

LITHIA MOTORS INC
Form 10-Q
July 31, 2015

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2015

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: **001-14733**

LITHIA MOTORS, INC.

(Exact name of registrant as specified in its charter)

Oregon

(State or other jurisdiction of incorporation

or organization)

93-0572810

(I.R.S. Employer
Identification No.)

150 N. Bartlett Street, Medford, Oregon
(Address of principal executive offices)

97501
(Zip Code)

Registrant's telephone number, including area code: **541-776-6401**

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. Large accelerated filer Accelerated filer Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class A common stock without par value	23,735,715
Class B common stock without par value	2,562,231
(Class)	(Outstanding at July 31, 2015)

LITHIA MOTORS, INC.

FORM 10-Q

INDEX

	Page
<u>PART I - FINANCIAL INFORMATION</u>	
Item 1. Financial Statements	
Consolidated Balance Sheets (Unaudited) – June 30, 2015 and December 31, 2014	2
Consolidated Statements of Operations (Unaudited) – Three and Six Months Ended June 30, 2015 and 2014	3
Consolidated Statements of Comprehensive Income (Unaudited) – Three and Six Months Ended June 30, 2015 and 2014	4
Consolidated Statements of Cash Flows (Unaudited) – Six Months Ended June 30, 2015 and 2014	5
Condensed Notes to Consolidated Financial Statements (Unaudited)	6
Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations	20
Item 3. Quantitative and Qualitative Disclosures About Market Risk	44
Item 4. Controls and Procedures	45
<u>PART II - OTHER INFORMATION</u>	
Item 1A. Risk Factors	45
Item 2. Unregistered Sales of Equity Securities and Use of Proceeds	45
Item 6. Exhibits	46
Signatures	47

LITHIA MOTORS, INC. AND SUBSIDIARIES**Consolidated Balance Sheets****(In thousands)****(Unaudited)**

	June 30, 2015	December 31, 2014
Assets		
Current Assets:		
Cash and cash equivalents	\$23,394	\$29,898
Accounts receivable, net of allowance for doubtful accounts of \$1,866 and \$2,191	287,808	295,379
Inventories, net	1,367,317	1,249,659
Other current assets	32,028	32,010
Assets held for sale	-	8,563
Total Current Assets	1,710,547	1,615,509
Property and equipment, net of accumulated depreciation of \$128,528 and \$117,679	836,889	816,745
Goodwill	199,129	199,375
Franchise value	150,856	150,892
Other non-current assets	107,434	98,411
Total Assets	\$3,004,855	\$2,880,932
Liabilities and Stockholders' Equity		
Current Liabilities:		
Floor plan notes payable	\$45,464	\$41,047
Floor plan notes payable: non-trade	1,169,717	1,137,632
Current maturities of long-term debt	37,963	31,912
Trade payables	78,885	70,853
Accrued liabilities	157,579	153,661
Deferred income taxes	3,494	2,603
Liabilities related to assets held for sale	-	4,892
Total Current Liabilities	1,493,102	1,442,600
Long-term debt, less current maturities	599,402	609,066
Deferred revenue	59,893	54,403
Deferred income taxes	36,077	42,795
Other long-term liabilities	64,079	58,963
Total Liabilities	2,252,553	2,207,827
Stockholders' Equity:		
Preferred stock - no par value; authorized 15,000 shares; none outstanding	-	-
	268,748	276,058

Edgar Filing: LITHIA MOTORS INC - Form 10-Q

Class A common stock - no par value; authorized 100,000 shares; issued and outstanding 23,742 and 23,671		
Class B common stock - no par value; authorized 25,000 shares; issued and outstanding 2,562 and 2,562	319	319
Additional paid-in capital	33,584	29,775
Accumulated other comprehensive loss	(622)	(926)
Retained earnings	450,273	367,879
Total Stockholders' Equity	752,302	673,105
Total Liabilities and Stockholders' Equity	\$3,004,855	\$2,880,932

See accompanying notes to consolidated financial statements.

LITHIA MOTORS, INC. AND SUBSIDIARIES**Consolidated Statements of Operations****(In thousands, except per share amounts)****(Unaudited)**

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Revenues:				
New vehicle	\$1,149,512	\$694,484	\$2,157,328	\$1,274,006
Used vehicle retail	488,801	310,475	951,732	612,368
Used vehicle wholesale	66,796	44,286	129,004	86,979
Finance and insurance	72,463	43,838	137,067	83,469
Service, body and parts	182,695	114,337	356,170	218,954
Fleet and other	36,680	14,382	54,824	24,132
Total revenues	1,996,947	1,221,802	3,786,125	2,299,908
Cost of sales:				
New vehicle	1,080,170	648,490	2,026,212	1,188,988
Used vehicle retail	426,108	266,408	829,597	527,505
Used vehicle wholesale	65,390	42,782	125,437	84,144
Service, body and parts	91,946	58,155	180,982	111,940
Fleet and other	35,684	13,667	52,873	22,970
Total cost of sales	1,699,298	1,029,502	3,215,101	1,935,547
Gross profit	297,649	192,300	571,024	364,361
Asset impairments	6,130	-	10,260	-
Selling, general and administrative	195,610	125,463	387,228	247,292
Depreciation and amortization	10,287	5,825	20,013	11,332
Operating income	85,622	61,012	153,523	105,737
Floor plan interest expense	(4,655)	(3,215)	(9,304)	(6,199)
Other interest expense	(4,972)	(1,869)	(9,800)	(3,843)
Other (expense) income, net	(356)	1,146	(724)	2,083
Income from continuing operations before income taxes	75,639	57,074	133,695	97,778
Income tax provision	(24,416)	(21,904)	(41,819)	(37,914)
Income from continuing operations, net of income tax	51,223	35,170	91,876	59,864
Income from discontinued operations, net of income tax	-	3,139	-	3,179
Net income	\$51,223	\$38,309	\$91,876	\$63,043
Basic income per share from continuing operations	\$1.95	\$1.35	\$3.49	\$2.30
Basic income per share from discontinued operations	-	0.12	-	0.12
Basic net income per share	\$1.95	\$1.47	\$3.49	\$2.42
Shares used in basic per share calculations	26,332	26,119	26,310	26,047

Edgar Filing: LITHIA MOTORS INC - Form 10-Q

Diluted income per share from continuing operations	\$1.93	\$1.34	\$3.47	\$2.27
Diluted income per share from discontinued operations	-	0.11	-	0.12
Diluted net income per share	\$1.93	\$1.45	\$3.47	\$2.39
Shares used in diluted per share calculations	26,496	26,331	26,509	26,326

See accompanying notes to consolidated financial statements.

LITHIA MOTORS, INC. AND SUBSIDIARIES**Consolidated Statements of Comprehensive Income****(In thousands)****(Unaudited)**

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Net income	\$51,223	\$38,309	\$91,876	\$63,043
Other comprehensive income, net of tax:				
Gain on cash flow hedges, net of tax expense of \$94, \$81, \$181, and \$174 respectively	165	130	304	279
Comprehensive income	\$51,388	\$38,439	\$92,180	\$63,322

See accompanying notes to consolidated financial statements.

LITHIA MOTORS, INC. AND SUBSIDIARIES**Consolidated Statements of Cash Flows****(In thousands)****(Unaudited)**

	Six Months Ended June 30,	
	2015	2014
Cash flows from operating activities:		
Net income	\$91,876	\$63,043
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Asset impairments	10,260	-
Depreciation and amortization	20,013	11,332
Stock-based compensation	5,822	3,259
Loss on disposal of other assets	44	62
Gain on disposal of franchise	(5,919)	(5,744)
Deferred income taxes	(1,145)	2,840
Excess tax benefit from share-based payment arrangements	(4,865)	(6,058)
(Increase) decrease (net of acquisitions and dispositions):		
Trade receivables, net	7,570	(20,709)
Inventories	(122,660)	(77,300)
Other assets	(3,815)	(5,951)
Increase (decrease) (net of acquisitions and dispositions):		
Floor plan notes payable	4,417	368
Trade payables	8,854	1,411
Accrued liabilities	7,717	17,594
Other long-term liabilities and deferred revenue	11,161	11,659
Net cash provided by (used in) operating activities	29,330	(4,194)
Cash flows from investing activities:		
Capital expenditures	(48,008)	(35,230)
Proceeds from sales of assets	145	103
Cash paid for other investments	(15,222)	(3,454)
Cash paid for acquisitions, net of cash acquired	(87)	(79,482)
Proceeds from sales of stores	12,966	10,617
Net cash used in investing activities	(50,206)	(107,446)
Cash flows from financing activities:		
Borrowings on floor plan notes payable, net: non-trade	35,685	112,910
Borrowings on lines of credit	557,394	578,000
Repayments on lines of credit	(602,818)	(567,000)
Principal payments on long-term debt, scheduled	(7,324)	(3,693)
Principal payments on long-term debt and capital leases, other	(9,189)	-

Edgar Filing: LITHIA MOTORS INC - Form 10-Q

Proceeds from issuance of long-term debt	59,425	5,392
Proceeds from issuance of common stock	2,589	2,253
Repurchase of common stock	(16,773)	(10,206)
Excess tax benefit from share-based payment arrangements	4,865	6,058
Dividends paid	(9,482)	(7,557)
Net cash provided by financing activities	14,372	116,157
(Decrease) increase in cash and cash equivalents	(6,504)	4,517
Cash and cash equivalents at beginning of period	29,898	23,686
Cash and cash equivalents at end of period	\$23,394	\$28,203
Supplemental disclosure of cash flow information:		
Cash paid during the period for interest	\$22,262	\$10,218
Cash paid during the period for income taxes, net	28,699	23,444
Supplemental schedule of non-cash activities:		
Debt issued in connection with acquisitions	\$-	\$3,161
Floor plan debt paid in connection with store disposals	4,400	3,311

See accompanying notes to consolidated financial statements.

LITHIA MOTORS, INC. AND SUBSIDIARIES

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1. Interim Financial Statements

Basis of Presentation

These condensed Consolidated Financial Statements contain unaudited information as of June 30, 2015 and for the three- and six-month periods ended June 30, 2015 and 2014. The unaudited interim financial statements have been prepared pursuant to the rules and regulations for reporting on Form 10-Q. Accordingly, certain disclosures required by accounting principles generally accepted in the United States of America for annual financial statements are not included herein. In management's opinion, these unaudited financial statements reflect all adjustments (which include only normal recurring adjustments) necessary for a fair presentation of the information when read in conjunction with our 2014 audited Consolidated Financial Statements and the related notes thereto. The financial information as of December 31, 2014 is derived from our Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 2, 2015. The interim condensed Consolidated Financial Statements should be read in conjunction with the Consolidated Financial Statements and the notes thereto included in our 2014 Annual Report on Form 10-K. The results of operations for the interim periods presented are not necessarily indicative of the results to be expected for the full year.

Reclassifications

Certain reclassifications of amounts previously reported have been made to the accompanying consolidated financial statements to maintain consistency and comparability between periods presented.

These reclassifications had no impact on previously reported net income.

Note 2. Accounts Receivable

Accounts receivable consisted of the following (in thousands):

June 30, 2015	December 31, 2014
--------------------------	------------------------------

Edgar Filing: LITHIA MOTORS INC - Form 10-Q

Contracts in transit	\$ 159,225	\$ 162,785
Trade receivables	33,637	37,194
Vehicle receivables	33,763	34,876
Manufacturer receivables	54,281	56,008
Auto loan receivables	31,375	25,424
Other receivables	4,551	4,554
	316,832	320,841
Less: Allowances	(2,993)	(3,130)
Less: Long-term portion of accounts receivable, net	(26,031)	(22,332)
Total accounts receivable, net	\$ 287,808	\$ 295,379

Accounts receivable classifications include the following:

Contracts in transit are receivables from various lenders for the financing of vehicles that we have arranged on behalf of the customer and are typically received within five to ten days of selling a vehicle.

Trade receivables are comprised of amounts due from customers, lenders for the commissions earned on financing and others for commissions earned on service contracts and insurance products.

Vehicle receivables represent receivables for the portion of the vehicle sales price paid directly by the customer.

Manufacturer receivables represent amounts due from manufacturers, including holdbacks, rebates, incentives and warranty claims.

Auto loan receivables include amounts due from customers related to retail sales of vehicles and certain finance and insurance products.

Interest income on auto loan receivables is recognized based on the contractual terms of each loan and is accrued until repayment, charge-off or repossession. Direct costs associated with loan originations are capitalized and expensed as an offset to interest income when recognized on the loans. All other receivables are recorded at invoice and do not bear interest until they are 60 days past due.

The allowance for doubtful accounts is estimated based on our historical write-off experience and is reviewed monthly. Consideration is given to recent delinquency trends and recovery rates. Account balances are charged against the allowance after all appropriate means of collection have been exhausted and the potential for recovery is considered remote. The annual activity for charges and subsequent recoveries is immaterial.

The long-term portion of accounts receivable, net, was included as a component of other non-current assets in the Consolidated Balance Sheets.

Note 3. Inventories

The components of inventories, net, consisted of the following (in thousands):

	June 30, 2015	December 31, 2014
New vehicles	\$1,024,686	\$958,876
Used vehicles	292,270	240,908
Parts and accessories	50,361	49,875
Total inventories	\$1,367,317	\$1,249,659

Note 4. Goodwill and Franchise Value

The changes in the carrying amounts of goodwill are as follows (in thousands):

	Domestic	Import	Luxury	Consolidated
Balance as of December 31, 2013⁽¹⁾	\$ 22,548	\$ 16,797	\$ 10,166	\$ 49,511
Additions through acquisitions	68,463	62,804	18,597	149,864
Balance as of December 31, 2014⁽¹⁾	91,011	79,601	28,763	199,375
Reduction related to divestiture	-	(246)	-	(246)
Balance as of June 30, 2015⁽¹⁾	\$ 91,011	\$ 79,355	\$ 28,763	\$ 199,129

(1) Net of accumulated impairment losses of \$299.3 million recorded during the year ended December 31, 2008.

