SONIC AUTOMOTIVE INC
Form 10-K
March 16, 2007

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2006

OR

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

For the transition period from to

Commission file number 1-13395

SONIC AUTOMOTIVE, INC.

(Exact Name of Registrant as Specified in its Charter)

DELAWARE	**56-2010790**
(State or Other Jurisdiction of Incorporation or Organization)	**(I.R.S. Employer Identification No.)**
6415 IDLEWILD ROAD,	**28212**

SUITE 109

CHARLOTTE, NORTH CAROLINA
(Address of Principle Executive Offices) **(Zip Code)**

(704) 566-2400

(Registrant s telephone number, including area code)

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

TITLE OF EACH CLASS	NAME OF EACH EXCHANGE ON WHICH REGISTERED
Class A Common Stock, $.01 Par Value	New York Stock Exchange

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

(Title of class)

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

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

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. x Yes ¨ No

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer ¨ Accelerated filer x Non-accelerated filer ¨

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

The aggregate market value of the voting common stock held by non-affiliates of the registrant was approximately $663,097,450 based upon the closing sales price of the registrant s Class A common stock on June 30, 2006 of $22.18 per share. As of March 8, 2007 there were 30,881,620 shares of Class A common stock, par value $.01 per share, and 12,029,375 shares of Class B common stock, par value $.01 per share, outstanding.

Documents incorporated by reference. Portions of the registrant s Proxy Statement for the Annual Meeting of Stockholders to be held April 19, 2007 are incorporated by reference into Part III of this Form 10-K.

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

- future acquisitions or dispositions;
- industry trends;
- general economic trends, including employment rates and consumer confidence levels;
- vehicle sales rates and same store sales growth;
- our financing plans; and
- our business and growth strategies.

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

- our ability to generate sufficient cash flows or obtain additional financing to support acquisitions, capital expenditures, our share repurchase program, dividends on our Common Stock and general operating activities;
- the reputation and financial condition of vehicle manufacturers whose brands we represent, the financial incentives they offer and their ability to design, manufacture, deliver and market their vehicles successfully;
- our relationships with manufacturers, which may affect our ability to complete additional acquisitions;
- changes in laws and regulations governing the operation of automobile franchises, accounting standards, taxation requirements, and environmental laws;
- general economic conditions in the markets in which we operate, including fluctuations in interest rates, employment levels, the level of consumer spending and consumer credit availability;
- high competition in the automotive retailing industry, which not only creates pricing pressures on the products and services we offer, but on businesses we seek to acquire; and

the timing of and our ability to successfully integrate recent and potential future acquisitions.

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PART I

Item 1. *Business*.

Sonic Automotive, Inc. was incorporated in Delaware in 1997. We are one of the largest automotive retailers in the United States. As of March 8, 2007, we operated 173 dealership franchises at 150 dealership locations, representing 36 different brands of cars and light trucks, and 38 collision repair centers in 15 states. Each of our dealerships provides comprehensive services including (1) sales of both new and used cars and light trucks; (2) sales of replacement parts and performance of vehicle maintenance, warranty, paint and repair services (collectively, Fixed Operations); and (3) arrangement of extended service contracts, financing and insurance and other aftermarket products (collectively, F&I) for our automotive customers.

The following charts depict the diversity of our sources of revenue and gross profit for the year ended December 31, 2006:

Our dealership network is geographically organized into divisional and regional dealership groups. As of December 31, 2006, we operated dealerships in the following geographic markets:

Market	Number of Dealerships	Number of Franchises	Percent of 2006 Total Revenue
North/South Carolina/Georgia	19	21	9.7%
Alabama/Tennessee	16	19	9.9%
Florida	14	17	8.6%
Ohio	6	9	2.3%
Michigan	6	6	3.1%
Mid-Atlantic	6	7	5.3%
Eastern Division	67	79	38.9%
Houston	18	21	15.7%
Dallas	7	9	7.9%
Oklahoma	7	7	4.8%
Central Division	32	37	28.4%
North Bay (San Francisco)	11	13	9.1%
South Bay (San Francisco)	13	14	7.3%
Los Angeles North	12	14	7.6%
Los Angeles South	6	6	3.3%
San Diego	2	2	1.7%
Las Vegas	4	4	2.6%
Colorado	2	2	1.1%
Western Division	50	55	32.7%

Total	149	171	100.0%

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During 2006, we acquired seven dealerships, representing eight franchises, and disposed of nine dealerships, representing 12 franchises. We expect our acquisition activity to provide approximately 10% to 15% of additional annual revenues each year and 2007 activity to be weighted toward the latter half of the year.

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

BUSINESS STRATEGY

Further Develop Strategic Markets and Brands. Our growth strategy is focused on large metropolitan markets, predominantly in the Southeast, Southwest, Midwest and California. We also seek to acquire stable franchises that we believe have above average sales prospects. A majority of our dealerships are either luxury or mid-line import brands. For the year ended December 31, 2006, 83.3% of our total revenue was generated by import and luxury dealerships, which generally have higher operating margins, more stable fixed operations departments, lower associate turnover and lower inventory levels. We expect this trend toward acquiring more import and luxury dealerships to continue in the near future.

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

	Percentage of New Vehicle Revenue Year Ended December 31,		
Brand (1)	**2004**	**2005**	**2006**
Honda	14.4%	15.3%	15.2%
BMW	13.5%	14.5%	13.7%
Toyota	12.7%	11.8%	13.0%
Mercedes	3.6%	6.5%	9.5%
Cadillac	11.2%	9.2%	8.8%
General Motors (2)	10.1%	8.8%	8.0%
Ford	8.9%	8.1%	7.7%
Lexus	6.9%	7.4%	6.8%
Volvo	3.5%	3.1%	2.5%
Nissan	2.2%	2.1%	1.8%
Hyundai	1.5%	1.4%	1.5%
Audi	1.6%	1.6%	1.4%
Chrysler (3)	1.5%	1.4%	1.0%
Volkswagen	0.9%	0.9%	0.9%
Other Luxury (4)	5.2%	5.3%	5.7%
Other (5)	2.3%	2.6%	2.5%
Total	100.0%	100.0%	100.0%

(1) In accordance with the provisions of SFAS No. 144, prior years income statement data reflect reclassifications to exclude additional franchises sold, identified for sale, or terminated subsequent to December 31, 2005 which had not been previously included in discontinued operations. See Notes 1 and 2 to our accompanying Consolidated Financial Statements which discusses these and other factors that affect the comparability of the information for the periods presented.
(2) Includes Buick, Chevrolet, GMC, Pontiac and Saturn
(3) Includes Chrysler, Dodge and Jeep
(4) Includes Acura, Hummer, Infiniti, Jaguar, Land Rover, Maybach, Morgan, Porsche and Saab
(5) Includes Isuzu, KIA, Mini, Scion and Subaru

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

Finance, Insurance and Other Aftermarket Products: Each sale of a new or used vehicle provides us with an opportunity to earn financing fees and insurance commissions and to sell extended service contracts and other aftermarket products. We currently offer a wide range of nonrecourse financing, leasing, other aftermarket products, service contracts and insurance products to our customers. We are continuing to emphasize menu-selling techniques and other best practices to increase our sales of F&I products at both newly acquired and existing dealerships.

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

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

Value Used Vehicles: A market segment that drives used vehicle volume that we have not historically participated in is vehicles with retail prices below $10,000. Historically, if we received a trade-in which did not meet our then existing internal criteria for used vehicles (in many instances these would be value vehicles), we would wholesale the vehicle. We believe the market for these value vehicles is deep and not as sensitive to market fluctuations as higher priced used vehicles. We have begun to more aggressively market and retail these vehicles.

Emphasize Expense Control. We continually focus on controlling expenses and expanding margins at the dealerships we acquire and integrate into our organization. We manage these costs, such as advertising and variable compensation expenses, so that they are generally related to vehicle sales and can be adjusted in response to changes in vehicle sales volume. The majority of our non-clerical dealership personnel are paid either a commission or a modest salary plus commissions. In addition, dealership management compensation is tied to individual dealership profitability. We believe we can further manage these types of costs through best practices, standardization of compensation plans, controlled oversight and accountability, reducing associate turnover and centralizing and standardizing processes and systems such as a single dealership management system, accounting office consolidation, payroll system consolidation and inventory management technology.

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

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Manage Leverage. Prior to 2004, we had maintained a long-term debt to total capital ratio of approximately 48% to 52%, depending on the timing of our acquisitions. We have been steadily reducing that ratio in recent years. We believe it prudent over time to maintain our long-term debt to total capital ratio to be between 35% and 40% over the long term. At December 31, 2006, our long-term debt to total capital ratio, net of cash and cash equivalents, was 39.4%.

Relationships with Manufacturers

Each of our dealerships operates under a separate franchise or dealer agreement that governs the relationship between the dealership and the manufacturer. In general, each dealer agreement specifies the location of the dealership for the sale of vehicles and for the performance of certain approved services in a specified market area. The designation of such areas generally does not guarantee exclusivity within a specified territory. In addition, most manufacturers allocate vehicles on a turn and earn basis that rewards high volume. A dealer agreement requires the dealer to meet specified standards regarding showrooms, facilities and equipment for servicing vehicles, inventories, minimum net working capital, personnel training and other aspects of the business. Each dealer agreement also gives the related manufacturer the right to approve the dealer operator and any material change in management or ownership of the dealership. Each manufacturer may terminate a dealer agreement under certain circumstances, such as a change in control of the dealership without manufacturer approval, the impairment of the reputation or financial condition of the dealership, the death, removal or withdrawal of the dealer operator, the conviction of the dealership or the dealership s owner or dealer operator of certain crimes, the failure to adequately operate the dealership or maintain new vehicle financing arrangements, insolvency or bankruptcy of the dealership or a material breach of other provisions of the dealer agreement.

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

- The ability to force the sale of their respective franchises upon a change in control of our company or a material change in the composition of our Board of Directors;
- The ability to force the sale of their respective franchises if an automobile manufacturer or distributor acquires more than 5% of the voting power of our securities; and
- The ability to force the sale of their respective franchises if an individual or entity (other than an automobile manufacturer or distributor) acquires more than 20% of the voting power of our securities, and the manufacturer disapproves of such individual s or entity s ownership interest.

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

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

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

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Competition

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

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

In addition to competition for vehicle sales, we also compete with other auto dealers, service stores, auto parts retailers and independent mechanics in providing parts and service. We believe that the principal competitive factors in parts and service sales are price, the use of factory-approved replacement parts, factory-trained technicians, the familiarity with a dealer s makes and models and the quality of customer service. A number of regional and national chains offer selected parts and service at prices that may be lower than our prices.

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

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

Governmental Regulations and Environmental Matters

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

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

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

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

We believe that we comply in all material respects with the laws affecting our business. However, claims arising out of actual or alleged violations of laws may be asserted against us or our dealerships by individuals or

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governmental entities, and may expose us to significant damages or other penalties, including possible suspension or revocation of our licenses to conduct dealership operations and fines.

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

We do not have any known material environmental liabilities and we believe that compliance with environmental laws and regulations will not, individually or in the aggregate, have a material adverse effect on our results of operations, financial condition and cash flows. However, soil and groundwater contamination is known to exist at certain properties used by us. Further, environmental laws and regulations are complex and subject to frequent change. In addition, in connection with our acquisitions, it is possible that we will assume or become subject to new or unforeseen environmental costs or liabilities, some of which may be material. We cannot assure you that compliance with current or amended, or new or more stringent, laws or regulations, stricter interpretations of existing laws or the future discovery of environmental conditions will not require additional expenditures by us, or that such expenditures will not be material.

Executive Officers of the Registrant

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

Name	Age	Position(s) with Sonic
O. Bruton Smith	80	Chairman, Chief Executive Officer and Director
B. Scott Smith	39	President, Chief Strategic Officer and Director
David P. Cosper	52	Vice Chairman and Chief Financial Officer
Mark J. Iuppenlatz	47	Executive Vice President of Corporate Development

O. Bruton Smith, 80, is our Chairman, Chief Executive Officer and a director and has served as such since our organization in January 1997, and he currently is a director and executive officer of many of our subsidiaries. Mr. Smith has worked in the retail automobile industry since 1966. Mr. Smith is also the Chairman and Chief Executive Officer, a director and controlling stockholder of Speedway Motorsports, Inc. (SMI). SMI is a public company traded on the New York Stock Exchange (the NYSE). Among other things, SMI owns and operates the following NASCAR racetracks: Atlanta Motor Speedway, Bristol Motor Speedway, Lowe s Motor Speedway, Las Vegas Motor Speedway, Infineon Raceway and Texas Motor Speedway. He is also an executive officer or a director of most of SMI s operating subsidiaries.

B. Scott Smith, 39, is our President and Chief Strategic Officer. He was appointed President on March 13, 2007. Prior to this appointment he served as our Vice Chairman and Chief Strategic Officer since October 2002. Mr. Smith was President and Chief Operating Officer from April 1997 until October 2002. Mr. Smith has been a director of our company since our organization in January 1997. Mr. Smith also serves as a director and executive officer of many of our subsidiaries. Mr. Smith, who is the son of O. Bruton Smith, has been an executive officer of Town & Country Ford since 1993, and was a minority owner of both Town & Country Ford and Fort Mill Ford before our acquisition of these dealerships in 1997. Mr. Smith became the General Manager of Town & Country Ford in November 1992 where he remained until his appointment as President and Chief Operating Officer in April 1997. Mr. Smith has over twenty years experience in the automobile dealership industry.

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David P. Cosper, 52, is our Vice Chairman and Chief Financial Officer. He was promoted from Executive Vice President to Vice Chairman on March 13, 2007. He joined Sonic Automotive on March 1, 2006 as our Executive Vice President and became our Chief Financial Officer and Treasurer on March 16, 2006. Mr. Cosper served as Treasurer through the end of 2006 and relinquished the position in February 2007. Prior to joining Sonic, he was Vice Chairman and Chief Financial Officer of Ford Motor Credit Company, a position held since 2003. From 1979, when he joined Ford Motor Company, Mr. Cosper served in a variety of positions in Ford Motor Company and Ford Motor Credit Company, including Vice President and Treasurer of Ford Motor Credit Company and Executive Director of Corporate Finance at Ford Motor Company. In such positions, he was responsible for worldwide profit analysis and treasury matters, risk management, business planning, and competitive and strategic analysis.

Mark J. Iuppenlatz, 47, is our Executive Vice President of Corporate Development. In April 2004, Mr. Iuppenlatz was promoted to Executive Vice President from Senior Vice President, a position which he had held since May 2002. Prior to May 2002, he served as our Vice President of Corporate Development from August 1999. Before joining us, Mr. Iuppenlatz served as the Executive Vice President Acquisitions and Chief Operating Officer of Mar Mar Realty Trust (MMRT), a real estate investment trust specializing in sale/leaseback financing of automotive-related real estate, from September 1998 to August 1999. From 1996 to September 1998, Mr. Iuppenlatz was employed by Brookdale Living Communities, Inc., a company that owns, operates, develops and manages luxury senior housing communities, where he was responsible for the company s development operations. From 1994 to 1996, he served as Vice President of Schlotzky s, Inc., a publicly traded restaurant chain. From 1991 to 1994, Mr. Iuppenlatz served in Spain as the director of marketing and the assistant director of development for Kepro S.A., a real estate development company.

Employees

As of March 1, 2007, we employed approximately 11,200 people. We believe that our relationships with our employees are good. Approximately 300 of our employees, primarily service technicians in our Northern California markets and certain sales associates and service department associates in Michigan, are represented by a labor union. Because of our dependence on the manufacturers, however, we may be affected by labor strikes, work slowdowns and walkouts at the manufacturer s manufacturing facilities.

Company Information

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

Item 1A: ***Risk Factors***

In addition to the other information contained in this Annual Report on Form 10-K, the following is a list of factors that could materially affect our business, financial condition or future results. These risks are not the only risks we face. Additional risks and uncertainties not currently known to us or that we currently consider immaterial may also have a material adverse effect on our business, financial condition or results of operations.

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Risks Related to Our Indebtedness

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

As of December 31, 2006, our total outstanding indebtedness was $1,762.1 million, including the following:

- $20.1 million under a portion of our four-year syndicated credit facility (the 2006 Revolving Credit Facility);
- $1,160.7 million under the secured new and used inventory floor plan facilities, including $96.3 million classified as liabilities associated with assets held for sale;
- $128.6 million in 5.25% convertible senior subordinated notes due 2009 (the 2002 Convertibles) representing $130.1 million in aggregate principal amount outstanding less unamortized discount of approximately $1.5 million;
- $156.8 million in 4.25% convertible senior subordinated notes due 2015, redeemable on or after November 30, 2010, (the 2005 Convertibles) representing $160.0 million in aggregate principal amount outstanding less unamortized discount of approximately $3.2 million;
- $272.5 million in 8.625% senior subordinated notes due 2013 (the 8.625% Notes) representing $275.0 million in aggregate principal amount outstanding less unamortized net discount of approximately $2.5 million; and
- $23.4 million of other secured debt, representing $23.3 million in aggregate principal amount plus unamortized premium of approximately $4.8 million and less $4.7 million for the fair value of fixed to variable interest rate swaps.

As of December 31, 2006, we had $252.1 million available for additional borrowings under the 2006 Revolving Credit Sub-Facility. We also have significant additional capacity under new and used floor plan facilities. In addition, the indentures relating to our 8.625% Notes, 2002 Convertibles and 2005 Convertibles and our other debt instruments allow us to incur additional indebtedness, including secured indebtedness. Our 2006 Revolving Credit Sub-Facility, up to $700.0 million in borrowing availability for new vehicle inventory floor plan financing and up to $150.0 million in borrowing availability for used vehicle inventory floor plan financing are collectively referred to as our 2006 Credit Facility .

In addition, the majority of our dealership properties are leased under long-term operating lease arrangements (which many view as debt financing) that generally have initial terms of fifteen to twenty years with one or two five-year renewal options. These operating leases require monthly payments of rent that may fluctuate based on interest rates and local consumer price indices. The total future minimum lease payments related to these operating leases and certain equipment leases are significant and are disclosed in the notes to our financial statements under the heading Commitments and Contingencies in this Annual Report on Form 10-K.

The degree to which we are leveraged could have important consequences to the holders of our securities, including the following:

our ability to obtain additional financing for acquisitions, capital expenditures, working capital or general corporate purposes may be impaired in the future;

a substantial portion of our current cash flow from operations must be dedicated to the payment of principal and interest on our indebtedness, thereby reducing the funds available to us for our operations and other purposes;

- some of our borrowings and facility leases are and will continue to be at variable rates of interest, which exposes us to the risk of increasing interest rates;

- the indebtedness outstanding under our 2006 Credit Facility and other floor plan facilities are secured by a pledge of substantially all the assets of our dealerships; and

- we may be substantially more leveraged than some of our competitors, which may place us at a relative competitive disadvantage and make us more vulnerable to changing market conditions and regulations.

In addition, our debt agreements contain numerous covenants that limit our discretion with respect to business matters, including mergers or acquisitions, paying dividends, incurring additional debt, making capital expenditures or disposing of assets.

