LITHIA MOTORS INC
Form 10-Q
October 31, 2014

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2014

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	**93-0572810**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

150 N. Bartlett Street, Medford, Oregon	**97501**
(Address of principal executive offices)	(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 [X] 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 [X] 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 [X] 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 [X]

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	**23,688,734**
Class B common stock without par value	**2,562,231**
(Class)	(Outstanding at October 31, 2014)

LITHIA MOTORS, INC.

FORM 10-Q

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LITHIA MOTORS, INC. AND SUBSIDIARIES

Consolidated Balance Sheets

(In thousands)

(Unaudited)

	September 30, 2014	December 31, 2013
Assets		
Current Assets:		
Cash and cash equivalents	$21,666	$23,686
Accounts receivable, net	181,855	170,519
Inventories, net	941,756	859,019
Deferred income taxes	500	1,548
Other current assets	11,088	15,251
Assets held for sale	8,920	11,526
Total Current Assets	1,165,785	1,081,549
Property and equipment, net of accumulated depreciation of $114,102 and $106,871	536,519	481,212
Goodwill	65,745	49,511
Franchise value	77,482	71,199
Deferred income taxes	12,450	10,256
Other non-current assets	46,922	31,394
Total Assets	$1,904,903	$1,725,121
Liabilities and Stockholders' Equity		
Current Liabilities:		
Floor plan notes payable	$21,362	$18,789
Floor plan notes payable: non-trade	718,227	695,066
Current maturities of long-term debt	9,305	7,083
Trade payables	59,481	51,159
Accrued liabilities	116,619	94,143
Liabilities related to assets held for sale	4,776	6,271
Total Current Liabilities	929,770	872,511
Long-term debt, less current maturities	263,117	245,471
Deferred revenue	51,913	44,005
Other long-term liabilities	36,190	28,412
Total Liabilities	1,280,990	1,190,399
Stockholders' Equity:		
Preferred stock - no par value; authorized 15,000 shares; none outstanding	-	-

Class A common stock - no par value; authorized 100,000 shares; issued and outstanding 23,546 and 23,329	266,075	268,255
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	27,657	22,598
Accumulated other comprehensive loss	(1,075)	(1,538)
Retained earnings	330,937	245,088
Total Stockholders' Equity	623,913	534,722
Total Liabilities and Stockholders' Equity	$1,904,903	$1,725,121

See accompanying condensed notes to consolidated financial statements.

LITHIA MOTORS, INC. AND SUBSIDIARIES

Consolidated Statements of Operations

(In thousands, except per share amounts)

(Unaudited)

	Three Months Ended September 30,		**Nine Months Ended September 30,**	
	2014	**2013**	**2014**	**2013**
Revenues:				
New vehicle	$732,121	$604,135	$2,006,127	$1,667,063
Used vehicle retail	340,522	280,734	952,890	778,427
Used vehicle wholesale	48,853	43,396	135,832	120,593
Finance and insurance	46,855	37,132	130,324	103,013
Service, body and parts	120,772	97,784	339,726	282,686
Fleet and other	7,988	6,109	32,120	29,093
Total revenues	1,297,111	1,069,290	3,597,019	2,980,875
Cost of sales:				
New vehicle	684,473	565,549	1,873,461	1,555,042
Used vehicle retail	296,624	239,093	824,129	662,920
Used vehicle wholesale	48,349	42,686	132,493	118,214
Service, body and parts	62,351	50,793	174,291	145,223
Fleet and other	7,474	5,780	30,444	27,816
Total cost of sales	1,099,271	903,901	3,034,818	2,509,215
Gross profit	197,840	165,389	562,201	471,660
Selling, general and administrative	131,627	108,570	378,919	318,984
Depreciation and amortization	6,067	5,099	17,399	14,719
Operating income	60,146	51,720	165,883	137,957
Floor plan interest expense	(3,127)	(2,909)	(9,326)	(9,394)
Other interest expense	(2,051)	(1,933)	(5,894)	(6,235)
Other income, net	1,027	835	3,110	2,220
Income from continuing operations before income taxes	55,995	47,713	153,773	124,548
Income tax provision	(21,458)	(16,822)	(59,372)	(46,494)
Income from continuing operations, net of income tax	34,537	30,891	94,401	78,054
Income from discontinued operations, net of income tax	-	127	3,179	574
Net income	$34,537	$31,018	$97,580	$78,628
Basic income per share from continuing operations	$1.32	$1.19	$3.62	$3.03
Basic income per share from discontinued operations	-	0.01	0.12	0.02
Basic net income per share	$1.32	$1.20	$3.74	$3.05
Shares used in basic per share calculations	26,118	25,866	26,071	25,776
Diluted income per share from continuing operations	$1.31	$1.18	$3.58	$2.98

Diluted income per share from discontinued operations	-	-	0.13	0.03
Diluted net income per share	$1.31	$1.18	$3.71	$3.01
Shares used in diluted per share calculations	26,359	26,237	26,337	26,159

See accompanying condensed notes to consolidated financial statements.

LITHIA MOTORS, INC. AND SUBSIDIARIES

Consolidated Statements of Comprehensive Income

(In thousands)

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	**2013**	**2014**	**2013**
Net income	$34,537	$31,018	$97,580	$78,628
Other comprehensive income, net of tax:				
Gain on cash flow hedges, net of tax expense of $114, $58, $288, and $582, respectively	184	94	463	938
Comprehensive income	$34,721	$31,112	$98,043	$79,566

See accompanying condensed notes to consolidated financial statements.

