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 September 30, 2004

OR

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

Commission file number 1-13395

SONIC AUTOMOTIVE, INC.
(Exact name of registrant as specified in its charter)

DELAWARE (State or other jurisdiction of incorporation or organization)	**56-2010790** (I.R.S. Employer Identification No.)
5401 E. Independence Blvd., Charlotte, North Carolina (Address of principal executive offices)	**28212** (Zip Code)

(704) 566-2400
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes ☒ No ☐

As of October 29, 2004, there were 29,344,693 shares of Class A Common Stock and 12,029,375 shares of Class B Common Stock outstanding.

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PART I - FINANCIAL INFORMATION

Item 1: Condensed Consolidated Financial Statements.

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(Dollars and shares in thousands except per share amounts)
(Unaudited)

	Three-Month Periods Ended September 30,	
	2003	2004
Revenues:		
New vehicles	$ 1,157,648	$ 1,209,668
Used vehicles	315,700	311,972
Wholesale vehicles	115,780	139,480
Total vehicles	1,589,128	1,661,120
Parts, service and collision repair	245,099	269,549
Finance, insurance and other	53,380	52,303
Total revenues	1,887,607	1,982,972
Cost of sales	1,604,267	1,686,851
Gross profit	283,340	296,121
Selling, general and administrative expenses	221,342	240,118
Depreciation and amortization	2,975	4,209
Operating income	59,023	51,794
Other income / (expense):		
Interest expense, floor plan	(4,626)	(6,516)
Interest expense, other, net	(10,273)	(9,628)
Other income / (expense), net	(13,937)	65
Total other expense	(28,836)	(16,079)
Income from continuing operations before income taxes	30,187	35,715
Provision for income taxes	10,932	13,409
Income from continuing operations	19,255	22,306
Discontinued operations:		
Loss from operations and the sale of discontinued franchises	(2,830)	(4,836)
Income tax benefit	1,116	1,811
Loss from discontinued operations	(1,714)	(3,025)
Net income	$ 17,541	$ 19,281
Basic net income (loss) per share:		
Income per share from continuing operations	$ 0.47	$ 0.54
Loss per share from discontinued operations	(0.04)	(0.07)
Net income per share	$ 0.43	$ 0.47
Weighted average common shares outstanding	40,926	41,349
Diluted net income (loss) per share:		
Income per share from continuing operations	$ 0.45	$ 0.53
Loss per share from discontinued operations	(0.04)	(0.07)
Net income per share	$ 0.41	$ 0.46
Weighted average common shares outstanding	43,022	42,164
Dividends declared per common share	$ 0.10	$ 0.12

See notes to unaudited condensed consolidated financial statements.

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SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(Dollars and shares in thousands except per share amounts)
(Unaudited)

	Nine-Month Periods Ended September 30,	
	2003	2004
Revenues:		
New vehicles	$ 3,202,143	$ 3,359,251
Used vehicles	895,571	895,356
Wholesale vehicles	314,791	380,735
Total vehicles	4,412,505	4,635,342
Parts, service and collision repair	704,147	773,123
Finance, insurance and other	150,483	144,547
Total revenues	5,267,135	5,553,012
Cost of sales	4,458,683	4,700,572
Gross profit	808,452	852,440
Selling, general and administrative expenses	636,729	673,978
Depreciation and amortization	7,797	12,207
Operating income	163,926	166,255
Other income / (expense):		
Interest expense, floor plan	(15,495)	(18,972)
Interest expense, other, net	(29,455)	(26,713)
Other income / (expense), net	(13,849)	61
Total other expense	(58,799)	(45,624)
Income from continuing operations before taxes and cummulative effect of change in accounting principle	105,127	120,631
Provision for income taxes	38,278	44,513
Income from continuing operations before cummulative effect of change in accounting principle	66,849	76,118
Discontinued operations:		
Loss from operations and the sale of discontinued franchises	(5,682)	(7,520)
Income tax benefit	2,195	2,860
Loss from discontinued operations	(3,487)	(4,660)
Income before cumulative effect of change in accounting principle	63,362	71,458
Cumulative effect of change in accounting principle, net of tax benefit of $3,325	(5,619)	—
Net income	$ 57,743	$ 71,458
Basic net income (loss) per share:		
Income per share from continuing operations	$ 1.64	$ 1.84
Loss per share from discontinued operations	(0.09)	(0.11)
Income per share before cumulative effect of change in accounting principle	1.55	1.73
Cumulative effect of change in accounting principle	(0.14)	—
Net income per share	$ 1.41	$ 1.73
Weighted average common shares outstanding	40,858	41,328
Diluted net income (loss) per share:		
Income per share from continuing operations	$ 1.58	$ 1.79
Loss per share from discontinued operations	(0.08)	(0.11)
Income per share before cumulative effect of change in accounting principle	1.50	1.68
Cumulative effect of change in accounting principle	(0.13)	—
Net income per share	$ 1.37	$ 1.68
Weighted average common shares outstanding	42,288	42,439
Dividends declared per common share	$ 0.10	$ 0.32