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

Our 2006 Credit Facility, the indenture governing our 8.625% Notes and many of our facility operating leases contain numerous financial and operating covenants. A breach of any of these covenants could result in a default under the applicable agreement or indenture. If a default were to occur, we may be unable to adequately finance our operations and the value of our common stock would be materially adversely affected. In addition, a default under one agreement or indenture could result in a default and acceleration of our repayment obligations under the other agreements or indentures, including the indentures governing our outstanding 2002 Convertibles, 2005 Convertibles and 8.625% Notes, under the cross default provisions in those agreements or indentures. If a cross default were to occur, we may not be able to pay our debts or borrow sufficient funds to refinance them. Even if new financing were available, it may not be on terms acceptable to us. As a result of this risk, we could be forced to take actions that we otherwise would not take, or not take actions that we otherwise might take, in order to comply with the covenants in these agreements and indentures.

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

Substantially all of our consolidated assets are held by our subsidiaries and substantially all of our consolidated cash flow and net income are generated by our subsidiaries. Accordingly, our cash flow and ability to service debt depends to a substantial degree on the results of operations of subsidiaries and upon the ability of our subsidiaries to provide us with cash. We may receive cash from our subsidiaries in the form of dividends, loans or otherwise. We may use this cash to service our debt obligations or for working capital. Our subsidiaries are separate and distinct legal entities and have no obligation, contingent or otherwise, to distribute cash to us or to make funds available to service debt. In addition, the ability of our subsidiaries to pay dividends or make loans to us are subject to contractual limitations under the floor plan facilities, minimum net capital requirements under manufacturer franchise agreements and laws of the state in which a subsidiary is organized and depend to a significant degree on the results of operations of our subsidiaries and other business considerations.

Risks Related to Our Relationships with Vehicle Manufacturers

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

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

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

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

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

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

- customer rebates or below market financing on new vehicles;
- employee pricing;
- dealer incentives on new vehicles;
- manufacturer floor plan interest and advertising assistance;
- warranties on new and used vehicles; and
- sponsorship of used vehicle sales by authorized new vehicle dealers.

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

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

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

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

During the year ended December 31, 2006, approximately 89.4% of our new vehicle revenue was derived from the sale of new vehicles manufactured by Ford, Honda, General Motors (including Cadillac), BMW, Mercedes and Toyota. Our success depends to a great extent on these manufacturers :

- financial condition;
- marketing;
- vehicle design;
- publicity concerning a particular manufacturer or vehicle model;
- production capabilities;
- management;
- reputation; and
- labor relations.

Events such as labor strikes that may adversely affect a manufacturer may also adversely affect us. In particular, labor strikes at a manufacturer that continue for a substantial period of time could have a material adverse effect on our business. Similarly, the delivery of vehicles from manufacturers at a time later than scheduled, which may occur particularly during periods of new product introductions, could limit sales of those vehicles during those periods. This has been experienced at some of our dealerships from time to time. Adverse conditions affecting these and other important aspects of manufacturers operations and public relations may adversely affect our ability to sell their automobiles and, as a result, significantly and detrimentally affect our profitability.

During 2005 and into 2006, the financial condition and operating results of both Ford and General Motors deteriorated significantly. As of December 31, 2006, we owned 28 Ford franchises (including Volvo, Jaguar, Land Rover, Lincoln and Mercury) and 42 General Motors franchises (including Cadillac, Saab, Saturn, Chevrolet, Buick, GMC, Hummer and Pontiac). Should the financial condition and operating results of either Ford or General Motors continue to significantly deteriorate, it is possible that the particular manufacturer could file for bankruptcy protection. Such a bankruptcy filing by either Ford or General Motors could have a material adverse effect on our future results of operations, financial condition or cash flows.

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

Some of our franchise agreements prohibit transfers of any ownership interests of a dealership and, in some cases, its parent, without prior approval of the applicable manufacturer. A number of manufacturers impose restrictions on the transferability of our Class A common stock and our ability to maintain franchises if a person acquires a significant percentage of the voting power of our common stock. Our existing franchise agreements could be terminated if a person or entity acquires a substantial ownership interest in us or acquires voting power above certain levels without the applicable manufacturer s approval. Violations of these levels by an investor are generally outside of our control and may result in the termination or non-renewal of existing franchise agreements or impair our ability to negotiate new franchise agreements for dealerships we acquire. In addition, if we cannot obtain any requisite approvals on a timely basis, we may not be able to issue additional equity or otherwise raise capital on terms acceptable to us. These restrictions may also prevent or deter a prospective acquiror from acquiring control of us. This could adversely affect the market price of our Class A common stock.

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

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

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

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

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

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

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

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

Risks Related to Our Acquisition Strategy

Manufacturers restrictions on acquisitions could limit our future growth.

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

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

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

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

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

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

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

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

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

The automobile retailing industry is considered a mature industry in which minimal growth is expected in total unit sales. Accordingly, our ability to generate higher revenue and earnings in future periods depends in large part on our ability to acquire additional dealerships, manage geographic expansion, control costs in our operations and consolidate both past and future dealership acquisitions into our existing operations. In pursuing a strategy of acquiring other dealerships, we face risks commonly encountered with growth through acquisitions. These risks include, but are not limited to:

- incurring significantly higher capital expenditures and operating expenses;

failing to assimilate the operations and personnel of acquired dealerships;

entering new markets with which we are unfamiliar;

potential undiscovered liabilities and operational difficulties at acquired dealerships;

disrupting our ongoing business;

diverting our management resources;

failing to maintain uniform standards, controls and policies;

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

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

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

incorrectly valuing entities to be acquired.

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

We may not be able to capitalize on acquisition opportunities because our financial resources available for acquisitions are limited.

We intend to finance our acquisitions with cash generated from operations, through issuances of our stock or debt securities and through borrowings under credit arrangements. We may not be able to obtain additional financing by issuing stock or debt securities due to the market price of our Class A common stock, overall market conditions or the need for manufacturer consent to the issuance of equity securities. Using cash to complete acquisitions could substantially limit our operating or financial flexibility. If we are unable to obtain financing on acceptable terms, we may be required to reduce the scope of our presently anticipated expansion, which could materially adversely affect our overall growth strategy.

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

Substantially all the assets of our dealerships are pledged to secure the indebtedness under the 2006 Credit Facility and our separate floor plan indebtedness with the respective captive finance subsidiaries of BMW, DaimlerChrysler, Ford and General Motors. Three of the lenders under the 2006 Credit Facility are the respective captive finance subsidiaries of BMW, Nissan and Toyota. These pledges may impede our ability to borrow from other sources. Moreover, because the identified manufacturer captive finance subsidiaries are either owned or affiliated with BMW, DaimlerChrysler, Ford, General Motors, Nissan and Toyota, respectively, any deterioration of our relationship with the particular captive finance subsidiary could adversely affect our relationship with the affiliated manufacturer, and vice-versa.

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

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

- the availability of suitable acquisition candidates;
- competition with other dealer groups for suitable acquisitions;
- the negotiation of acceptable terms;
- our financial capabilities;

our stock price; and

the availability of skilled employees to manage the acquired companies.

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

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

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

Our obligations under the 2006 Credit Facility are secured with a pledge of shares of common stock of Speedway Motorsports, Inc., a publicly traded owner and operator of automobile racing facilities. These shares of Speedway Motorsports common stock are beneficially owned by Sonic Financial Corporation (SFC), an entity controlled by Mr. Smith. Presently, the $350.0 million borrowing limit of our 2006 Revolving Credit Sub-Facility is subject to a borrowing base calculation that is based, in part, on the value of the Speedway Motorsports shares pledged by SFC. Consequently, a withdrawal of this pledge by SFC or a significant decrease in the value of Speedway Motorsports common stock could reduce the amount we can borrow under the 2006 Revolving Credit Sub-Facility.

Mr. Smith has also guaranteed additional indebtedness incurred to complete certain dealership acquisitions. Mr. Smith may not be willing or able to provide similar guarantees or credit support in the future. This could impair our ability to obtain acquisition financing on favorable terms.

Risks Related to the Automotive Retail Industry

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

Automobile retailing is a highly competitive business. Our competitors include publicly and privately owned dealerships, some of which are larger and have greater financial and marketing resources than we do. Many of our competitors sell the same or similar makes of new and used vehicles that we offer in our markets at competitive prices. We do not have any cost advantage in purchasing new vehicles from manufacturers due to economies of scale or otherwise. In addition, the popularity of short-term vehicle leasing in the past few years has resulted, as these leases expire, in a large increase in the number of late model used vehicles available in the market, which puts added pressure on new and used vehicle margins. We typically rely on advertising, merchandising, sales expertise, service reputation and dealership location to sell new vehicles. Our revenues and profitability could be materially adversely affected if manufacturers decide to enter the retail market directly.

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

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

Our franchise agreements do not grant us the exclusive right to sell a manufacturer s product within a given geographic area. Our revenues or profitability could be materially adversely affected if any of our manufacturers

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award franchises to others in the same markets where we operate or if existing franchised dealers increase their market share in our markets.

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

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

Our business is heavily dependent on consumer demand and preferences. Our revenues will be materially and adversely affected if there is a severe or sustained downturn in overall levels of consumer spending. Retail vehicle sales are cyclical and historically have experienced periodic downturns characterized by oversupply and weak demand. These cycles are often dependent on general economic conditions and consumer confidence, as well as the level of discretionary personal income and credit availability. Future recessions may have a material adverse effect on our retail business, particularly sales of new and used automobiles.

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

A decline of available financing in the sub-prime lending market has, and may continue to, adversely affect our sales of used vehicles.

A significant portion of vehicle buyers, particularly in the used car market, finance their purchases of automobiles. Sub-prime lenders have historically provided financing for consumers who, for a variety of reasons including poor credit histories and lack of down payment, do not have access to more traditional finance sources. Our recent experience suggests that sub-prime lenders have tightened their credit standards and may continue to apply these higher standards in the future. This has adversely affected our used vehicle sales. If sub-prime lenders continue to apply these higher standards or if there is any further tightening of credit standards used by sub-prime lenders or if there is any additional decline in the overall availability of credit in the sub-prime lending market, the ability of these consumers to purchase vehicles could be limited which could have a material adverse effect on our used car business, revenues and profitability.

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

A significant portion of our new vehicle business involves the sale of vehicles, parts or vehicles composed of parts that are manufactured outside the United States. As a result, our operations are subject to customary risks of importing merchandise, including fluctuations in the relative values of currencies, import duties, exchange controls, trade restrictions, work stoppages and general political and socio-economic conditions in other countries. The United States or the countries from which our products are imported may, from time to time, impose new quotas, duties, tariffs or other restrictions, or adjust presently prevailing quotas, duties or tariffs, which may affect our operations and our ability to purchase imported vehicles and/or parts at reasonable prices.

The seasonality of our business magnifies the importance of second and third quarter operating results.

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

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General Risks Related to Investing in Our Securities

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

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

- going private transaction;
- disposition of substantially all of our assets;
- transfer resulting in a change in the nature of our business; or
- merger or consolidation in which current holders of common stock would own less than 50% of the common stock following such transaction.

The holders of Class B common stock currently hold less than a majority of our outstanding common stock, but a majority of our voting power. This may prevent or discourage a change of control of us even if the action was favored by holders of Class A common stock.

Our charter and bylaws make it more difficult for our stockholders to take corporate actions at stockholders meetings. In addition, options under our 1997 Stock Option Plan and 2004 Stock Incentive Plan become immediately exercisable upon a change in control. Delaware law also makes it difficult for stockholders who have recently acquired a large interest in a company to consummate a business combination transaction with the company against its directors wishes. Finally, restrictions imposed by our dealer agreements may impede or prevent any potential takeover bid. Generally, our franchise agreements allow the manufacturers the right to terminate the agreements upon a change of control of our company and impose restrictions upon the transferability of any significant percentage of our stock to any one person or entity who may be unqualified, as defined by the manufacturer, to own one of its dealerships. The inability of a person or entity to qualify with one or more of our manufacturers may prevent or seriously impede a potential takeover bid. In addition, provisions of our lending arrangements create an event of default on a change in control. These agreements, corporate governance documents and laws may have the effect of delaying or preventing a change in control or preventing stockholders from realizing a premium on the sale of their shares if we were acquired.

The outcome of legal and administrative proceedings we are or may become involved in could have an adverse effect on our business, results of operations and profitability.

We are involved, and expect to continue to be involved, in numerous legal and administrative proceedings arising out of the conduct of our business, including regulatory investigations and private civil actions brought by plaintiffs purporting to represent a potential class or for which a class has been certified, such as the following.

Several private civil actions have been filed against Sonic Automotive, Inc. and several of our dealership subsidiaries that purport to represent classes of customers as potential plaintiffs and make allegations that certain products sold in the finance and insurance departments were done so in a deceptive or otherwise illegal manner. One of these private civil actions has been filed in South Carolina state court against Sonic Automotive, Inc. and 10 of our South Carolina subsidiaries. We have been advised that the plaintiffs attorneys in this South Carolina private civil action intend to file private civil class actions against Sonic Automotive, Inc. and certain of its subsidiaries in other states. This group of plaintiffs attorneys has filed another one of these private civil class action lawsuits in state court in North Carolina seeking certification of a multi-state class of plaintiffs. The South Carolina state court action and the North Carolina state court action have since been consolidated into a single proceeding in private arbitration. Another one of these private civil actions has been filed in Tennessee state

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court against Sonic Automotive, Inc. and one of our Tennessee subsidiaries. Additionally, a private civil action has also been filed against one of our dealerships in Los Angeles County stating allegations of deceptive sales practices by that dealership. The plaintiffs in this private civil action purport to represent a class of customers as potential plaintiffs, although no motion for class certification has been filed.

The outcomes of the civil actions brought by plaintiffs purporting to represent a class of customers, as well as other pending and future legal proceedings arising out of the conduct of our business, including litigation with customers, employment related lawsuits, contractual disputes, class actions, purported class actions and actions brought by governmental authorities, cannot be predicted with certainty. An unfavorable resolution of one or more of these matters could have a material adverse effect on our business, financial condition, results of operations, cash flows or prospects.

Our company is a defendant in the matter of *Galura, et al. v. Sonic Automotive, Inc.*, a private civil action filed in the Circuit Court of Hillsborough County, Florida. In this action, originally filed on December 30, 2002, the plaintiffs allege that we and our Florida dealerships sold an antitheft protection product in a deceptive or otherwise illegal manner, and further sought representation on behalf of any customer of any of our Florida dealerships who purchased the antitheft protection product since December 30, 1998. The plaintiffs are seeking monetary damages and injunctive relief on behalf of this class of customers. In June 2005, the court granted the plaintiffs motion for certification of the requested class of customers, but the court has made no finding to date regarding actual liability in this lawsuit. We have subsequently filed a notice of appeal of the court s class certification ruling with the Florida Court of Appeals. We intend to continue our vigorous defense of this lawsuit, including the aforementioned appeal of the trial court s class certification order, and to assert available defenses. However, an adverse resolution of this lawsuit could result in the payment of significant costs and damages, which could have a material adverse effect on our future results of operations, financial condition and cash flows.

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

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

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

Our performance is subject to local economic, competitive, weather and other conditions prevailing in geographic areas where we operate. For example, our current results of operations depend substantially on general economic conditions and consumer spending habits in our Northern California and Houston markets. Revenues in our Northern California and Houston markets represented approximately 32.1% of our total revenues for the year ended December 31, 2006. We may not be able to expand geographically and any geographic expansion may not adequately insulate us from the adverse effects of local or regional economic conditions. In addition, due to the provisions and terms contained in our operating lease agreements, we may not be able to relocate a dealership operation to a more favorable location without incurring significant costs or penalties.

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

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

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

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

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

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

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

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

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

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

Seven of our dealership subsidiaries in Northern California currently make fixed-dollar contributions to the Automotive Industries Pension Plan pursuant to collective bargaining agreements between our subsidiaries and the International Association of Machinists. The AI Pension Plan is a multi-employer pension plan as defined under the Employee Retirement Income Security Act of 1974, as amended, and our seven dealership subsidiaries are among approximately 120 automobile dealerships that make contributions to the AI Pension Plan pursuant to collective bargaining agreements with the IAM. In June 2006, we received information that the AI Pension Plan was substantially underfunded as of December 31, 2005. Under applicable federal law, any employer contributing to a multiemployer pension plan that completely ceases participating in the plan while the plan is underfunded is subject to payment of such employer s assessed share of the aggregate unfunded vested benefits of the plan. In certain circumstances, an employer can be assessed withdrawal liability for a partial withdrawal from a multi-employer pension plan. In addition, if the financial condition of the AI Pension Plan were to continue to deteriorate to the point that the Plan is forced to terminate and be assumed by the Pension Benefit Guaranty Corporation, the participating employers could be subject to assessments by the PBGC to cover the participating employers assessed share of the unfunded vested benefits. If any of these adverse events were to occur in the future, it could result in a substantial withdrawal liability assessment that could have a material adverse effect on our business, financial condition, results of operations or cash flows.

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

As described in Item 7 under the heading Management s Discussion and Analysis of Financial Condition and Results of Operations Use of Estimates and Critical Accounting Policies in this Annual Report on Form 10-K, our estimates for finance, insurance and service contracts, insurance reserves and Cornerstone Acceptance allowance for credit losses is based on historical experience. Differences between actual results and our historical experiences and/or our assumptions could have a material impact on our earnings in the period of the change and in periods subsequent to the change.

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

Pursuant to applicable accounting pronouncements, we test goodwill for impairment annually or more frequently if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. We describe the process for testing goodwill more thoroughly in this Annual Report on Form 10-K in Item 7 under the heading Management s Discussion and Analysis of Financial Condition and Results of Operations Use of Estimates and Critical Accounting Policies. If we determine that the amount of our goodwill is impaired at any point in time, we will be required to reduce goodwill on our balance sheet. As of December 31, 2006, our balance sheet reflected a carrying amount of approximately $1,167.8 million in goodwill (including goodwill classified as assets held for sale), which was allocated between three geographic reporting units. If the goodwill in any of our reporting units is impaired, we will record a significant non-cash impairment charge that would likely have a material adverse effect on our earnings for the period in which the impairment of goodwill occurred.

Item 1B: ***Unresolved Staff Comments***

None.

Item 2: ***Properties.***

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

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

We lease the majority of the properties utilized by our dealership operations from affiliates of Capital Automotive REIT (CARS) and other individuals and entities. We believe that our facilities are adequate for our current needs.

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

Item 3: ***Legal Proceedings.***

We are a defendant in the matter of *Galura, et al. v. Sonic Automotive, Inc.*, a private civil action filed in the Circuit Court of Hillsborough County, Florida. In this action, originally filed on December 30, 2002, the plaintiffs allege that we and our Florida dealerships sold an antitheft protection product in a deceptive or otherwise illegal manner, and further sought representation on behalf of any customer of any of our Florida dealerships who purchased the antitheft protection product since December 30, 1998. The plaintiffs are seeking monetary damages and injunctive relief on behalf of this class of customers. In June 2005, the court granted the plaintiffs motion for certification of the requested class of customers, but the court has made no finding to date regarding actual liability in this lawsuit. We subsequently filed a notice of appeal of the court s class certification ruling with the Florida Court of Appeals. We intend to continue vigorous defense of this lawsuit, including the appeal of the trial court s class certification order, and to assert available defenses. However, an adverse resolution of this lawsuit could result in the payment of significant costs and damages, which could have a material adverse effect on our future results of operations, financial condition and cash flows.

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

Item 4: ***Submission of Matters to a Vote of Security Holders.***

Not applicable.

PART II

Item 5: ***Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.***

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

As of March 8, 2007, there were 30,881,620 shares of Sonic s Class A common stock and 12,029,375 shares of our Class B common stock outstanding. As of March 8, 2007, there were 69 record holders of the Class A common stock and three record holders of the Class B common stock. As of March 8, 2007, the closing stock price for the Class A common stock was $29.51.