The changes in the carrying amounts of franchise value are as follows (in thousands):

	Franchise Value
Balance as of December 31, 2013	\$ 71,199
Additions through acquisitions	80,233
Transfers to assets held for sale	(540)
Balance as of December 31, 2014	150,892
Reduction related to divestiture	(36)
Balance as of June 30, 2015	\$ 150,856

Note 5. Stockholders' Equity***Reclassification From Accumulated Other Comprehensive Loss***

The reclassification from accumulated other comprehensive loss was as follows (in thousands):

	Three Months Ended June 30, 2015	2014	Affected Line Item in the Consolidated Statements of Operations
Loss on cash flow hedges	\$(108)	\$(118)	Floor plan interest expense
Taxes	42	45	Income tax provision
Loss on cash flow hedges, net	\$(66)	\$(73)	

	Six Months Ended June 30, 2015	2014	Affected Line Item in the Consolidated Statements of Operations
Loss on cash flow hedges	\$(233)	\$(252)	Floor plan interest expense
Taxes	90	96	Income tax provision
Loss on cash flow hedges, net	\$(143)	\$(156)	

See Note 8 for more details regarding our derivative contracts.

Repurchases of Class A Common Stock

In August 2011, our Board of Directors authorized the repurchase of up to 2,000,000 shares of our Class A common stock and, on July 20, 2012, our Board of Directors authorized the repurchase of 1,000,000 additional shares of our Class A common stock. Through June 30, 2015, we have repurchased 1,598,723 shares under this program at an average price of \$35.56 per share. Of this amount, 98,947 shares were repurchased during the first six months of 2015 at an average price of \$100.29 per share for a total of \$9.9 million. As of June 30, 2015, 1,401,277 shares remained available for repurchase pursuant to this program. The authority to repurchase does not have an expiration date.

In addition, during the first six months of 2015, we repurchased 77,438 shares at an average price of \$88.45 per share, for a total of \$6.9 million, related to tax withholdings associated with the vesting of restricted stock units (“RSUs”). The repurchase of shares related to tax withholdings associated with stock awards does not reduce the number of shares available for repurchase as approved by our Board of Directors.

Dividends

Dividends paid on our Class A and Class B common stock were as follows:

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2015	2014	2015	2014
Dividend amount per share	\$0.20	\$0.16	\$0.36	\$0.29
Total amount of dividend (in thousands)	5,266	4,179	9,482	7,557

See Note 14 for a discussion of a dividend related to our second quarter 2015 financial results.

Note 6. Deferred Compensation and Long-Term Incentive Plan

We offer a deferred compensation and long-term incentive plan (the “LTIP”) to provide certain employees the ability to accumulate assets for retirement on a tax-deferred basis. We may make discretionary contributions to the LTIP. Discretionary contributions vest over one to seven years depending on the employee’s age and position. Additionally, a participant may defer a portion of his or her compensation and receive the deferred amount upon certain events, including termination or retirement. The following is a summary related to our LTIP (dollars in thousands):

	Three Months Ended		Six Months Ended	
	June 30, 2015	2014	June 30, 2015	2014
Compensation expense	\$463	\$377	\$920	\$1,077
Discretionary contribution	\$153	\$-	\$2,249	\$2,100
Guaranteed annual return	5.25%	5.25%	5.25%	5.25%

As of June 30, 2015 and December 31, 2014, the balance due to participants was \$16.0 million and \$14.2 million, respectively, and was included as a component of accrued liabilities and other long-term liabilities in the Consolidated Balance Sheets.

Note 7. Fair Value Measurements

Factors used in determining the fair value of our financial assets and liabilities are summarized into three broad categories:

Level 1 – quoted prices in active markets for identical securities;

Level 2 – other significant observable inputs, including quoted prices for similar securities, interest rates, prepayment spreads, credit risk; and

Level 3 – significant unobservable inputs, including our own assumptions in determining fair value.

The inputs or methodology used for valuing financial assets and liabilities are not necessarily an indication of the risk associated with investing in them.

We use the income approach to determine the fair value of our interest rate swap using observable Level 2 market expectations at each measurement date and an income approach to convert estimated future cash flows to a single present value amount (discounted) assuming that participants are motivated, but not compelled, to transact. Level 2 inputs for the swap valuation are limited to quoted prices for similar assets or liabilities in active markets (specifically

futures contracts on LIBOR for the first two years) and inputs other than quoted prices that are observable for the asset or liability (specifically LIBOR cash and swap rates and credit risk at commonly quoted intervals). Mid-market pricing is used as a practical expedient for fair value measurements. Key inputs, including the cash rates for very short term borrowings, futures rates for up to two years and LIBOR swap rates beyond the derivative maturity, are used to predict future reset rates to discount those future cash flows to present value at the measurement date.

Inputs are collected from Bloomberg on the last market day of the period and used to determine the rate used to discount the future cash flows. The valuation of the interest rate swap also takes into consideration estimates of our own, as well as the counterparty's, risk of non-performance under the contract. See Note 8 for more details regarding our derivative contracts.

We estimate the value of our equity-method investment that is recorded at fair value on a non-recurring basis based on a market valuation approach. We use prices and other relevant information generated primarily by recent market transactions involving similar or comparable assets. Because these valuations contain unobservable inputs, we classified the measurement of fair value of our equity-method investment as Level 3.

We estimate the value of long-lived assets that are recorded at fair value based on a market valuation approach. We use prices and other relevant information generated primarily by recent market transactions involving similar or comparable assets, as well as our historical experience in divestitures, acquisitions and real estate transactions. Additionally, we may use a cost valuation approach to value long-lived assets when a market valuation approach is unavailable. Under this approach, we determine the cost to replace the service capacity of an asset, adjusted for physical and economic obsolescence. When available, we use valuation inputs from independent valuation experts, such as real estate appraisers and brokers, to corroborate our estimates of fair value. Real estate appraisers' and brokers' valuations are typically developed using one or more valuation techniques including market, income and replacement cost approaches. Because these valuations contain unobservable inputs, we classified the measurement of fair value of long-lived assets as Level 3.

There were no changes to our valuation techniques during the six-month period ended June 30, 2015.

Assets and Liabilities Measured at Fair Value

Following are the disclosures related to our assets and (liabilities) that are measured at fair value (in thousands):

Fair Value at June 30, 2015	Level 1	Level 2	Level 3
Measured on a recurring basis:			
Derivative contracts, net	\$ -	\$(1,187)	\$-
Measured on a non-recurring basis:			
Equity-method investment	\$ -	\$-	\$34,009
Long-lived assets held and used: Certain buildings and improvements			3,367
Fair Value at December 31, 2014	Level 1	Level 2	Level 3
Measured on a recurring basis:			
Derivative contracts, net	\$ -	\$(1,750)	\$-
Measured on a non-recurring basis:			
Equity-method investment	\$ -	\$-	\$33,282

See Note 8 for more details regarding our derivative contracts.

Based on operating losses recognized by the equity-method investment, we determined that an impairment of our investment had occurred. Accordingly, we performed a fair value calculation for this investment and determined that a \$4.1 million and an \$8.3 million impairment, respectively, was required to be recorded as asset impairments in our Consolidated Statements of Operations for the three and six months ended June 30, 2015. See Note 11.

Long-lived assets classified as held and used are reviewed for impairment whenever events or circumstances indicate that the carrying amount of the assets may not be recoverable. An estimate of future undiscounted net cash flows associated with the long-lived assets is used to determine if the carrying value of the assets is recoverable. An impairment charge is recorded if the carrying value of the asset is determined to not be recoverable and exceeds its fair value. Due to changes in the expected future use for certain properties, we evaluated the future undiscounted net cash flows for each property. It was determined the carrying value was not recoverable and exceeded the estimated fair value. As a result of this evaluation, we recorded \$2.0 million of impairment charges associated with these properties

in the second quarter of 2015.

Fair Value Disclosures for Financial Assets and Liabilities

We determined the carrying value of cash equivalents, accounts receivable, trade payables, accrued liabilities and short-term borrowings approximate their fair values because of the nature of their terms and current market rates of these instruments. We believe the carrying value of our variable rate debt approximates fair value.

We have fixed rate debt and calculate the estimated fair value of our fixed rate debt using a discounted cash flow methodology. Using estimated current interest rates based on a similar risk profile and duration (Level 2), the fixed cash flows are discounted and summed to compute the fair value of the debt. As of June 30, 2015, this debt had maturity dates between November 2016 and October 2034. A summary of the aggregate carrying values and fair values of our long-term fixed interest rate debt is as follows (in thousands):

	June 30,	December
	2015	31,
		2014
Carrying value	\$253,934	\$257,780
Fair value	260,408	270,781

Note 8. Derivative Financial Instrument

From time to time, we enter into interest rate swaps to fix a portion of our interest expense. We do not enter into derivative instruments for any purpose other than to manage interest rate exposure to fluctuations in the one-month LIBOR benchmark. That is, we do not engage in interest rate speculation using derivative instruments.

As of June 30, 2015, we had a \$25 million interest rate swap outstanding with U.S. Bank Dealer Commercial Services. This interest rate swap matures on June 15, 2016 and has a fixed rate of 5.587% per annum. The variable rate on the interest rate swap is the one-month LIBOR rate. At June 30, 2015, the one-month LIBOR rate was 0.19% per annum, as reported in the Wall Street Journal.

Typically, we designate all interest rate swaps as cash flow hedges and, accordingly, we record the change in fair value for the effective portion of these interest rate swaps in comprehensive income rather than net income until the underlying hedged transaction affects net income. If a swap is no longer designated as a cash flow hedge and the forecasted transaction remains probable or reasonably possible of occurring, the gain or loss recorded in accumulated other comprehensive loss is recognized in income as the forecasted transaction occurs. If the forecasted transaction is probable of not occurring, the gain or loss recorded in accumulated other comprehensive loss is recognized in income immediately. See Note 7.

The estimated amount that we expect to reclassify from accumulated other comprehensive loss to net income within the next twelve months is \$1.0 million at June 30, 2015.

The fair value of our derivative instruments was included in our Consolidated Balance Sheets as follows (in thousands):

Balance Sheet Information Fair Value of Liability Derivatives

Derivatives Designated as	Location in Balance Sheet	June 30, 2015
Hedging Instruments		
Interest Rate Swap Contract	Accrued liabilities	\$1,187
	Other long-term liabilities	-
		\$1,187

Balance Sheet Information Fair Value of Liability Derivatives

Derivatives Designated as	Location in Balance Sheet	December 31, 2014
Hedging Instruments		
Interest Rate Swap Contract	Accrued liabilities	\$ 1,194
	Other long-term liabilities	556
		\$ 1,750

The effect of derivative instruments on our Consolidated Statements of Operations was as follows (in thousands):

	Amount of Gain	Location of Loss	Amount of Loss	Location of Loss	Amount of Loss
Derivatives in Cash	Recognized in Accumulated OCI	Reclassified from Accumulated OCI into Income	Reclassified from Accumulated OCI into Income	Recognized in Income on Derivative	Recognized in Income on Derivative
Flow Hedging Relationships	(Effective Portion)	(Effective Portion)	(Effective Portion)	Ineffective Portion and Amount Excluded from Effectiveness Testing)	(Ineffective Portion and Amount Excluded from Effectiveness Testing)
Three Months Ended June 30, 2015					
Interest Rate Swap Contract	\$ 151	Floor plan interest expense	\$ (108)	Floor plan interest expense	\$ (191)
Three Months Ended June 30, 2014					
Interest Rate Swap Contract	\$ 93	Floor plan interest expense	\$ (118)	Floor plan interest expense	\$ (188)
Six Months Ended June 30, 2015					
Interest Rate Swap Contract	\$ 252	Floor plan interest expense	\$ (233)	Floor plan interest expense	\$ (368)
Six Months Ended June 30, 2014					
Interest Rate Swap Contract	\$ 201	Floor plan interest expense	\$ (252)	Floor plan interest expense	\$ (359)

See also Note 8.

Note 9. Assets Held for Sale and Discontinued Operations

Assets Held for Sale

We classify an asset group as held for sale if we have ceased operations at that location or the store meets the criteria required by U.S. generally accepted accounting standards as follows:

- our management team, possessing the necessary authority, commits to a plan to sell the store;
- the store is available for immediate sale in its present condition;
- an active program to locate buyers and other actions that are required to sell the store are initiated;
- a market for the store exists and we believe its sale is likely within one year;
- active marketing of the store commences at a price that is reasonable in relation to the estimated fair market value;
- and
- our management team believes it is unlikely changes will be made to the plan or the plan to dispose of the store will be withdrawn.

As of December 31, 2014, we had two Import stores classified as held for sale. During the first six months of 2015, we completed the sale of both of these Import stores, and recognized a gain of \$5.9 million as a component of selling, general and administrative on our Consolidated Statements of Operations for the six months ended June 30, 2015.

As of June 30, 2015, we no longer had any stores classified as held for sale. Assets held for sale included the following (in thousands):

	June 30,	December 31,
	2015	2014
Inventories	\$ -	\$ 6,284
Property, plant and equipment	-	1,739
Intangible assets	-	540
	\$ -	\$ 8,563

Liabilities related to assets held for sale included the following (in thousands):

	June 30,	December 31,
	2015	2014
Floor plan notes payable	\$ -	\$ 4,892

Discontinued Operations and the Sales of Stores

In the third quarter of 2014, we early-adopted guidance that redefined discontinued operations. As a result, we determined that individual stores which met the criteria for held for sale after our adoption date would no longer qualify for classification as discontinued operations. We had previously reclassified a store's operations to discontinued operations in our Consolidated Statements of Operations, on a comparable basis for all periods presented, provided we did not expect to have any significant continuing involvement in the store's operations after its disposal.