LITHIA MOTORS, INC. AND SUBSIDIARIES

Consolidated Statements of Cash Flows

(In thousands)

(Unaudited)

	Nine Months Ended September 30,	
	2014	**2013**
Cash flows from operating activities:		
Net income	$97,580	$78,628
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	17,399	14,719
Stock-based compensation	5,054	4,161
Loss on disposal of other assets	307	107
Gain from disposal activities within discontinued operations	(5,744)	-
Deferred income taxes	4,725	8,504
Excess tax benefit from share-based payment arrangements	(6,160)	(5,956)
(Increase) decrease (net of acquisitions and dispositions):		
Trade receivables, net	(11,336)	(6,937)
Inventories, net	(44,349)	(18,187)
Other assets	(13,700)	1,660
Increase (decrease) (net of acquisitions and dispositions):		
Floor plan notes payable, net	1,132	5,721
Trade payables	4,246	4,848
Accrued liabilities	21,913	13,099
Other long-term liabilities and deferred revenue	16,635	12,307
Net cash provided by operating activities	87,702	112,674
Cash flows from investing activities:		
Principal payments received on notes receivable	2,882	88
Capital expenditures	(54,149)	(33,803)
Proceeds from sales of assets	3,243	474
Payments for life insurance policies	(3,385)	(2,508)
Cash paid for acquisitions	(81,558)	(31,786)
Proceeds from sales of stores	10,617	-
Net cash used in investing activities	(122,350)	(67,535)
Cash flows from financing activities:		
Borrowings on floor plan notes payable: non-trade, net	30,375	2,685
Borrowings on lines of credit	836,156	499,000
Repayments on lines of credit	(891,000)	(542,446)
Principal payments on long-term debt, scheduled	(5,528)	(5,375)
Principal payments on long-term debt and capital leases, other	-	(25,770)

Proceeds from issuance of long-term debt	76,530	4,720
Proceeds from issuance of common stock	3,411	3,967
Repurchase of common stock	(11,745)	(7,903)
Excess tax benefit from share-based payment arrangements	6,160	5,956
Dividends paid	(11,731)	(6,719)
Net cash provided by (used in) financing activities	32,628	(71,885)
Decrease in cash and cash equivalents	(2,020)	(26,746)
Cash and cash equivalents at beginning of period	23,686	42,839
Cash and cash equivalents at end of period	$21,666	$16,093
Supplemental disclosure of cash flow information:		
Cash paid during the period for interest	$15,556	$15,988
Cash paid during the period for income taxes, net	44,918	25,880
Supplemental schedule of non-cash activities:		
Debt issued in connection with acquisitions	3,161	-
Floorplan debt paid in connection with dealership disposals	3,311	-

See accompanying condensed 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 September 30, 2014 and for the three- and nine-month periods ended September 30, 2014 and 2013. 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 2013 audited Consolidated Financial Statements and the related notes thereto. The financial information as of December 31, 2013 is derived from our 2013 Annual Report on Form 10-K. The interim condensed Consolidated Financial Statements should be read in conjunction with the Consolidated Financial Statements and the notes thereto included in our 2013 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):

	September 30, 2014	December 31,

		2013
Contracts in transit	$ 91,920	$ 85,272
Trade receivables	24,873	23,154
Vehicle receivables	25,093	23,606
Manufacturer receivables	34,282	31,662
Auto loan receivables	21,807	$ 11,438
Other receivables	2,697	5,622
	200,672	180,754
Less: Allowance	(966)	(546)
Less: Long-term portion of accounts receivable, net	(17,851)	(9,689)
Total accounts receivable, net	$ 181,855	$ 170,519

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 third parties 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 interest income is 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 was included as a component of other non-current assets in the Consolidated Balance Sheets.

<u>Note 3. Inventories</u>

The components of inventory consisted of the following (in thousands):

	September 30, 2014	**December 31, 2013**
New vehicles	$ 711,090	$ 657,043
Used vehicles	192,801	167,814
Parts and accessories	37,865	34,162
Total inventories	$ 941,756	$ 859,019

<u>Note 4. Goodwill</u>

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

	Goodwill
Balance as of December, 31, 2012, gross	$331,313
Accumulated impairment loss	(299,266)
Balance as of December 31, 2012, net	32,047
Additions through acquisitions	17,464
Balance as of December 31, 2013, net	49,511
Additions through acquisition	16,234

Balance as of September 30, 2014, net	$65,745

Note 5. Commitments and Contingencies

Litigation

We are party to numerous legal proceedings arising in the normal course of our business. Although we do not anticipate that the resolution of legal proceedings arising in the normal course of business or the proceedings described below will have a material adverse effect on our business, results of operations, financial condition, or cash flows, we cannot predict this with certainty.

