

AUTONATION, INC.

Form 10-K

February 13, 2012

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2011

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 1-13107

AutoNation, Inc.

(Exact name of registrant as specified in its charter)

Delaware

73-1105145

(State or other jurisdiction of incorporation or organization)

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

200 SW 1st Ave

33301

Fort Lauderdale, Florida

(Zip Code)

(Address of principal executive offices)

(954) 769-6000

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class

Name of each exchange on which registered

Common Stock, Par Value \$0.01 Per Share

New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

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

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

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 new registrant was required to submit and post such files). Yes  No

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

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

As of June 30, 2011, the aggregate market value of the common stock of the registrant held by non-affiliates was approximately \$1.4 billion based on the closing price of the common stock on the New York Stock Exchange on such date (for the purpose of this calculation only, the registrant assumed that each of its directors, executive officers, and greater than 10% stockholders was an affiliate of the registrant as of June 30, 2011).

As of February 8, 2012, the registrant had 131,921,417 shares of common stock outstanding.

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the registrant's Proxy Statement relating to its 2012 Annual Meeting of Stockholders to be filed with the SEC within 120 days after the end of the fiscal year ended December 31, 2011 are incorporated herein by reference in Part III.

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AUTONATION, INC.

FORM 10-K

FOR THE FISCAL YEAR ENDED DECEMBER 31, 2011

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PART I

ITEM 1. BUSINESS

General

AutoNation, Inc., through its subsidiaries, is the largest automotive retailer in the United States. As of December 31, 2011, we owned and operated 258 new vehicle franchises from 215 stores located in the United States, predominantly in major metropolitan markets in the Sunbelt region. Our stores, which we believe are some of the most recognizable and well-known stores in our key markets, sell 32 different brands of new vehicles. The core brands of vehicles that we sell, representing approximately 90% of the new vehicles that we sold in 2011, are manufactured by Ford, Toyota, Nissan, General Motors, Honda, Mercedes-Benz, BMW, and Chrysler.

We offer a diversified range of automotive products and services, including new vehicles, used vehicles, parts and automotive repair and maintenance services (also referred to as “parts and service”), and automotive finance and insurance products (also referred to as “finance and insurance”), which includes the arranging of financing for vehicle purchases through third-party finance sources. The following charts present the contribution to total revenue and gross profit by each of new vehicle sales, used vehicle sales, parts and service, and finance and insurance in 2011.

We believe that the significant scale of our operations and the quality of our managerial talent allow us to achieve efficiencies in our key markets by, among other things, leveraging our market brands and advertising, improving asset management, implementing standardized processes, and increasing productivity across all of our stores.

We were incorporated in Delaware in 1991. For convenience, the terms “AutoNation,” “Company,” and “we” are used to refer collectively to AutoNation, Inc. and its subsidiaries, unless otherwise required by the context. Our store operations are conducted by our subsidiaries.

Operating Segments

As of December 31, 2011, we had three operating segments: Domestic, Import, and Premium Luxury. Our Domestic segment is comprised of retail automotive franchises that sell new vehicles manufactured by General Motors, Ford, and Chrysler. Our Import segment is comprised of retail automotive franchises that sell new vehicles manufactured primarily by Toyota, Honda, and Nissan. Our Premium Luxury segment is comprised of retail automotive franchises that sell new vehicles manufactured primarily by Mercedes-Benz, BMW, and Lexus. The franchises in each segment also sell used vehicles, parts and automotive repair and maintenance services, and automotive finance and insurance products. For the year ended December 31, 2011, Domestic revenue represented 34% of total revenue, Import revenue represented 37% of total revenue, and Premium Luxury revenue represented 28% of total revenue. For additional financial information regarding our three operating segments, please refer to Note 20 of the Notes to Consolidated Financial Statements set forth in Part II, Item 8 of this Form 10-K.

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Except to the extent that differences among operating segments are material to an understanding of our business taken as a whole, the description of our business in this report is presented on a consolidated basis.