Certain financial information related to discontinued operations and sales of stores was as follows (in thousands):

	Three Months Ended		Six Months Ended	
	June 30, 2015	2014	June 30, 2015	2014
Revenue	\$-	\$3,920	\$-	\$12,569

Edgar Filing: LITHIA MOTORS INC - Form 10-Q

Pre-tax loss from discontinued operations	\$-	\$(532)	\$-	\$(467)
Net gain on disposal activities	-	5,744	-	5,744
	-	5,212	-	5,277
Income tax expense	-	(2,073)	-	(2,098)
Income from discontinued operations, net of income tax expense	\$-	\$3,139	\$-	\$3,179
Goodwill and other intangible assets disposed of	\$157	\$221	\$246	\$221
Cash generated from disposal activities	9,286	10,617	12,966	10,617
Floor plan debt paid in connection with disposal activities	2,192	3,311	4,400	3,311

Note 10. Net Income Per Share of Class A and Class B Common Stock

We compute net income per share of Class A and Class B common stock using the two-class method. Under this method, basic net income per share is computed using the weighted average number of common shares outstanding during the period excluding unvested common shares subject to repurchase or cancellation. Diluted net income per share is computed using the weighted average number of common shares and, if dilutive, potential common shares outstanding during the period. Potential common shares consist of the incremental common shares issuable upon the exercise of stock options and unvested restricted shares subject to repurchase or cancellation. The dilutive effect of outstanding stock options and other grants is reflected in diluted earnings per share by application of the treasury stock method. The computation of the diluted net income per share of Class A common stock assumes the conversion of Class B common stock, while the diluted net income per share of Class B common stock does not assume the conversion of those shares.

Except with respect to voting and transfer rights, the rights of the holders of our Class A and Class B common stock are identical. Under our Restated Articles of Incorporation, the Class A and Class B common stock must share equally in any dividends, liquidation proceeds or other distribution with respect to our common stock and the Articles of Incorporation can only be amended by a vote of the shareholders. Additionally, Oregon law provides that amendments to our Articles of Incorporation that would adversely alter the rights, powers or preferences of a given class of stock, must be approved by the class of stock adversely affected by the proposed amendment. As a result, the undistributed earnings for each year are allocated based on the contractual participation rights of the Class A and Class B common shares as if the earnings for the year had been distributed. Because the liquidation and dividend rights are identical, the undistributed earnings are allocated on a proportionate basis.

Following is a reconciliation of the income from continuing operations and weighted average shares used for our basic earnings per share (“EPS”) and diluted EPS (in thousands, except per share amounts):

Three Months Ended June 30,	2015		2014	
	Class A	Class B	Class A	Class B
Basic EPS from Continuing Operations				
<i>Numerator:</i>				
Income from continuing operations applicable to common stockholders	\$46,239	\$4,984	\$31,720	\$3,450
Distributed income applicable to common stockholders	(4,754)	(512)	(3,769)	(410)
Basic undistributed income from continuing operations applicable to common stockholders	\$41,485	\$4,472	\$27,951	\$3,040
<i>Denominator:</i>				
Weighted average number of shares outstanding used to calculate basic income per share	23,770	2,562	23,557	2,562
Basic income per share from continuing operations applicable to common stockholders	\$1.95	\$1.95	\$1.35	\$1.35
Basic distributed income per share from continuing operations applicable to common stockholders	(0.20)	(0.20)	(0.16)	(0.16)
Basic undistributed income per share from continuing operations applicable to common stockholders	\$1.75	\$1.75	\$1.19	\$1.19

Three Months Ended June 30,	2015		2014	
Diluted EPS from Continuing Operations	Class A	Class B	Class A	Class B
<i>Numerator:</i>				
Distributed income applicable to common stockholders	\$4,754	\$512	\$3,769	\$410
Reallocation of distributed income as a result of conversion of dilutive stock options	3	(3)	3	(3)
Reallocation of distributed income due to conversion of Class B to Class A common shares outstanding	509	-	407	-
Diluted distributed income applicable to common stockholders	\$5,266	\$509	\$4,179	\$407
Undistributed income from continuing operations applicable to common stockholders	\$41,485	\$4,472	\$27,951	\$3,040
Reallocation of undistributed income as a result of conversion of dilutive stock options	28	(28)	25	(25)
Reallocation of undistributed income due to conversion of Class B to Class A	4,444	-	3,015	-
Diluted undistributed income from continuing operations applicable to common stockholders	\$45,957	\$4,444	\$30,991	\$3,015
<i>Denominator:</i>				
Weighted average number of shares outstanding used to calculate basic income per share from continuing operations	23,770	2,562	23,557	2,562
Weighted average number of shares from stock options	164	-	212	-
Conversion of Class B to Class A common shares outstanding	2,562	-	2,562	-
Weighted average number of shares outstanding used to calculate diluted income per share from continuing operations	26,496	2,562	26,331	2,562
Diluted income per share from continuing operations applicable to common stockholders	\$1.93	\$1.93	\$1.34	\$1.34
Diluted distributed income per share from continuing operations applicable to common stockholders	(0.20)	(0.20)	(0.16)	(0.16)
Diluted undistributed income per share from continuing operations applicable to common stockholders	\$1.73	\$1.73	\$1.18	\$1.18

**Three Months
Ended June
30,**
**Diluted EPS
Antidilutive
Securities**

 Shares issuable
pursuant to
stock options
not included
since they were
antidilutive

2015
Class A

17

Class B

-

2014
Class A

12

Class B

-

Six Months Ended June 30,
Basic EPS from Continuing Operations
Numerator:

Income from continuing operations applicable to common stockholders

Distributed income applicable to common stockholders

 Basic undistributed income from continuing operations applicable to common
stockholders

2015
Class A

\$82,929

(8,559)

\$74,370

**Class
B**

\$8,947

(923)

\$8,024

2014
Class A

\$53,976

(6,814)

\$47,162

**Class
B**

\$5,888

(743)

\$5,145

Denominator:

 Weighted average number of shares outstanding used to calculate basic income
per share

23,748

2,562

23,485

2,562

 Basic income per share from continuing operations applicable to common
stockholders

\$3.49

\$3.49

\$2.30

\$2.30

 Basic distributed income per share from continuing operations applicable to
common stockholders

(0.36)

(0.36)

(0.29)

(0.29)

 Basic undistributed income per share from continuing operations applicable to
common stockholders

\$3.13

\$3.13

\$2.01

\$2.01

Six Months Ended June 30,	2015		2014	
	Class A	Class B	Class A	Class B
Diluted EPS from Continuing Operations				
<i>Numerator:</i>				
Distributed income applicable to common stockholders	\$8,559	\$923	\$6,814	\$743
Reallocation of distributed income as a result of conversion of dilutive stock options	7	(7)	8	(8)
Reallocation of distributed income due to conversion of Class B to Class A common shares outstanding	916	-	735	-
Diluted distributed income applicable to common stockholders	\$9,482	\$916	\$7,557	\$735
Undistributed income from continuing operations applicable to common stockholders	\$74,370	\$8,024	\$47,162	\$5,145
Reallocation of undistributed income as a result of conversion of dilutive stock options	61	(61)	55	(55)
Reallocation of undistributed income due to conversion of Class B to Class A	7,963	-	5,090	-
Diluted undistributed income from continuing operations applicable to common stockholders	\$82,394	\$7,963	\$52,307	\$5,090
<i>Denominator:</i>				
Weighted average number of shares outstanding used to calculate basic income per share from continuing operations	23,748	2,562	23,485	2,562
Weighted average number of shares from stock options	199	-	279	-
Conversion of Class B to Class A common shares outstanding	2,562	-	2,562	-
Weighted average number of shares outstanding used to calculate diluted income per share from continuing operations	26,509	2,562	26,326	2,562
Diluted income per share from continuing operations applicable to common stockholders	\$3.47	\$3.47	\$2.27	\$2.27
Diluted distributed income per share from continuing operations applicable to common stockholders	(0.36)	(0.36)	(0.29)	(0.29)
Diluted undistributed income per share from continuing operations applicable to common stockholders	\$3.11	\$3.11	\$1.98	\$1.98

Six Months Ended June 30,	2015		2014	
	Class A	Class B	Class A	Class B
Diluted EPS Antidilutive Securities				
Shares issuable pursuant to stock options not included since they were antidilutive	16	-	14	-

Note 11. Equity-Method Investment

In October 2014, we acquired a 99.9% membership interest in a limited liability company managed by U.S. Bancorp Community Development Corporation with an initial equity contribution of \$4.1 million. We made additional equity contributions to the entity of \$5.7 million and \$11.4 million, respectively, in the three and six-month periods ended June 30, 2015. We are obligated to make \$49.8 million of contributions to the entity over a two-year period ending October 2016, \$15.5 million of which had been paid as of June 30, 2015.

This investment generates new markets tax credits under the New Markets Tax Credit Program (“NMTC Program”). The NMTC Program was established by Congress in 2000 to spur new or increased investments into operating businesses and real estate projects located in low-income communities.

While U.S. Bancorp Community Development Corporation exercises management control over the limited liability company, due to the economic interest we hold in the entity, we determined our ownership portion of the entity was appropriately accounted for using the equity method.

The following amounts related to this equity-method investment were recorded in our Consolidated Balance Sheets (in thousands):

	June 30,	December 31,
	2015	2014
Carrying value, recorded as a component of other non-current assets	\$34,009	\$ 33,282
Present value of obligation associated with future equity contributions, recorded as a component of accrued liabilities and other long-term liabilities	33,582	32,177

The following amounts related to this equity-method investment were recorded in our Consolidated Statements of Operations (in thousands):

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2015	2014	2015	2014
Asset impairments to write investment down to fair value	\$4,130	\$ -	\$8,260	\$ -
Our portion of the partnership’s operating losses	1,733	-	3,465	-
Non-cash interest expense related to the amortization of the discounted fair value of future equity contributions	183	-	394	-
Tax benefits and credits generated	7,652	-	14,902	-

Note 12. Segments

While we have determined that each individual store is an operating segment, we have aggregated our operating segments into three reportable segments based on their economic similarities: Domestic, Import and Luxury.

Our Domestic segment is comprised of retail automotive franchises that sell new vehicles manufactured by Chrysler, General Motors and Ford. Our Import segment is comprised of retail automotive franchises that sell new vehicles manufactured primarily by Honda, Toyota, Subaru, Nissan and Volkswagen. Our Luxury segment is comprised of retail automotive franchises that sell new vehicles manufactured primarily by BMW, Mercedes-Benz and Lexus. The franchises in each segment also sell used vehicles, parts and automotive services, and automotive finance and insurance products.

Corporate and other is comprised of our stand-alone collision center; unallocated corporate overhead expenses, such as corporate personnel costs, certain interest expense and depreciation expense, and retrospective commissions for certain finance and insurance transactions that we arrange under agreements with third parties.

We define our chief operating decision maker (“CODM”) to be certain members of our executive management group. Historical and forecasted operational performance is evaluated on a store-by-store basis and on a consolidated basis by the CODM. We derive the operating results of the segments directly from our internal management reporting system. The accounting policies used to derive segment results are substantially the same as those used to determine our consolidated results. Management measures the performance of each operating segment based on several metrics, including earnings from operations. Management uses these results, in part, to evaluate the performance of, and to allocate resources to, each of the operating segments.

Certain financial information on a segment basis is as follows (in thousands):

	Three Months Ended		Six Months Ended	
	June 30, 2015	2014	June 30, 2015	2014
Revenues:				
Domestic	\$768,989	\$641,378	\$1,460,393	\$1,210,308
Import	853,444	394,924	1,612,082	745,985
Luxury	372,369	185,826	709,290	344,437
	1,994,802	1,222,128	3,781,765	2,300,730
Corporate and other	2,145	(326)	4,360	(822)
	\$1,996,947	\$1,221,802	\$3,786,125	\$2,299,908
Segment income*:				
Domestic	\$31,045	\$25,288	\$58,174	\$47,710
Import	25,904	14,768	42,005	24,033
Luxury	9,515	5,832	15,414	8,017
	66,464	45,888	115,593	79,760
Corporate and other	9,175	11,186	18,102	18,018
Income from continuing operations before income taxes	\$75,639	\$57,074	\$133,695	\$97,778

*Segment income is defined as operating income less floor plan interest expense.

Floor plan interest expense:

Domestic	\$4,932	\$4,404	\$9,669	\$8,463
Import	3,724	1,904	7,422	3,711
Luxury	2,308	1,036	4,369	2,165
	10,964	7,344	21,460	14,339
Corporate and other	(6,309)	(4,129)	(12,156)	(8,140)
	\$4,655	\$3,215	\$9,304	\$6,199

June 30,

	2015	December 31, 2014
Total assets:		
Domestic	\$922,933	\$831,574
Import	711,944	696,162
Luxury	422,318	405,222
Corporate and other	947,660	947,974
	\$3,004,855	\$2,880,932

Note 13. Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (“FASB”) issued accounting standards update (“ASU”) 2014-09, “Revenue from Contracts with Customers,” which amends the accounting guidance related to revenues. This amendment will replace most of the existing revenue recognition guidance when it becomes effective. The new standard, as amended in July 2015, is effective for fiscal years beginning after December 15, 2017 and entities are allowed to adopt the standard as early as annual periods beginning after December 15, 2016, and interim periods therein. The standard permits the use of either the retrospective or cumulative effect transition method. We are evaluating the effect this amendment will have on our consolidated financial statements and related disclosures and believe the financial impact is not material. We have not yet selected a transition method nor have we determined the effect of the standard on our ongoing financial reporting.

In June 2014, the FASB issued ASU 2014-12, “Compensation – Stock Compensation (Topic 718).” ASU 2014-12 addresses accounting for share-based payments when the terms of an award provide that a performance target could be achieved after the requisite service period. ASU 2014-12 indicates that, in such situations, the performance target should be treated as a performance condition and, accordingly, the performance target should not be reflected in estimating the grant-date fair value of the award. Instead, compensation cost should be recognized in the period in which it becomes probable that the performance target will be achieved. ASU 2014-12 is effective for annual periods and interim periods within those annual periods beginning after December 15, 2015. We do not expect the adoption of ASU 2014-12 to have a material effect on our financial position, results of operations or cash flows.

In February 2015, the FASB issued ASU 2015-02, “Consolidation (Topic 810).” ASU 2015-02 amends guidance regarding the consolidation of certain legal entities. ASU 2015-02 is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015, with early adoption permitted provided that the guidance is applied from the beginning of the fiscal year of adoption. We do not expect the adoption of ASU 2015-02 to have any effect on our financial position, results of operations or cash flows.