See notes to unaudited condensed consolidated financial statements.

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SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(Dollars in thousands)

	December 31, 2003	September 30, 2004 (Unaudited)
ASSETS		
Current Assets:		
Cash	$ 82,082	$ —
Receivables, net	306,498	330,512
Inventories	1,046,909	1,015,026
Assets held for sale	88,990	83,930
Other current assets	29,718	19,540
Total current assets	1,554,197	1,449,008
Property and equipment, net	125,356	160,781
Goodwill, net	909,091	1,051,782
Other intangible assets, net	75,230	90,847
Other assets	22,355	32,025
Total assets	$2,686,229	$ 2,784,443
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Notes payable - floor plan	$ 996,370	$ 925,356
Trade accounts payable	63,577	64,322
Accrued interest	13,851	10,315
Other accrued liabilities	121,744	175,325
Current maturities of long-term debt	1,387	3,984
Total current liabilities	1,196,929	1,179,302
Long-term debt	694,898	747,808
Other long-term liabilities	19,136	22,859
Deferred income taxes	76,933	78,441
Stockholders' Equity:		
Class A Common Stock; $.01 par value; 100,000,000 shares authorized; 38,588,913 shares issued and 29,192,549 shares outstanding at December 31, 2003; 39,673,697 shares issued and 29,325,833 shares outstanding at September 30, 2004	384	394
Class B Common Stock; $.01 par value; 30,000,000 shares authorized; 12,029,375 shares issued and outstanding at December 31, 2003 and September 30, 2004	121	121
Paid-in capital	416,892	434,927
Retained earnings	402,799	461,013
Accumulated other comprehensive loss	(4,419)	(2,061)
Treasury Stock, at cost (9,396,364 shares held at December 31, 2003 and 10,347,864 shares held at September 30, 2004)	(117,444)	(138,361)
Total stockholders' equity	698,333	756,033
Total liabilities and stockholders' equity	$2,686,229	$ 2,784,443

See notes to unaudited condensed consolidated financial statements.

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SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY
(Dollars and shares in thousands)
(Unaudited)

	Class A Common Stock		Class B Common Stock						
	Shares	Amount	Shares	Amount	Paid-In Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Loss	Total Stockholders' Equity
Balance at December 31, 2003	**38,589**	**$ 384**	**12,029**	**$ 121**	**$ 416,892**	**$ 402,799**	**$ (117,444)**	**$ (4,419)**	**$ 698,333**
Comprehensive Income:									
Net Income						71,458			71,458
Change in fair value of interest rate swaps, net of tax expense of $1,508								2,358	2,358
Total comprehensive income, net of tax									73,816
Shares issued under stock compensation plans	1,085	10			13,686				13,696
Income tax benefit associated with stock compensation plans					4,349				4,349
Dividends declared ($0.32 per share)						(13,244)			(13,244)
Purchases of treasury stock							(20,917)		(20,917)
Balance at September 30, 2004	**39,674**	**$ 394**	**12,029**	**$ 121**	**$ 434,927**	**$ 461,013**	**$ (138,361)**	**$ (2,061)**	**$ 756,033**

See notes to unaudited condensed consolidated financial statements.