Alaska Consumer Protection Act Claims

In December 2006, a class action suit was filed against us (Jackie Neese, et al vs. Lithia Chrysler Jeep of Anchorage, Inc., et al, Case No. 3AN-06-13341 CI), and in April 2007, a second class action suit (Jackie Neese, et al vs. Lithia Chrysler Jeep of Anchorage, Inc, et al, Case No. 3AN-06-4815 CI) was filed against us, in the Superior Court for the State of Alaska, Third Judicial District at Anchorage. These suits were subsequently consolidated. In the consolidated suit, plaintiffs alleged that we, through our Alaska dealerships, engaged in three practices that purportedly violate Alaska consumer protection laws: (i) charging customers dealer fees and costs (including document preparation fees) not disclosed in the advertised price, (ii) failing to disclose the acquisition, mechanical and accident history of used vehicles or whether the vehicles were originally manufactured for sale in a foreign country, and (iii) engaging in deception, misrepresentation and fraud by providing to customers financing from third parties without disclosing that we receive a fee or discount for placing that loan. The suit sought statutory damages of $500 for each violation or three times plaintiff’s actual damages, whichever was greater, and attorney fees and costs.

In June 2013, the parties agreed to mediate the claims. The mediation resulted in a settlement agreement that received the final approval of the Court on December 11, 2013. Under the settlement agreement, we agreed to reimburse plaintiffs' legal fees and to pay (i) $450 in the form of cash and vouchers to valid claimants and (ii) $3,000 for each claim representative. The majority of cash and vouchers have been mailed.

We have recorded expenses of $6.7 million to settle all claims against us and to pay plaintiffs' legal fees. Of this amount, $0.7 million was recorded in the nine months ended September 30, 2014, as a component of selling, general and administrative expense in our Consolidated Statements of Operations. As of September 30, 2014, the liability for unused vouchers, assuming an expected redemption rate, was $1.1 million and is recorded as a component of accrued liabilities in the Consolidated Balance Sheet. We believe that these estimates are reasonable; however, actual costs could differ materially.

<u>Note 6. Stockholders' Equity</u>

Reclassification From Accumulated Other Comprehensive Loss

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

	Three Months Ended September 30, 2014	Nine Months Ended September 30, 2014	Affected Line Item in the Consolidated Statements of Operations
Loss on cash flow hedges	$ (119)	$ (370)	Floor plan interest expense
Taxes	46	141	Income tax provision
Loss on cash flow hedges, net	$ (73)	$ (229)	

	Three Months Ended September 30, 2013	Nine Months Ended September 30, 2013	Affected Line Item in the Consolidated Statements of Operations
Loss on cash flow hedges	$ (134)	$ (606)	Floor plan interest expense
Taxes	51	232	Income tax provision
Loss on cash flow hedges, net	$ (83)	$ (374)	

See Note 9 for more details regarding our derivative contracts.

Share Repurchases

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. In the nine months ended September 30, 2014, we repurchased 62,500 shares at an average price of $76.28 per share, for a total of $4.8 million. Through September 30, 2014, we have repurchased 1,335,547 shares and 1,664,453 shares remained available for repurchase. This authority to repurchase shares does not have an expiration date and we may continue to repurchase shares from time to time as conditions warrant.

In addition, we repurchased 106,772 shares related to tax withholdings associated with the vesting of restricted stock units during the first nine months of 2014 at an average price of $65.36, for a total of $7.0 million.

Dividends

Dividends paid on our Class A and Class B common stock in the nine months ended September 30, 2014 were as follows:

Quarter paid:	**Dividend amount per share**	**Total amount of dividend (in thousands)**
First quarter	$ 0.13	$ 3,378
Second quarter	0.16	4,179
Third quarter	0.16	4,174

See Note 14 for a discussion of a dividend related to our third quarter 2014 financial results.

Note 7. 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 between one and seven years based 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.

In 2014, we made discretionary contributions of $2.4 million to the LTIP. Participants will receive a guaranteed return of 5.25% in 2014. We recognized compensation expense related to the LTIP as follows (in thousands):

	Three Months Ended September 30,	**Nine Months Ended September 30,**

	2014	2013	2014	2013
Compensation expense	$381	$357	$1,458	$1,042

As of September 30, 2014 and December 31, 2013, the balance due to participants was $10.8 million and $7.1 million, respectively, and was included as a component of other long-term liabilities in the Consolidated Balance Sheets.

Note 8. 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 and 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 our own, as well as the counterparty's, risk of non-performance under the contract.

There were no changes to our valuation techniques during the nine-month period ended September 30, 2014.

Liabilities Measured at Fair Value on a Recurring Basis

Following are the disclosures related to our liabilities that are measured at fair value on a recurring basis (in thousands):

Fair Value at September 30, 2014	**Level 1**	**Level 2**	**Level 3**
Measured on a recurring basis:			
Derivative contract, net	$ -	$(2,032)	$ -

Fair Value at December 31, 2013	**Level 1**	**Level 2**	**Level 3**
Measured on a recurring basis:			
Derivative contract, net	$ -	$(2,900)	$ -

We did not have any assets measured at fair value on a recurring basis at September 30, 2014 or December 31, 2013.

See Note 9 for more details regarding our derivative contracts.

Fair Value Disclosures for Financial Assets and Liabilities

We determined that 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 September 30, 2014, 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):

	September 30, 2014	**December 31, 2013**
Carrying value	$ 208,541	$ 132,616
Fair value	208,574	126,786

Note 9. Derivative Financial Instrument

From time to time, we may 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 September 30, 2014, 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 September 30, 2014, the one-month LIBOR rate was 0.15% 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. The estimated amount that we expect to reclassify from accumulated other comprehensive loss to net income within the next twelve months is $1.1 million at September 30, 2014.