### Business Strategy

We seek to be the best-run, most profitable automotive retailer in the nation. The foundation of our business model is operational excellence, with a focus on developing and maintaining satisfied relationships with our customers. In order to achieve and sustain operational excellence, we are pursuing the following strategies:

#### • Create an industry-leading automotive retail consumer experience

- Leverage our significant scale and cost structure to improve our operating efficiency

#### • Leverage information technology to enhance customer relationships and improve productivity

#### • Build powerful local brands while also building consumer awareness of the AutoNation brand

We have a well-diversified brand portfolio. In 2011, approximately 39% of our new vehicle revenue was generated by Import franchises, approximately 28% by Premium Luxury franchises, and approximately 33% was generated by Domestic franchises. While we will continue to look for acquisition and new store opportunities that meet our market and brand criteria and return on investment threshold, we do not expect significant shifts in our overall store mix in 2012.

A key component of our long-term strategy is to maximize the return on investment generated by the use of cash flow that our business generates, while maintaining a strong balance sheet. We expect to use our cash flow to make capital investments in our business, to complete dealership acquisitions, and to repurchase our common stock and/or debt. Our capital allocation decisions will be based on factors such as the expected rate of return on our investment, the market price of our common stock versus our view of its intrinsic value, the market price of our debt, the potential impact on our capital structure, our ability to complete dealership acquisitions that meet our market and brand criteria and return on investment threshold, and limitations set forth in our debt agreements. For additional information regarding our capital allocation strategy, please refer to “Liquidity and Capital Resources – Capital Allocation” in Part II, Item 7 of this Form 10-K.

Finally, we believe that our business benefits from diverse revenue streams generated by our new and used vehicle sales, parts and service business, and finance and insurance sales. Our higher-margin parts and service business has historically been less sensitive to macroeconomic trends as compared to new vehicle sales.

#### Create an Industry-Leading Automotive Retail Consumer Experience

One of our goals is to provide an industry-leading retail consumer experience at our stores in order to build customer loyalty to our brand. The following practices and initiatives support an enhanced customer retail experience:

**Improving Customer Service:** The success of our stores depends in significant part on our ability to deliver positive experiences to our customers, which generate recurring and referral business. We have developed and implemented standardized, customer-friendly sales and service processes, including a customer-friendly sales menu designed to provide clear disclosure of purchase or lease transaction terms. We also offer our customers a limited-mileage, money-back guarantee on both our new and used vehicles as an indication of our commitment to their satisfaction.

We believe these policies improve the sales and service experiences of our customers. We emphasize the importance of customer satisfaction to our key store personnel by basing a portion of their compensation on the quality of customer service they provide in connection with vehicle sales and service.

**Increasing Parts and Service Sales:** One of our goals is to have our customers bring their vehicles to our stores for all of their vehicle service, maintenance, and collision needs. Our key initiatives for our parts and service business are focused on optimizing our processes, pricing, and promotion, thus improving customer retention. Across all of our stores, we have implemented standardized service processes and marketing communications, which offer the complete range of vehicle maintenance and repair services and are focused on increasing our customer-pay service, collision, and parts business. As a result of our significant scale, we can communicate effectively with our customers. We optimize our pricing to maintain a competitive offering for commonly-performed vehicle services and repairs for like-brand vehicles within each of our markets.



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**Increasing Finance, Insurance, and Other Aftermarket Product Sales:** We continue to improve our finance and insurance business by using our standardized processes across our store network. One of our goals is to improve customer retention after the sale of the vehicle through our finance and insurance products. Our customers are presented with the “AutoNation Pledge,” which provides clear disclosure relating to the finance and insurance sales process, and with a customer-friendly finance and insurance menu, which is designed to ensure that we offer our customers the complete range of finance, insurance, protection, and other aftermarket products in a transparent manner. We offer our customers aftermarket products such as extended service contracts, maintenance programs, theft deterrent systems, and various insurance products. We continue to focus on optimizing the mix of financing sources available to promote vehicle sales and improve the customer experience.

