew disproportionately to gross profit, as well as the impact of a country mix, since Brazil and the U.K. generally experience a higher ratio of SG&A expenses to gross profit.

For the three and nine months ended September 30, 2013, floorplan interest expense increased 34.6% and 32.0%, respectively, as compared to the same periods in 2012, primarily as a result of an increase in our floorplan borrowings from dealership acquisitions, particularly in Brazil, and expanded inventory levels necessary to support higher sales rates. Other interest expense, net increased 3.7% and 3.4%, respectively, for the three and nine months ended September 30, 2013, as compared to the same periods in 2012.

We address these items further, and other variances between the periods presented, in the “Results of Operations” section below.

Critical Accounting Policies and Accounting Estimates

The preparation of our Consolidated Financial Statements in conformity with U.S. generally accepted accounting principles requires management to make certain estimates and assumptions.

We disclosed certain critical accounting policies and estimates in our Form 10-K for the year ended December 31, 2012 (the "2012 Form 10-K"), and no significant changes have occurred since that time.

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Results of Operations

The following tables present comparative financial and non-financial data for the three and nine months ended September 30, 2013 and 2012 of (a) our "Same Store" locations, (b) those locations acquired or disposed of during the periods ("Transactions"), and (c) the consolidated company. Same Store amounts include the results of dealerships for the identical months in each period presented in the comparison, commencing with the first full month in which the dealership was owned by us and, in the case of dispositions, ending with the last full month it was owned by us. Same Store results also include the activities of our corporate headquarters.

Total Same Store Data

The following table summarizes our combined Same Store results for the three and nine months ended September 30, 2013, as compared to 2012:

(dollars in thousands, except per unit amounts)

| | Three Months Ended September 30, | | | Nine Months Ended September 30, | | |
|---|---|---|---|---|---|---|
| | 2013 | % Change | 2012 | 2013 | % Change | 2012 |
| Revenues | | | | | | |
| New vehicle retail | $1,148,915 | 7.7% | $1,066,782 | $3,233,449 | 7.7% | $3,003,079 |
| Used vehicle retail | 467,093 | 6.4% | 438,868 | 1,354,555 | 5.4% | 1,285,471 |
| Used vehicle wholesale | 70,965 | (3.8)% | 73,767 | 201,109 | (3.5)% | 208,297 |
| Parts and service | 226,981 | 8.0% | 210,261 | 677,732 | 7.4% | 631,012 |
| Finance, insurance and other | 75,779 | 14.5% | 66,200 | 214,889 | 15.4% | 186,140 |
| Total revenues | $1,989,733 | 7.2% | $1,855,878 | $5,681,734 | 6.9% | $5,313,999 |
| Cost of Sales | | | | | | |
| New vehicle retail | $1,090,263 | 8.7% | $1,003,427 | $3,060,540 | 8.3% | $2,825,946 |
| Used vehicle retail | 430,508 | 6.8% | 402,978 | 1,242,529 | 5.6% | 1,176,185 |
| Used vehicle wholesale | 72,024 | (3.0)% | 74,245 | 199,752 | (2.9)% | 205,706 |
| Parts and service | 106,087 | 6.2% | 99,895 | 317,270 | 6.0% | 299,320 |
| Total cost of sales | $1,698,882 | 7.5% | $1,580,545 | $4,820,091 | 6.9% | $4,507,157 |
| Gross profit | $290,851 | 5.6% | $275,333 | $861,643 | 6.8% | $806,842 |
| SG&A | $214,526 | 6.7% | $201,034 | $647,778 | 7.7% | $601,687 |
| Depreciation and amortization expenses | $8,239 | 6.7% | $7,725 | $23,924 | 6.9% | $22,384 |
| Floorplan interest expense | $8,176 | 7.5% | $7,606 | $24,960 | 10.2% | $22,660 |
| Gross Margin | | | | | | |
| New vehicle retail | 5.1 % | | 5.9 % | 5.3 % | | 5.9 % |
| Total used vehicle | 6.6 % | | 6.9 % | 7.3 % | | 7.5 % |
| Parts and service | 53.3 % | | 52.5 % | 53.2 % | | 52.6 % |
| Total gross margin | 14.6 % | | 14.8 % | 15.2 % | | 15.2 % |
| SG&A as a % of gross profit | 73.8 % | | 73.0 % | 75.2 % | | 74.6 % |
| Operating margin | 3.4 % | | 3.6 % | 3.3 % | | 3.4 % |
| Finance and insurance revenues per retail unit sold | $1,338 | 7.1% | $1,249 | $1,331 | 9.5% | $1,215 |