In April 2015, the FASB issued ASU 2015-03, “Interest – Imputation of Interest (Subtopic 835-30).” ASU 2015-03 amends guidance in order to simplify the presentation of debt issuance costs. ASU 2015-03 is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015, with early adoption permitted for financial statements that have not been previously issued. We do not expect the adoption of ASU 2015-03 to have any effect on our financial position, results of operations or cash flows.

Note 14. Subsequent Events

Common Stock Dividend

On July 20, 2015, our Board of Directors approved a dividend of \$0.20 per share on our Class A and Class B common stock related to our second quarter 2015 financial results. The dividend will total approximately \$5.3 million and will be paid on August 21, 2015 to shareholders of record on August 7, 2015.

Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations

Forward-Looking Statements and Risk Factors

Certain statements under the sections entitled “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and “Risk Factors” and elsewhere in this Form 10-Q constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Generally, you can identify forward-looking

statements by terms such as “project”, “outlook,” “target”, “may,” “will,” “would,” “should,” “seek,” “expect,” “plan,” “intend,” “anticipate,” “believe,” “estimate,” “predict,” “potential,” “likely,” “goal,” “strategy,” “future,” “maintain,” and “continue” or other similar terms or other comparable terms. Examples of forward-looking statements in this Form 10-Q include, among others, statements we make regarding:

Future market conditions;

Expected operating results, such as improved store performance; maintaining incremental throughput between 45% and 50%; continued improvement of SG&A as a percentage of gross profit and all projections;

Anticipated continued success, integration and growth of DCH;

Anticipated ability to capture additional market share; ability to find accretive acquisitions; and additions of dealership locations to the company’s portfolio in the future;

Anticipated availability of liquidity from our unfinanced operating real estate; and

Anticipated levels of capital expenditures in the future.

The forward-looking statements contained in this Form 10-Q involve known and unknown risks, uncertainties and situations that may cause our actual results to materially differ from the results expressed or implied by these statements. Certain important factors that could cause actual results to differ from our expectations are discussed in Part II - Other Information, Item 1A in this Form 10-Q and in the Risk Factors section of our 2014 Annual Report on Form 10-K, as supplemented and amended from time to time in Quarterly Reports on Form 10-Q and our other filings with the Securities and Exchange Commission.

By their nature, forward-looking statements involve risks and uncertainties because they relate to events that depend on circumstances that may or may not occur in the future. You should not place undue reliance on these forward-looking statements. Any forward-looking statement speaks only as of the date on which it is made. We assume no obligation to update or revise any forward-looking statement.

Overview

We are a leading operator of automotive franchises and a retailer of new and used vehicles and related services. As of July 31, 2015, we offered 31 brands of new vehicles and all brands of used vehicles in 129 stores in the United States and online at Lithia.com and DCHauto.com. We sell new and used cars and replacement parts; provide vehicle maintenance, warranty, paint and repair services; arrange related financing; and sell service contracts, vehicle protection products and credit insurance.

Our dealerships are located across the United States. We seek domestic, import and luxury franchises in cities ranging from mid-sized regional markets to metropolitan markets. We evaluate all brands for expansion opportunities provided the market is large enough to support adequate new vehicle sales to justify the required capital investment.

Our mission statement is: "Driven by our employees and preferred by our customers, Lithia is the leading automotive retailer in each of our markets." We offer customers personal, convenient, flexible personalized service combined with the large company advantages of selection, competitive pricing, broad access to financing, and warranties. We strive for diversification in our products, services, brands and geographic locations to insulate us from market risk and to maintain profitability. We have developed a centralized support structure to reduce store level administrative functions. This allows store personnel to focus on providing a positive customer experience. With our management information systems and centrally-performed administrative functions in Medford, Oregon, and regional accounting processing centers, we seek to gain economies of scale from our dealership network.

Results of Continuing Operations

For the three months ended June 30, 2015 and 2014, we reported income from continuing operations, net of tax, of \$51.2 million, or \$1.93 per diluted share, and \$35.2 million, or \$1.34 per diluted share, respectively.

For the six months ended June 30, 2015 and 2014, we reported income from continuing operations, net of tax, of \$91.9 million, or \$3.47 per diluted share, and \$59.9 million, or \$2.27 per diluted share, respectively.

Discontinued Operations

In the third quarter of 2014, we early-adopted guidance that redefined discontinued operations. As a result, we determined that individual stores that met the criteria for held for sale after our adoption date would no longer qualify for classification as discontinued operations. We had previously reclassified a store's operations to discontinued operations in our Consolidated Statements of Operations, on a comparable basis for all periods presented, provided we did not expect to have any significant continuing involvement in the store's operations after its disposal.

We realized income from discontinued operations, net of tax, of \$3.1 million, or \$0.11 per diluted share for the three months ended June 30, 2014 and \$3.2 million, or \$0.12 per diluted share, for the six months ended June 30, 2014. See Note 9 of the Condensed Notes to Consolidated Financial Statements for additional information.

Key Revenue and Gross Profit Metrics

Key performance metrics for revenue and gross profit were as follows (dollars in thousands):

Three months ended June 30, 2015	Revenues	Percent of		Gross Profit	Gross Profit Margin	Percent of Total		
		Total Revenues	%			Gross Profit	%	
New vehicle	\$1,149,512	57.6	%	\$69,342	6.0	%	23.3	%
Used vehicle retail	488,801	24.5		62,693	12.8		21.1	
Used vehicle wholesale	66,796	3.3		1,406	2.1		0.5	
Finance and insurance ⁽¹⁾	72,463	3.6		72,463	100.0		24.3	
Service, body and parts	182,695	9.2		90,749	49.7		30.5	
Fleet and other	36,680	1.8		996	2.7		0.3	
	\$1,996,947	100.0	%	\$297,649	14.9	%	100.0	%

Three months ended June 30, 2014	Revenues	Percent of		Gross Profit	Gross Profit Margin	Percent of Total		
		Total Revenues	%			Gross Profit	%	

Edgar Filing: LITHIA MOTORS INC - Form 10-Q

						Gross Profit	
New vehicle	\$694,484	56.8	% \$45,994	6.6	%	23.9	%
Used vehicle retail	310,475	25.4	44,067	14.2		22.9	
Used vehicle wholesale	44,286	3.6	1,504	3.4		0.8	
Finance and insurance ⁽¹⁾	43,838	3.6	43,838	100.0		22.8	
Service, body and parts	114,337	9.4	56,182	49.1		29.2	
Fleet and other	14,382	1.2	715	5.0		0.4	
	\$1,221,802	100.0	% \$192,300	15.7	%	100.0	%

Six months ended June 30, 2015	Revenues	Percent of Total Revenues	Gross Profit	Gross Profit Margin	Percent of Total Gross Profit		
New vehicle	\$2,157,328	57.0	% \$131,116	6.1	%	23.0	%
Used vehicle retail	951,732	25.1	122,135	12.8		21.4	
Used vehicle wholesale	129,004	3.4	3,567	2.8		0.6	
Finance and insurance ⁽¹⁾	137,067	3.6	137,067	100.0		24.0	
Service, body and parts	356,170	9.4	175,188	49.2		30.7	
Fleet and other	54,824	1.5	1,951	3.6		0.3	
	\$3,786,125	100.0	% \$571,024	15.1	%	100.0	%

Six months ended June 30, 2014	Revenues	Percent of Total Revenues	Gross Profit	Gross Profit Margin		Percent of Total Gross Profit	
New vehicle	\$1,274,006	55.4	% \$85,018	6.7	%	23.3	%
Used vehicle retail	612,368	26.6	84,863	13.9		23.3	
Used vehicle wholesale	86,979	3.8	2,835	3.3		0.8	
Finance and insurance ⁽¹⁾	83,469	3.6	83,469	100.0		22.9	
Service, body and parts	218,954	9.5	107,014	48.9		29.4	
Fleet and other	24,132	1.1	1,162	4.8		0.3	
	\$2,299,908	100.0	% \$364,361	15.8	%	100.0	%

(1) Commissions reported net of anticipated cancellations.

Same Store Operating Data

In 2014, we acquired 36 stores. As a result, we experienced significant growth in the first six months of 2015 compared to the same period in 2014. We believe that same store comparisons are an important indicator of our financial performance. Same store measures demonstrate our ability to grow revenues in our existing locations. As a result, same store measures have been integrated into the discussion below.

Same store measures reflect results for stores that were operating in each comparison period and only include the months when operations occurred in both periods. For example, a store acquired in May 2014 would be included in same store operating data beginning in June 2015, after its first full complete comparable month of operation. The second quarter operating results for the same store comparisons would include results for that store in only the period of June for both comparable periods.

New Vehicle Revenue and Gross Profit

(Dollars in thousands, except per unit amounts) Reported	Three Months Ended		Increase (Decrease)	% Increase (Decrease)	
	June 30, 2015	2014			
Revenue	\$1,149,512	\$694,484	\$455,028	65.5	%
Gross profit	\$69,342	\$45,994	\$23,348	50.8	
Gross margin	6.0	% 6.6	% (60)	bp	
Retail units sold	35,112	20,446	14,666	71.7	

Edgar Filing: LITHIA MOTORS INC - Form 10-Q

Average selling price per retail unit	\$32,738	\$33,967	\$ (1,229)	(3.6)
Average gross profit per retail unit	\$1,975	\$2,250	\$ (275)	(12.2)

Same store

Revenue	\$742,347	\$689,006	\$ 53,341	7.7 %
Gross profit	\$45,475	\$45,578	\$ (103)	(0.2)
Gross margin	6.1 %	6.6 %	(50) bp	

Retail units sold	21,411	20,260	1,151	5.7
Average selling price per retail unit	\$34,671	\$34,008	\$ 663	1.9
Average gross profit per retail unit	\$2,124	\$2,250	\$ (126)	(5.6)

(1) A basis point is equal to 1/100th of one percent.

Six Months Ended

(Dollars in thousands, except per unit amounts)	June 30,		Increase (Decrease)	% Increase (Decrease)
	2015	2014		
Reported				
Revenue	\$2,157,328	\$1,274,006	\$ 883,322	69.3 %
Gross profit	\$131,116	\$85,018	\$ 46,098	54.2
Gross margin	6.1 %	6.7 %	(60) bp	
Retail units sold	65,735	37,720	28,015	74.3
Average selling price per retail unit	\$32,819	\$33,775	\$ (956)	(2.8)
Average gross profit per retail unit	\$1,995	\$2,254	\$ (259)	(11.5)
Same store				
Revenue	\$1,379,617	\$1,260,741	\$ 118,876	9.4 %
Gross profit	\$85,494	\$83,957	\$ 1,537	1.8
Gross margin	6.2 %	6.7 %	(50) bp	
Retail units sold	39,894	37,268	2,626	7.0
Average selling price per retail unit	\$34,582	\$33,829	\$ 753	2.2
Average gross profit per retail unit	\$2,143	\$2,253	\$ (110)	(4.9)

New vehicle sales increased 65.5% and 69.3%, respectively, in the three- and six-month periods ended June 30, 2015 compared to the same periods of 2014 primarily driven by the acquisition of 27 stores from the DCH Auto Group in the fourth quarter of 2014. On a same store basis, new vehicle sales increased 7.7% and 9.4%, respectively, primarily due to unit volume growth of 5.7% and 7.0%, respectively, in the three- and six-month periods ended June 30, 2015 compared to the same periods in 2014. Same store unit sales increased in all reportable segments in the 2015 periods compared to the comparable 2014 periods as follows:

	Three months ended		National growth in the three months ended		Six months ended		National growth in the six months ended	
	June 30, 2015		June 30, 2015		June 30, 2015		June 30, 2015	
	compared to the same period of 2014		compared to the same period of 2014		compared to the same period of 2014		compared to the same period of 2014	
Domestic	8.8	%	3.0	%	7.9	%	3.6	%
Import	3.3		2.8		6.4		4.3	
Luxury	0.3		10.0		5.5		10.9	
Overall	5.7	%	3.4	%	7.0	%	4.4	%

Our unit volume growth rate for the 2015 periods was higher than the national average for our domestic and import stores, while growth in our luxury stores was flat for the three months ended June 30, 2015. We continue to focus on increasing our share of overall new vehicle sales within our markets.

New vehicle gross profit increased 50.8% and 54.2%, respectively, for the three- and six-month periods ended June 30, 2015 compared to the same periods of 2014, primarily driven by the acquisition of the DCH Auto Group in the fourth quarter of 2014. On a same store basis, new vehicle gross profit decreased 0.2% and increased 1.8%, respectively, for the three- and six-month periods ended June 30, 2015 compared to the same periods of 2014. In the three-month period ended June 30, 2015, lower gross profit per unit and gross margins resulted in a slight decline in gross profits. In the six-month period ended June 30, 2015, gross profit increases were due to a greater number of vehicles sold, offset by lower gross profit per unit and gross margins.

With our volume-based strategy, on a same store basis, the average gross profit per new retail unit decreased \$126, or 5.6%, and \$110, or 4.9%, respectively, in the three- and six-month periods ended June 30, 2015 compared to the same periods of 2014. We believe our volume-based strategy creates additional used vehicle trade-in opportunities, finance and insurance sales and future service work, which will generate incremental business in future periods that will more than offset the lower new vehicle gross profit per unit that has occurred with the pursuit of a volume-based strategy.