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Our Board of Directors approved four quarterly cash dividends on all outstanding shares of common stock totaling $0.48 per share during 2006. During 2005, our Board of Directors approved four quarterly dividends on all outstanding shares of common stock totaling $0.48 per share. Our Board of Directors has also approved a dividend of $0.12 per share on all outstanding shares of common stock for stockholders of record on March 15, 2007, which will be paid on April 15, 2007. See Note 6 to our Consolidated Financial Statements for a description of restrictions on the payment of dividends.

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

	Market Price		
2006	**High**	**Low**	**Cash Dividend Declared**
First Quarter	$ 28.43	$ 22.72	$ 0.12
Second Quarter	28.53	21.85	0.12
Third Quarter.	23.31	21.08	0.12
Fourth Quarter	29.50	22.76	0.12
2005			
First Quarter	$ 24.27	$ 21.66	$ 0.12
Second Quarter	22.76	19.23	0.12
Third Quarter	24.37	21.36	0.12
Fourth Quarter	22.81	19.79	0.12

During 2006, all sales of our equity securities were registered under the Securities Act.

Issuer Purchases of Equity Securities

The following table sets forth information about the shares of Class A Common Stock we repurchased during the quarter ended December 31, 2006.

	Total Number of Shares Purchased (1)	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (2)	Approximate Dollar Value of Shares That May Yet Be Purchased Under the Plans or Programs
	(amounts in thousands, except per share amounts)			
October 2006	5,000	$ 23.97	5,000	$ 14,505
November 2006	40,000	$ 28.56	40,000	$ 13,362
December 2006	40,000	$ 29.11	40,000	$ 12,198

Total	85,000	$ 28.55	85,000

(1) All shares repurchased were part of publicly announced share repurchase programs
(2) Our publicly announced Class A Common Stock repurchase authorizations occurred as follows:

	(Amounts in Thousands)
November 1999	$ 25,000
February 2000	25,000
December 2000	25,000
May 2001	25,000
August 2002	25,000
February 2003	20,000
December 2003	20,000
July 2004	20,000
Total	$ 185,000

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Item 6: ***Selected Financial Data.***

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

We have accounted for all of our dealership acquisitions using the purchase method of accounting and, as a result, we do not include in our consolidated financial statements the results of operations of these dealerships prior to the date we acquired them. Our selected consolidated financial data reflect the results of operations and financial positions of each of our dealerships acquired prior to December 31, 2006. As a result of the effects of our acquisitions and other potential factors in the future, the historical consolidated financial information described in selected consolidated financial data is not necessarily indicative of the results of our operations and financial position in the future or the results of operations and financial position that would have resulted had such acquisitions occurred at the beginning of the periods presented in the selected consolidated financial data.

	Year Ended December 31,				
	2002	**2003**	**2004**	**2005**	**2006**
Income Statement Data (1) (2):					
Total revenues	$ 5,561,139	$ 6,026,171	$ 6,470,050	$ 7,278,720	$ 7,972,074
Income from continuing operations before income taxes	$ 157,969	$ 122,294	$ 142,085	$ 167,389	$ 165,357
Income from continuing operations	$ 97,847	$ 80,909	$ 88,145	$ 104,844	$ 98,566
Basic earnings per share from continuing operations	$ 2.34	$ 1.98	$ 2.13	$ 2.51	$ 2.33
Diluted earnings per share from continuing operations	$ 2.24	$ 1.89	$ 2.04	$ 2.40	$ 2.22
Consolidated Balance Sheet Data (2):					
Total assets	$ 2,375,308	$ 2,685,113	$ 2,897,884	$ 3,025,501	$ 3,124,764
Total long-term debt	$ 645,809	$ 696,285	$ 671,796	$ 715,058	$ 601,334
Total long-term liabilities (including long-term debt)	$ 703,183	$ 791,239	$ 799,436	$ 876,956	$ 791,938
Cash dividends declared per common share	$	$ 0.20	$ 0.44	$ 0.48	$ 0.48

(1) In accordance with the provisions of Statement of Financial Accounting Standards (SFAS) No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets , income statement data reflect reclassifications from the prior years presentation to exclude franchises sold, identified for sale, or terminated subsequent to December 31, 2005 which had not been previously included in discontinued operations. See Note 2 to our accompanying Consolidated Financial Statements, *Business Acquisitions and Dispositions*, which discusses these and other factors that affect the comparability of the information for the periods presented.

(2) As mentioned in *Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources* and Note 2 to our accompanying Consolidated Financial Statements, business combinations and dispositions have had a material impact on our reported financial information.

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

The following discussion and analysis of the results of operations and financial condition should be read in conjunction with the Sonic Automotive, Inc. and Subsidiaries Consolidated Financial Statements and the related notes thereto appearing elsewhere in this Annual Report on Form 10-K. The financial and statistical data contained in the following discussion for all periods presented reflects our December 31, 2006 classification of franchises between continuing and discontinued operations in accordance with SFAS No. 144.

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Overview

We are one of the largest automotive retailers in the United States. As of March 8, 2007 we operated 173 dealership franchises, representing 36 different brands of cars and light trucks, at 150 locations and 38 collision repair centers in 15 states. Our dealerships provide comprehensive services including sales of both new and used cars and light trucks, sales of replacement parts, performance of vehicle maintenance, manufacturer warranty repairs, paint and collision repair services, and arrangement of extended service contracts, financing, insurance and other aftermarket products for our customers. Although vehicle sales are cyclical and are affected by many factors, including general economic conditions, consumer confidence, levels of discretionary personal income, interest rates and available credit, our parts, service and collision repair services are not closely tied to vehicle sales and are not as dependent upon near-term sales volume. As a result, we believe the diversity of these products and services reduces the risk of periodic economic downturns.

The automobile industry s total amount of new vehicles sold decreased by 2.5% to 16.6 million vehicles in 2006 from 17.0 million vehicles in 2005. From an industry perspective, new vehicle unit sales on a year-over-year basis grew 4.8% for import brands and contracted 8.1% for domestic brands. Many factors such as brand and geographic concentrations have caused our past results to differ from the industry s overall trend. In 2006, both our import and domestic stores outperformed the overall new vehicle industry s year-over-year unit sales change.

We sell similar products and services that exhibit similar economic characteristics, use similar processes in selling our products and services and sell our products and services to similar classes of customers. As a result of this and the way we manage our business, we have aggregated our operating segments into a single segment for purposes of reporting financial condition and results of operations.

In the ordinary course of business we evaluate our dealership franchises for possible disposition based on various performance criteria. During the year ended December 31, 2006, we sold 12 franchises and had approved, but not completed, the disposition of 30 additional franchises. These franchises have been identified as held for sale because of unprofitable operations or other strategic considerations. We believe the disposition of these franchises will allow us to focus our management attention on those remaining stores with the highest potential return on investment.

Use of Estimates and Critical Accounting Policies

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

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

Finance, Insurance and Service Contracts We arrange financing for customers through various financial institutions and receive a commission from the lender either in a flat fee amount or in an amount equal to the difference between the actual interest rates charged to customers and the predetermined base rates set by the financing institution. We also receive commissions from the sale of various insurance contracts and non-recourse third party extended service contracts to customers. Under these contracts, the applicable manufacturer or third party warranty company is directly liable for all warranties provided within the contract.

In the event a customer terminates a financing, insurance or extended service contract prior to the original termination date, we may be required to return a portion of the commission revenue originally recorded to the third party provider (chargebacks). The commission revenue for the sale of these products and services is recorded net of estimated chargebacks at the time of sale. Our estimate of future chargebacks is established based on our historical chargeback rates, termination provisions of the applicable contracts and industry data. While chargeback rates vary depending on the type of contract sold, a 100 basis point change in the estimated chargeback rates used in determining our estimates of future chargebacks would have changed our estimated reserve for chargebacks at December 31, 2006 by approximately $1.6 million. Our estimate of chargebacks ($15.1 million as of December 31, 2006) is influenced by early contract termination events such as vehicle repossessions, refinancings and early pay-off. If these factors change, the resulting impact is a change in our estimate for chargebacks.

Goodwill Goodwill is tested for impairment at least annually, or more frequently when events or circumstances indicate that impairment might have occurred. Based on criteria established by the applicable accounting pronouncements, we allocate the carrying value of goodwill and test it for impairment based on our three geographic divisions. The $1,167.8 million of goodwill on our balance sheet, including approximately $12.3 million classified in assets held for sale, at December 31, 2006 was allocated to the following geographic divisions (dollars in millions):

Eastern Division	$ 429.8
Central Division	$ 356.4
Western Division	$ 381.6

In evaluating goodwill for impairment, if the fair value of a division is less than the carrying value of that division, we are then required to proceed to the second step of the impairment test. The second step involves allocating the calculated fair value to all of the assets of the respective division as if the calculated fair value was the purchase price of the business combination. This allocation would include assigning value to any previously unrecognized identifiable assets (including franchise assets) which means the remaining fair value that would be allocated to goodwill would be significantly reduced. See discussion regarding franchise agreements acquired prior to July 1, 2001 in Note 1 to our Consolidated Financial Statements. We would then compare the fair value of the goodwill resulting from this allocation process to the carrying value of the goodwill in the respective division with the difference representing the amount of impairment.

We use several assumptions and various fair value approaches in evaluating our goodwill for impairment. These assumptions and approaches include various earnings multiple approaches along with a discounted cash flow model utilizing estimated future earnings and our weighted average cost of capital.

At December 31, 2006, we were not required to conduct the second step of the impairment test described above, and we recognized no impairment of the carrying value of our goodwill on our balance sheet at December 31, 2006.

However, if in future periods we determine that the fair value of one or more of our divisions is less than their carrying value, we believe that application of the second step of the impairment test would result in a substantial impairment charge to the goodwill allocated to such division(s) and the amount of such impairment charge would likely be materially adverse to our consolidated operating results and financial position.

Insurance Reserves We have various self-insured and high deductible insurance programs which require us to make estimates in determining the ultimate liability we may incur for claims arising under these programs. We accrue for insurance reserves on a pro-rata basis throughout the year based on the expected year-end liability. These estimates, judgments and assumptions are made quarterly by our management based on available information and take into consideration annual actuarial evaluations based on historical claims experience, claims processing procedures, medical cost trends and, in certain cases, a discount factor. If our management receives information which causes us to change our estimate of the year end liability, the amount of expense or expense reduction required to be recorded in any particular quarter could be material to our operating results, financial position and cash flows. We estimate the ultimate liability under these programs is between $21.9 million and $24.2 million. At December 31, 2006, we had $22.6 million reserved for such programs. We used a discount rate

of 4.0% to calculate the present value of our estimated workers compensation claims. A discount rate of 4.0% was used to calculate the present value of our general liability claim reserves. A 100 bps change in the discount rate or a 5 basis point change in the Selected Loss Cost Estimate would not have a significant impact on the reserve balance.

Lease Exit Accruals The majority of our dealership properties are leased under long-term operating lease arrangements. When leased properties are no longer utilized in operations, we record lease exit accruals. These situations could include the relocation of an existing facility or the sale of a franchise where the buyer will not be subleasing the property for either the remaining term of the lease or for an amount equal to our obligation under the lease. The lease exit accruals represent the present value of the lease payments, net of estimated sublease rentals, for the remaining life of the operating leases and other accruals necessary to satisfy the lease commitment to the landlord. At December 31, 2006, we had $8.7 million accrued for lease exit costs.

Legal Proceedings We are involved, and expect to continue to be involved, in numerous legal proceedings arising out of the conduct of our business, including litigation with customers, employment related lawsuits, contractual disputes and actions brought by governmental authorities. As of December 31, 2006, we had $2.0 million in legal reserves included in other accrued liabilities. Currently, with the exception of the Galura litigation matter discussed in Item 3: Legal Proceedings herein, no legal proceedings are pending against or involve us that, in the opinion of management, could reasonably be expected to have a material adverse effect on our business, financial condition or results of operations. However, the results of legal proceedings cannot be predicted with certainty, and an unfavorable resolution of one or more of these proceedings could have a material adverse effect on our business, financial condition, results of operations, cash flows and prospects.

Classification of Franchises in Continuing and Discontinued Operations We classify the results from operations of our continuing and discontinued operations in our consolidated statements of income based on the provisions of SFAS No. 144. Many of these provisions involve judgment in determining whether a franchise will be reported as continuing or discontinued operations. Such judgments include whether a franchise will be sold or terminated, the period required to complete the disposition and the likelihood of changes to a plan for sale. If in future periods we determine that a franchise should be either reclassified from continuing operations to discontinued operations or from discontinued operations to continuing operations, previously reported consolidated statements of income may be reclassified in order to reflect the current classification.

Income Taxes As a matter of course, we are regularly audited by various taxing authorities and from time to time, these audits result in proposed assessments where the ultimate resolution may result in us owing additional taxes. We believe that our tax positions comply, in all material respects, with applicable tax law and that we have adequately provided for any reasonably foreseeable outcome related to these matters. Included in other accrued liabilities at December 31, 2006 is $3.4 million in reserves that we have provided for these matters.

We have $9.3 million in deferred tax assets related to state net operating loss carryforwards that will expire between 2014 and 2026. Management reviews these carryforward positions, the time remaining until expiration and other opportunities to utilize these carryforwards in making an assessment as to whether it is more likely than not that these carryforwards will be utilized. We have recorded a valuation allowance of $0.1 million in 2006 based on our judgment that certain state carryforwards will not be utilized. We have not recorded a valuation allowance related to our remaining carryforwards because it is more likely than not that taxable income for these other states will be sufficient to realize the benefits of the associated deferred tax assets. However, the results of future operations, regulatory framework of these taxing authorities and other related matters cannot be predicted with certainty. Therefore, actual utilization of the losses which created these deferred tax assets which differs from the assumptions used in the development of our judgment could result in a charge that would be materially adverse to our consolidated operating results, financial position and cash flows.

We accrue for income taxes on a pro-rata basis throughout the year based on the expected year end liability. These estimates, judgments and assumptions are made quarterly by our management based on available

information and take into consideration estimated income taxes based on prior year income tax returns, changes in income tax law, our income tax strategies and other factors. If our management receives information which causes us to change our estimate of the year end liability, the amount of expense or expense reduction required to be recorded in any particular quarter could be material to our operating results, financial position and cash flows.

Cornerstone Acceptance Allowance for Credit Losses As of December 31, 2006, we had outstanding notes receivable arising from operations of our wholly-owned finance subsidiary, Cornerstone Acceptance Corporation (Cornerstone), of $28.5 million, net of an allowance for credit losses of $4.9 million. These notes receivable have average terms of approximately forty-three months and are secured by the related vehicles. Our assessment of allowance for credit losses considers historical loss ratios, the performance of the current portfolio with respect to past due accounts, and the average age of the accounts in the current portfolio. As of December 31, 2006, the average loss ratio for mature accounts was 20.8% and the average percentage of losses remaining to be incurred on the current portfolio as a result of the average age of the current portfolio was 44.0%. A change of 100 basis points in both of these percentages would have changed our estimated allowance for credit losses by $0.2 million at December 31, 2006. These notes receivable are recorded in receivables, net, and other assets on the accompanying Consolidated Balance Sheets. Sonic s management is currently evaluating strategic alternatives for Cornerstone. These alternatives include selling Cornerstone or selling all or a portion of Cornerstone s outstanding notes receivable.

Recent Accounting Pronouncement

On January 1, 2006, we adopted SFAS No. 123R, Accounting for Stock-Based Compensation . SFAS No. 123R requires a public entity to measure the cost of employee services received in exchange for an award of equity instruments based on the grant- date fair value of the award. That cost will be recognized over the period during which an employee is required to provide service in exchange for the award (usually the vesting period). Tax benefits associated with share-based payments will be recognized as an addition to paid-in capital. Cash retained as a result of these tax benefits will be presented in the statement of cash flows as financing cash inflows and operating cash outflows.

On December 22, 2005, a committee of our Board of Directors approved the accelerated vesting of all outstanding options to purchase our Class A common stock with an exercise price of more than $22.55 per share. The purpose of the accelerated vesting of these stock options was to reduce the non-cash compensation expense we would have recorded in future periods pursuant to SFAS No. 123R. This accelerated vesting reduced future expense pursuant to SFAS No. 123R by approximately $2.1 million. We recognized approximately $4.5 million of expense related to stock options during the year ended December 31, 2006. See Note 9 to our Consolidated Financial Statements for additional discussion and disclosures.

In June 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation (FIN) No. 48, Accounting for Uncertainty in Income Taxes . FIN No. 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN No. 48 also provides guidance on derecognition, classification and the treatment of interest and penalties. Sonic is currently evaluating the provisions of FIN No. 48, which will be effective for Sonic in the first quarter of 2007, and has not determined the impact on Sonic s consolidated operating results, financial position and cash flows.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measures (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value and enhances disclosures about fair value measures required under other accounting pronouncements, but does not change existing guidance as to whether or not an instrument is carried at fair value. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007. Sonic is currently reviewing the provisions of SFAS No. 157 to determine the impact on its consolidated operating results, financial position and cash flows.

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In September 2006, the Securities and Exchange Commission issued Staff Accounting Bulletin No. 108, Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements (SAB 108), which provides interpretive guidance on the consideration of the effects of prior year misstatements in quantifying current year misstatements for the purpose of a materiality assessment. SAB 108 is effective as of the end of Sonic s 2006 fiscal year, allowing a one-time transitional cumulative effect adjustment to beginning retained earnings as of January 1, 2006 for errors that were not previously deemed material, but are material under the guidance in SAB 108. See Note 1 to accompanying consolidated financial statements for a discussion of the effects of adopting SAB 108.

In February 2007, the FASB issued Statements of Financial Accounting Standards (SFAS) No. 159, The Fair Value Option for Financial Assets and Financial Liabilities . SFAS No. 159 permits entities to choose to measure eligible items at fair value at specified election dates and report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting date. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. We are currently reviewing the provisions of SFAS No. 159 to determine the impact on our consolidated operating results, financial position and cash flows.

Results of Operations

On July 19, 2006, we issued a press release describing charges recorded during the second quarter of 2006 in connection with the decision to exit certain facility leases and cancel various facility improvement projects, asset impairments and other asset write-offs, finance chargeback reserves, litigation matters and an adjustment of certain tax strategies. These charges are discussed in more detail in the respective areas under the subsequent heading Results of Operations when discussing results for the year ended December 31, 2006. The amount and location of the charges in the accompanying consolidated statements of income for the year ended December 31, 2006 are presented in the following table:

	Continuing Operations						
(in millions)	Finance, insurance and other revenue	Cost of sales	Selling, general and administrative expenses	Depreciation and amortization	Provision for income taxes	Loss from operations and sale of discontinued franchises	Total
Real estate and other asset impairments/write-offs and lease exit costs	$ 0.4	$ 0.3	$ 8.1	$ 2.1	$	$ 7.8	$ 18.7
Finance chargeback reserves	6.2						6.2
Legal accruals			1.2			0.5	1.7
Effective income tax rate adjustment					1.0		1.0
	$ 6.6	$ 0.3	$ 9.3	$ 2.1	$ 1.0	$ 8.3	$ 27.6

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

	Percentage of Total Revenue (1) for the Year Ended December 31,		
	2004	2005	2006
Revenues:			
New vehicles	61.4%	61.6%	61.4%
Used vehicles	15.7%	15.5%	16.0%
Wholesale vehicles	6.8%	6.8%	6.2%
Parts, service and collision repair	13.6%	13.6%	14.0%
Finance, insurance and other	2.5%	2.5%	2.4%
Total revenue	100.0%	100.0%	100.0%
Cost of sales (2)	84.7%	84.7%	84.6%
Gross profit	15.3%	15.3%	15.4%
Selling, general and administrative expenses	11.9%	11.7%	11.7%
Depreciation and amortization	0.2%	0.2%	0.3%
Operating income	3.2%	3.4%	3.4%
Interest expense, floor plan	0.4%	0.5%	0.8%
Interest expense, other, net	0.6%	0.6%	0.5%
Other expense, net	0.0%	0.0%	0.0%
Income from continuing operations before income taxes	2.2%	2.3%	2.1%
Income tax expense	0.8%	0.9%	0.9%
Income from continuing operations	1.4%	1.4%	1.2%

(1) In accordance with the provisions of SFAS No. 144, prior years income statement data reflects reclassifications to exclude additional franchises sold, identified for sale or terminated subsequent to December 31, 2005 which had not been previously included in discontinued operations. See Note 2 to our accompanying Consolidated Financial Statements, *Business Acquisitions and Dispositions*, which discusses these and other factors that affect the comparability of the information for the periods presented.