### **Leverage Our Significant Scale and Cost Structure to Improve our Operating Efficiency**

We leverage our scale as the largest automotive retailer in the United States to drive significant cost savings in our business. The following practices and initiatives reflect our commitment to leveraging our scale and managing cost:

**Managing New Vehicle Inventories and Optimizing New Vehicle Pricing:** We manage our new vehicle inventories to optimize our stores’ supply and mix of vehicle inventory. Through the use of our planning and tracking systems in markets where our stores have critical mass in a particular brand, we view new vehicle inventories at those same brand stores in the aggregate and coordinate vehicle ordering and inventories across those stores. We manage our new vehicle inventory to achieve specific days supply targets in order to support sales volumes. We also target our new vehicle inventory purchasing to our core, or highest-volume, model packages. We are focused on maintaining appropriate inventory levels in order to minimize carrying costs. We believe our inventory management enables us to (1) respond to customer requests better than independent automotive retailers, (2) minimize carrying costs by optimizing days supply, and (3) better plan and forecast inventory levels. See also “Inventory Management” in Part II, Item 7 of this Form 10-K. Further, during 2011 we implemented a pricing strategy across our store portfolio that included the deployment of a proprietary pricing tool to capture various market pricing metrics and establish target and floor prices.

**Increasing Used Vehicle Sales and Managing Used Vehicle Inventories:** Each of our stores offers a variety of used vehicles. As the largest retailer of new vehicles, we believe that we have superior access to desirable used vehicle inventory. We are also able to realize the benefits of vehicle manufacturer-supported certified pre-owned vehicle programs, which are typically more profitable than our non-certified used vehicle sales. Our used vehicle business strategy is focused on (1) utilizing our web-based vehicle inventory management system to optimize our supply, mix, and pricing, (2) leveraging our used vehicle inventory to offer our customers a wide selection of desirable lower-cost vehicles, which are often in high demand by consumers, and (3) leveraging our scale with comprehensive used vehicle marketing programs, such as market-wide promotional events and standardized approaches to advertising that we can implement more effectively than smaller automotive retailers because of our size. We have deployed used vehicle specialists in each of our key markets to assist us in executing our strategy.

**Centralizing Store Back-Office Operations in Our Shared Services Center:** We have centralized key store-level accounting and administrative activities in our Shared Services Center located in Irving, Texas. The initial or “core” phase included the centralization of basic accounting functions. We have implemented the core phase in substantially all of our stores. In the “extended” phase, we are transferring additional accounting responsibilities, including the accounting for vehicle sales, lien payoffs, receipt of vehicles, floorplan transactions, and manufacturer payables, as well as certain other reconciliation processes. We have substantially implemented the extended phase in 156 of our 215 stores as of December 31, 2011, and we plan to implement the extended phase in substantially all remaining stores in 2012. By shifting these functions from the stores to the Shared Services Center, we have improved financial controls and lowered servicing costs. We also believe that the standardization of these processes across our stores improves the customer experience.

**Increasing Employee Productivity:** Our compensation and employee training programs drive productivity through standardized operating practices. Our standardized compensation guidelines and common element pay plans at our stores take into account our sales volume, customer satisfaction, gross margin objectives, vehicle brand, and store size. Our goals related to compensation are to improve employee productivity, to reward and retain high-performing employees, and to ensure appropriate variability of our compensation expense. Further, our customized

comprehensive training program for key store employees facilitates standardized operating practices

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and policies across all of our stores. Our training program educates our key store employees about their respective job roles and responsibilities, applicable laws and regulations, and our standardized processes in all of our areas of operation, including sales, finance and insurance, and parts and service. We also require all of our employees, from our senior management to our technicians, to participate in our Business Ethics Program. In addition, we run several AutoNation University programs for our general managers and sales and service managers and associates to develop leadership skills and to ensure consistent execution of our practices and policies. We expect our comprehensive training program to improve our productivity by ensuring that all of our employees consistently execute our business strategy and manage our daily operations in accordance with our common processes and policies, applicable laws and regulations, and our high standards of business ethics.