The discussion that follows provides explanation for the material variances noted above. In addition, each table presents, by primary statement of operations line item, comparative financial and non-financial data of our Same Store locations, Transactions and the consolidated company for the three and nine months ended September 30, 2013 and 2012.

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New Vehicle Retail Data
(dollars in thousands, except per unit amounts)

| | Three Months Ended September 30, | | | Nine Months Ended September 30, | | |
|---|---|---|---|---|---|---|
| | 2013 | % Change | 2012 | 2013 | % Change | 2012 |
| Retail Unit Sales | | | | | | |
| Same Stores | | | | | | |
| U.S. | 31,294 | 6.2% | 29,460 | 89,951 | 5.8% | 85,039 |
| U.K. | 2,880 | 17.8% | 2,444 | 6,203 | 9.7% | 5,656 |
| Total - Same Stores | 34,174 | 7.1% | 31,904 | 96,154 | 6.0% | 90,695 |
| Transactions | | | | | | |
| U.S. | 1,572 | | 2,502 | 4,282 | | 4,486 |
| U.K. | 1,426 | | 126 | 4,535 | | 205 |
| Brazil | 5,139 | | — | 11,967 | | — |
| Total | 42,311 | 22.5% | 34,532 | 116,938 | 22.6% | 95,386 |
| Retail Sales Revenues | | | | | | |
| Same Stores | | | | | | |
| U.S. | $1,046,722 | 6.9% | $979,516 | $3,016,595 | 7.6% | $2,802,581 |
| U.K. | 102,193 | 17.1% | 87,266 | 216,854 | 8.2% | 200,498 |
| Total - Same Stores | 1,148,915 | 7.7% | 1,066,782 | 3,233,449 | 7.7% | 3,003,079 |
| Transactions | | | | | | |
| U.S. | 44,499 | | 69,378 | 115,866 | | 122,872 |
| U.K. | 34,547 | | 5,126 | 125,184 | | 8,640 |
| Brazil | 158,706 | | — | 398,622 | | — |
| Total | $1,386,667 | 21.5% | $1,141,286 | $3,873,121 | 23.6% | $3,134,591 |
| Gross Profit | | | | | | |
| Same Stores | | | | | | |
| U.S. | $51,678 | (8.9)% | $56,725 | $157,496 | (2.9)% | $162,201 |
| U.K. | 6,974 | 5.2% | 6,630 | 15,413 | 3.2% | 14,932 |
| Total - Same Stores | 58,652 | (7.4)% | 63,355 | 172,909 | (2.4)% | 177,133 |
| Transactions | | | | | | |
| U.S. | 2,408 | | 2,937 | 6,498 | | 5,561 |
| U.K. | 874 | | 258 | 6,228 | | 518 |
| Brazil | 11,361 | | — | 30,661 | | — |
| Total | $73,295 | 10.1% | $66,550 | $216,296 | 18.1% | $183,212 |
| Gross Profit per Retail Unit Sold | | | | | | |
| Same Stores | | | | | | |
| U.S. | $1,651 | (14.2)% | $1,925 | $1,751 | (8.2)% | $1,907 |
| U.K. | $2,422 | (10.7)% | $2,713 | $2,485 | (5.9)% | $2,640 |
| Total - Same Stores | $1,716 | (13.6)% | $1,986 | $1,798 | (7.9)% | $1,953 |
| Transactions | | | | | | |
| U.S. | $1,532 | | $1,174 | $1,518 | | $1,240 |
| U.K. | $613 | | $2,048 | $1,373 | | $2,527 |