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

During the year ended December 31, 2006, we sold 12 franchises, and had approved, but not completed, the disposition of 30 additional franchises. The results of operations of these dealerships, including gains or losses on disposition, have been included in discontinued operations on the accompanying Consolidated Statements of Income for all periods presented. In addition to these dispositions, during the years ended December 31, 2004 and 2005, we disposed or terminated seven and 22 franchises, respectively.

Annual same store results of operations represent the aggregate of the same store results for each of the four quarters in that year. Same store results for each quarter include dealerships that were owned and operated for the entire quarter in both periods and were classified as continuing operations under SFAS No. 144 at December 31, 2006. Unless otherwise noted, our discussion of the Results of Operations from New Vehicles to Gross Profit and Gross Margins is on a same store basis.

New Vehicles

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

The automobile manufacturing industry is cyclical and historically has experienced periodic downturns characterized by oversupply and weak demand. As an automotive retailer, we seek to mitigate the effects of this cyclicality by maintaining a diverse mix of domestic and import branded dealerships. Our brand diversity allows us to offer a broad range of products at a wide range of prices from lower priced, or economy vehicles, to luxury vehicles. We believe that this diversity reduces the risk of changes in customer preferences, product supply shortages and aging products. For the year ended December 31, 2006, 83.3% of our total new vehicle revenue was generated by import and luxury dealerships compared to 81.7% for 2005. We expect this trend toward more import and domestic luxury dealerships to continue. We believe demographic and other trends favor import and luxury brands and expect our acquisition activity in the future to concentrate primarily, but not completely, on these brands.

	For the Year Ended		Units or $	%	For the Year Ended		Units or $	%
	12/31/2005	12/31/2006	Change	Change	12/31/2004	12/31/2005	Change	Change
Total New Vehicle Units								
Same Store	146,560	149,257	2,697	1.8%	132,682	141,330	8,648	6.5%
Acquisitions and Other	486	6,990	6,504	1338.3%	1,030	5,716	4,686	455.0%
Total as Reported	147,046	156,247	9,201	6.3%	133,712	147,046	13,334	10.0%
Total New Vehicle Revenues (in thousands)								
Same Store	$ 4,459,580	$ 4,623,409	$ 163,829	3.7%	$ 3,929,861	$ 4,216,483	$ 286,622	7.3%
Acquisitions and Other	24,340	273,875	249,535	1025.2%	42,929	267,437	224,508	523.0%
Total as Reported	$ 4,483,920	$ 4,897,284	$ 413,364	9.2%	$ 3,972,790	$ 4,483,920	$ 511,130	12.9%
Total New Vehicle Unit Price								
Same Store	$ 30,428	$ 30,976	$ 548	1.8%	$ 29,619	$ 29,834	$ 215	0.7%
Total Dealerships as Reported	$ 30,493	$ 31,343	$ 850	2.8%	$ 29,712	$ 30,493	$ 781	2.6%

The increase in our same store new vehicle unit sales was driven entirely by our import dealerships, which experienced an increase of 3,290 units, or 3.2%, while our domestic dealerships experienced a decrease of 593 units, or 1.3%. Our import stores underperformed the industry unit volume increase of 4.8%, while our domestic stores outperformed the industry decrease of 8.1%. Our top performing import brands for 2006 were Toyota and Mercedes, which posted increases of 4,125 units, or 17.7%, and 435 units, or 8.8%, respectively. These increases can be attributed to the introduction of new models, in addition to new body styling and design on existing models. Additionally, our BMW stores posted a 2.3% revenue increase despite a slight decline in unit volume. Our Honda dealerships experienced the most significant decline in sales volume among our import stores, decreasing by 648 units, or 2.1%, as compared to 2005. Our top performing domestic brand was Ford, which posted an increase of 325 units, or 1.9%. Our GM (excluding Cadillac) dealerships experienced a decline in new retail unit volume of 1,043 units, or 8.2%, but strong fleet sales with an increase of 647 units, or 14.5%, helped to offset that decline. Additionally, our Cadillac stores posted an improvement in fleet sales of 118 units, or 37.7%, which offset the domestic decline in new unit volume.

The increase in our sales price per unit can be attributed mainly to the fact that a larger percentage of our sales are being generated by higher priced luxury vehicles. Many of our import dealerships experienced price per unit increases, most notably being Mercedes, BMW and Honda (up 5.5%, 3.1% and 2.5%, respectively). On the domestic side, our Ford and Cadillac dealerships experienced the most significant increases in sales price per unit (up 3.5% and 2.9%, respectively). The increases at these dealerships can be attributed to both the various pricing strategies put in place by Ford and GM during 2005, which lowered 2005 pricing, and a shift from car sales to truck and SUV sales during the current year.

During 2005, both our import and domestic dealerships experienced increases in total same store new vehicle unit sales, as compared to 2004. Our import dealerships experienced an increase of 7,510 units, or 8.4%,

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during this time period. This is compared to an industry increase in unit sales at import dealerships of 4.7%. This increase can be mainly attributed to our Honda and Toyota dealerships, which experienced unit volume increases of 13.0% and 6.4%, respectively, when compared to 2004. Management stability at our Honda dealerships contributed to the improvement in new vehicle sales volume. Our domestic dealerships experienced a unit sales increase of 1,138 units, or 2.6%, during 2005. This is compared to an industry decrease in unit sales at domestic dealerships of 2.5%. Our GM (excluding Cadillac) and Ford dealerships experienced declines in new retail unit volume, but strong fleet sales led to an overall improvement in total new unit sales volume. The declines experienced at our domestic dealerships in 2004 can be mainly attributed to declining truck and SUV sales, which resulted from significant increases in gas prices. Conversely, our Cadillac stores managed only a small increase in new retail unit volume, while a decline in fleet sales led to an overall decline in new unit volume. All of our import dealerships except Volvo, Acura and VW experienced sales price per unit increases during 2005. Our Honda dealerships experienced the most significant improvement in sales price per unit, increasing by $1,239, or 5.8%, when compared to 2004. All of our domestic dealerships experienced price per unit decreases.

Used Vehicles

Used vehicle revenues are directly affected by the level of manufacturer incentives on new vehicles, the number and quality of trade-ins and lease turn-ins and the availability of consumer credit. In addition, various manufacturers provide franchised dealers the opportunity to certify pre-owned vehicles based on criteria established by the manufacturer. This certification process extends the standard manufacturer warranty. On a continuing operations basis, our sales of CPO vehicles decreased in 2006 to 34.4% of total used vehicle units from 38.2% in 2005, a decrease of 2.0%. This decrease was partially due to the increase in non-CPO vehicles related to the implementation of a standardized merchandising process, that includes the retailing of value used vehicles, along with an inventory management system at a number of our stores. We expect to continue the rollout and refinement of the process in 2007. Additionally, industry pricing improvements affected the value of used vehicles, as the Manheim Used Vehicle Value Index increased by 1.6% from December 2005 to December 2006.

	For the Year Ended		Units or $	%	For the Year Ended		Units or $	%
	12/31/2005	12/31/2006	Change	Change	12/31/2004	12/31/2005	Change	Change
Total Used Vehicle Units								
Same Store	61,336	64,341	3,005	4.9%	56,725	59,304	2,579	4.5%
Acquisitions and Other	120	2,550	2,430	2025.0%	390	2,152	1,762	451.8%
Total as Reported	61,456	66,891	5,435	8.8%	57,115	61,456	4,341	7.6%
Total Used Vehicle Revenues (in thousands)								
Same Store	$ 1,122,584	$ 1,213,001	$ 90,417	8.1%	$ 1,000,630	$ 1,061,789	$ 61,159	6.1%
Acquisitions and Other	4,067	62,019	57,952	1424.9%	13,187	64,862	51,675	391.9%
Total as Reported	$ 1,126,651	$ 1,275,020	$ 148,369	13.2%	$ 1,013,817	$ 1,126,651	$ 112,834	11.1%
Total Used Vehicle Unit Price								
Same Store	$ 18,302	$ 18,853	$ 551	3.0%	$ 17,640	$ 17,904	$ 264	1.5%
Total Dealerships as Reported	$ 18,333	$ 19,061	$ 728	4.0%	$ 17,750	$ 18,333	$ 583	3.3%

In 2006, our import dealerships contributed to the overall improvement in used unit volume by posting an increase of 2,490 units, or 6.3%, when compared to 2005. Of our import stores, BMW, Honda and Toyota posted the most significant increases in used unit volume. Our domestic dealerships also posted an improvement in used unit sales volume, increasing by 515 units, or 2.4%. Cadillac was the largest contributor to the domestic increase in unit volume.

Our overall price per unit increase of 3.0% is due mainly to a favorable used vehicle market. Based on the improvement in the Manheim Used Vehicle Value Index as stated above, we believe that our price per unit increase is consistent with the industry as a whole.

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During 2005, the increase in used unit sales volume was driven entirely by our import dealerships, which posted an increase of 2,786 units, or 8.0%, when compared to 2004. Of our import stores, Honda and BMW posted the most significant increases in used unit volume. Our Ford and GM (excluding Cadillac) stores posted the only increases in used unit volume among our domestic brands. Our Cadillac dealerships experienced the largest decline in unit volume among all of our brands.

Wholesale Vehicles

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

	For the Year Ended		Units or $	%	For the Year Ended		Units or $	%
	12/31/2005	12/31/2006	Change	Change	12/31/2004	12/31/2005	Change	Change
Total Wholesale Vehicle Units								
Same Store	52,834	49,364	(3,470)	(6.6%)	48,960	51,038	2,078	4.2%
Acquisitions and Other	2,969	4,337	1,368	46.1%	2,527	4,765	2,238	88.6%
Total as Reported	55,803	53,701	(2,102)	(3.8%)	51,487	55,803	4,316	8.4%
Total Wholesale Vehicle Revenues (in thousands)								
Same Store	$ 464,642	$ 437,035	$ (27,607)	(5.9%)	$ 403,204	$ 435,409	$ 32,205	8.0%
Acquisitions and Other	33,947	56,477	22,530	66.4%	35,644	63,180	27,536	77.3%
Total as Reported	$ 498,589	$ 493,512	$ (5,077)	(1.0%)	$ 438,848	$ 498,589	$ 59,741	13.6%
Total Wholesale Unit Price								
Same Store	$ 8,794	$ 8,853	$ 59	0.7%	$ 8,235	$ 8,531	$ 296	3.6%
Total Dealerships as Reported	$ 8,935	$ 9,190	$ 255	2.9%	$ 8,523	$ 8,935	$ 412	4.8%

The decline in wholesale unit volume can be mainly attributed to the implementation of our merchandising and inventory management process (see Used Vehicles above for further discussion). We believe this improved process allowed us to retail used vehicles we historically would have disposed of through the wholesale market.

During 2005, higher revenues realized were driven by both an increase in wholesale unit sales volume and higher unit sales prices at our import dealerships. Unit sales volume at our import dealerships increased by 1,996 units, or 6.3%, while price per unit increased by $495, or 5.8%. Favorable pricing increases followed the increases experienced in used retail sales and were consistent with the industry. Additionally, our domestic dealerships experienced only a slight increase in unit volume. Improvements in retail vehicle sales volume, the principal source of wholesale vehicle revenues via trade-in, contributed to the higher overall volume in 2005, as compared to 2004.

Parts, Service and Collision Repair (Fixed Operations)

Same store revenue from these items was as follows (amounts in thousands):

	For the Year Ended		$	%	For the Year Ended		$	%
	12/31/2005	12/31/2006	Change	Change	12/31/2004	12/31/2005	Change	Change
Parts	$ 528,965	$ 554,172	$ 25,207	4.8%	$ 463,206	$ 487,205	$ 23,999	5.2%
Service	395,198	420,656	25,458	6.4%	348,321	$ 366,271	17,950	5.2%
Collision repair	57,568	57,699	131	0.2%	54,312	$ 54,586	274	0.5%
	$ 981,731	$ 1,032,527	$ 50,796	5.2%	$ 865,839	$ 908,062	$ 42,223	4.9%

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

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warranty programs. During 2006, 18.8% of our service and parts revenue was generated by warranty repairs and 48.5% by customer pay repairs compared to 20.6% by warranty repairs and 46.6% by customer pay repairs in 2005.

We believe that over time, vehicle quality will improve, but vehicle complexity will offset any revenue lost from improvement in vehicle quality. We also believe that we have the ability, through our access to capital, to continue to add service capacity and increase revenues. During 2006, we added 163 service stalls, or 5.0%, to our overall stall capacity In addition, manufacturers continue to extend new vehicle warranty periods and have also begun to include regular maintenance items in the warranty coverage. These factors, combined with the extended manufacturer warranties on CPO vehicles (see the discussion in Business Business Strategy Certified Pre-Owned Vehicles above), should facilitate continued growth in our service and parts business.

Parts revenue is driven by the mix of warranty repairs versus customer pay repairs as prices for warranty parts are established by the manufacturer. We believe that long-term trends in retail parts sales will be affected by the same trends as discussed above for service (additional capacity, customer satisfaction, etc.).

As of December 31, 2006, we operated 37 collision repair centers. Collision revenues are heavily impacted by trends in the automotive insurance industry. Over the last few years, collision repair revenues have either declined or remained flat because customers are choosing higher deductible policies, thus choosing not to make minor repairs that were previously covered by lower deductible policies. In addition, when insurance companies declare a vehicle totaled , the model year of that vehicle often determines where it is repaired. Late model vehicles tend to be repaired at franchised dealership body shops, while older vehicles tend to be repaired at stand-alone collision centers.

	For the Year Ended		$	%	For the Year Ended		$	%
	12/31/2005	12/31/2006	Change	Change	12/31/2004	12/31/2005	Change	Change
Total Parts, Service and Collision Repair (in thousands)								
Same Store	$ 981,731	$ 1,032,527	$ 50,796	5.2%	$ 865,839	$ 908,062	$ 42,223	4.9%
Acquisitions and Other	6,701	82,343	75,642	1128.8%	13,337	80,370	67,033	502.6%
Total as Reported	$ 988,432	$ 1,114,870	$ 126,438	12.8%	$ 879,176	$ 988,432	$ 109,256	12.4%

Same store Fixed Operations revenues increased during 2006, primarily due to the performance of our import dealerships (up $55.7 million, or 8.2%) outpacing decreases in our domestic dealerships (down $5.8 million, or 2.0%). Customer pay sales at our import dealerships increased $41.9 million, or 13.8%. Our BMW dealerships experienced significant increases in Fixed Operations revenues, increasing by $22.3 million, or 12.3%, compared to 2005 as a continued result of BMW s vehicle maintenance programs and strong same store new vehicle sales. These import increases were partially offset by decreases of $5.8 million, or 2.0%, at our domestic dealerships. Warranty sales declines of $6.9 million, or 14.2%, were offset by an increase in customer pay of $0.4 million, or 0.3%, at our domestic stores. Our GM and Cadillac dealerships, which decreased $2.5 million, or 2.4%, and $3.7 million, or 3.1%, respectively, as compared to 2005 contributed to lower domestic sales. The declines in our GM dealerships were primarily caused by a decrease in warranty repair services and wholesale parts sales of $8.9 million, or 13.2%. Warranty sales at our Cadillac stores experienced declines of $3.4 million, or 14.3%, as compared to 2005.

Same store Fixed Operations revenues increased during 2005 compared to 2004, primarily due to the performance of our import dealerships (up $42.0 million, or 7.4%) outpacing decreases in our domestic dealerships (down $0.9 million, or 0.3%). Warranty sales at our import dealerships increased $1.9 million, or 1.4%. Our BMW dealerships experienced significant increases in Fixed Operations revenues, increasing by $18.4 million, or 12.9%, compared to 2004 as a continued result of BMW s vehicle maintenance programs and strong same store new vehicle sales. In addition, our BMW stores posted increases in warranty sales of $3.0 million, or 6.7%. These import increases were partially offset by decreases in warranty sales at our domestic

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dealerships, which declined $2.0 million, or 3.9%, compared to 2004. The overall domestic dealership Fixed Operations revenue declines primarily relate to our Cadillac dealerships, which decreased $3.0 million, or 2.5% as compared to 2004. Warranty sales at our Cadillac stores experienced declines of $2.3 million, or 8.8%, as compared to 2004.

Finance, Insurance and Other

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

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

- Lower cost, sub-vented financing is often available only from the manufacturers captives and franchised dealers;
- Lease-financing alternatives are largely available only from manufacturers captives or other indirect lenders;
- Customers with substandard credit frequently do not have direct access to potential sources of sub-prime financing; and
- Customers with significant negative equity in their current vehicle (i.e., the customer s current vehicle is worth less than the balance of their vehicle loan or lease obligation) frequently are unable to pay off the loan on their current vehicle and finance the purchase or lease of a replacement new or used vehicle without the assistance of a franchised dealer.

Finance, insurance and other revenues are driven by the level of new and used vehicle sales, manufacturer financing or leasing incentives and our penetration rate. The penetration rate represents the percentage of vehicle sales on which we are able to originate financing or sell extended service contracts, other aftermarket products or insurance contracts. Our finance penetration rate decreased slightly to 67.6% in 2006 from 68.1% in 2005. Our extended service contract penetration rate increased to 34.7% in 2006 from 34.3% in 2005. We expect our finance and insurance penetration rate to increase over time as we continue to emphasize the use of menu selling techniques.

	For the Year Ended		**$**	**%**	**For the Year Ended**		**$**	**%**
	12/31/2005	**12/31/2006**	**Change**	**Change**	**12/31/2004**	**12/31/2005**	**Change**	**Change**
Total Finance, Insurance and Other Revenue (in thousands)								
Same Store	$ 176,435	$ 181,386	$ 4,951	2.8%	$ 157,888	$ 169,078	$ 11,190	7.1%
Acquisitions and Other	4,693	10,002	5,309	113.1%	7,531	12,050	4,519	60.0%

Total as Reported	$ 181,128	$ 191,388	$ 10,260	5.7%	$ 165,419	$ 181,128	$ 15,709	9.5%
Total F&I per Unit (excluding fleet)								
Same Store	$ 911	$ 915	$ 4	0.4%	$ 889	$ 906	$ 17	1.9%
Total Dealerships as Reported	$ 932	$ 922	$ (10)	(1.1%)	$ 924	$ 932	$ 8	0.9%

Same store finance, insurance and other revenues increased during 2006 when compared to 2005 due to a 2.7% increase in retail vehicle unit sales volume. Our import dealerships reported an increase of revenues by

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$ 4.5 million, or 3.6%, primarily due to revenue increases in our Toyota, Mercedes, and Lexus dealerships of $3.2 million, or 11.8%, $1.0 million, or 14.2%, and $0.8 million, or 10.5%, respectively. Our domestic stores also experienced a slight increase in revenues of $0.5 million, or 0.9%. The increase was led by our Cadillac and GM stores of $0.5 million, or 4.1%, and $0.2 million, or 0.8%, respectively. The revenue increase was partially offset by a $6.2 million increase in our allowance for estimated finance chargebacks that was recorded in the second quarter ended June 30, 2006 as a result of a change in estimate for the allowance.