At September 30, 2014 and December 31, 2013, the fair value of our derivative instrument was included in our Consolidated Balance Sheets as follows (in thousands):

Balance Sheet Information	**Fair Value of Liability Derivatives**	
Derivatives Designated as Hedging Instruments	**Location in Balance Sheet**	**September 30, 2014**
Interest Rate Swap Contract	Accrued liabilities	$ 1,213
	Other long-term liabilities	819
		2,032

Balance Sheet Information	**Fair Value of Liability Derivatives**	
Derivatives Designated as Hedging Instruments	**Location in Balance Sheet**	**December 31, 2013**
Interest Rate Swap Contract	Accrued liabilities	$ 1,215
	Other long-term liabilities	1,685
		$ 2,900

The effect of derivative instruments on our Consolidated Statements of Operations for the three- and nine-month periods ended September 30, 2014 and 2013 was as follows (in thousands):

Derivatives in Cash Flow Hedging Relationships	**Amount of Gain Recognized in**	**Location of Loss Reclassified from Accumulated OCI into Income (Effective**	**Amount of Loss Reclassified from**	**Location of Loss Recognized in Income on Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing)**	**Amount of Loss Recognized in Income on**

	Accumulated OCI (Effective Portion)	Portion)	Accumulated OCI into Income (Effective Portion)		Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing)
Three Months Ended					
September 30, 2014					
Interest Rate Swap Contract	$ 179	Floor plan interest expense	$ (119)	Floor plan interest expense	$ (184)
Three Months Ended					
September 30, 2013					
Interest Rate Swap Contracts	$ 18	Floor plan interest expense	$ (134)	Floor plan interest expense	$ (173)

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Derivatives in Cash Flow Hedging Relationships	Amount of Gain Recognized in Accumulated OCI (Effective Portion)	Location of Loss Reclassified from Accumulated OCI into Income (Effective Portion)	Amount of Loss Reclassified from Accumulated OCI into Income (Effective Portion)	Location of Loss Recognized in Income on Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing)	Amount of Loss Recognized in Income on Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing)
Nine Months Ended					
September 30, 2014					
Interest Rate Swap Contract	$ 381	Floor plan interest expense	$ (370)	Floor plan interest expense	$ (543)
Nine Months Ended					
September 30, 2013					
Interest Rate Swap Contracts	$ 914	Floor plan interest expense	$ (606)	Floor plan interest expense	$ (1,064)

See also Note 8.

Note 10. Acquisitions

In the first nine months of 2014, we completed the following acquisitions, which contributed revenues of $114.6 million for the nine months ended September 30, 2014:

On January 31, 2014, we acquired Island Honda in Kahului, Hawaii.
On February 3, 2014, we acquired Stockton Volkswagen in Stockton, California.
On March 5, 2014, we acquired Honolulu Buick GMC Cadillac and Honolulu Volkswagen in Honolulu, Hawaii.
On April 1, 2014, we acquired Corpus Christi Ford in Corpus Christi, Texas.
On June 11, 2014, we acquired Beaverton GMC Buick and Portland Cadillac in Portland, Oregon.

On July 28, 2014, we acquired Bellingham GMC Buick in Bellingham, Washington.

All acquisitions were accounted for as business combinations under the acquisition method of accounting. The results of operations of the acquired stores are included in our consolidated financial statements from the date of acquisition.

No portion of the purchase price was paid with our equity securities. The following table summarizes the consideration paid for the acquisitions and the amount of identified assets acquired and liabilities assumed as of the acquisition date (in thousands):

	Consideration
Cash paid, net of cash acquired	$ 81,558
Debt issued	3,161
	84,719

	Assets Acquired and Liabilities Assumed
Inventories	$ 44,026
Franchise value	6,823
Property and equipment	17,313
Other assets	430
Other liabilities	(107)
	68,485
Goodwill	16,234
	$ 84,719

For the three- and nine-month periods ended September 30, 2014, we recorded acquisition expense of $0.9 million and $1.1 million, respectively, primarily related to the DCH acquisition which was completed on October 1, 2014. See also Note 14. Additionally, in the first quarter of 2014, we assumed a contract associated with an acquisition and determined the remaining term would not provide economic benefit. As a result, we recorded costs of $1.4 million associated with the contract. These amounts are included as a component of selling, general and administrative expense in our Consolidated Statements of Operations. We did not have any material acquisition-related expenses in 2013.

We account for franchise value as an indefinite-lived intangible asset. We expect the full amount of the goodwill recognized to be deductible for tax purposes.

The following unaudited pro forma summary presents consolidated information as if all acquisitions in the three- and nine-month periods ended September 30, 2013 and 2014 had occurred on January 1, 2013 (in thousands, except for per share amounts):

Three Months Ended September 30,	2014	2013
Revenue	$1,297,479	$1,162,850
Income from continuing operations, net of tax	34,542	31,959
Basic income per share from continuing operations, net of tax	1.32	1.24
Diluted income per share from continuing operations, net of tax	1.31	1.22

Nine Months Ended September 30,	2014	2013
Revenue	$3,652,673	$3,280,183
Income from continuing operations, net of tax	95,141	81,387
Basic income per share from continuing operations, net of tax	3.65	3.16
Diluted income per share from continuing operations, net of tax	3.61	3.11

These amounts have been calculated by applying our accounting policies and estimates. The results of the acquired stores have been adjusted to reflect the following: depreciation on a straight-line basis over the expected lives for property and equipment; accounting for inventory on a specific identification method; and recognition of interest expense for real estate financing related to stores where we purchased the facility. No nonrecurring pro forma adjustments directly attributable to the acquisitions are included in the reported pro forma revenues and earnings.