Used Vehicle Retail Revenue and Gross Profit

	Three Months Ended				
	June 30,		Increase	%	
(Dollars in thousands, except per unit amounts)	2015	2014	(Decrease)	(Decrease)	
Reported					
Retail revenue	\$488,801	\$310,475	\$ 178,326	57.4	%
Retail gross profit	\$62,693	\$44,067	\$ 18,626	42.3	
Retail gross margin	12.8	% 14.2	% (140)	bp	
Retail units sold	24,689	16,086	8,603	53.5	
Average selling price per retail unit	\$19,798	\$19,301	\$ 497	2.6	
Average gross profit per retail unit	\$2,539	\$2,739	\$ (200)	(7.3))
Same store					
Retail revenue	\$357,673	\$307,616	\$ 50,057	16.3	%
Retail gross profit	\$47,933	\$43,720	\$ 4,213	9.6	
Retail gross margin	13.4	% 14.2	% (80)	bp	
Retail units sold	17,769	15,924	1,845	11.6	
Average selling price per retail unit	\$20,129	\$19,318	\$ 811	4.2	
Average gross profit per retail unit	\$2,698	\$2,746	\$ (48)	(1.7))
Six Months Ended					
	June 30,		Increase	%	
(Dollars in thousands, except per unit amounts)	2015	2014	(Decrease)	(Decrease)	
Reported					
Retail revenue	\$951,732	\$612,368	\$ 339,364	55.4	%
Retail gross profit	\$122,135	\$84,863	\$ 37,272	43.9	
Retail gross margin	12.8	% 13.9	% (110)	bp	
Retail units sold	48,893	32,402	16,491	50.9	
Average selling price per retail unit	\$19,466	\$18,899	\$ 567	3.0	
Average gross profit per retail unit	\$2,498	\$2,619	\$ (121)	(4.6))
Same store					
Retail revenue	\$689,918	\$604,960	\$ 84,958	14.0	%
Retail gross profit	\$92,650	\$84,052	\$ 8,598	10.2	
Retail gross margin	13.4	% 13.9	% (50)	bp	
Retail units sold	34,942	31,971	2,971	9.3	
Average selling price per retail unit	\$19,745	\$18,922	\$ 823	4.3	
Average gross profit per retail unit	\$2,652	\$2,629	\$ 23	0.9	

Used vehicle retail sales are a strategic focus for organic growth. We offer three categories of used vehicles: manufacturer certified pre-owned vehicles; core vehicles, or late-model vehicles with lower mileage; and value autos, or vehicles with over 80,000 miles. Additionally, our volume-based strategy for new vehicle sales increases the organic opportunity to convert vehicles acquired via trade to retail used vehicle sales.

Same store sales increased in all three categories of used vehicles as follows:

	Three months ended	Six months ended
	June 30, 2015	June 30, 2015
	compared to the	compared to the
	same period of 2014	same period of 2014
Certified pre-owned vehicles	20.6%	19.1%
Core vehicles	16.1	13.7
Value autos	9.2	6.7
Overall	16.3	14.0

On an annualized average as of June 30, 2015 and 2014, each of our stores sold 59 and 55 retail used vehicle units, respectively, per month. We continue to target increasing sales to 75 units per store per month.

Used retail vehicle gross profit increased 42.3% and 43.9%, respectively, for the three- and six-month periods ended June 30, 2015 compared to the same periods of 2014, primarily driven by the acquisition of the DCH Auto Group in the fourth quarter of 2014. On a same store basis, gross profit increased 9.6% and 10.2%, respectively, for the three- and six-month periods ended June 30, 2015 compared to the same periods of 2014. These increases were mainly related to increased unit volume. The unit volume growth was driven by a mix shift toward certified pre-owned and core vehicles, which have higher average selling prices and lower gross margins than value autos.

Used Vehicle Wholesale Revenue and Gross Profit

	Three Months Ended		Increase (Decrease)	% Increase Decrease	
	June 30, 2015	2014			
(Dollars in thousands, except per unit amounts) Reported					
Wholesale revenue	\$66,796	\$44,286	\$ 22,510	50.8	%
Wholesale gross profit	\$1,406	\$1,504	\$ (98)	(6.5)
Wholesale gross margin	2.1 %	3.4 %	(130)bp		
Wholesale units sold	9,439	6,047	3,392	56.1	
Average selling price per wholesale unit	\$7,077	\$7,324	\$ (247)	(3.4)
Average gross profit per retail unit	\$149	\$249	\$ (100)	(40.2)
Same store					
Wholesale revenue	\$49,157	\$44,043	\$ 5,114	11.6	%
Wholesale gross profit	\$1,369	\$1,560	\$ (191)	(12.2)
Wholesale gross margin	2.8 %	3.5 %	(70)bp		
Wholesale units sold	6,259	5,981	278	4.6	
Average selling price per wholesale unit	\$7,854	\$7,364	\$ 490	6.7	
Average gross profit per retail unit	\$219	\$261	\$ (42)	(16.1)
Six Months Ended					
	June 30, 2015	2014	Increase (Decrease)	% Increase Decrease	
(Dollars in thousands, except per unit amounts) Reported					
Wholesale revenue	\$129,004	\$86,979	\$ 42,025	48.3	%

Edgar Filing: LITHIA MOTORS INC - Form 10-Q

Wholesale gross profit	\$3,567	\$2,835	\$ 732	25.8
Wholesale gross margin	2.8	% 3.3	% (50)bp
Wholesale units sold	18,583	11,900	6,683	56.2
Average selling price per wholesale unit	\$6,942	\$7,309	\$ (367) (5.0)
Average gross profit per retail unit	\$192	\$238	\$ (46) (19.3)
Same store				
Wholesale revenue	\$94,161	\$86,573	\$ 7,588	8.8 %
Wholesale gross profit	\$3,051	\$2,902	\$ 149	5.1
Wholesale gross margin	3.2	% 3.4	% (20)bp
Wholesale units sold	12,211	11,785	426	3.6
Average selling price per wholesale unit	\$7,711	\$7,346	\$ 365	5.0
Average gross profit per retail unit	\$250	\$246	\$ 4	1.6

Wholesale transactions are vehicles we have purchased from customers or vehicles we have attempted to sell via retail that we elect to dispose of due to inventory age or other factors. Wholesale vehicles are typically sold at or near inventory cost and do not comprise a meaningful component of our gross profit.

Finance and Insurance

	Three Months Ended		Increase	%	
	June 30, 2015	2014		Increase	Increase
(Dollars in thousands, except per unit amounts)					
Reported					
Revenue	\$72,463	\$43,838	\$28,625	65.3	%
Average finance and insurance per retail unit	\$1,212	\$1,200	\$12	1.0	%
Same store					
Revenue	\$50,160	\$43,508	\$6,652	15.3	%
Average finance and insurance per retail unit	\$1,280	\$1,202	\$78	6.5	%

	Six Months Ended		Increase	%	
	June 30, 2015	2014		Increase	Increase
(Dollars in thousands, except per unit amounts)					
Reported					
Revenue	\$137,067	\$83,469	\$53,598	64.2	%
Average finance and insurance per retail unit	\$1,196	\$1,190	\$6	0.5	%
Same store					
Revenue	\$94,133	\$82,548	\$11,585	14.0	%
Average finance and insurance per retail unit	\$1,258	\$1,192	\$66	5.5	%

The increases in total finance and insurance revenue were primarily due to higher unit volume, as a result of the acquisition of the DCH Auto Group in the fourth quarter of 2014. On a same store basis, the increases were due to higher unit volume sales and an increase in the average finance and insurance revenue earned per unit. Trends in penetration rates for total new and used retail vehicles sold are detailed below:

	Three Months Ended		Six Months Ended	
	June 30, 2015	2014	June 30, 2015	2014
Finance and insurance	77%	80%	77%	79%
Service contracts	41	43	41	43
Lifetime lube, oil and filter contracts	25	36	25	37

We believe the availability of credit is one of the key indicators of our ability to retail automobiles, as we arrange financing on almost 80% of the vehicles we sell and believe a significant amount of the vehicles we do not arrange financing for are financed elsewhere. To evaluate the availability of credit, we categorize our customers based on their Fair, Isaac and Company (FICO) credit score.

The distribution by credit score for the customers we arranged financing for was as follows:

		Three Months Ended June 30,		Six Months Ended June 30,	
	FICO Score Range	2015	2014	2015	2014
Prime	680 and above	69.5%	70.0%	68.9%	68.8%
Non-prime	620 - 679	18.6	18.5	18.8	18.6
Sub-prime	619 or less	11.9	11.5	12.3	12.5

We continued to see the availability of consumer credit expand in the first six months of 2015 compared to the same period of 2014.

Service, Body and Parts Revenue and Gross Profit

(Dollars in thousands)	Three Months Ended June 30,		Increase	% Increase	
	2015	2014			
Reported					
Customer pay	\$104,354	\$64,331	\$40,023	62.2	%
Warranty	39,996	19,908	20,088	100.9	
Wholesale parts	27,012	19,950	7,062	35.4	
Body shop	11,333	10,148	1,185	11.7	
Total service, body and parts	\$182,695	\$114,337	\$68,358	59.8	%
Service, body and parts gross profit	\$90,749	\$56,182	\$34,567	61.5	%
Service, body and parts gross margin	49.7	% 49.1	% 60		bp
Same store					
Customer pay	\$68,203	\$63,618	\$4,585	7.2	%
Warranty	25,008	19,758	5,250	26.6	
Wholesale parts	20,640	19,765	875	4.4	
Body shop	10,235	10,112	123	1.2	
Total service, body and parts	\$124,086	\$113,253	\$10,833	9.6	%
Service, body and parts gross profit	\$61,333	\$55,593	\$5,740	10.3	%
Service, body and parts gross margin	49.4	% 49.1	% 30		bp
Six Months Ended June 30,					
(Dollars in thousands)	2015	2014	Increase (Decrease)	% Increase Decrease	
Reported					
Customer pay	\$201,323	\$121,160	\$80,163	66.2	%
Warranty	77,367	37,826	39,541	104.5	
Wholesale parts	54,603	39,744	14,859	37.4	
Body shop	22,877	20,224	2,653	13.1	
Total service, body and parts	\$356,170	\$218,954	\$137,216	62.7	%
Service, body and parts gross profit	\$175,188	\$107,014	\$68,174	63.7	%
Service, body and parts gross margin	49.2	% 48.9	% 30		bp
Same store					
Customer pay	\$129,414	\$119,709	\$9,705	8.1	%
Warranty	48,346	37,500	10,846	28.9	
Wholesale parts	41,285	39,385	1,900	4.8	
Body shop	20,056	20,188	(132)	(0.7))

Edgar Filing: LITHIA MOTORS INC - Form 10-Q

Total service, body and parts	\$239,101	\$216,782	\$22,319	10.3	%
Service, body and parts gross profit	\$117,028	\$105,844	\$11,184	10.6	%
Service, body and parts gross margin	48.9	% 48.8	% 10		bp

Our service, body and parts sales grew in all areas except same store body shop in the six-month period ended June 30, 2015 compared to the same periods of 2014. There are more late-model vehicles in operation as new vehicle sales volumes have been increasing since 2010. We believe this increase in units in operation will benefit our service, body and parts sales in the coming years as more late-model vehicles age, necessitating repairs and maintenance.

We focus on retaining customers by offering competitively priced routine maintenance and through our marketing efforts. We increased our same store customer pay business 7.2% and 8.1%, respectively, in the three- and six-month periods ended June 30, 2015 compared to the same periods in 2014.

Same store warranty sales increased 26.6% and 28.9%, respectively, in the three- and six-month periods ended June 30, 2015 compared to the same periods of 2014, primarily due to significant numbers of vehicle recalls. Additionally, we continue to see increases due to the growing number of units in operation. Routine maintenance, such as oil changes, offered by certain brands, including BMW, Toyota and General Motors, for two to four years after a vehicle is sold, provides for future work as consumers return to the franchised dealer for this 'prepaid' maintenance item.

Increases in same-store warranty work by segment were as follows:

	Three months ended		Six months ended	
	June 30, 2015		June 30, 2015	
	compared to the		compared to the	
	same period of 2014		same period of 2014	
Domestic	33.5	%	36.6	%
Import	9.9	%	11.1	%
Luxury	32.6	%	35.2	%

Wholesale parts represented 16.6% and 17.3%, respectively, of our same store service, body and parts revenue mix in the three- and six-month periods ended June 30, 2015 and 17.5% and 18.2%, respectively, in the same periods of 2014. Same store wholesale parts grew 4.4% and 4.8%, respectively, in the three- and six-month periods ended June 30, 2015 compared to the same periods of 2014, primarily due to targeting fleet and mechanical wholesale accounts.

Body shop represented 8.2% and 8.4%, respectively, of our same store service, body and parts revenue mix in the three- and six-month periods ended June 30, 2015, and 8.9% and 9.3%, respectively, in the same periods of 2014. Same store body shop increased 1.2% and decreased 0.7%, respectively, in the three- and six-month periods ended June 30, 2015 compared to the same periods of 2014. During the first quarter of 2015, our body shops were impacted by a milder winter in the Pacific Northwest in 2015 where the majority of our body shops are located.

Same store service, body and parts gross profit increased 10.6% in both the three- and six-month periods ended June 30, 2015 compared to the same periods of 2014, which is in line with our revenue growth. Our gross margins were consistent in the three- and six-month periods ended June 30, 2015 compared to the same periods of 2014.

Segments

Certain financial information by segment is as follows:

Three Months Ended					
June 30,					
(Dollars in thousands)	2015	2014	Increase	%	
				Increase	
Revenues:					
Domestic	\$768,989	\$641,378	\$127,611	19.9	%
Import	853,444	394,923	458,521	116.1	
Luxury	372,369	185,826	186,543	100.4	
	1,994,802	1,222,127	772,675	63.2	
Corporate and other	2,145	(325)	2,470	NM	
	\$1,996,947	\$1,221,802	\$775,145	63.4	%
Six Months Ended					
June 30,					
(Dollars in thousands)	2015	2014	Increase	%	
				Increase	
Revenues:					
Domestic	\$1,460,393	\$1,210,308	\$250,085	20.7	%
Import	1,612,082	745,985	866,097	116.1	
Luxury	709,290	344,437	364,853	105.9	
	3,781,765	2,300,730	1,481,035	64.4	
Corporate and other	4,360	(822)	5,182	NM	
	\$3,786,125	\$2,299,908	\$1,486,217	64.6	%

NM – not meaningful.

(Dollars in thousands)	Three Months Ended				% Increase
	June 30,				
	2015	2014	Increase		
Segment income*:					
Domestic	\$31,045	\$25,288	\$5,757	22.8	%
Import	25,904	14,768	11,136	75.4	
Luxury	9,515	5,832	3,683	63.2	
	66,464	45,888	20,576	44.8	
Corporate and other	9,175	11,186	(2,011)	(18.0)	
Income from continuing operations before income taxes	\$75,639	\$57,074	\$18,565	32.5	%

(Dollars in thousands)	Six Months Ended				% Increase
	June 30,				
	2015	2014	Increase		
Segment income*:					
Domestic	\$58,174	\$47,710	\$10,464	21.9	%
Import	42,005	24,033	17,972	74.8	
Luxury	15,414	8,017	7,397	92.3	
	115,593	79,760	35,833	44.9	
Corporate and other	18,102	18,018	84	0.5	
Income from continuing operations before income taxes	\$133,695	\$97,778	\$35,917	36.7	%

*Segment income is defined as operating income less floor plan interest expense.