Same store finance, insurance, and other revenues increased in 2005 compared to 2004 due to a 5.9% increase in retail unit sales volume. The increase in revenues was primarily attributed to our import stores with an $11.7 million, or 11.1% increase over 2004. Our Honda, BMW, and Lexus dealerships led the rise in revenues with increases of $6.0 million, or 20.3%, $1.9 million, or 10.9%, and $1.3 million, or 20.0%, respectively. The increase at our import stores was slightly offset by a decrease of $0.9 million or 1.6% at our domestic stores, due to a decline in new and used retail units sold of 3.9% and 0.9%, respectively. The domestic decline was partially offset by our GM stores (excluding Cadillac), which experienced increases of $0.3 million, or 1.4%.

Gross Profit and Gross Margins

The cost of sales line item includes the cost of new and used vehicles, vehicle parts and all costs directly linked to servicing customer vehicles (labor for parts, service and collision repair associates, depreciation on service equipment and service consumables). Our overall gross profit and gross margin (gross profit as a percentage of revenues) as a percentage of revenues generally vary depending on changes in our revenue mix. Although sales of new vehicles comprise the majority of our total revenues, new vehicles generally carry the lowest margin rate of any product or service we offer. As a result, sales of new vehicles comprise a relatively small portion of total gross profits when compared to revenue. Retail sales of used vehicles generally carry a slightly higher gross margin rate than new vehicles. Parts, service and collision repair carry a much higher gross margin rate than vehicle sales. Product mix also has an impact on the gross margins that we realize. Historically, our import and luxury brands provide higher margins than our domestic brands. As we continue to acquire more import and luxury dealerships, we would expect our gross margins to increase. Our same store revenue mix between different products is shown in the following table:

	For the Year Ended		Basis Point	For the Year Ended		Basis Point
	12/31/2005	12/31/2006	Change	12/31/2004	12/31/2005	Change
Revenues as a Percentage of Total Revenues						
New Vehicles	61.9%	61.7%	(20)	61.8%	62.1%	30
Used Vehicles	15.6%	16.2%	60	15.7%	15.6%	(10)
Wholesale Vehicles	6.4%	5.8%	(60)	6.3%	6.4%	10
Fixed Operations	13.6%	13.8%	20	13.6%	13.4%	(20)
Finance, Insurance and Other	2.5%	2.5%	0	2.6%	2.5%	(10)
Total as Reported	100.0%	100.0%		100.0%	100.0%	

	For the Year Ended		$	%	For the Year Ended		$	%
	12/31/2005	12/31/2006	Change	Change	12/31/2004	12/31/2005	Change	Change
Total Gross Profit (in thousands)								
Same Store	$ 1,106,963	$ 1,156,086	$ 49,123	4.4%	$ 973,704	$ 1,038,561	$ 64,857	6.7%
Acquisitions and Other	10,082	75,496	65,414	648.8%	18,550	78,484	59,934	323.1%

Total as Reported	$ 1,117,045	$ 1,231,582	$ 114,537	10.3%	$ 992,254	$ 1,117,045	$ 124,791	12.6%

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The overall gross margin rates on our various revenue lines on a same store basis were as follows:

	For the Year Ended		Basis Point	For the Year Ended		Basis Point
	12/31/2005	12/31/2006	Change	12/31/2004	12/31/2005	Change
New vehicles	7.3%	7.3%		7.4%	7.3%	(10)
Used vehicles	10.6%	10.3%	(30)	10.3%	10.8%	50
Wholesale vehicles	(0.4%)	(1.1%)	(70)	(1.3%)	(0.5%)	80
Parts, service and collision repair	49.5%	49.9%	40	49.4%	49.6%	20
Finance and insurance	100.0%	100.0%		100.0%	100.0%	
Overall gross margin	15.4%	15.4%		15.3%	15.3%	

Our same store gross margin percentage was flat in 2006, when compared to 2005. Gross margin improvements experienced in Fixed Operations were offset by declines in both the used and wholesale vehicle gross margin percentages. Our Toyota dealerships posted the most significant increase in Fixed Operations gross margin percentage among our import dealerships, improving by 130 basis points. In addition, the majority of our domestic dealerships contributed to the Fixed Operations increase. Specifically, our GM (excluding Cadillac), Ford and Cadillac dealerships experienced Fixed Operations margin increases of 80 basis points, 40 basis points and 30 basis points, respectively, when compared to 2005.

The overall same store gross margin percentage remained flat at 15.3% in 2005 and 2004. Improvements experienced in all other categories were offset by a 10 basis point decline in the new vehicle gross margin percentage. The largest increases in margin percentage related to used and wholesale vehicles, which were primarily attributed to price increases driven by a lower supply of higher quality used vehicles than in previous years. Fixed Operations gross margin percentages improved primarily due to a 240 basis point increase experienced at our Ford dealerships.

Selling, General and Administrative Expenses

Selling, general and administrative (SG&A) expenses are comprised of four major groups: compensation expense, advertising expense, rent and rent related expense, and other expense. Compensation expense primarily relates to dealership personnel who are paid a commission or a modest salary plus commission (which typically vary depending on gross profits realized) and support personnel who are paid a fixed salary. Due to the salary component for certain dealership and corporate personnel, gross profits and compensation expense are not 100% correlated. Advertising expense and other expenses vary based on the level of actual or anticipated business activity and number of dealerships owned. Rent and rent related expense typically varies with the number of dealerships owned, investments made for facility improvements and interest rates. Although not completely correlated, we believe the best way to measure SG&A expenses is as a percentage of gross profit.

Total SG&A expenses increased $89.4 million, or 10.5%, in 2006 compared to 2005. As a percentage of gross profit, reported SG&A expense increased by 20 basis points, from 76.1% in 2005 to 76.3% in 2006. These increases, both the dollar increase and the increase as a percentage of gross profits, can be attributed to current year acquisitions, a number of charges recorded during 2006 and the effect of a $3.0 million favorable legal settlement in 2005. Acquisitions in 2006 contributed $39.0 million to the year over year dollar increase. The charges recorded in 2006 included property and equipment impairment charges and other asset write-offs of approximately $7.9 million, which represent a 70 basis point increase in SG&A as a percentage of gross profit. In addition, legal accruals of $2.0 million and lease exit accruals of $2.0 million were recorded during 2006, each representing a 20 basis point increase in SG&A as a percentage of gross profit, respectively. Finance reserve chargeback accruals of $6.2 million recorded in the second quarter of 2006 also negatively affected the percentage of SG&A to gross profit in 2006 by 40 basis points. In 2005, reported SG&A expense as a percentage of gross profit improved by 170 basis points, when compared to 2004.

Total reported compensation expense increased $44.0 million, or 8.8%, in 2006, as compared to 2005 due to acquistions and higher gross profit levels. As a percentage of gross profit, total compensation expense improved by 60 basis points to 44.1% in 2006 from 44.7% in 2005. In 2005, total reported compensation expense increased by $45.8 million, or 10.1%, when compared to 2004, while decreasing by 100 basis points as a percentage of gross profit from 45.7% in 2004 to 44.7% in 2005. The decline as a percentage of gross profit was due to standardized pay plans implemented in 2004, tying compensation more closely with gross profit.

Advertising expense increased $5.6 million, or 9.5%, in 2006, as compared to 2005. Of this increase, $3.3 million was due to acquisitions. The remaining increase in advertising expense can be attributed to a targeted approach to allocate advertising dollars to certain brands in key markets, which was implemented in 2005. Despite the dollar increase, the advertising expense to gross profit ratio declined by 10 basis points to 5.2% in 2006 from 5.3% in 2005. In 2005, advertising expense increased $5.2 million, or 9.7%, when compared to 2004, while also improving by 10 basis points as a percentage of gross profit.

Rent and rent related expenses increased $22.8 million, or 19.1%, in 2006, as compared to 2005. As a percentage of gross profit, rent and rent related expenses increased by 80 basis points to 11.5% in 2006 from 10.7% in 2005. Acquisitions contributed $5.9 million to the increase. We also experienced increases in rent expense as a result of the completion of facility improvement projects and the resulting sale-leaseback of these facilities, the effect of rising interest rates on our variable rate leases and the establishment of lease exit accruals. In 2005, rent and rent related expenses increased $16.7 million, or 16.3%, as compared to 2004. The majority of the increase was due to acquisitions, new facilities and improvements on existing facilities.

Other SG&A expenses increased $17.0 million, or 9.8%, in 2006, as compared to 2005. Acquisitions accounted for approximately $9.3 million of the increase. The remaining increase is primarily attributed to higher service loaner expense, data processing, legal expenses and impairment charges. In 2005, other SG&A expenses increased $10.7 million, or 6.6%, as compared to 2004.

Depreciation and Amortization

Depreciation expense increased $5.0 million, or 27.3%, in 2006 compared to 2005. This increase was due primarily to a $72.1 million increase in gross property and equipment related to continuing operations, excluding land and construction in progress, as well as an adjustment to depreciation expense of $2.1 million which was recorded in the year ended December 31, 2006. This adjustment was related to the reclassification of certain assets from other current assets construction in progress to depreciable property and equipment based on strategic capital decisions which resulted in decisions not to sell these assets. The increase in depreciable property was due to dealership acquisitions and facility projects on existing dealerships.

Depreciation expense increased $4.0 million, or 27.5%, in 2005 compared to 2004. This increase was due primarily to a $21.9 million increase in gross property and equipment related to continuing operations, excluding land and construction in progress. The increase in depreciable property was due to dealership acquisitions and facility projects on existing dealerships.

Interest Expense, Floor Plan

Interest expense, floor plan for new vehicles increased $19.2 million, or 54.2%, in 2006 compared to 2005. The average new vehicle floor plan interest rate related to new vehicles incurred by continuing dealerships was 5.9% for the year ended December 31, 2006, compared to 4.3% for the year ended December 31, 2005, which increased interest expense by approximately $13.4 million. In addition, during 2006 the average floor plan balance for new vehicles increased by $98.8 million, resulting in an increase in expense of approximately $5.8 million. Approximately $27.3 million of the increase in the average floor plan balance for new vehicles was due to additional dealerships we acquired in 2006. The average floor plan balance for new vehicles also increased due to an increase in the average price of vehicles due to general trends in the industry and our continued focus on luxury vehicles.

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Interest expense, floor plan for used vehicles increased expense in 2006 by $4.9 million. The floor plan interest expense associated with used vehicles was the result of borrowings under the 2006 Used Vehicle Floor Plan Sub-Facility (see Note 6 in the accompanying Consolidated Financial Statements). The average balance of the Used Vehicle Floor Plan Sub-Facility was $100.9 million in 2006 and bore an interest rate of between 5.7% and 6.5%. This facility was not in place in 2005.

Interest expense, floor plan for new vehicles increased $13.2 million, or 59.3%, in 2005 compared to 2004. The average floor plan interest rate for new vehicles incurred by continuing dealerships was 4.3% for the year ended December 31, 2005, compared to 2.8% for the year ended December 31, 2004, which increased interest expense by approximately $11.6 million. In addition to this, during 2005 the average floor plan balance for new vehicles increased $38.7 million which resulted in an increase in expense of approximately $1.6 million. Approximately $24.6 million of the increase in the average new vehicle floor plan balance was due to additional dealerships we acquired in 2005.

Our floor plan expenses related to new vehicles are partially offset by amounts received from manufacturers in the form of floor plan assistance. These payments are credited against our cost of sales upon the sale of the vehicle. For franchises classified as continuing operations, the amounts we recognized in our Consolidated Income Statements from floor plan assistance exceeded our floor plan interest expense by approximately $9.5 million in 2004. In 2005 and 2006 our floor plan interest expense exceeded our floor plan assistance by $2.0 million and $22.8 million, respectively.

Interest Expense, Other, Net

See discussion in *Liquidity and Capital Resources* regarding the new credit facility and the changes in related interest rates compared to our previous revolving credit facility.

In order to reduce our exposure to market risks from fluctuations in interest rates, we had two separate interest rate swap agreements (the Fixed Swaps) to effectively convert a portion of our LIBOR-based variable rate debt to a fixed rate. The first swap agreement matured October 31, 2004 and had a notional principal amount of $100.0 million. The second swap agreement matured June 6, 2006 and had a notional principal of $100.0 million. Under the terms of the first swap agreement, we received interest payments on the notional amount at a rate equal to the one month LIBOR rate and made interest payments at a fixed rate of 3.88%. Under the terms of the second swap agreement, we received interest payments on the notional amount at a rate equal to the one month LIBOR rate, and made interest payments at a fixed rate of 4.50%. The incremental expense incurred (the difference between interest paid and interest received as a result of the Fixed Swaps) was $5.4 million and $1.2 million in 2004 and 2005, respectively. A benefit of $0.1 million was realized in 2006. The incremental expenses/benefits of the Fixed Swaps are included in interest expense, other, net in the accompanying Consolidated Statements of Income.

In 2003, we entered into five separate interest rate swaps totaling $150.0 million (collectively, the Old Variable Swaps) to effectively convert a portion of our fixed rate debt to a LIBOR-based variable rate debt. Under the Old Variable Swaps agreements, we received 8.625% on the respective notional amounts and paid interest payments on the respective notional amounts at a rate equal to the six month LIBOR in arrears (as determined on February 15 and August 15 of each year) plus a spread ranging from 3.50% to 3.84% with a weighted average spread of 3.64%. In the second quarter of 2005, we canceled all of the Old Variable Swaps. The Old Variable Swaps had a collective mark-to-market of $0.4 million at cancellation. In connection with this cancellation, we entered into five separate new interest rate swaps with identical terms to the Old Variable Swaps except that we pay a variable rate equal to the fixed six month LIBOR rate which will be fixed on February 15 and August 15 of each year plus a spread ranging from 3.825% to 3.85% (with a weighted average spread of 3.83%) (collectively, the New Variable Swaps). The benefit realized (the difference between interest paid and interest received) as a result of the Old and New Variable Swaps was $4.2 million and $1.5 million in 2004 and 2005, respectively, and $0.4 million of expense in 2006. The incremental expenses/benefits of the Old and New

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Variable swaps are included in interest expense, other, net in the accompanying Consolidated Statements of Income.

These changes and other changes in other interest expense are summarized in the schedule below:

	2005 Increase/(Decrease) in Interest Expense (in millions)	2006 Increase/(Decrease) in Interest Expense (in millions)
Interest rates		
Changes in the average interest rate on the revolving facilities (4.14% in 2004, 5.94% in 2005 and 6.81% in 2006)	$ 6.0	$ 2.2
Rate spread benefit due to repayment of revolving credit facilities with proceeds from 4.25% Convertible Notes issuance	(0.1)	(1.4)
Debt balances		
Increase/(Decrease) in debt balances	(1.3)	(3.6)
Other factors		
Decrease/(increase) in capitalized interest	0.5	(1.3)
Incremental interest savings related to the Fixed Swaps	(4.2)	(1.3)
Incremental interest expense related to the Old and New Variable Swaps	2.6	1.9
Increase in other expense, net	0.4	0.9
	$3.9	$(2.6)

Other Income / Expense, Net

Other income / expense increased approximately $0.6 million in 2006 compared to 2005 due mostly to fees related to the termination of the 2001 Revolving Credit Facility, as amended.

Provision for Income Taxes

The effective tax rate from continuing operations was 40.4% in 2006 and 37.4% in 2005. The effective rate from continuing operations decreased in 2005 to 37.4% from 38.0% in 2004. The effective rate in 2006 was higher than 2005 primarily due to the effect of adjustments in certain tax planning strategies and due to the shift of taxable income to states with higher tax rates in 2006. We expect the effective tax rate in future periods to fall within a range of 37 % to 39 %.

Liquidity and Capital Resources

We require cash to finance acquisitions and fund debt service and working capital requirements. We rely on cash flows from operations, borrowings under our 2006 Credit Facility and offerings of debt and equity securities to meet these requirements.

Because the majority of our consolidated assets are held by our dealership subsidiaries, the majority of our cash flows from operations are generated by these subsidiaries. As a result, our cash flows and ability to service debt depends to a substantial degree on the results of operations of these subsidiaries and their ability to provide us with cash based on their ability to generate cash. Uncertainties in the economic environment as well as uncertainties associated with the ultimate resolution of geopolitical conflicts may therefore affect our overall liquidity.

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A significant portion of our cash flow is used to fund dealership acquisitions. Following is a summary of acquisition activity in recent years:

	(in millions)	
Acquisitions	Subsequent Year Revenues	Cash Portion of Purchase Price (net of cash acquired)
2003	$ 362.7	$ 113.6
2004	589.4	268.7
2005	448.9	138.8
2006 (a)	250.8	110.4

(a) Revenues are estimated

Prior to 2004, we had maintained a long-term debt to total capital ratio of approximately 48% to 52% depending on the timing of our dealership acquisitions. We expect our acquisition activity to approximate 10% to 15% of annual revenues each year and 2007 activity to be weighted toward the latter half of the year. We believe it prudent to maintain our long-term debt to total capital ratio of 35% to 40% over the next few years. At December 31, 2006, our long-term debt to total capital ratio net of cash and cash equivalents was 39.4%. Our long-term debt structure consists of the 2006 Credit Facility due in 2010 and various senior subordinated notes due or redeemable in 2009, 2010, 2013 and 2015. These are discussed in more detail below. We believe the combination of cash flows from operations, floor plan facilities, the availability under our 2006 Credit Facility (approximately $252.1 million was available under the 2006 Revolving Credit Sub-Facility at December 31, 2006) and our ability to raise funds in the public capital markets is sufficient to fund both our working capital needs and the targeted acquisition level discussed above.

Long-Term Debt and Credit Facilities

2006 Credit Facility

On February 17, 2006, we entered into a new four-year syndicated credit facility (the 2006 Credit Facility) with 14 financial institutions, including three manufacturer-affiliated finance companies, providing for up to $1.2 billion in revolving credit and floor plan financing. The 2006 Credit Facility replaces the 2001 Revolving Credit Facility, as amended, (which was terminated February 17, 2006) and a portion of our existing floor plan financing arrangements.

The 2006 Credit Facility has a borrowing limit of $1.2 billion, which may be expanded up to $1.45 billion in total credit availability upon satisfaction of certain conditions. Under the terms of the 2006 Credit Facility, up to $700.0 million is available for new vehicle inventory floor plan financing (the 2006 New Vehicle Floor Plan Sub-Facility), up to $150.0 million is available for used vehicle inventory floor plan financing (the 2006 Used Vehicle Floor Plan Sub-Facility) and up to $350.0 million is available for working capital and general corporate purposes (the 2006 Revolving Credit Sub-Facility). The amount available for borrowing under the 2006 Revolving Credit Sub-Facility is reduced on a dollar-for-dollar basis by the aggregate face amount of any outstanding letters of credit under the 2006 Revolving Credit Sub-Facility. The 2006 Revolving Credit Sub-Facility matures on February 17, 2010. The 2006 New Vehicle Floor Plan Sub-Facility and the 2006 Used Vehicle Floor

Plan Sub-Facility mature on the earlier of February 17, 2010 or upon demand by the administrative agent at the request of more than 80% of the lenders under those facilities.