Note 11. Discontinued Operations

We classify an asset group as held for sale if the location has been sold, 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.

In April 2014, the Financial Accounting Standards Board (FASB) issued an accounting standard update that amends the accounting guidance related to discontinued operations. This amendment defines discontinued operations as a component or group of components that is disposed of or is classified as held for sale and represents a strategic shift that has or will have a major effect on an entity's operations and financial results. We early adopted this guidance in the third quarter of 2014 and, as a result, 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.

On May 1, 2014, we completed the sale of one store which had been classified as held for sale since October 2012. This store's operations have been reclassified to discontinued operations in our Consolidated Statement of Operations, on a comparable basis for all periods presented.

In September 2014, we determined two operating stores met the criteria to be classified as held for sale. One of the stores was under contract to sell and the other was being actively marketed for sale by us and third party brokers. For the nine months ended September 30, 2014 and 2013, income from continuing operations before income taxes of the two operating stores was immaterial.

Assets held for sale included the following (in thousands):

	September 30, 2014	**December 31, 2013**
Inventories	$ 6,551	$ 8,260
Property, plant and equipment	1,829	1,194
Intangible assets	540	2,072

	$ 8,920	$ 11,526

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

	September 30, 2014	**December 31, 2013**
Floor plan notes payable	$ 4,776	$ 6,271

Certain financial information related to discontinued operations was as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2014	2013	2014	2013
Revenue	$-	$8,712	$12,569	$27,590
Pre-tax income (loss) from discontinued operations	$-	$237	$(467)	$929
Net gain on disposal activities	-	-	5,744	-
	-	237	5,277	929
Income tax expense	-	(110)	(2,098)	(355)
Income from discontinued operations, net of income tax expense	$-	$127	$3,179	$574
Goodwill and other intangible assets disposed of	-	-	221	-
Cash generated from disposal activities	-	-	10,617	-
Floor plan debt paid in connection with disposal activities	-	-	3,311	-

Actual floor plan interest expense for a store classified as discontinued operations is directly related to the store's new vehicles. Interest expense related to our used vehicle inventory financing and revolving line of credit is allocated based on the working capital level of the store. For the nine months ended September 30, 2014 and 2013, interest expense included as a component of discontinued operations was immaterial.

Note 12. 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. Our Restated Articles of Incorporation require that the Class A and Class B common stock 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, which would have the effect of adversely altering 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 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 for the three- and nine-month periods ended September 30, 2014 and 2013 (in thousands, except per share amounts):

Three Months Ended September 30,	**2014**		**2013**	
Basic EPS from Continuing Operations	**Class A**	**Class B**	**Class A**	**Class B**
Numerator:				
Income from continuing operations applicable to common stockholders	$31,149	$3,388	$27,831	$3,060
Distributed income applicable to common stockholders	(3,765)	(409)	(3,030)	(333)
Basic undistributed income from continuing operations applicable to common stockholders	$27,384	$2,979	$24,801	$2,727
Denominator:				
Weighted average number of shares outstanding used to calculate basic income per share	23,556	2,562	23,304	2,562
Basic income per share from continuing operations applicable to common stockholders	$1.32	$1.32	$1.19	$1.19
Basic distributed income per share from continuing operations applicable to common stockholders	(0.16)	(0.16)	(0.13)	(0.13)
Basic undistributed income per share from continuing operations applicable to common stockholders	$1.16	$1.16	$1.06	1.06

Three Months Ended September 30,	**2014**		**2013**	
Diluted EPS from Continuing Operations	**Class A**	**Class B**	**Class A**	**Class B**
Numerator:				
Distributed income applicable to common stockholders	$3,765	$409	$3,030	$333
Reallocation of distributed income as a result of conversion of dilutive stock options	3	(3)	5	(5)
Reallocation of distributed income due to conversion of Class B to Class A common shares outstanding	406	-	328	-
Diluted distributed income applicable to common stockholders	$4,174	$406	$3,363	$328
Undistributed income from continuing operations applicable to common stockholders	$27,384	$2,979	$24,801	$2,727
Reallocation of undistributed income as a result of conversion of dilutive stock options	28	(28)	39	(39)
Reallocation of undistributed income due to conversion of Class B to Class A	2,951	-	2,688	-
Diluted undistributed income from continuing operations applicable to common stockholders	$30,363	$2,951	$27,528	$2,688
Denominator:				
Weighted average number of shares outstanding used to calculate basic income per share from continuing operations	23,556	2,562	23,304	2,562
Weighted average number of shares from stock options	241	-	371	-
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	26,359	2,562	26,237	2,562
Diluted income per share from continuing operations applicable to common stockholders	$1.31	$1.31	$1.18	$1.18
Diluted distributed income per share from continuing operations applicable to common stockholders	(0.16)	(0.16)	(0.13)	(0.13)
Diluted undistributed income per share from continuing operations applicable to common stockholders	$1.15	1.15	1.05	1.05