Retail new vehicle unit sales:	Three Months Ended				% Increase
	June 30,				
	2015	2014	Increase (Decrease)	Increase (Decrease)	
Domestic	11,517	10,050	1,467	14.6	%
Import	19,313	8,479	10,834	127.8	
Luxury	4,330	1,982	2,348	118.5	
	35,160	20,511	14,649	71.4	
Allocated to management	(48)	(65)	(17)	(26.2)	
	35,112	20,446	14,666	71.7	%

	Six Months Ended		Increase	% Increase	
	June 30,				
	2015	2014	(Decrease)	(Decrease)	
Retail new vehicle unit sales:					
Domestic	21,560	18,684	2,876	15.4	%
Import	36,087	15,618	20,469	131.1	
Luxury	8,195	3,577	4,618	129.1	
	65,842	37,879	27,963	73.8	
Allocated to management	(107)	(159)	(52)	(32.7))
	65,735	37,720	28,015	74.3	%

Domestic

A summary of financial information for our Domestic segment follows:

	Three Months Ended		Increase	% Increase	
	June 30,				
(Dollars in thousands)	2015	2014	Increase	% Increase	
Revenue	\$768,989	\$641,378	\$127,611	19.9	%
Segment income	\$31,045	\$25,288	\$5,757	22.8	
Retail new vehicle unit sales	11,517	10,050	1,467	14.6	

	Six Months Ended		Increase	% Increase	
	June 30,				
(Dollars in thousands)	2015	2014	Increase	% Increase	
Revenue	\$1,460,393	\$1,210,308	\$250,085	20.7	%
Segment income	\$58,174	\$47,710	\$10,464	21.9	
Retail new vehicle unit sales	21,560	18,684	2,876	15.4	

Improvements in our Domestic operating results in the three- and six-month periods ended June 30, 2015 compared to the same periods of 2014 were primarily a result of the improvements in all revenue categories as discussed above, overall improvements in the economy, acquisitions and overall growth in the market share of our Chrysler stores, which comprised 19% of our total overall new vehicle unit sales and over 50% of our Domestic segment revenue in the three- and six-month periods ended June 30, 2015. We acquired six Domestic locations in 2014.

Import

A summary of financial information for our Import segment follows:

	Three Months Ended				
	June 30,				
(Dollars in thousands)	2015	2014	Increase	% Increase	
Revenue	\$853,444	\$394,923	\$458,521	116.1	%
Segment income	\$25,904	\$14,768	\$11,136	75.4	
Retail new vehicle unit sales	19,313	8,479	10,834	127.8	

	Six Months Ended				
	June 30,				
(Dollars in thousands)	2015	2014	Increase	% Increase	
Revenue	\$1,612,082	\$745,985	\$866,097	116.1	%
Segment income	\$42,005	\$24,033	\$17,972	74.8	
Retail new vehicle unit sales	36,087	15,618	20,469	131.1	

Improvements in our Import operating results in the three- and six-month periods ended June 30, 2015 compared to the same periods of 2014 were primarily a result of the improvements in all revenue categories as discussed above, overall improvements in the economy and a strategic focus to diversify our dependence on Domestic brands through the acquisition of Import branded stores. We added 21 import locations in 2014. As of June 30, 2015, Honda and Toyota were our largest brands, representing 23% and 19% of our total overall new vehicle unit sales in the first six months of 2015, respectively.

Luxury

A summary of financial information for our Luxury segment follows:

Three Months Ended

(Dollars in thousands)	June 30,		Increase	% Increase	
	2015	2014			
Revenue	\$372,369	\$185,826	\$186,543	100.4	%
Segment income	\$9,515	\$5,832	\$3,683	63.2	
Retail new vehicle unit sales	4,330	1,982	2,348	118.5	

Six Months Ended

(Dollars in thousands)	June 30,		Increase	% Increase	
	2015	2014			
Revenue	\$709,290	\$344,437	\$364,853	105.9	%
Segment income	\$15,414	\$8,017	\$7,397	92.3	
Retail new vehicle unit sales	8,195	3,577	4,618	129.1	

Improvements in our Luxury operating results in the three- and six-month periods ended June 30, 2015 compared to the same periods of 2014 were primarily a result of the improvements in all revenue categories as discussed above, overall improvements in the economy and a strategic focus to diversify our dependence on Domestic brands through the acquisition of Luxury branded stores. We added nine luxury locations in 2014.

Asset Impairments

Asset impairments recorded as a component of continuing operations consist of the following (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Equity investments	\$4,130	\$ -	\$8,260	\$ -
Long-lived assets	2,000	-	2,000	-

For the three and six months ended June 30, 2015, we recorded asset impairments of \$4.1 million and \$8.3 million, respectively, associated with our equity-method investment in a limited liability company that participates in the New Markets Tax Credit Program (“NMTC Program”). The equity-method investment generates operating losses on a quarterly basis and, accordingly, we will be required to assess the investment for other than temporary impairment on a quarterly basis. The investment provides a return in the form of tax credits. We recorded a reduction to our income tax provision of \$7.7 million and \$14.9 million, respectively, related to tax credits under the NMTC Program in the three- and six-month periods ended June 30, 2015. See Note 11 of Condensed Notes to Consolidated Financial Statements elsewhere in this Form 10-Q for additional information.

In the second quarter of 2015, we recorded \$2.0 million of impairment charges associated with certain properties. As the expected future use of these facilities changed, the long-lived assets were tested for recoverability and were determined to have a carrying value exceeding the fair value of these properties.

Selling, General and Administrative Expense (“SG&A”)

SG&A includes salaries and related personnel expenses, advertising (net of manufacturer cooperative advertising credits), rent, facility costs, and other general corporate expenses.

	Three Months Ended June 30,				
(Dollars in thousands)	2015	2014	Increase	% Increase	
Personnel	\$ 134,003	\$ 85,332	\$ 48,671	57.0	%
Advertising	16,806	10,374	6,432	62.0	

Edgar Filing: LITHIA MOTORS INC - Form 10-Q

Rent	5,694	3,757	1,937	51.6	
Facility costs	8,459	7,301	1,158	15.9	
Other	30,648	18,699	11,949	63.9	
Total SG&A	\$ 195,610	\$ 125,463	\$ 70,147	55.9	%

**Three
Months
Ended**

Increase

As a % of gross profit	June 30,			
	2015	2014	(Decrease)	
Personnel	45.0%	44.4%	60	bp
Advertising	5.6	5.4	20	
Rent	1.9	2.0	(10)
Facility costs	2.8	3.8	(100)
Other	10.4	9.6	80	
Total SG&A	65.7%	65.2%	50	bp

Six Months Ended

June 30,

(Dollars in thousands)	2015	2014	Increase	% Increase	
Personnel	\$ 267,017	\$ 166,008	\$ 101,009	60.8	%
Advertising	32,150	20,059	12,091	60.3	
Rent	11,614	7,318	4,296	58.7	
Facility costs	16,804	14,885	1,919	12.9	
Other	59,643	39,022	20,621	52.8	
Total SG&A	\$ 387,228	\$ 247,292	\$ 139,936	56.6	%

	Six Months Ended		Increase	
As a % of gross profit	June 30,		(Decrease)	
	2015	2014		
Personnel	46.8%	45.6%	120	bp
Advertising	5.6	5.5	10	
Rent	2.0	2.0	-	
Facility costs	2.9	4.1	(120))
Other	10.5	10.7	(20))
Total SG&A	67.8%	67.9%	(10)	bp

SG&A expense increased \$70.1 million and \$139.9 million in the three- and six-month periods ended June 30, 2015 compared to the same periods in 2014. SG&A as a percentage of gross profit was 65.7% and 65.2%, respectively, for the three months ended June 30, 2015 and 2014, and 67.8% and 67.9%, respectively, for the six months ended June 30, 2015 and 2014.

These increases in SG&A expense were primarily driven by increased variable cost associated with increased sales volume and store count, offset by a gain of \$2.6 million and \$5.9 million, respectively, associated with the sale of one store and two stores, respectively, in the three and six months ended June 30, 2015. Additionally, the first quarter of 2014 includes non-core charges of \$3.9 million related to a reserve associated with a lawsuit filed in 2006 and settled in 2013, a loss reserve for a hailstorm in Texas and a reserve for a contract assumed in an acquisition. The second quarter of 2014 includes non-core charges of \$0.2 million related to acquisition expenses for the acquisition of DCH Auto Group.

SG&A expense adjusted for non-core charges was as follows (in thousands):

	Three Months Ended		Increase		
(Dollars in thousands)	June 30,		Increase		% Increase
	2015	2014			
Personnel	\$ 134,003	\$ 85,332	\$ 48,671	57.0	%
Advertising	16,806	10,374	6,432	62.0	
Rent	5,694	3,757	1,937	51.6	
Adjusted facility costs	11,029	7,301	3,728	51.1	
Other	30,648	18,536	12,112	65.3	
Adjusted total SG&A	\$ 198,180	\$ 125,300	\$ 72,880	58.2	%

**Three
Months
Ended** **Increase**

As a % of gross profit	June 30,			
	2015	2014	(Decrease)	
Personnel	45.0%	44.4%	60	bp
Advertising	5.6	5.4	20	
Rent	1.9	2.0	(10)
Adjusted facility costs	3.7	3.8	(10)
Other	10.4	9.6	80	
Adjusted total SG&A	66.6%	65.2%	140	bp

Six Months Ended

	June 30,					
(Dollars in thousands)	2015	2014	Increase	%	Increase	
Personnel	\$267,017	\$166,008	\$101,009	60.8	%	
Advertising	32,150	20,059	12,091	60.3		
Rent	11,614	7,318	4,296	58.7		
Adjusted facility costs	22,723	14,885	7,838	52.7		
Other	59,643	34,929	24,713	70.8		
Adjusted total SG&A	\$393,147	\$243,199	\$149,948	61.7	%	

As a % of gross profit	Six Months Ended		Increase	
	June 30, 2015	2014	(Decrease)	
Personnel	46.8%	45.6%	120	bp
Advertising	5.6	5.5	10	
Rent	2.0	2.0	-	
Adjusted facility costs	4.0	4.1	(10)
Other	10.4	9.5	90	
Adjusted total SG&A	68.8%	66.7%	210	bp

See “Non-GAAP Reconciliations” for more details of the non-GAAP reconciliation.

Due to the effects of the integration of DCH Auto Group, which we acquired in October 2014, we expect SG&A expense to increase in 2015 compared to pre-acquisition levels.

We also measure the leverage of our cost structure by evaluating throughput, which is the incremental percentage of gross profit retained after deducting SG&A expense.

(Dollars in thousands)	Three Months Ended			% of Change in Gross Profit	
	June 30, 2015	2014	Change		
Gross profit	\$297,649	\$192,300	\$105,349	100.0	%
SG&A expense	(195,610)	(125,463)	(70,147)	(66.6)
Throughput contribution			\$35,202	33.4	%

(Dollars in thousands)	Six Months Ended			% of Change in Gross Profit	
	June 30, 2015	2014	Change		
Gross profit	\$571,024	\$364,361	\$206,663	100.0	%
SG&A expense	(387,228)	(247,292)	(139,936)	(67.7)
Throughput contribution			\$66,727	32.3	%

Throughput, excluding non-core gains of \$2.6 million and \$5.9 million, respectively, for the three- and six-month periods ended June 30, 2015 and non-core charges of \$0.2 million and \$4.1 million, respectively, for the three- and six-month periods ended June 30, 2014, was as follows:

	Three Months Ended			% of	
	June 30,			Change	
(Dollars in thousands)	2015	2014	Change	in	Gross Profit
Gross profit	\$297,649	\$192,300	\$105,349	100.0	%
SG&A expense	(198,179)	(125,300)	(72,879)	(69.2))
Throughput contribution			\$32,470	30.8	%

	Six Months Ended			% of	
	June 30,			Change	
(Dollars in thousands)	2015	2014	Change	in	Gross Profit
Gross profit	\$571,024	\$364,361	\$206,663	100.0	%
SG&A expense	(393,146)	(243,198)	(149,948)	(72.6))
Throughput contribution			\$56,715	27.4	%

See “Non-GAAP Reconciliations” for more details.

Throughput contributions for newly opened or acquired stores reduce overall throughput because, in the first year of operation, a store’s throughput is equal to the inverse of its SG&A as a percentage of gross profit. For example, a store which achieves SG&A as a percentage of gross profit of 70% will have throughput of 30% in the first year of operation.

We opened two new stores and acquired 33 stores since June 30, 2014. Adjusting for these locations and the adjustments discussed above, our throughput contribution on a same store basis was 25.9% and 35.8%, respectively for the three- and six-month periods ended June 30, 2015. We continue to target a same store throughput contribution in a range of 45% to 50%.

Depreciation and Amortization

Depreciation and amortization is comprised of depreciation expense related to buildings, significant remodels or improvements, furniture, tools, equipment and signage and amortization of certain intangible assets, including trade name, customer lists and non-compete agreements.

	Three Months Ended				
					<i>%</i>
(Dollars in thousands)	June 30, 2015	2014	Increase	Increase	
Depreciation and amortization	\$ 10,287	\$ 5,825	\$ 4,462	76.6	<i>%</i>

	Six Months Ended				
					<i>%</i>
(Dollars in thousands)	June 30, 2015	2014	Increase	Increase	
Depreciation and amortization	\$ 20,013	\$ 11,332	\$ 8,681	76.6	<i>%</i>

Depreciation and amortization increased \$4.5 million and \$8.7 million, respectively, for the three- and six-month periods ended June 30, 2015 compared to the same periods of 2014. A majority of these increases was due to our acquisition activity since June 30, 2014. Additionally, we purchased previously leased facilities, built new facilities subsequent to the acquisition of stores and invested in improvements at our facilities and replacement of equipment. These investments increase the amount of depreciable assets and amortizable expenses. In the full year of 2014 and the first six months of 2015, we had capital expenditures of \$86.0 million and \$48.0 million, respectively.