At December 31, 2006, our 2006 Revolving Credit Sub-Facility had a borrowing limit of $350.0 million, subject to a borrowing base calculated on the basis of our receivables, inventory and equipment and a pledge of certain additional collateral by one of our affiliates (the borrowing base exceeded the borrowing limit at December 31, 2006). The amount available to be borrowed under the Revolving Credit Facility is reduced on a dollar-for-dollar basis by the cumulative face amount of outstanding letters of credit. At December 31, 2006, we had $77.8 million in letters of credit outstanding and $252.1 million of borrowing availability.

The amounts outstanding under the 2006 Revolving Credit Sub-Facility bear interest at a specified percentage above LIBOR according to a performance-based pricing grid determined by our Total Senior Secured Debt to EBITDA Ratio as of the last day of the immediately preceding fiscal quarter. The range of the performance-based pricing grid is from 1.75% above LIBOR to 2.75% above LIBOR. The weighted average rate of the 2006 Revolving Credit Sub-Facility during the year ended December 31, 2006 was 6.81%. In addition, there is a quarterly commitment fee payable by us on the unused portion of the 2006 Revolving Credit Sub-Facility according to a performance-based pricing grid determined by our Total Senior Secured Debt to EBITDA Ratio as of the last day of the immediately preceding fiscal quarter. The range of the performance-based pricing grid for the quarterly commitment fee is 0.20% to 0.45% on the unused portion of the 2006 Revolving Credit Sub-Facility.

The amounts outstanding under the 2006 New Vehicle Floor Plan Sub-Facility bear interest at 1.00% above LIBOR. The amounts outstanding under the 2006 Used Vehicle Floor Plan Sub-Facility bear interest at 1.125% above LIBOR. In addition, there are quarterly commitment fees of 0.20% payable by us on the unused portion of both the 2006 New Vehicle Floor Plan Sub-Facility and the 2006 Used Vehicle Floor Plan Sub-Facility.

Under the terms of collateral documents entered into with the lenders under the 2006 Credit Facility, outstanding balances under the 2006 Credit Facility are secured by a pledge of substantially all of our assets and the assets of substantially all of our domestic subsidiaries, which domestic subsidiaries also guarantee our obligations under the 2006 Credit Facility, and the pledge of certain additional collateral by one of our affiliates. The collateral for the New Credit Facility also includes the pledge of the stock or equity interests of our dealership franchise subsidiaries, except where such a pledge is prohibited by the applicable vehicle manufacturer.

We agreed under the 2006 Credit Facility not to pledge any assets to any third party, subject to certain stated exceptions, including floor plan financing arrangements. In addition, the 2006 Credit Facility contains certain negative covenants, including covenants which could restrict or prohibit the payment of dividends, capital expenditures and material dispositions of assets as well as other customary covenants and default provisions. Specifically, the 2006 Credit Facility permits cash dividends on our Class A and Class B common stock so long as no event of default or unmatured default (as defined in the New Credit Facility) has occurred and is continuing and provided that, after giving effect to the payment of a dividend, we remain in compliance with other terms and conditions of the 2006 Credit Facility.

The 2006 Credit Facility contains events of default, including cross-defaults to other material indebtedness, change of control events and events of default customary for syndicated commercial credit facilities. Upon the occurrence of an event of default, we could be required to immediately repay all outstanding amounts under the 2006 Credit Facility.

On February 17, 2006, in conjunction with the entrance into the 2006 Credit Facility, we and substantially all of our domestic subsidiaries entered into collateral documents with the lenders, pursuant to which we and substantially all of our domestic subsidiaries granted a security interest in substantially all their assets to secure our obligations under the 2006 Credit Facility, including a pledge of the stock or equity interests of our dealership franchise subsidiaries except where such a pledge is prohibited by the applicable vehicle manufacturer. This grant of security interests replaces the grant under the 2001 Revolving Credit Facility, as amended.

2001 Revolving Credit Facility, as Amended

Prior to entering into the 2006 Credit Facility, we utilized the 2001 Revolving Credit Facility, as amended. This facility was with Ford Credit, DaimlerChrysler Financial, Toyota Financial, Bank of America, JP Morgan

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Chase Bank and Merrill Lynch and had a borrowing limit of $550.0 million, subject to a borrowing base calculated on the basis of receivables, inventory and equipment and a pledge of certain additional collateral by one of our affiliates. The amounts outstanding under the Revolving Facility bore interest at 2.55 percentage points above LIBOR. The Revolving Facility included an annual commitment fee equal to 0.25% of the unused portion of the Revolving Facility.

Senior Subordinated 8.625% Notes

In August 2003, we issued $200.0 million in aggregate principal amount of 8.625% Notes. In November 2003, we issued an additional $75.0 million in aggregate principal amount of the 8.625% Notes. This $75.0 million issuance contains the same provisions and terms as the $200.0 million issuance. The 8.625% Notes are unsecured obligations that rank equal in right of payment to all of our existing and future senior subordinated indebtedness, mature on August 15, 2013 and are redeemable at our option after August 15, 2008. The redemption premiums for the twelve-month periods beginning August 15 of the years 2008, 2009 and 2010 are 104.313%, 102.875% and 101.438%, respectively. In addition, up to 35% of the aggregate principal amount of the 8.625% Notes may be redeemed on or before August 15, 2006 with net cash proceeds from certain equity offerings. Our obligations under the 8.625% Notes are guaranteed by our operating domestic subsidiaries.

We have five separate interest rate swaps totaling $150.0 million to effectively convert a portion of our fixed rate debt under the 8.625% Notes to a LIBOR-based variable rate debt. See Note 1 to our Consolidated Financial Statements and Item 7A: *Quantitative and Qualitative Disclosures About Market Risk Interest Rate Risk.* If the Standard & Poor s or Moody s Investor Services rating on our 8.625% Notes drops to B or B2 , respectively, or is withdrawn, the counterparty for $125.0 million of the total interest rate swap notional value of $150.0 million has the option to terminate their interest rate swaps with us. If this counterparty terminates these options, the mark-to-market value of these interest rate swaps must be paid by either us or the counterparty. Further, if the counterparty terminates, it is likely that we will be required to pay the mark-to-market value of these interest rate swaps. Additionally, if such a termination occurs, the fair value of $125.0 million of our 8.625% Notes will no longer be hedged.

Convertible Senior Subordinated Notes

In May 2002, we issued $149.5 million in aggregate principal amount of convertible senior subordinated notes (2002 Convertibles) with net proceeds, before expenses, of approximately $145.1 million. The 2002 Convertibles are unsecured obligations that rank equal in right of payment to all of our existing and future senior subordinated indebtedness, mature on May 7, 2009 and are redeemable at our option after May 7, 2005. The redemption premiums for the twelve-month periods beginning May 7 of the years 2005, 2006, 2007 and 2008 are 103.00%, 102.25%, 101.50% and 100.75%, respectively. Our obligations under the 2002 Convertibles are not guaranteed by any of our subsidiaries. The 2002 Convertibles are convertible into shares of Class A common stock, at the option of the holder, based on certain conditions. See Note 6 to our Consolidated Financial Statements for a discussion regarding these conversion conditions. Also see Off-Balance Sheet Arrangements (subsequent heading also within this Item 7) for a discussion regarding the off-balance sheet aspects of this financing. None of the conversion features on the 2002 Convertibles were triggered in 2006 and none of the 2002 Convertibles were redeemed in 2006.

In November and December 2005, we issued $160.0 million in aggregate principal amount of convertible senior subordinated notes (2005 Convertibles) with net proceeds, before expenses, of approximately $156.2 million. The 2005 Convertibles bear interest at an annual rate of 4.25% until November 30, 2010 and 4.75% thereafter. The net proceeds were used to repay a portion of the amounts outstanding under our 2001 Revolving Credit Facility, as amended, and to pay the net cost of convertible note hedge and warrant transactions. The 2005 Convertibles are unsecured obligations that rank equal in right of payment to all of our existing and future senior subordinated indebtedness, mature on November 30, 2015 and are redeemable on or after October 31, 2010. Our obligations under the 2005 Convertibles are not guaranteed by any of our

subsidiaries. Holders of the 2005 Convertibles may convert them into cash and shares of our Class A common stock based on certain conditions. Upon conversion of the 2005 Convertibles, we will be required to deliver cash equal to the lesser of the aggregate principal amount of the 2005 Convertibles being converted or our total conversion obligation. If our total conversion obligation exceeds the aggregate principal amount of the 2005 Convertibles being converted, we will deliver shares of our Class A common stock to the extent of the excess amount, if any. We used $18.5 million of the net proceeds from the sale of the 2005 Convertibles to pay the net cost of convertible note hedge and warrant transactions. See Note 6 to our Consolidated Financial Statements for a discussion regarding these conversion conditions. Also see Off-Balance Sheet Arrangements (subsequent heading also within this Item 7) for a discussion regarding the off-balance sheet aspects of this financing and the convertible note hedge and warrant transactions. None of the conversion features on the 2005 Convertibles were triggered in 2006.

Notes Payable to a Finance Company

Three notes payable totaling $26.6 million in aggregate principal were assumed with the purchase of certain dealerships during the second quarter of 2004 (the Assumed Notes). The Assumed Notes bear interest rates from 9.52% to 10.52% (with a weighted average of 10.19%), have a combined monthly principal and interest payment of $0.3 million, mature November 1, 2015 through September 1, 2016 and are collateralized by letters of credit. We recorded the Assumed Notes at fair value using an interest rate of 5.35%. The interest rate used to calculate the fair value was based on a quoted market price for notes with similar terms as of the date of assumption. As a result of calculating the fair value, a premium of $7.3 million was recorded that will be amortized over the lives of the Assumed Notes. Although the Assumed Notes allow for prepayment, the penalties and fees are disproportionately burdensome relative to the Assumed Notes principal balance. Therefore, we do not currently intend to prepay the Assumed Notes.

The Mortgage Facility

We had approximately $100 million of borrowing availability related to a revolving real estate and construction (the Construction Loan) and mortgage refinancing (the Permanent Loan) line of credit with Toyota Credit (collectively, the Mortgage Facility). Subsequent to December 31, 2006, this line of credit was terminated. There were no borrowings outstanding during the years ended December 31, 2005 and 2006.

Floor Plan Facilities

We finance all of our new and certain of our used vehicle inventory through standardized floor plan facilities. These floor plan facilities bear interest at variable rates based on prime and LIBOR. The weighted average interest rate for our floor plan facilities was 4.4% for 2005 and 6.0% for 2006. Our floor plan interest expense is partially offset by amounts received from manufacturers, in the form of floor plan assistance. Floor plan assistance received is capitalized in inventory and charged against cost of sales when the associated inventory is sold. In 2006, we recognized approximately $42.2 million in manufacturer assistance, which resulted in an effective borrowing rate under the floor plan facilities of approximately 2.3%. Interest payments under each of our floor plan facilities are due monthly and we are generally not required to make principal repayments prior to the sale of the vehicles.

Prior to February 17, 2006, we engaged in financing our new vehicle inventory with DaimlerChrysler Financial Company, LLC (DaimlerChrysler Financial), Ford Motor Credit Company (Ford Credit), General Motors Acceptance Corporation (GMAC), Toyota Financial Services (Toyota Financial), Bank of America and JP Morgan Chase Bank. On February 17, 2006 and shortly thereafter, we also entered into or renewed separate floor plan credit arrangements with DaimlerChrysler Services North America LLC, Ford Motor Credit Company, General Motors Acceptance Corporation and BMW Financial Services NA, LLC. These separate floor plan credit facilities provide a total of approximately $617.0 million of availability to finance new vehicle inventory purchased from the respective manufacturer affiliates of these captive finance companies and

$150.0 million of availability to finance used vehicle inventory. Each of these separate floor plan facilities bear interest at variable rates based on prime and LIBOR. Our obligation under each of these separate floor plan facilities are secured, or will be secured, by liens on all of the new vehicle inventory financed under the respective floor plan credit facility, as well as the proceeds from the sale of such vehicles, and certain other collateral.

Covenants and Default Provisions

Noncompliance with covenants, including a failure to make any payment when due, under our 2006 Credit Facility, floor plan facilities, 8.625% Notes, 2002 Convertibles and 2005 Convertibles (collectively, our Material Debt Agreements) could result in a default and an acceleration of our repayment obligation under our 2006 Credit Facility. A default under our New Credit Facility would constitute a default under our floor plan facilities and could entitle these lenders to accelerate our repayment obligations under the one or more of the floor plan facilities. A default under our 2006 Credit Facility and one or more floor plan facilities would not result in a default under our 8.625% Notes, 2002 Convertibles or 2005 Convertibles unless our repayment obligations under the 2006 Credit Facility, Mortgage Facility and/or one or more of the floor plan facilities were accelerated. An acceleration of our repayment obligation under any of our Material Debt Agreements could result in an acceleration of our repayment obligations under our other Material Debt Agreements. We expect to be in compliance with the covenants for all of our long-term debt agreements for the foreseeable future. We were in compliance with all of the restrictive and financial covenants on all of our floor plan and long-term debt facilities required to be submitted as of and for the period ended December 31, 2006. The 2006 Credit Facility includes the following financial covenants:

Covenant	**Required**	
Consolidated liquidity ratio	≥	1.15
Consolidated fixed charge coverage ratio	≥	1.20
Consolidated total senior secured debt to EBITDA ratio	≤	2.25

Acquisitions and Dispositions

During 2006, we acquired eight franchises for a combined purchase price of $110.4 million in cash. The cash utilized for these acquisitions was financed by cash generated from our existing operations and by borrowings under our revolving credit facilities. During 2006, we disposed of 12 franchises. These disposals generated cash of $51.0 million.

In January 2007, we purchased two franchises for $16.5 million in cash.

Sale-Leaseback Transactions

In an effort to generate additional cash flow, we periodically seek to minimize the ownership of real property. As a result, facilities either constructed by us or obtained in acquisitions are sold to third parties in sale-leaseback transactions. The resulting leases generally have initial terms of 10-20 years and include a series of five-year renewal options. We have no continuing obligations under these arrangements other than lease payments. In 2006, we sold $26.6 million in dealership property and equipment in sale-leaseback transactions. There were no material gains or losses on these sales.

Capital Expenditures

Our capital expenditures include the construction of new dealerships and collision repair centers, building improvements and equipment purchased for use in our dealerships. Capital expenditures in 2006 were approximately $99.8 million, of which approximately $66.0 million related to the construction of new dealerships and collision repair centers and real estate acquired in connection with such construction. Once completed, these new dealerships and collision repair centers are either held or sold in sale-leaseback transactions. New dealership and collision repair center capital expenditures incurred during 2006 expected to be sold within a year or sold in 2006 in sale-leaseback transactions were $40.5 million. We do not expect any significant gains or losses from these sales. As of December 31, 2006, commitments for facilities construction projects totaled approximately $13.4 million. We expect $7.8 million of this amount to be financed through future sale-leaseback transactions.

Stock Repurchase Program

Our Board of Directors has authorized us to expend up to $185.0 million to repurchase shares of our Class A common stock or redeem securities convertible into Class A common stock. In 2006, we repurchased 584,000 shares for approximately $15.1 million which was offset by proceeds received from the exercise of stock options under stock compensation plans of $19.2 million. As of December 31, 2006 we had $12.2 million remaining under our Board authorization.

Dividends

Our Board of Directors approved four quarterly cash dividends totaling $0.48 per share during 2006. On February 27, 2007, our Board of Directors approved a dividend of $.12 per share for shareholders of record on March 15, 2007 that will be paid on April 15, 2007. We intend to pay dividends in the future based on available cash flows, covenant compliance and other factors. See Note 6 to our Consolidated Financial Statements for a description of restrictions on the payment of dividends.

Cash Flows

Since the majority of our inventories are financed through floor plan notes payable and a significant portion of our receivables represent contracts in transit which are typically funded within ten days of the sale of the vehicle, we are not required to make significant investments in working capital that would negatively impact our operating cash flows.

In 2006, cash flows used by operations were $61.9 million. Cash used in investing activities in 2006 was $118.0 million, the majority of which was related to dealership acquisitions and capital expenditures on construction in progress projects offset by proceeds received from dealership dispositions and the sales of property and equipment. Net cash provided by financing activities was $185.0 million, comprised mostly of the increase of floor plan notes payable non-trade offset by net payments on our revolving credit facilities.

During the third quarter of 2006, we generated cash of approximately $26.8 million from the sale of a portion of Cornerstone s notes receivable to a third party. This inflow of cash is included in cash flows from operating activities, change in receivables, in the accompanying consolidated statements of cash flows for the year ended December 31, 2006. This transaction resulted in no material gains or losses. The proceeds from the sale were used to pay down our 2006 Credit Facility. Cornerstone s outstanding notes receivable at December 31, 2006 were $28.5 million, net of an allowance for credit losses of $4.9 million. We are currently evaluating strategic alternatives for our wholly owned finance subsidiary, Cornerstone Acceptance Corporation (Cornerstone), which include selling all or a portion of Cornerstone s outstanding notes receivable. We anticipate that proceeds from either type of sale will be used to reduce our leverage.

Our Consolidated Statement of Cash Flows includes both continuing and discontinued operations. Net cash used in operating activities associated with discontinued operations was approximately $61.4 million and was substantially comprised of an adjustment for depreciation, gains on the disposal of franchises and property and equipment and changes in assets and liabilities that relate to dealership operations. In our Consolidated Statement of Cash Flows, cash flows from investing activities includes the line item Proceeds from sale of franchises which is entirely related to discontinued operations. With the exception of Proceeds from sale of franchises in the amount of $51.0 million and Net payments on notes payable floor plan non-trade in the amount of $2.2 million, cash flows from investing and financing activities contain an immaterial amount of cash flows from

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discontinued operations. Since discontinued operations typically contain unprofitable franchises, the absence of these cash flows would generally increase consolidated cash flows from operations.

Guarantees and Indemnifications

In connection with the operation and disposition of dealership franchises, we have entered into various guarantees and indemnifications. See Note 11 to our Consolidated Financial Statements for a discussion regarding the guarantees and indemnifications. Also see Off-Balance Sheet Arrangements (subsequent heading also within this Item 7) for a discussion regarding the off-balance sheet aspects of these guarantees and indemnifications.

Future Liquidity Outlook

Our future contractual obligations are as follows:

	(Amounts in thousands)						
	2007	**2008**	**2009**	**2010**	**2011**	**Thereafter**	**Total**
Floor Plan Facilities (1)	$ 1,160,749	$	$	$	$	$	$ 1,160,749
Long-Term Debt (2)	2,707	2,842	131,353	179,777	3,051	281,604	601,334
Estimated Interest Payments on Floor Plan Facilities (3)	11,646						11,646
Estimated Interest Payments on Long-Term Debt (4)	42,115	41,771	37,124	33,967	1,445	2,884	159,306
Operating Leases	129,369	121,795	110,798	108,443	111,080	832,624	1,414,109
Construction Contracts	13,399						13,399
Other Purchase Obligations	10,085	5,299	3,515				18,899
Acquisition Purchase Commitments (5)	16,457						16,457
Total	$ 1,386,527	$ 171,707	$ 282,790	$ 322,187	$ 115,576	$ 1,117,112	$ 3,395,899

(1) Floor plan facilities includes amounts classified as liabilities associated with assets held for sale.