Three Months Ended September 30,	**2014**		**2013**	
Diluted EPS	**Class A**	**Class B**	**Class A**	**Class B**
Antidilutive Securities				
Shares issuable pursuant to stock options not included since they were antidilutive	13	-	14	-

Nine Months Ended September 30,	2014		2013	
Basic EPS from Continuing Operations	**Class A**	**Class B**	**Class A**	**Class B**
Numerator:				
Income from continuing operations applicable to common stockholders	$85,124	$9,277	$70,063	$7,991
Distributed income applicable to common stockholders	(10,578)	(1,153)	(6,031)	(688)
Basic undistributed income from continuing operations applicable to common stockholders	$74,546	$8,124	$64,032	$7,303
Denominator:				
Weighted average number of shares outstanding used to calculate basic income per share	23,509	2,562	23,137	2,639
Basic income per share from continuing operations applicable to common stockholders	$3.62	$3.62	$3.03	$3.03
Basic distributed income per share from continuing operations applicable to common stockholders	(0.45)	(0.45)	(0.26)	(0.26)
Basic undistributed income per share from continuing operations applicable to common stockholders	$3.17	$3.17	$2.77	$2.77

Nine Months Ended September 30,	2014		2013	
Diluted EPS from Continuing Operations	**Class A**	**Class B**	**Class A**	**Class B**
Numerator:				
Distributed income applicable to common stockholders	$10,578	$1,153	$6,031	$688
Reallocation of distributed income as a result of conversion of dilutive stock options	12	(12)	10	(10)
Reallocation of distributed income due to conversion of Class B to Class A common shares outstanding	1,141	-	678	-
Diluted distributed income applicable to common stockholders	$11,731	$1,141	$6,719	$678
Undistributed income from continuing operations applicable to common stockholders	$74,546	$8,124	$64,032	$7,303
Reallocation of undistributed income as a result of conversion of dilutive stock options	82	(82)	107	(107)
Reallocation of undistributed income due to conversion of Class B to Class A	8,042	-	7,196	-
Diluted undistributed income from continuing operations applicable to common stockholders	$82,670	$8,042	$71,335	$7,196
Denominator:				
Weighted average number of shares outstanding used to calculate basic income per share from continuing operations	23,509	2,562	23,137	2,639
Weighted average number of shares from stock options	266	-	383	-
Conversion of Class B to Class A common shares outstanding	2,562	-	2,639	-
Weighted average number of shares outstanding used to calculate diluted income per share from continuing operations	26,337	2,562	26,159	2,639
Diluted income per share from continuing operations applicable to common stockholders	$3.58	$3.58	$2.98	$2.98
Diluted distributed income per share from continuing operations applicable to common stockholders	(0.45)	(0.45)	(0.26)	(0.26)
Diluted undistributed income per share from continuing operations applicable to common stockholders	$3.13	$3.13	$2.72	2.72

Nine Months Ended September 30,	2014		2013	
Diluted EPS	**Class A**	**Class B**	**Class A**	**Class B**
Antidilutive Securities				
Shares issuable pursuant to stock options not included since they were antidilutive	13	-	17	-

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Note 13. Recent Accounting Pronouncements

On May 28, 2014, the FASB issued an accounting standard update 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 is effective for fiscal years beginning after December 15, 2016. Early application is not permitted. 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. We have not yet selected a transition method nor have we determined the effect of the standard on our ongoing financial reporting.

Note 14. Subsequent Events

Acquisitions

On October 1, 2014, we completed the purchase of all of the issued and outstanding shares of the capital stock of DCH Auto Group (USA) Inc., which includes 27 stores located in New York, New Jersey and California. The purchase price was $669.5 million, comprised of $364 million in cash, the issuance of 268,770 shares of Lithia Class A common stock with a value of $22.5 million, incurring $230 million of vehicle floor plan debt financing, and the assumption of non-floor plan debt of $53 million. In conjunction with the transaction, we increased our syndicated credit facility by $700 million and we expect to increase outstanding mortgage debt by $100 million.

On October 6, 2014, we acquired the inventory, equipment and intangible assets of Harris Nissan in Clovis, California for $7.8 million in cash.

Credit Facility

On October 1, 2014, we amended our existing credit facility to increase the total financing commitment to $1.7 billion. 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.

New Market Tax Credit

In October 2014, we acquired a 99.9% membership interest in USB NMTC Fund 2014-1, LLC (“the LLC”). The LLC was formed by U.S. Bancorp Community Development Corporation, which invests in a variety of entities providing capital for businesses in distressed or low income areas. We expect these investments will generate new market tax credits that may be used to reduce our federal income tax liability. The transaction obligates us to contribute $37.1

million to the entity over the next 24 months.

Common Stock Dividend

On October 27, 2014, our Board of Directors approved a dividend of $0.16 per share on our Class A and Class B common stock related to our third quarter 2014 financial results. The dividend will total approximately $4.2 million and will be paid on December 5, 2014 to shareholders of record on November 21, 2014.