Operating Income

Operating income as a percentage of revenue, or operating margin, was as follows:

Three Months	Six Months Ended
---------------------	-------------------------

	Ended		June 30,	
	June 30,			
	2015	2014	2015	2014
Operating margin	4.3 %	5.0 %	4.1 %	4.6 %
Operating margin adjusted for non-core charges ⁽¹⁾	4.5 %	5.0 %	4.2 %	4.8 %

⁽¹⁾ See “Non-GAAP Reconciliations” for more details.

Due to the effects of the integration of the DCH Auto Group, which has a lower operating efficiency than our other stores, we expect our operating margin to be in the low 4% range throughout 2015. We continue to focus on cost control, which allows us to leverage our cost structure in an environment of improving sales and aspire to increase our operating margin to our historical level.

Floor Plan Interest Expense and Floor Plan Assistance

Floor plan interest expense increased \$1.4 million and \$3.1 million, respectively, in the three- and six-month periods ended June 30, 2015 compared to the same periods of 2014 primarily as a result of increase in the average outstanding balances on our floor plan facilities due to our increase in vehicle sales as discussed above.

Floor plan assistance is provided by manufacturers to support store financing of new vehicle inventory. Under accounting standards, floor plan assistance is recorded as a component of new vehicle gross profit when the specific vehicle is sold. However, because manufacturers provide this assistance to offset inventory carrying costs, we believe a comparison of floor plan interest expense to floor plan assistance is a useful measure of the efficiency of our new vehicle sales relative to stocking levels.

The following tables detail the carrying costs for new vehicles and include new vehicle floor plan interest net of floor plan assistance earned.

(Dollars in thousands)	Three Months Ended			
	%			
	June 30, 2015	2014	Change	Change
Floor plan interest expense (new vehicles)	\$4,655	\$3,215	\$1,440	44.8 %
Floor plan assistance (included as an offset to cost of sales)	(10,547)	(6,806)	3,741	55.0
Net new vehicle carrying costs	\$(5,892)	\$(3,591)	\$(2,301)	(64.1)%

(Dollars in thousands)	Six Months Ended			
	%			
	June 30, 2015	2014	Change	Change
Floor plan interest expense (new vehicles)	\$9,304	\$6,199	\$3,105	50.1 %
Floor plan assistance (included as an offset to cost of sales)	(19,675)	(12,424)	7,251	58.4
Net new vehicle carrying costs	\$(10,371)	\$(6,225)	\$(4,146)	(66.6)%

Other Interest Expense

Other interest expense includes interest on debt incurred related to acquisitions, real estate mortgages, our used vehicle inventory financing facility and our revolving line of credit.

(Dollars in thousands)	Three Months Ended			
	%			
	June 30, 2015	2014	Increase (Decrease)	Increase (Decrease)
Mortgage interest	\$3,340	\$1,446	\$ 1,894	131.0 %
Other interest	1,727	523	1,204	230.2
Capitalized interest	(95)	(100)	5	(5.0)
Total other interest expense	\$4,972	\$1,869	\$ 3,103	166.0 %

(Dollars in thousands)	Six Months Ended			
	%			
	June 30, 2015	2014	Increase (Decrease)	Increase (Decrease)
Mortgage interest	\$6,356	\$3,004	\$ 3,352	111.6 %

Other interest	3,616	969	2,647	273.2	
Capitalized interest	(172)	(130)	(42)	32.3	
Total other interest expense	\$9,800	\$3,843	\$ 5,957	155.0	%

Other interest expense increased \$3.1 million and \$6.0 million, respectively, in the first three and six months of 2015 compared to the same periods of 2014 primarily due to higher volumes of borrowing on our credit facility and higher mortgage interest due to additional mortgage financings, partially offset by increased capitalized interest in the six-month period.

Other (Expense) Income, Net

Other (expense) income, net primarily includes interest income and the gains and losses related to an equity-method investment.

Three Months Ended

June 30, 2015

(Dollars in thousands)	2015	2014	Increase
Other (expense) income, net	\$(356)	\$1,146	\$ 1,502

Six Months Ended

June 30, 2015

(Dollars in thousands)	2015	2014	Increase
Other (expense) income, net	\$(724)	\$2,083	\$ 2,807

Income Tax Expense

Our effective income tax rate was 32.3% and 31.1% for the three- and six-month periods ended June 30, 2015 compared to 38.4% and 38.8%, respectively, in the comparable periods of 2014. For the full year of 2015, we forecast our income tax rate to be approximately 32.5%.

Our effective income tax rate in the first six months of 2015 was positively affected by new markets tax credits that are generated through our equity-method investment with U.S. Bancorp Community Development Corporation. Excluding the non-core tax attributes associated with the treatment of the tax credits generated through this investment and adjusting for other non-core items, our effective income tax rate was 39.0% in the three- and six-month periods ended June 30, 2015. Excluding this investment and adjusting for other non-core items, we forecast our income tax rate to be 39.3% for the full year 2015.

See “Non-GAAP Reconciliations” for more details.

Non-GAAP Reconciliations

We believe each of the non-GAAP financial measures below improves the transparency of our disclosures, provides a meaningful presentation of our results from the core business operations because they exclude adjustments for items not related to our ongoing core business operations and other non-cash adjustments, and improves the period-to-period comparability of our results from the core business operations. Our management uses these measures in conjunction with GAAP financial measures to assess our business, including our compliance with covenants in our credit facility and in communications with our Board of Directors concerning financial performance. These measures should not be considered an alternative to GAAP measures.

The following tables reconcile certain reported non-GAAP measures to the most comparable GAAP measure from our Consolidated Statements of Operations (dollars in thousands, except per share amounts):

	Three Months Ended June 30, 2015				
	Disposal				
	As reported	gain on sale	Asset impairment	Equity-method investment	Adjusted
		of stores			
Asset impairment	\$6,130	\$-	\$ (2,000)	\$ (4,130)	\$-
Selling, general and administrative	195,610	2,570	-	-	198,180
Operating income (loss)	85,622	(2,570)	2,000	4,130	89,182

Edgar Filing: LITHIA MOTORS INC - Form 10-Q

Other (expense) income	(356)	-	-	1,733	1,377
Income (loss) from continuing operations before income taxes	\$75,639	\$(2,570)	\$ 2,000	\$ 5,863	\$80,932
Income tax (provision) benefit	(24,416)	1,305	(780)	(7,652)	(31,543)
Income (loss) from continuing operations, net of income tax	\$51,223	\$(1,265)	\$ 1,220	\$ (1,789)	\$49,389
Diluted income (loss) per share from continuing operations	\$1.93	\$(0.05)	\$ 0.05	\$ (0.07)	\$1.86
Diluted share count	26,496				

Three Months Ended June 30, 2014

	As reported	Acquisition expenses	Tax attributes	Adjusted
Selling, general and administrative	\$125,463	\$ (163)	\$ -	\$125,300
Income from operations	61,012	163	-	61,175
Income from continuing operations before income taxes	\$57,074	\$ 163	\$ -	\$57,237
Income tax expense	(21,904)	(63)	(73)	(22,040)
Net income from continuing operations	\$35,170	\$ 100	\$ (73)	\$35,197
Diluted earnings per share from continuing operations	\$1.34	\$ -	\$ -	\$1.34
Diluted share count	26,331			

Six Months Ended June 30, 2015

	As reported	Disposal gain on sale of stores	Asset impairment	Equity-method investment	Adjusted
Asset impairment	\$10,260	\$-	\$ (2,000)	\$ (8,260)	\$-
Selling, general and administrative	387,228	5,919	-	-	393,147
Operating income (loss)	153,523	(5,919)	2,000	8,260	157,864
Other (expense) income	(724)	-	-	3,465	2,741
Income (loss) from continuing operations before income taxes	\$133,695	\$ (5,919)	\$ 2,000	\$ 11,725	\$141,501
Income tax (provision) benefit	(41,819)	2,309	(780)	(14,902)	(55,192)
Income (loss) from continuing operations, net of income tax	\$91,876	\$ (3,610)	\$ 1,220	\$ (3,177)	\$86,309
Diluted income (loss) per share from continuing operations	\$3.47	\$ (0.14)	\$ 0.05	\$ (0.12)	\$3.26
Diluted share count	26,509				

Six Months Ended June 30, 2014

	As reported	Reserve adjustments	Acquisition expenses	Tax attribute	Adjusted
Selling, general and administrative	\$247,292	\$ (3,931)	\$ (163)	\$ -	\$243,198
Income from operations	105,737	3,931	163	-	109,831
Income from continuing operations before income taxes	\$97,778	\$ 3,931	\$ 163	\$ -	\$101,872
Income tax expense	(37,914)	(1,545)	(63)	(73)	(39,595)
Net income from continuing operations	\$59,864	\$ 2,386	\$ 100	\$ (73)	\$62,277
Diluted earnings per share from continuing operations	\$2.27	\$ 0.09	\$ -	\$ -	\$2.36

Diluted share count

26,326

38

Liquidity and Capital Resources

We manage our liquidity and capital resources to fund our operating, investing and financing activities. We rely primarily on cash flows from operations and borrowings under our credit facilities as the main sources for liquidity. We use those funds to invest in capital expenditures, increase working capital and fulfill contractual obligations. Remaining funds are used for acquisitions, debt retirement, cash dividends, share repurchases and general business purposes.

Available Sources

Below is a summary of our available funds (in thousands):

	As of June 30,		Increase	%	
	2015	2014	(Decrease)	(Decrease)	
Cash and cash equivalents	\$23,394	\$28,203	\$ (4,809)	(17.1)	%
Available credit on the Credit Facility	164,058	83,980	80,078	95.4	
Total current available funds	187,452	112,183	75,269	67.1	
Estimated funds from unfinanced real estate	115,515	161,842	(46,327)	(28.6)	
Total estimated available funds	\$302,967	\$274,025	\$ 28,942	10.6	%

Cash flows generated by operating activities and from our credit facility are our most significant sources of liquidity. We also have the ability to raise funds through mortgaging real estate. As of June 30, 2015, our unencumbered owned operating real estate had a book value of \$154.0 million. Assuming we can obtain financing on 75% of this value, we estimate we could have obtained additional funds of approximately \$115.5 million at June 30, 2015; however, no assurances can be provided that the appraised value of these properties will match or exceed their book values or that this capital source will be available on terms acceptable to us.

In addition to the above sources of liquidity, potential sources include the placement of subordinated debentures or loans, the sale of equity securities and the sale of stores or other assets. We evaluate all of these options and may select one or more of them depending on overall capital needs and the availability and cost of capital, although no assurances can be provided that these capital sources will be available in sufficient amounts or with terms acceptable to us.

Information about our cash flows, by category, is presented in our Consolidated Statements of Cash Flows. The following table summarizes our cash flows (in thousands):

	Six Months Ended		Increase (Decrease)
	June 30, 2015	2014	
Net cash provided by (used in) operating activities	\$29,330	\$(4,194)	\$33,524
Net cash used in investing activities	(50,206)	(107,446)	(57,240)
Net cash provided by financing activities	14,372	116,157	(101,785)

Operating Activities

Cash provided by operating activities for the six months ended June 30, 2015 compared to the same period of 2014 increased \$33.5 million, primarily as a result of increased profitability and improved trade receivables collections, partially offset by increased inventory purchases.

Borrowings from and repayments to our syndicated lending group related to our new vehicle inventory floor plan financing are presented as financing activities. To better understand the impact of changes in inventory and the associated financing, we also consider our net cash provided by operating activities adjusted to include cash activity associated with our new vehicle credit facility and excluding cash activity associated with acquired inventory.

Adjusted net cash provided by operating activities is presented below (in thousands):

	Six Months Ended		Increase (Decrease) in Cash Flow
	June 30, 2015	2014	
Net cash provided by (used in) operating activities – as reported	\$29,330	\$(4,194)	\$ 33,524
Add: Net borrowings on floor plan notes payable, non-trade	35,685	112,910	(77,225)
Net cash provided by operating activities – adjusted	\$65,015	\$108,716	\$ (43,701)

Inventories are the most significant component of our cash flow from operations. As of June 30, 2015, our new vehicle days supply was 65, or three days higher than our days supply as of December 31, 2014. Our days supply of used vehicles was 54 days as of June 30, 2015, or one day higher than our days supply as of December 31, 2014. We calculate days supply of inventory based on current inventory levels, excluding in-transit vehicles, and a 30-day historical cost of sales level. We have continued to focus on managing our unit mix and maintaining an appropriate level of new and used vehicle inventory.

Investing Activities

Net cash used in investing activities totaled \$50.2 million and \$107.4 million, respectively, for the six-month periods ended June 30, 2015 and 2014. Cash flows from investing activities relate primarily to capital expenditures, acquisition and divestiture activity and sales of property and equipment.

Below are highlights of significant activity related to our cash flows from investing activities (in thousands):

	Six Months Ended		Increase (Decrease)
	June 30, 2015	2014	
Capital expenditures	\$(48,008)	\$(35,230)	\$ 12,778
Cash paid for acquisitions, net of cash acquired	(87)	(79,482)	(79,395)
Cash paid for other investments	(15,222)	(3,454)	11,768
Proceeds from sales of stores	12,966	10,617	2,349

Capital expenditures

Below is a summary of our capital expenditure activities (in thousands):

	Six Months Ended	
	June 30,	
	2015	2014
Post-acquisition capital improvements	\$3,114	\$4,201
Facilities for open points	3,222	3,031
Purchases of previously leased facilities	8,808	17,124
Existing facility improvements	18,730	6,134
Maintenance	14,134	4,740
Total capital expenditures	\$48,008	\$35,230

Many manufacturers provide assistance in the form of additional incentives or assistance if facilities meet manufacturer image standards and requirements. We expect that certain facility upgrades and remodels will generate additional manufacturer incentive payments.

We expect to make a portion of our future capital expenditures to upgrade facilities that we recently acquired. This additional capital investment is contemplated in our initial evaluation of the investment return metrics applied to each acquisition and is usually associated with manufacturer image standards and requirements.