(2) Amounts under the 8.625% Notes and the 2002 Convertibles are redeemable at our option (see preceding discussion regarding long-term debt and credit facilities) but have been classified in this schedule according to contractual maturity. The 2005 Convertibles are redeemable at both our option and the option of the holders of the 2005 Convertibles in November 2010 and have, therefore, been classified for maturity in 2010.

(3) Floor plan facilities balances (including amounts classified as liabilities associated with assets held for sale) are correlated with the amount of vehicle inventory and are generally due at the time that a vehicle is sold. Estimated interest payments were calculated using the December 31, 2006 floor plan facilities balance, the weighted average interest rate for the fourth quarter of 2006 of 6.81% and the assumption that floor plan facilities balances at December 31, 2006 would be relieved within sixty days in connection with the sale of the associated vehicle inventory.

(4) Estimated interest payments calculated assuming contractual maturities, no principal payments on the 2006 Revolving Credit Sub-Facility before the contractual maturity and the interest rate in effect at December 31, 2006 (7.32%) for the 2006 Revolving Credit Sub-Facility. Estimated interest payments do include net interest expense from our interest rate swaps. *See Management s Discussion and Analysis of Financial Condition and Results of Operations Results of Operations Interest Expense, Other, Net , and Quantitative and Qualitative Disclosures About Market Risk Interest Rate Risk* , for discussion regarding our interest rate swaps.

(5) Amount represents estimated purchase price of tangible and intangible assets net of floor plan facilities balances.

We believe our best source of liquidity for future growth remains cash flows generated from operations combined with our availability of borrowings under our floor plan facilities (or any replacements thereof), our 2006 Revolving Credit Facility and our ability to raise funds in the public capital markets. Though uncertainties in the economic environment as well as uncertainties associated with geopolitical conflicts may affect our ability to generate cash from operations, we expect to generate more than sufficient cash flow to fund our debt service and working capital requirements and any seasonal operating requirements, including our currently anticipated internal growth for our existing businesses, for the foreseeable future. Once these needs are met, we may use remaining cash flow to support our acquisition strategy or repurchase shares of our Class A common stock or publicly traded debt securities, as market conditions warrant.

Seasonality

Our operations are subject to seasonal variations. The first and fourth quarters generally contribute less revenue and operating profits than the second and third quarters. Weather conditions, the timing of manufacturer incentive programs and model changeovers cause seasonality in, and may adversely affect our profitability and new vehicle demand. Parts and service demand remains more stable throughout the year.

Off-Balance Sheet Arrangements

Guarantees and Indemnifications

In connection with the operation and disposition of dealership franchises, we have entered into various guarantees and indemnifications. We expect the aggregate amount of the obligations we guarantee to increase as we dispose of additional franchises. See Note 11 to our Consolidated Financial Statements for a discussion regarding these guarantees and indemnifications. Past performance under these guarantees and indemnifications and their estimated fair value has been immaterial to our liquidity and capital resources. Although we seek to mitigate our exposure in connection with these matters, these guarantees and indemnifications, including environmental exposures and the financial performance of lease assignees and sublessees, cannot be predicted with certainty. An unfavorable resolution of one or more of these matters could have a material adverse effect on our liquidity and capital resources.

5.25% Convertible Senior Subordinated Notes

The 2002 Convertibles are convertible into shares of our Class A common stock, at the option of the holder, based on certain conditions. See Note 6 to our Consolidated Financial Statements for a discussion regarding these conversion conditions which are primarily linked to the per share price of our Class A common stock and the relationship between the trading values of our Class A Common Stock and the 2002 Convertibles. This type of financing arrangement was selected by us in order to achieve a more favorable interest rate (as opposed to other forms of available financing). The 2002 Convertibles are material to our liquidity and capital resources.

4.25% Convertible Senior Subordinated Notes, Hedge and Warrants

The 2005 Convertibles are convertible at the option of the holder into cash and shares of our Class A common stock, based on certain conditions. See Note 6 to our Consolidated Financial Statements for a discussion regarding these conversion conditions which are primarily linked to the relationship between the trading values of our Class A common stock and the 2005 Convertibles. Since both the holders of the 2005 Convertibles and we can redeem these notes on or after October 31, 2010, we expect that either a conversion or a redemption of these notes will occur in 2010. This type of financing arrangement was selected by us in order to achieve a more favorable interest rate (as opposed to other forms of available financing). The 2005 Convertibles are material to our liquidity and capital resources.

In connection with the issuance of the 2005 Convertibles we entered into convertible hedge and warrant transactions. The convertible note hedge and warrant transactions are designed to increase the effective

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conversion price per share of our Class A common stock from $24.14 to $33.00 and, therefore, mitigate the potential dilution upon conversion of the 2005 Convertibles at the time of conversion. The convertible note hedge and warrant transactions have been recorded at cost within stockholders equity on our Consolidated Financial Statements in accordance with EITF No. 00-19, Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company s Own Stock and EITF No. 01-6, The Meaning of Indexed to a Company s Own Stock . See Note 1 to our Consolidated Financial Statements, Derivative Instruments and Hedging Activities, for a discussion regarding the convertible note hedge and warrant transactions.

Item 7A: ***Quantitative and Qualitative Disclosures About Market Risk.***

Interest Rate Risk

Our variable rate floor plan facilities, revolving credit facility borrowings and other variable rate notes expose us to risks caused by fluctuations in the applicable interest rates. The total outstanding balance of such variable instruments after considering the effect of our interest rate swaps (see below) was approximately $1,181.3 million at December 31, 2006 and approximately $1,174.8 million at December 31, 2005. A change of 100 basis points in the underlying interest rate would have caused a change in interest expense of approximately $14.5 million in 2006 and approximately $14.3 million in 2005. Of the total change in interest expense, approximately $10.9 million in 2006 and approximately $9.0 million in 2005 would have resulted from the floor plan facilities.

In addition to our variable rate debt, approximately 20% of our dealership facilities have monthly lease payments that fluctuate based on LIBOR interest rates. A change in interest rates of 100 basis points would have had an estimated impact on rent expense of approximately $2.9 million in 2006.

In order to reduce our exposure to market risks from fluctuations in interest rates, we had an interest rate swap agreement (the Fixed Swap) to effectively convert a portion of our LIBOR-based variable rate debt to a fixed rate. The Fixed Swap matured June 6, 2006 and had a notional principal of $100.0 million. Under the terms of the Fixed Swap, we received interest payments on the notional amount at a rate equal to the one month LIBOR rate, adjusted monthly, and made interest payments at a fixed rate of 4.50%.

We have five separate interest rate swaps totaling $150.0 million (collectively, the New Variable Swaps) to effectively convert a portion of our fixed rate debt under the 8.625% Notes to a LIBOR-based variable rate debt. Under the New Variable Swaps, we receive 8.625% on the respective notional amounts and pay interest payments on the respective notional amounts at a rate equal to the six month LIBOR which is fixed on February 15 and August 15 of each year plus a spread ranging from 3.825% to 3.85% with a weighted average spread of 3.83%. The New Variable Swaps expire on August 15, 2013.

Future maturities of variable and fixed rate debt, and related interest rate swaps are as follows:

	2007	2008	2009	2010	2011	Thereafter	Total	Fair Value
	(Amounts in thousands, except for interest rates)							
Liabilities								
Long-term Debt:								

Fixed Rate	2,465	2,599	131,353	159,691	3,051	281,604	580,763	649,169
Average Stated Interest Rate	10.19%	10.19%	5.32%	4.33%	10.19%	8.70%	6.75%	
Variable Rate	242	243		20,086			20,571	20,571
Average Stated Interest Rate	8.00%	8.00%		7.32%			4.97%	
Interest Rate Derivatives								
Interest Rate Swaps:								
Fixed to Variable						150,000	150,000	4,710
Average pay rate						3.83% +6 month LIBOR	3.83% + 6 month LIBOR	
Receive rate						8.625%	8.625%	

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Foreign Currency Risk

In common with other automotive retailers, we purchase certain of our new vehicle and parts inventories from foreign manufacturers. Although we purchase our inventories in U.S. Dollars, our business is subject to foreign exchange rate risk which may influence automobile manufacturers ability to provide their products at competitive prices in the United States. To the extent that we cannot recapture this volatility in prices charged to customers or if this volatility negatively impacts consumer demand for our products, this volatility could adversely affect our future operating results.

Item 8. ***Financial Statements and Supplementary Data.***

See Consolidated Financial Statements and Notes that appears on page F-1 herein.

Item 9. ***Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.***

None.

Item 9A. ***Controls and Procedures.***

Controls and Procedures

Our management, under the supervision and with the participation of our principal executive officer and principal financial officer, evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) as of the end of the period covered by this Annual Report on Form 10-K. Based on this evaluation, our principal executive officer and principal financial officer have concluded that the design and operation of our disclosure controls and procedures are effective. During our last fiscal quarter, there were no significant changes in our internal control over financial reporting that have materially affected or are reasonably likely to materially affect our internal control over financial reporting.

Report on Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f). Our internal control over financial reporting is a process designed to provide a reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on our evaluation under the framework in *Internal Control Integrated Framework*, our management concluded that our internal control over financial reporting was effective as of December 31, 2006.

During 2006, Sonic acquired six automotive dealerships which were not included in our assessment of the effectiveness of our internal control over financial reporting. As a result, management s conclusion regarding the effectiveness of our internal control over financial reporting does not extend to these dealerships. These dealerships represented approximately 2.2% of Sonic s 2006 revenues from continuing operations and 1.3% of Sonic s 2006 revenues related to discontinued operations. See Note 2 to our accompanying Consolidated Financial Statements for additional information on these 2006 acquisitions.

Our management s assessment of the effectiveness of our internal control over financial reporting as of December 31, 2006 has been attested to by Deloitte and Touche LLP, the independent registered public accounting firm that audited our financial statements included in this Annual Report on Form 10-K, as stated in their report which is included herein.

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of

Sonic Automotive, Inc.

Charlotte, North Carolina

We have audited management s assessment, included in the accompanying Report on Internal Control Over Financial Reporting, that Sonic Automotive, Inc. and subsidiaries (the Company) maintained effective internal control over financial reporting as of December 31, 2006, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. As described in the Report on Internal Control Over Financial Reporting, management excluded from their assessment the internal control over financial reporting at RRR, LLC, RRR II, LLC, Fred Oakley Motors, Lynch Motors, Inc., Piercey South, Inc. and Freemont Motorcars (the 2006 Acquisitions) which were acquired on January 9, 2006, January 9, 2006, March 6, 2006, April 24, 2006, July 11, 2006 and December 21, 2006, respectively, and whose financial statements constitute 0.2 percent and 3.9 percent of net and total assets, respectively, 2.2 percent of revenues, and 1.3 percent of net income of the consolidated financial statement amounts as of and for the year ended December 31, 2006. Accordingly, our audit did not include the internal control over financial reporting at the 2006 Acquisitions. The Company s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management s assessment and an opinion on the effectiveness of the Company s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management s assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinions.

A company s internal control over financial reporting is a process designed by, or under the supervision of, the company s principal executive and principal financial officers, or persons performing similar functions, and effected by the company s board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management s assessment that the Company maintained effective internal control over financial reporting as of December 31, 2006, is fairly stated, in all material respects, based on the criteria

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established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2006, based on the criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements as of and for the year ended December 31, 2006 of the Company and our report dated March 16, 2007 expressed an unqualified opinion on those financial statements and included an explanatory paragraph regarding the adoption of the provisions of Statement of Financial Accounting Standards No. 123(R), *Share-Based Payment*, and application of the provisions of Securities and Exchange Commission Staff Accounting Bulletin No. 108, *Considering the Effects of Prior Year Misstatements When Quantifying Misstatements in Current Year Financial Statements.*

/s/ Deloitte & Touche LLP

Charlotte, North Carolina

March 16, 2007

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Item 9B. ***Other Information.***

None.

PART III

Item 10. ***Directors, Executive Officers and Corporate Governance.***

Information required by this item is furnished by incorporation by reference to the information under the captions entitled Election of Directors , Section 16(a) Beneficial Ownership Reporting Compliance, and Additional Corporate Governance and Other Information Corporate Governance Guidelines, Code of Business Conduct and Ethics and Committee Charters in the Proxy Statement (to be filed hereafter) for our Annual Meeting of the Stockholders to be held on April 19, 2007 (the Proxy Statement). The information required by this item with respect to our executive officers appears in Part I of this Annual Report on Form 10-K under the caption Executive Officers of the Registrant.

Item 11. ***Executive Compensation.***

The information required by this item is furnished by incorporation by reference to the information under the captions entitled Executive Compensation and Director Compensation for 2006 in the Proxy Statement.

Item 12. ***Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters***

The information required by this item is furnished by incorporation by reference to the information under the captions General Ownership of Voting Stock and Equity Compensation Plan Information in the Proxy Statement.

Item 13. ***Certain Relationships and Related Transactions and Director Independence***

The information required by this item is furnished by incorporation by reference to all information under the captions Certain Transactions and Election of Directors Board and Committee Member Independence in the Proxy Statement.

Item 14. ***Principal Accountant Fees and Services.***

The information required by this item is furnished by incorporation by reference to the information under the caption Selection of Independent Registered Public Accounting Firm in the Proxy Statement.

PART IV

Item 15. ***Exhibits and Financial Statement Schedules.***

The exhibits and other documents filed as a part of this Annual Report on Form 10-K, including those exhibits that are incorporated by reference herein, are:

(a) (1) Financial Statements: Consolidated Balance Sheets as of December 31, 2005 and 2006. Consolidated Statements of Income for the Years Ended December 31, 2004, 2005 and 2006. Consolidated Statements of Stockholders Equity for the Years Ended December 31, 2004, 2005 and 2006. Consolidated Statements of Cash Flows for the Years Ended December 31, 2004, 2005 and 2006.

(2) Financial Statement Schedules: No financial statement schedules are required to be filed (no respective financial statement captions) as part of this Annual Report on Form 10-K.

(3) Exhibits: Exhibits required in connection with this Annual Report on Form 10-K are listed below. Certain of such exhibits, indicated by an asterisk, are hereby incorporated by reference to other documents on file with the SEC with which they are physically filed, to be a part hereof as of their respective dates.

EXHIBIT NO.	DESCRIPTION
1.1*	Purchase Agreement dated November 18, 2005 among Sonic, Bank of America Securities LLC, J.P. Morgan Securities, Inc. and Merrill Lynch, Pierce, Fenner & Smith Incorporated (incorporated by reference to Exhibit 1.1 to Sonic s Current Report on Form 8-K filed November 23, 2005) (the November 2005 Form 8-K)).
3.1*	Amended and Restated Certificate of Incorporation of Sonic (incorporated by reference to Exhibit 3.1 to Sonic s Registration Statement on Form S-1 (Reg. No. 333-33295) (the Form S-1)).
3.2*	Certificate of Amendment to Sonic s Amended and Restated Certificate of Incorporation effective June 18, 1999 (incorporated by reference to Exhibit 3.2 to Sonic s Annual Report on Form 10-K for the year ended December 31, 1999 (the 1999 Form 10-K)).
3.3*	Certificate of Designation, Preferences and Rights of Class A Convertible Preferred Stock (incorporated by reference to Exhibit 4.1 to Sonic s Quarterly Report on Form 10-Q for the quarter ended March 31, 1998).
3.4*	Amended and Restated Bylaws of Sonic (as amended February 9, 2006) (incorporated by reference to Exhibit 3.1 to Sonic s Current Report on Form 8-K filed February 13, 2006)).
4.1*	Specimen Certificate representing Class A Common Stock (incorporated by reference to Exhibit 4.1 to the Form S-1)
4.2*	Registration Rights Agreement dated as of June 30, 1997 among Sonic, O. Bruton Smith, Bryan Scott Smith, William S. Egan and Sonic Financial Corporation (incorporated by reference to Exhibit 4.2 to the Form S-1).
4.3*	Form of 5.25% Convertible Senior Subordinated Note due 2009 (incorporated by reference to Exhibit 4.2 to Sonic s Amended Current Report on Form 8-K/A filed on May 6, 2002 (the May 2002 Form 8-K/A)).
4.4*	Supplemental Indenture by and among Sonic and U.S. Bank National Association (incorporated by reference to Exhibit 4.1 to the May 2002 Form 8-K/A).
4.5*	Form of 8 5/8% Senior Subordinated Note due 2013, Series B (incorporated by reference to Exhibit 4.3 to Sonic s Registration Statement on Form S-4 (Reg. Nos. 333-109426 and 333-109426-1 through 109426-261) (the 2003 Exchange Offer Form S-4)).
4.6*	Indenture dated as of August 12, 2003 among Sonic Automotive, Inc., as issuer, the subsidiaries of Sonic named therein, as guarantors, and U.S. Bank National Association, as trustee (the Trustee), relating to the 8 5/8% Senior Subordinated Notes due 2013 (incorporated by reference to Exhibit 4.4 to the 2003 Exchange Offer Form S-4).
4.7*	Form of 4.25% Convertible Senior Subordinated Note due 2015 (incorporated by reference to Exhibit 4.2 to the November 2005 Form 8-K).
4.8*	Subordinated Indenture, dated as of May 7, 2002, among Sonic, the guarantors named there in and U.S. Bank National Association, as trustee (incorporated by reference to Exhibit 4.1 to Sonic s Current Report on Form 8-K filed November 21, 2005).