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 constitutes 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, "intend," "forecast," "anticipate," "believe," "estimate," "predict," "potential," "likely," "goal," "strategy," "future," "maintain the negative of these terms or other comparable terminology. 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 maintaining SG&A as a percentage of gross profit in the mid to upper 60% range and targeting incremental throughput of 50% on a same store basis.
- Our belief that the compressed used vehicle retail gross profit margins are limited to the third and fourth quarters of 2014.
- Anticipated availability of liquidity from our unfinanced operating real estate.
- Anticipated levels of capital expenditures in the future.
- Our strategies for customer retention, growth, market position, financial results and risk management.

The forward-looking statements contained in this Form 10-Q involve known and unknown risks, uncertainties and situations that may cause our actual results, level of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements 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 Annual Report on Form 10-K, as supplemented and amended from time to time in Quarterly Reports on Form 10-Q and in 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. While we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements, and our actual results of operations, financial condition and liquidity and development of the industries in which we operate may differ materially from those made in or suggested by the forward-looking statements in this Form 10-Q. 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 October 31, 2014, we offer 30 brands of new vehicles and all brands of used vehicles in 129 stores in the United

States and online at Lithia.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 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 our customers 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, 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 September 30, 2014 and 2013, we reported income from continuing operations, net of tax, of $34.5 million, or $1.31 per diluted share, and $30.9 million, or $1.18 per diluted share, respectively.

For the nine months ended September 30, 2014 and 2013, we reported income from continuing operations, net of tax, of $94.4 million, or $3.58 per diluted share, and $78.1 million, or $2.98 per diluted share, respectively.

Discontinued Operations

We early adopted the amendment to the accounting guidance related to discontinued operations in the third quarter of 2014. This amendment defines discontinued operations as a component or group of components that is disposed of or is classified as held for sale and represents a strategic shift that has or will have a major effect on an entity's operations and financial results. 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.

We realized income from discontinued operations, net of tax, for the three months ended September 30, 2013, of $127,000. Due to our early adoption of the amended accounting guidance, no income from discontinued operations was recorded for the three months ended September 30, 2014. Income from discontinued operations, net of tax, for the nine months ended September 30, 2014 and 2013 totaled $3.2 million and $574,000, respectively. See Note 11 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 for the three and nine months ended September 30, 2014 and 2013 (dollars in thousands):

Three months ended September 30, 2014	**Revenues**	**Percent of Total Revenues**		**Gross Profit**	**Gross Profit Margin**		**Percent of Total Gross Profit**	
New vehicle	$732,121	56.4	%	$47,648	6.5	%	24.1	%
Used vehicle retail	340,522	26.3		43,898	12.9		22.2	
Used vehicle wholesale	48,853	3.8		504	1.0		0.3	
Finance and insurance(1)	46,855	3.6		46,855	100.0		23.7	

Service, body and parts	120,772	9.3		58,421	48.4		29.5		
Fleet and other	7,988	0.6		514	6.4		0.2		
	$1,297,111	100.0	%	$197,840	15.3	%	100.0	%	

Three months ended September 30, 2013	**Revenues**	**Percent of Total Revenues**		**Gross Profit**	**Gross Profit Margin**		**Percent of Total Gross Profit**	
New vehicle	$604,135	56.5	%	$38,586	6.4	%	23.3	%
Used vehicle retail	280,734	26.3		41,641	14.8		25.2	
Used vehicle wholesale	43,396	4.1		710	1.6		0.4	
Finance and insurance(1)	37,132	3.5		37,132	100.0		22.5	
Service, body and parts	97,784	9.1		46,991	48.1		28.4	
Fleet and other	6,109	0.5		329	5.4		0.2	
	$1,069,290	100.0	%	$165,389	15.5	%	100.0	%

Nine months ended September 30, 2014	**Revenues**	**Percent of Total Revenues**		**Gross Profit**	**Gross Profit Margin**		**Percent of Total Gross Profit**	
New vehicle	$2,006,127	55.8	%	$132,666	6.6	%	23.6	%
Used vehicle retail	952,890	26.5		128,761	13.5		22.9	
Used vehicle wholesale	135,832	3.8		3,339	2.5		0.6	
Finance and insurance(1)	130,324	3.6		130,324	100.0		23.2	
Service, body and parts	339,726	9.4		165,435	48.7		29.4	
Fleet and other	32,120	0.9		1,676	5.2		0.3	
	$3,597,019	100.0	%	$562,201	15.6	%	100.0	%

Nine months ended September 30, 2013	**Revenues**	**Percent of Total Revenues**		**Gross Profit**	**Gross Profit Margin**		**Percent of Total Gross Profit**	
New vehicle	$1,667,063	55.9	%	$112,021	6.7	%	23.8	%
Used vehicle retail	778,427	26.1		115,507	14.8		24.5	
Used vehicle wholesale	120,593	4.0		2,379	2.0		0.5	
Finance and insurance(1)	103,013	3.5		103,013	100.0		21.8	
Service, body and parts	282,686	9.5		137,463	48.6		29.1	
Fleet and other	29,093	1.0		1,277	4.4		0.3	
	2,980,875	100.0	%	$471,660	15.8	%	100.0	%

(1) Commissions reported net of anticipated cancellations.

Same Store Operating Data

We believe that same store comparisons are an important indicator of our financial performance. Same store measures demonstrate our ability to grow our business at 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 August 2013 would be included in same store operating data beginning in September 2014, after its first full complete comparable month of operation. The third quarter operating results for the same store comparisons would include results for that store in only the period of September for both comparable periods.