We expect to make capital expenditures in 2015 of approximately \$110 million for capital improvements at recently acquired stores, purchases of land for expansion of existing stores, facility image improvements, purchases of store facilities, purchases of previously leased facilities and replacement of equipment.

Acquisitions

In the first six months of 2015, we acquired a smart franchise which was added to one of our existing stores. We acquired seven stores in the first six months of 2014.

We focus on acquiring stores at opportunistic purchase prices that meet our return thresholds and strategic objectives. We look for acquisitions that diversify our brand and geographic mix as we continue to evaluate our portfolio to minimize exposure to any one manufacturer and achieve financial returns.

We evaluate potential capital investments based on certain criteria, primarily associated with targeted rates of return on assets and return on our net equity investment.

Other Investments

Our cash paid associated with other investments increased \$11.8 million in the six months ended June 30, 2015 compared to the same period in 2014 mainly associated with our equity investment related to the NMTC Program.

Financing Activities

Net cash provided by financing activities totaled \$14.4 million and \$116.2 million for six-month periods ended June 30, 2015 and 2014, respectively.

Net cash provided by financing activities, adjusted for borrowing on floor plan facilities: non-trade was as follows (in thousands):

	Six Months Ended	
	June 30,	
	2015	2014
Cash provided by financing activities, as reported	\$ 14,372	\$ 116,157
Adjust: cash provided by borrowings on floor plan notes payable: non-trade	(35,685)	(112,910)
Cash (used in) provided by financing activities, as adjusted	\$(21,313)	\$3,247

Below are highlights of significant activity related to our cash flows from financing activities, excluding net borrowings on floor plan notes payable: non-trade, which are discussed above:

Six Months Ended

(Dollars in thousands)	June 30,		Increase
	2015	2014	(Decrease)
Net borrowings (repayments) on lines of credit	\$ (45,424)	\$ 11,000	\$ (56,424)
Proceeds from issuance of long-term debt	59,425	5,392	54,033
Principal payments on long-term debt, unscheduled	(9,189)	-	9,189
Repurchases of common stock	(16,773)	(10,206)	6,567
Dividends paid	(9,482)	(7,557)	1,925

Borrowing and Repayment Activity

During the first six months of 2015, we had net repayments of \$45.4 million associated with our lines of credit. We raised net mortgage proceeds of \$50.2 million during the first six months of 2015, which were used to pay down our line of credit, increasing availability on our credit facility.

Our debt to total capital ratio, excluding floor plan notes payable, was 45.9% at June 30, 2015 compared to 31.2% at June 30, 2014. We partially funded our 2014 acquisition activity, including the DCH Auto Group acquisition, with additional debt.

Equity Transactions

Under the share repurchase program authorized by our Board of Directors and repurchases associated with stock compensation activity, we repurchased 176,385 shares of our Class A common stock at an average price of \$95.09 per share in the first six months of 2015. As of June 30, 2015, we had 1,401,277 shares available for repurchase under our share repurchase program. The authority to repurchase does not have an expiration date.

In the first six months of 2015, we declared and paid dividends on our Class A and Class B common stock as follows:

Date	Dividend amount	Total amount of dividend (in thousands)
dividend paid	per share	
March 2015	\$ 0.16	\$ 4,216
May 2015	0.20	5,266

Management evaluates performance and makes a recommendation to the Board of Directors on dividend payments on a quarterly basis.

Summary of Outstanding Balances on Credit Facilities and Long-Term Debt

Below is a summary of our outstanding balances on credit facilities and long-term debt (in thousands):

	Outstanding	Remaining Available
	as of	as of
	June 30, 2015	June 30, 2015
Floor plan note payable: non-trade	\$ 1,169,717	\$ - (1)
Floor plan notes payable	45,464	-
Used vehicle inventory financing facility	168,500	- (2)
Revolving lines of credit	54,845	164,058 (2),(3)
Real estate mortgages	377,494	-
Other debt	36,526	-
Total debt	\$ 1,852,546	\$ 164,058

- (1) As of June 30, 2015, we had a \$1.25 billion new vehicle floor plan commitment as part of our credit facility.
- (2) The amount available on the credit facility is limited based on a borrowing base calculation and fluctuates monthly.
- (3) Available credit is based on the borrowing base amount effective as of June 30, 2015. This amount is reduced by \$7.4 million for outstanding letters of credit.

Credit Facility

We have a \$1.7 billion revolving syndicated credit facility. This syndicated credit facility is comprised of 16 financial institutions, including seven manufacturer-affiliated finance companies. Our credit facility provides for up to \$1.25 billion in new vehicle inventory floor plan financing, up to \$150 million in used vehicle inventory floor plan financing and a maximum of \$300 million in revolving financing for general corporate purposes, including acquisitions and working capital. This credit facility may be expanded to \$1.85 billion total availability, subject to lender approval.

We may request a reallocation of any unused portion of our credit facility provided that the used vehicle inventory floor plan commitment does not exceed \$250 million, the revolving financing commitment does not exceed \$300 million, and the sum of those commitments plus the new vehicle inventory floor plan financing commitment does not exceed the total aggregate financing commitment. All borrowings from, and repayments to, our lending group are presented in the Consolidated Statements of Cash Flows as financing activities.

The new vehicle floor plan commitment is collateralized by our new vehicle inventory. Our used vehicle inventory financing facility is collateralized by our used vehicle inventory that has been in stock for less than 180 days. Our revolving line of credit is secured by our outstanding receivables related to vehicle sales, unencumbered vehicle inventory, other eligible receivables, parts and accessories and equipment.

We have the ability to deposit up to \$50 million in cash in Principal Reduction (PR) accounts associated with our new vehicle inventory floor plan commitment. The PR accounts are recognized as offsetting credits against outstanding amounts on our new vehicle floor plan commitment and would reduce interest expense associated with the outstanding principal balance. As of June 30, 2015, we had no balances in our PR accounts.

If the outstanding principal balance on our new vehicle inventory floor plan commitment, plus requests on any day, exceeds 95% of the loan commitment, a portion of the revolving line of credit must be reserved. The reserve amount is equal to the lesser of \$15.0 million or the maximum revolving line of credit commitment less the outstanding balance on the line less outstanding letters of credit. The reserve amount will decrease the revolving line of credit availability and may be used to repay the new vehicle floor plan commitment balance.

The interest rate on the credit facility varies based on the type of debt, with the rate of one-month LIBOR plus 1.25% for new vehicle floor plan financing, one-month LIBOR plus 1.50% for used vehicle floor plan financing; and a variable interest rate on the revolving financing ranging from the one-month LIBOR plus 1.25% to 2.50%, depending on our leverage ratio. The annual interest rate associated with our new vehicle floor plan commitment, excluding the effects of our interest rate swaps, was 1.4% at June 30, 2015. The annual interest rate associated with our used vehicle inventory financing facility and our revolving line of credit was 1.7% and 2.2%, respectively, at June 30, 2015.

Under the terms of our credit facility we are subject to financial covenants and restrictive covenants that limit or restrict our incurring additional indebtedness, making investments, selling or acquiring assets and granting security interests in our assets.

Under our credit facility, we are required to maintain the ratios detailed in the following table:

		As of
Debt Covenant Ratio	Requirement	June 30, 2015
Current ratio	Not less than 1.10 to 1	1.24 to 1
Fixed charge coverage ratio	Not less than 1.20 to 1	3.21 to 1
Leverage ratio	Not more than 5.00 to 1	1.97 to 1
Funded debt restriction	Not to exceed \$600 million	\$414.4 million

As of June 30, 2015, we were in compliance with all covenants. We expect to remain in compliance with the financial and restrictive covenants in our credit facility and other debt agreements. However, no assurances can be provided that we will continue to remain in compliance with the financial and restrictive covenants.

If we do not meet the financial and restrictive covenants and are unable to remediate or cure the condition or obtain a waiver from our lenders, a breach would give rise to remedies under the agreement, the most severe of which are the termination of the agreement, acceleration of the amounts owed and the seizure and sale of our assets comprising the collateral for the loans. A breach would also trigger cross-defaults under other debt agreements.

Floor Plan Notes Payable

We have floor plan agreements with manufacturer-affiliated finance companies for vehicles that are designated for use as service loaners. The variable interest rates on these floor plan notes payable commitments vary by manufacturer. At June 30, 2015, \$45.5 million was outstanding on these arrangements. Borrowings from, and repayments to, manufacturer-affiliated finance companies are classified as operating activities in the Consolidated Statements of Cash Flows.

Real Estate Mortgages and Other Debt

We have mortgages associated with our owned real estate. Interest rates related to this debt ranged from 1.7% to 5.0% at June 30, 2015. The mortgages are payable in various installments through October 2034. As of June 30, 2015, we had fixed interest rates on 80% of our outstanding mortgage debt.

Our other debt includes capital leases, sellers' notes and our equity contribution obligations associated with the new markets tax credit equity investment. The interest rates associated with our other debt ranged from 2.0% to 9.0% at June 30, 2015. This debt, which totaled \$36.5 million at June 30, 2015, is due in various installments through January 2024.

Recent Accounting Pronouncements

See Note 13 of the Condensed Notes to Consolidated Financial Statements in this Quarterly Report on Form 10-Q.

Critical Accounting Policies and Use of Estimates

There have been no material changes in the critical accounting policies and use of estimates described in our 2014 Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 2, 2015.

Seasonality and Quarterly Fluctuations

Historically, our sales have been lower in the first and fourth quarters of each year due to consumer purchasing patterns during the holiday season, inclement weather in certain of our markets and the reduced number of business days during the holiday season. As a result, financial performance is expected to be lower during the first and fourth quarters than during the second and third quarters of each fiscal year. More recently, our franchise diversification and cost control efforts have moderated the significance of our seasonality. We believe that interest rates, levels of consumer debt, consumer confidence and manufacturer sales incentives, as well as general economic conditions, also contribute to fluctuations in sales and operating results.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements that have or are reasonably likely to have a material current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

There have been no material changes in our reported market risks or risk management policies since the filing of our 2014 Annual Report on Form 10-K, which was filed with the Securities and Exchange Commission on March 2, 2015.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our management evaluated, with the participation and under the supervision of our Chief Executive Officer and our Chief Financial Officer, the effectiveness of our disclosure controls and procedures as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on this evaluation, our Chief Executive Officer and our Chief Financial Officer concluded that our disclosure controls and procedures are effective to ensure that information we are required to disclose in reports that we file or submit under the Securities Exchange Act of 1934 is accumulated and communicated to our management, including our Chief Executive Officer and our Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure and that such information is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms.

Changes in Internal Control Over Financial Reporting

There was no change in our internal control over financial reporting that occurred during our last fiscal quarter that has materially affected or is reasonably likely to materially affect our internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1A. Risk Factors

Except for the risk factor set forth below, there have been no material changes from the risk factors previously disclosed in our 2014 Annual Report on Form 10-K. The information in this Form 10-Q should be read in conjunction with the risk factors and information disclosed in that report, which was filed with the Securities and Exchange Commission on March 2, 2015.

We may not be able to utilize certain income tax benefits.

Our ability to utilize the income tax benefits and credits generated by our equity investments intended to generate new market tax credits (NMTC) depends on compliance with NMTC program requirements, which we do not control. Our ability to utilize NMTC, and other deferred tax assets, also depends on our generating sufficient taxable income from operations in the future. The inability to utilize the income tax benefits could have a material adverse impact on our business, results of operations, financial condition and cash flows.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

We repurchased the following shares of our Class A common stock during the second quarter of 2015:

	Total number of shares purchased	Average price paid per share	Total number of shares purchased as part of publicly announced plan⁽¹⁾	Maximum number of shares that may yet be purchased under the plans
April 1 to April 30	20,902	\$ 101.67	20,902	1,440,877
May 1 to May 31	19,800	105.16	19,800	1,421,077
June 1 to June 30	19,800	112.25	19,800	1,401,277
Total	60,502	106.27	60,502	1,401,277

In 2011 and 2012, our Board of Directors authorized the repurchase of up to a total of 3,000,000 shares of our Class A common stock. Through June 30, 2015, we have repurchased 1,598,723 shares at an average price of (1) \$35.47 per share. This authority to repurchase shares does not have an expiration date or a maximum aggregate dollar amount for repurchases.

Item 6. Exhibits

The following exhibits are filed herewith and this list is intended to constitute the exhibit index:

- 3.1 Restated Articles of Incorporation of Lithia Motors, Inc., as amended May 13, 1999 (incorporated by reference to exhibit 3.1 to our Form 10-K for the year ended December 31, 1999).
- 3.2 2013 Amended and Restated Bylaws of Lithia Motors, Inc. (incorporated by reference to exhibit 3.1 to Form 8-K dated August 20, 2013 and filed with the Securities and Exchange Commission on August 26, 2013).
- 31.1 Certification of Chief Executive Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934.
- 31.2 Certification of Chief Financial Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934.
- 32.1 Certification of Chief Executive Officer pursuant to Rule 13a-14(b) or Rule 15d-14(b) of the Securities Exchange Act of 1934 and 18 U.S.C. Section 1350.
- 32.2 Certification of Chief Financial Officer pursuant to Rule 13a-14(b) or Rule 15d-14(b) of the Securities Exchange Act of 1934 and 18 U.S.C. Section 1350.
- 101.INS XBRL Instance Document.
- 101.SCH XBRL Taxonomy Extension Schema Document.
- 101.CAL XBRL Taxonomy Extension Calculation Linkbase Document.
- 101.DEF XBRL Taxonomy Extension Definition Linkbase Document.
- 101.LAB XBRL Taxonomy Extension Label Linkbase Document.
- 101.PRE XBRL Taxonomy Extension Presentation Linkbase Document.

SIGNATURES

Pursuant to the requirements 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.

Date: July 31, 2015 LITHIA MOTORS, INC.

By: /s/ Christopher S. Holzshu
Christopher S. Holzshu

Senior Vice President,
Chief Financial Officer and Secretary
(Principal Financial Officer)

By: /s/ John F. North III
John F. North III

Vice President
(Principal Accounting Officer)