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EXHIBIT NO.	DESCRIPTION
4.9*	Second Supplemental Indenture dated as of November 23, 2005, between Sonic and U.S. Bank National Association (incorporated by reference to Exhibit 4.1 to the November 2005 Form 8-K).
10.1*	Sonic Automotive, Inc. 2004 Stock Incentive Plan (incorporated by reference to Exhibit 10.1 to Sonic s Quarterly Report on Form 10-Q for the quarter ended June 30, 2004). (1)
10.2*	Sonic Automotive, Inc. 1997 Stock Option Plan, Amended and Restated as of April 22, 2003 (incorporated by reference to Exhibit 10.10 to Sonic s Quarterly Report on Form 10-Q for the quarter ended March 31, 2003). (1)
10.3*	Sonic Automotive, Inc. Employee Stock Purchase Plan, Amended and Restated as of May 8, 2002 (incorporated by reference to Exhibit 10.15 to the 2002 Annual Report). (1)
10.4*	Sonic Automotive, Inc. Nonqualified Employee Stock Purchase Plan, Amended and Restated as of October 23, 2002 (incorporated by reference to Exhibit 10.16 to the 2002 Annual Report). (1)
10.5*	FirstAmerica Automotive, Inc. 1997 Stock Option Plan, Amended and Restated as of December 10, 1999 (incorporated by reference to Exhibit 4.1 to Sonic s Registration Statement on Form S-8 (Reg. No. 333-95791)). (1)
10.6*	Employment Agreement dated November 4, 2004 between Sonic and Jeffrey C. Rachor (incorporated by reference to Exhibit 10.24 to the 2004 Annual Report). (1)
10.7*	Employment Agreement dated December 27, 2004 between Sonic and Mark J. Iuppenlatz (incorporated by reference to Exhibit 10.26 to the 2004 Annual Report). (1)
10.8*	Sonic Automotive, Inc. 2005 Formula Restricted Stock Plan for Non-Employee Directors (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed April 27, 2005). (1)
10.9*	Purchased call option confirmation, dated November 18, 2005, between Sonic and Bank of America, N.A. (incorporated by reference to Exhibit 10.1 to the November 2005 Form 8-K).
10.10*	Purchased call option confirmation, dated November 18, 2005, between Sonic and JPMorgan Chase Bank, National Association (incorporated by reference to Exhibit 10.2 to the November 2005 Form 8-K).
10.11*	Warrant confirmation, dated November 18, 2005, between Sonic and Bank of America, N.A. (incorporated by reference to Exhibit 10.3 to the November 2005 Form 8-K).
10.12*	Warrant confirmation, dated November 18, 2005, between Sonic and JPMorgan Chase Bank, National Association (incorporated by reference to Exhibit 10.4 to the November 2005 Form 8-K).
10.13*	Employment Agreement dated January 30, 2006 between Sonic and Mr. David P. Cosper (incorporated by reference to Exhibit 10.1 to Sonic s Quarterly Report on Form 10-Q for the quarter ended March 31, 2006 (the March 2006 Form 10-Q)). (1)

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EXHIBIT NO.	DESCRIPTION
10.14*	Credit Agreement, dated as of February 17, 2006 (the Credit Agreement), among Sonic; the subsidiaries of Sonic named therein; Bank of America, N.A., as Administrative Agent, Lender and L/C Issuer; JPMorgan Chase Bank, N.A., as Syndication Agent and Lender, Toyota Motor Credit Corporation, as Documentation Agent and Lender; and BMW Financial Services NA, LLC, Carolina First Bank, Comerica Bank, Fifth Third Bank, General Electric Capital Corporation, KeyBank National Association, Nissan Motor Acceptance Corporation, Sovereign Bank, SunTrust Bank, Wachovia Bank, National Association and World Omni Financial Corp., each as a Lender and, collectively, the Lenders (incorporated by reference to Exhibit 10.2 to the March 2006 Form 10-Q).
10.15*	Promissory Note, dated February 17, 2006, executed by Sonic and the subsidiaries of Sonic named therein in favor of Bank of America, N.A., pursuant to the Credit Agreement (incorporated by reference to Exhibit 10.32 to the March 2006 Form 10-Q).
10.16*	Promissory Note, dated February 17, 2006, executed by Sonic and the subsidiaries of Sonic named therein in favor of JPMorgan Chase Bank, N.A., pursuant to the Credit Agreement (incorporated by reference to Exhibit 10.4 to the March 2006 Form 10-Q).
10.17*	Promissory Note, dated February 17, 2006, executed by Sonic and the subsidiaries of Sonic named therein in favor of Toyota Motor Credit Corporation pursuant to the Credit Agreement (incorporated by reference to Exhibit 10.5 to the March 2006 Form 10-Q).
10.18*	Promissory Note, dated February 17, 2006, executed by Sonic and the subsidiaries of Sonic named therein in favor of BMW Financial Services NA, LLC, pursuant to the Credit Agreement (incorporated by reference to Exhibit 10.6 to the March 2006 Form 10-Q).
10.19*	Promissory Note, dated February 17, 2006, executed by Sonic and the subsidiaries of Sonic named therein in favor of Carolina First Bank pursuant to the Credit Agreement (incorporated by reference to Exhibit 10.7 to the March 2006 Form 10-Q).
10.20*	Promissory Note, dated February 17, 2006, executed by Sonic and the subsidiaries of Sonic named therein in favor of Comerica Bank pursuant to the Credit Agreement (incorporated by reference to Exhibit 10.8 to the March 2006 Form 10-Q).
10.21*	Promissory Note, dated February 17, 2006, executed by Sonic and the subsidiaries of Sonic named therein in favor of Fifth Third Bank pursuant to the Credit Agreement (incorporated by reference to Exhibit 10.9 to the March 2006 Form 10-Q).
10.22*	Promissory Note, dated February 17, 2006, executed by Sonic and the subsidiaries of Sonic named therein in favor of General Electric Capital Corporation pursuant to the Credit Agreement (incorporated by reference to Exhibit 10.10 to the March 2006 Form 10-Q).
10.23*	Promissory Note, dated February 17, 2006, executed by Sonic and the subsidiaries of Sonic named therein in favor of KeyBank National Association pursuant to the Credit Agreement (incorporated by reference to Exhibit 10.11 to the March 2006 Form 10-Q).
10.24*	Promissory Note, dated February 17, 2006, executed by Sonic and the subsidiaries of Sonic named therein in favor of Nissan Motor Acceptance Corporation pursuant to the Credit Agreement (incorporated by reference to Exhibit 10.12 to the March 2006 Form 10-Q).
10.25*	Promissory Note, dated February 17, 2006, executed by Sonic and the subsidiaries of Sonic named therein in favor of Sovereign Bank pursuant to the Credit Agreement (incorporated by reference to Exhibit 10.13 to the March 2006 Form 10-Q).
10.26*	Promissory Note, dated February 17, 2006, executed by Sonic and the subsidiaries of Sonic named therein in favor of SunTrust Bank pursuant to the Credit Agreement (incorporated by reference to Exhibit 10.14 to the March 2006 Form 10-Q).

EXHIBIT NO.	DESCRIPTION
10.27*	Promissory Note, dated February 17, 2006, executed by Sonic and the subsidiaries of Sonic named therein in favor of Wachovia Bank, National Association, pursuant to the Credit Agreement (incorporated by reference to Exhibit 10.15 to the March 2006 Form 10-Q).
10.28*	Promissory Note, dated February 17, 2006, executed by Sonic and the subsidiaries of Sonic named therein in favor of World Omni Financial Corp. pursuant to the Credit Agreement (incorporated by reference to Exhibit 10.16 to the March 2006 Form 10-Q).
10.29*	Security Agreement, dated as of February 17, 2006, by Sonic, the subsidiaries of Sonic named therein and Bank of America, N.A., as Administrative Agent for the Lenders under the Credit Agreement (incorporated by reference to Exhibit 10.17 to the March 2006 Form 10-Q).
10.30*	Company Guaranty Agreement, dated as of February 17, 2006, by Sonic, as Guarantor, to Bank of America, N.A., as Administrative Agent for the Lenders under the Credit Agreement (incorporated by reference to Exhibit 10.18 to the March 2006 Form 10-Q).
10.31*	Subsidiary Guaranty Agreement, dated as of February 17, 2006, by the subsidiaries of Sonic named therein, as Guarantors, to Bank of America, N.A, as Administrative Agent for the Lenders under the Credit Agreement (incorporated by reference to Exhibit 10.19 to the March 2006 Form 10-Q).
10.32*	Securities Pledge Agreement, dated as of February 17, 2006, by Sonic, the subsidiaries of Sonic named therein and Bank of America, N.A., as Administrative Agent for the Lenders under the Credit Agreement (incorporated by reference to Exhibit 10.20 to the March 2006 Form 10-Q).
10.33	Sonic Automotive, Inc. 2004 Stock Incentive Plan Form of Performance-Based Restricted Stock Unit Award Agreement. (1)
10.34	Sonic Automotive, Inc. 2004 Stock Incentive Plan Form of Performance-Based Restricted Stock Award Agreement. (1)
21.1	Subsidiaries of Sonic.
23.1	Consent of Deloitte & Touche LLP.
31.1	Certification of Mr. David P. Cosper pursuant to Rule 13a-14(a).
31.2	Certification of Mr. O. Bruton Smith pursuant to Rule 13a-14(a).
32.1	Certification of Mr. David P. Cosper pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Mr. O. Bruton Smith pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

* Filed Previously

(1) Indicates a management contract or compensatory plan or arrangement.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

SONIC AUTOMOTIVE, INC.

BY /s/ DAVID P. COSPER

Mr. David P. Cosper
Chief Financial Officer

Date: March 16, 2007

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date
/s/ O. BRUTON SMITH **O. Bruton Smith**	Chairman, Chief Executive Officer (principal executive officer) and Director	March 16, 2007
/s/ B. SCOTT SMITH **B. Scott Smith**	President, Chief Strategic Officer and Director	March 16, 2007
/s/ DAVID P. COSPER **David P. Cosper**	Vice Chairman and Chief Financial Officer (principal financial officer and principal accounting officer)	March 16, 2007
/s/ WILLIAM R. BROOKS **William R. Brooks**	Director	March 16, 2007
/s/ WILLIAM P. BENTON **William P. Benton**	Director	March 16, 2007
/s/ WILLIAM I. BELK **William I. Belk**	Director	March 16, 2007
/s/ H. ROBERT HELLER **H. Robert Heller**	Director	March 16, 2007

/s/ Jeffrey C. Rachor **Jeffrey C. Rachor**	Director	March 16, 2007
/s/ Robert L. Rewey **Robert L. Rewey**	Director	March 16, 2007
/s/ Victor H. Doolan **Victor H. Doolan**	Director	March 16, 2007

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of

Sonic Automotive, Inc.

Charlotte, North Carolina

We have audited the accompanying consolidated balance sheets of Sonic Automotive, Inc. and subsidiaries (the Company) as of December 31, 2005 and 2006, and the related consolidated statements of income, stockholders equity, and cash flows for each of the three years in the period ended December 31, 2006. These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on the financial statements based on our audits.

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

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2005 and 2006, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2006, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 10 to the consolidated financial statements, the Company changed its method of accounting for compensation expense for share-based awards to conform to Statement of Financial Accounting Standards No. 123(R), *Share-Based Payment*. Also, as discussed in Note 1 to the consolidated financial statements, the Company applied the provisions of Securities and Exchange Commission Staff Accounting Bulletin No. 108, *Considering the Effects of Prior Year Misstatements When Quantifying Misstatements in Current Year Financial Statements*.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the Company s internal control over financial reporting as of December 31, 2006, based on the criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 16, 2007 expressed an unqualified opinion on management s assessment of the effectiveness of the Company s internal control over financial reporting and an unqualified opinion on the effectiveness of the Company s internal control over financial reporting.

/s/ DELOITTE & TOUCHE LLP

Charlotte, North Carolina

March 16, 2007

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SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

December 31, 2005 and 2006

(Dollars in thousands)

	December 31,	
	2005	**2006**
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 7,566	$ 12,696
Receivables, net	396,225	385,849
Inventories	1,016,457	991,984
Assets held for sale	73,837	160,571
Construction in progress expected to be sold in sale-leaseback transactions	95,131	26,198
Other current assets	27,484	35,834
Total current assets	1,616,700	1,613,132
Property and Equipment, net	148,267	220,551
Goodwill, net	1,122,538	1,155,428
Other Intangible Assets, net	88,696	94,136
Other Assets	49,300	41,517
Total Assets	$ 3,025,501	$ 3,124,764
LIABILITIES AND STOCKHOLDERS EQUITY		
Current Liabilities:		
Notes payable floor plan trade	$ 579,022	$ 377,943
Notes payable floor plan non-trade	410,296	686,515
Trade accounts payable	91,101	68,016
Accrued interest	17,378	19,336
Other accrued liabilities	167,060	180,884
Liabilities associated with assets held for sale trade	45,953	54,229
Liabilities associated with assets held for sale non-trade	6,937	42,063
Current maturities of long-term debt	2,747	2,707
Total current liabilities	1,320,494	1,431,693
Long-Term Debt	712,311	598,627
Other Long-Term Liabilities	29,479	39,570
Deferred Income Taxes	132,419	151,034
Commitments and Contingencies		
Stockholders Equity:		
Class A convertible preferred stock, none issued		
Class A common stock, $.01 par value; 100,000,000 shares authorized; 40,561,149 shares issued and 29,945,785 shares outstanding at December 31, 2005; 41,890,540 shares issued and 30,691,576 shares	403	416

outstanding at December 31, 2006		
Class B common stock; $.01 par value; 30,000,000 shares authorized; 12,029,375 shares issued and outstanding at December 31, 2005 and December 31, 2006	121	121
Paid-in capital	433,654	464,011
Retained earnings	542,374	598,293
Accumulated other comprehensive income	20	
Deferred compensation related to restricted stock	(1,829)	
Treasury stock, at cost (10,615,364 Class A shares held at December 31, 2005 and 11,198,964 Class A shares held at December 31, 2006)	(143,945)	(159,001)
Total stockholders equity	830,798	903,840
Total Liabilities and Stockholders Equity	$ 3,025,501	$ 3,124,764

See notes to consolidated financial statements.

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SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

Years Ended December 31, 2004, 2005 and 2006

(Dollars and shares in thousands, except per share amounts)

	Year Ended December 31,		
	2004	2005	2006
Revenues:			
New vehicles	$ 3,972,790	$ 4,483,920	$ 4,897,284
Used vehicles	1,013,817	1,126,651	1,275,020
Wholesale vehicles	438,848	498,589	493,512
Total vehicles	5,425,455	6,109,160	6,665,816
Parts, service and collision repair	879,176	988,432	1,114,870
Finance, insurance and other	165,419	181,128	191,388
Total revenues	6,470,050	7,278,720	7,972,074
Cost of sales	5,477,796	6,161,675	6,740,492
Gross profit	992,254	1,117,045	1,231,582
Selling, general and administrative expenses	772,042	850,450	939,825
Depreciation and amortization	14,429	18,390	23,409
Operating income	205,783	248,205	268,348
Other income / (expense):			
Interest expense, floor plan	(22,286)	(35,493)	(59,609)
Interest expense, other, net	(41,456)	(45,368)	(42,785)
Other income / (expense), net	44	45	(597)
Total other expense	(63,698)	(80,816)	(102,991)
Income from continuing operations before taxes	142,085	167,389	165,357
Provision for income taxes	53,940	62,545	66,791
Income from continuing operations	88,145	104,844	98,566
Discontinued operations:			
Loss from operations and the sale of discontinued franchises	(2,271)	(16,647)	(26,090)
Income tax benefit	197	3,664	8,641
Loss from discontinued operations	(2,074)	(12,983)	(17,449)
Net income	$ 86,071	$ 91,861	$ 81,117

Basic earnings (loss) per share:			
Earnings per share from continuing operations	$ 2.13	$ 2.51	$ 2.33
Loss per share from discontinued operations	(0.05)	(0.31)	(0.41)
Earnings per share	$ 2.08	$ 2.20	$ 1.92
Weighted average common shares outstanding	41,375	41,817	42,336
Diluted earnings (loss) per share:			
Earnings per share from continuing operations	$ 2.04	$ 2.40	$ 2.22
Loss per share from discontinued operations	(0.04)	(0.28)	(0.37)
Earnings per share	$ 2.00	$ 2.12	$ 1.85
Weighted average common shares outstanding	45,217	45,533	46,265
Dividends declared per common share	$ 0.44	$ 0.48	$ 0.48

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SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY

Years Ended December 31, 2004, 2005 and 2006

(Dollars and shares in thousands)

	Class A Common Stock		Class B Common Stock		Deferred Compensation Related to Restricted Stock	Paid-In Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive (Loss)/Income	Total Stockholders Equity	Comprehensive Income
	Shares	Amount	Shares	Amount							
BALANCE AT DECEMBER 31, 2003	38,589	$ 384	12,029	$ 121	$	$ 416,892	$ 402,799	$ (117,444)	$ (4,419)	$ 698,333	
Shares awarded under stock compensation plans	1,391	13			(3,570)	19,341				15,784	
Purchases of treasury stock								(20,917)		(20,917)	
Income tax benefit associated with stock compensation plans						5,270				5,270	
Fair value of interest rate swap agreements, net of tax expense of $2,040									3,191	3,191	3,191
Restricted stock amortization					162					162	
Net income							86,071			86,071	86,071
Dividends ($0.44 per share)							(18,207)			(18,207)	
BALANCE AT DECEMBER 31, 2004	39,980	$ 397	12,029	$ 121	$ (3,408)	$ 441,503	$ 470,663	$ (138,361)	$ (1,228)	$ 769,687	$ 89,262
Shares awarded under stock compensation plans	631	7			(651)	9,873				9,229	
Stock-based compensation stock options						114				114	
Purchases of treasury stock								(5,584)		(5,584)	
Income tax benefit associated with stock compensation plans						1,504				1,504	
Income tax benefit associated with convertible note hedge						175				175	
Fair value of interest rate swap agreements, net of tax expense of $798									1,248	1,248	1,248
Restricted stock amortization					1,485					1,485	
Restricted stock forfeiture	(50)	(1)			745	(1,055)				(311)	
Purchase of convertible note hedge and warrants, net						(18,460)				(18,460)	
Net income							91,861			91,861	91,861
Dividends ($0.48 per share)							(20,150)			(20,150)	
	40,561	$ 403	12,029	$ 121	$ (1,829)	$ 433,654	$ 542,374	$ (143,945)	$ 20	$ 830,798	$ 93,109

BALANCE AT DECEMBER 31, 2005											
Adoption of SAB 108							(4,607)			(4,607)	
Adoption of SFAS No. 123-R					1,829	(1,829)					
Shares awarded under stock compensation plans	1,329	13				19,226				19,239	
Purchases of treasury stock								(15,056)		(15,056)	
Income tax benefit associated with stock compensation plans						4,396				4,396	
Income tax benefit associated with convertible note hedge						1,762				1,762	
Fair value of interest rate swap agreements, net of tax benefit of $13									(20)	(20)	(20)
Stock-based compensation expense						4,511				4,511	
Restricted stock amortization						2,291				2,291	
Restricted stock forfeiture											
Net income							81,117			81,117	81,117
Dividends ($0.48 per share)							(20,591)			(20,591)	
BALANCE AT DECEMBER 31, 2006	41,890	$ 416	12,029	$ 121	$	$ 464,011	$ 598,293	$ (159,001)	$	$ 903,840	$ 81,097

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SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in thousands)

	Years Ended December 31,		
	2004	**2005**	**2006**
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income	$ 86,071	$ 91,861	$ 81,117
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization of property, plant and equipment	17,131	21,982	23,903
Provision for bad debt expense	7,638	13,078	9,210
Other amortization	281	309	715
Debt issuance cost amortization	526	401	1,054
Debt discount amortization, net of premium amortization	78	77	691
Stock based compensation expense	162	1,288	6,802
Deferred income taxes	15,781	30,731	10,572
Equity interest in earnings of investees	(807)	(819)	(915)
Impairment of franchise agreements	1,075		2,525
Impairment of property and equipment	3,188	1,950	10,988
(Gain)/Loss on disposal of franchises and property and equipment	(4,577)	6	(3,582)
Loss on exit of leased dealerships		649	9,598
Changes in assets and liabilities that relate to operations:			
Receivables	(58,044)	(49,770)	1,472
Inventories	28,055	36,123	(20,049)
Other assets	10	(17,589)	15,079
Notes payable floor plan trade	70,049	(40,535)	(192,803)
Trade accounts payable and other liabilities	92,210	(5,661)	(18,241)
Total adjustments	172,756	(7,780)	(142,981)
Net cash provided by/(used in) operating activities	258,827	84,081	(61,864)
CASH FLOWS FROM INVESTING ACTIVITIES:			
Purchase of businesses, net of cash acquired	(268,666)	(138,760)	(110,371)
Purchases of property and equipment	(105,603)	(81,638)	(99,848)
Proceeds from sales of property and equipment	68,136	26,435	40,698
Proceeds from sale of franchises	54,957	61,572	50,961
Distributions from equity investees		500	600
Net cash used in investing activities	(251,176)	(131,891)	(117,960)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Net borrowings/(repayments) on notes payable floor plan non-trade	(3,214)	32,060	311,344
Borrowings on revolving credit facilities	742,610	671,776	849,758
Repayments on revolving credit facilities	(799,537)	(778,663)	(961,418)
Proceeds from long-term debt	164	156,159	
Debt issuance costs		(640)	(2,776)