New Vehicle Revenue and Gross Profit

(Dollars in thousands, except per unit amounts)	Three Months Ended September 30, 2014	2013	Increase	% Increase
Reported				
Revenue	$732,121	$604,135	$127,986	21.2 %
Gross profit	$47,648	$38,586	$9,062	23.5
Gross margin	6.5 %	6.4 %	10 bp(1)	
Retail units sold	21,320	18,109	3,211	17.7
Average selling price per retail unit	$34,340	$33,361	$979	2.9
Average gross profit per retail unit	$2,235	$2,131	$104	4.9
Same store				
Revenue	$668,677	$604,135	$64,542	10.7 %
Gross profit	$43,366	$38,586	$4,780	12.4
Gross margin	6.5 %	6.4 %	10 bp	
Retail units sold	19,344	18,109	1,235	6.8
Average selling price per retail unit	$34,568	$33,361	$1,207	3.6
Average gross profit per retail unit	$2,242	$2,131	$111	5.2

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

(Dollars in thousands, except per unit amounts)	Nine Months Ended September 30, 2014	2013	Increase (Decrease)	% Increase (Decrease)
Reported				
Revenue	$2,006,127	$1,667,063	$ 339,064	20.3 %
Gross profit	$132,666	$112,021	$ 20,645	18.4
Gross margin	6.6 %	6.7 %	(10)bp[1]	
Retail units sold	59,040	49,853	9,187	18.4
Average selling price per retail unit	$33,979	$33,440	$ 539	1.6
Average gross profit per retail unit	$2,247	$2,247	$ -	-
Same store				
Revenue	$1,844,436	$1,664,438	$ 179,998	10.8 %
Gross profit	$121,770	$111,822	$ 9,948	8.9
Gross margin	6.6 %	6.7 %	(10)bp	
Retail units sold	53,667	49,766	3,901	7.8
Average selling price per retail unit	$34,368	$33,445	$ 923	2.8
Average gross profit per retail unit	$2,269	$2,247	$ 22	1.0

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

New vehicle sales improved primarily due to volume growth as same store unit sales increased 6.8% and 7.8%, respectively, in the three- and nine-month periods ended September 30, 2014 compared to the same periods in 2013. The number of new vehicles sold in the U.S. during the first nine months of 2014 grew approximately 5.7% compared to the same period of 2013.

During the three- and nine-month periods ended September 30, 2014, same store unit sales increased in all three categories of new vehicles compared to the same periods of 2013:

Our domestic brand same store unit sales grew 7.3% and 7.8%, respectively, compared to national domestic unit sales growth of 9.0% and 5.2%, respectively.
Our import brand same store unit sales grew 4.7% and 7.2%, respectively. National import brand unit sales grew 6.5% and 5.3%, respectively.
Our luxury brand same store unit sales grew 13.2% and 10.7%, respectively, compared to national luxury brand unit sales of 21.1% and 11.8%, respectively.

Additionally, average selling prices increased on a same store basis 3.6% and 2.8%, respectively, for the three- and nine-month periods ended September 30, 2014 compared to the same period in 2013, which also contributed to new vehicle sales growth.

Recovery from the recession in our specific markets is different than the national average. Certain of our markets saw an increase in sales volumes that exceeded the national average, while others continued to lag behind the national average. As of the most recent data available, six of the twelve states where we operate, representing approximately 46% of our revenues for the nine-month period ended September 30, 2014, continue to be below the pre-recessionary vehicle registration levels experienced in 2006.

New vehicle gross profit dollars increased 23.5% and 18.4%, respectively, for the three- and nine-month periods ended September 30, 2014 compared to the same periods of 2013. On a same store basis, gross profit increased 12.4% and 8.9%, respectively, for the three- and nine-month periods ended September 30, 2014 compared to the same periods of 2013. These increases were due to a greater number of vehicles sold as well as an increase in gross profit per unit.

We focus on gross profit dollars earned per unit, not on gross margin percentage. On a same store basis, the average gross profit per new retail unit increased $111 and $22, respectively, for the three- and nine-month periods ended September 30, 2014 compared to the same periods of 2013.

New vehicle unit sales create additional used vehicle trade-in opportunities, finance and insurance sales and future service work. We balance the gross profits earned on a volume-based strategy with the incremental business generated in future periods.

Used Vehicle Retail Revenue and Gross Profit

(Dollars in thousands, except per unit amounts)	Three Months Ended September 30, 2014	2013	Increase (Decrease)	% Increase (Decrease)
Reported				
Retail revenue	$340,522	$280,734	$ 59,788	21.3 %
Retail gross profit	$43,898	$41,641	$ 2,257	5.4
Retail gross margin	12.9 %	14.8 %	(190)bp	
Retail units sold	17,710	15,496	2,214	14.3
Average selling price per retail unit	$19,228	$18,117	$ 1,111	6.1
Average gross profit per retail unit	$2,479	$2,687	$ (208)	(7.7)
Same store				
Retail revenue	$317,342	$280,734	$ 36,608	13.0 %
Retail gross profit	$41,733	$41,641	$ 92	0.2
Retail gross margin	13.2 %	14.8 %	(160)bp	
Retail units sold	16,451	15,496	955	6.2