**Managing Costs:** We actively manage our business and leverage our scale to reduce costs. We continue to focus on developing national vendor relationships to standardize our stores' approach to purchasing certain equipment, supplies, and services, and to improve our cost efficiencies. For example, we realize cost efficiencies with respect to advertising and facilities maintenance that are generally not available to smaller automotive retailers.

**Leverage Information Technology to Enhance Customer Relationships and Improve Productivity**

We use a web-based customer relationship management tool across all of our stores, which enables us to promote and sell our vehicles and other products more effectively by facilitating better understanding of our customer traffic flows and better management of our showroom sales processes and customer relationships. We have developed a company-wide customer database that captures information on our stores' existing and potential customers. We believe our customer database enables us to implement more effectively our vehicle sales and service marketing programs. We expect our customer database and other tools to empower us to implement our customer relationship strategy more effectively and improve our productivity.

We also use the Internet to acquire and develop customer leads and referrals. Our website facilitates consumer research about vehicle purchases, including vehicle specifications and financing options. In addition, we are focused on connecting with our customers through social media websites, such as Facebook, Twitter, and YouTube. See "Sales and Marketing" below.

**Build a Powerful Local Brand in Each of Our Markets While Also Building Consumer Awareness of the AutoNation Brand**

In many of our key markets where we have significant presence, we are marketing our non-premium luxury stores under a local retail brand. We continue to position these local retail brands to communicate to customers the key features that we believe differentiate our stores in our branded markets from our competitors, such as the large inventory available for customers, our sales, service, and finance and insurance standardized processes, and the competitive pricing we offer for widely available vehicle repair services. We believe that this consolidated local market strategy enables us to achieve marketing and advertising cost savings and efficiencies that generally are not available to many of our local competitors. We also believe that we can create strong retail brand awareness in our markets.

Further, through our website, store signage, and media presence, we are creating consumer awareness of the AutoNation brand. Our goal is that our customers will increasingly associate their local dealership not only with the local-market brand, but also with the national AutoNation brand.

We have fifteen local brands in our key markets, including "Maroone" in South Florida; "GO" in Denver, Colorado; "AutoWay" in Tampa, Florida; "Bankston" in Dallas, Texas; "Courtesy" in Orlando, Florida; "Desert" in Las Vegas, Nevada; "Team" in Atlanta, Georgia; "Mike Shad" in Jacksonville, Florida; "Dobbs" in Memphis, Tennessee; "Fox" in Baltimore, Maryland; "Mullinax" in Cleveland, Ohio; "Appleway" in Spokane, Washington; "Champion" in South Texas; "Power" in Southern California and Arizona; and "AutoWest" in Northern California. The stores we operate under these local retail brands as of December 31, 2011, accounted for approximately 69% of our total revenue during 2011.

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## Operations

As of December 31, 2011, we operated stores in the following states:

State	Number of Stores	Number of Franchises	% of Total Revenue <sup>(1)</sup>
Florida	58	66	27
Texas	34	42	20
California	36	43	19
Colorado	17	24	7
Arizona	13	15	5
Nevada	10	11	4
Georgia	10	11	4
Washington	12	19	3
Illinois	5	5	3
Tennessee	7	8	3
Ohio	4	4	1
Minnesota	1	1	1
Virginia	2	2	1
Maryland	4	5	1
Alabama	2	2	1
Total	215	258	100

<sup>(1)</sup> Revenue by state includes non-store activities, such as collision centers, e-commerce activities, and an auction operation.

The following table sets forth information regarding new vehicle revenues and retail new vehicle unit sales for the year ended, and the number of franchises owned as of, December 31, 2011:

	New Vehicle Revenues (in millions)	Retail New Vehicle Unit Sales	% of Total Retail New Vehicle Units Sold	Franchises Owned
Domestic:				
Ford, Lincoln	\$1,341.5	41,821	18.7	42
Chevrolet, Buick, Cadillac, GMC	887.8	27,082	12.1	44
Chrysler, Jeep, Dodge	242.4	7,432	3.3	21
Domestic Total	2,471.7			