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in thousands)
(Unaudited)

	Nine Months Ended September 30,	
	2003	**2004**
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 57,743	$ 71,458
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	9,293	12,235
Debt issue cost amortization	348	428
Debt discount amortization, net of premium amortization	749	109
Cumulative effect of change in accounting principle, net of tax	5,619	—
Equity interest in gains of investees	(521)	(549)
(Gain) / Loss on disposal of assets	(4,725)	947
Loss on retirement of debt	13,928	—
Income tax benefit associated with stock compensation plans	2,003	4,349
Changes in assets and liabilities that relate to operations:		
Receivables	(7,631)	(23,930)
Inventories	50,963	107,937
Other assets	(11,465)	826
Notes payable - floor plan	(65,949)	(110,836)
Trade accounts payable and other liabilities	35,813	56,801
Total adjustments	28,425	48,317
Net cash provided by operating activities	86,168	119,775
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of businesses, net of cash acquired	(53,590)	(194,012)
Purchases of property and equipment	(58,368)	(73,266)
Proceeds from sales of property and equipment	25,975	32,324
Proceeds from sales of dealerships	24,821	32,477
Net cash used in investing activities	(61,162)	(202,477)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net borrowings on revolving credit facilities	9,361	21,878
Proceeds from long-term debt	194,389	164
Payments on long-term debt	(2,275)	(1,815)
Repurchase of debt securities	(192,391)	—
Purchases of treasury stock	(17,814)	(20,917)
Issuance of shares under stock compensation plans	8,099	13,696
Dividends paid	—	(12,386)
Net cash (used in)/provided by financing activities	(631)	620
NET INCREASE / (DECREASE) IN CASH	24,375	(82,082)
CASH, BEGINNING OF PERIOD	10,576	82,082
CASH, END OF PERIOD	$ 34,951	$ —
SUPPLEMENTAL SCHEDULE OF NON-CASH FINANCING ACTIVITIES:		
Long-term debt assumed in purchase of businesses, including premium of $7,254	$ —	$ 33,824
Change in fair value of cash flow hedging instruments (net of tax benefit of $460 for the nine months ended September 30, 2003 and net of tax expense of $1,508 for the nine months ended September 30, 2004)	$ 720	$ 2,358
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid for interest, net of amount capitalized	$ 52,368	$ 53,626
Cash paid for income taxes	$ 20,792	$ 12,871

See notes to unaudited condensed consolidated financial statements.

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation - The accompanying unaudited financial information for the three and nine months ended September 30, 2004 has been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. All significant intercompany accounts and transactions have been eliminated. These unaudited condensed consolidated financial statements reflect, in the opinion of management, all material adjustments (which include only normal recurring adjustments) necessary to fairly state the financial position and the results of operations for the periods presented. The results for interim periods are not necessarily indicative of the results to be expected for the entire fiscal year. These interim financial statements should be read in conjunction with the audited consolidated financial statements of Sonic for the year ended December 31, 2003, which were included in Sonic's Annual Report on Form 10-K.

Stock-Based Compensation - Sonic accounts for stock-based compensation plans under the recognition and measurement provisions of APB Opinion No. 25, "Accounting for Stock Issued to Employees", and related interpretations. In accordance with those provisions, because the exercise price of all options granted under those plans equaled the market value of the underlying stock at the grant date, no stock-based employee compensation cost is recorded in the accompanying unaudited condensed consolidated financial statements. Using the Black-Scholes option pricing model for all options granted, the following table illustrates the effect on net income and earnings per share if Sonic had applied the fair value recognition provisions of SFAS No. 123, "Accounting for Stock-Based Compensation", to stock-based employee compensation:

	(Dollars in thousands except per share amounts)			
	Three Months Ended September 30,		Nine Months Ended September 30,	
	2003	2004	2003	2004
Net income as reported	$ 17,541	$ 19,281	$ 57,743	$ 71,458
Fair value compensation cost, net of tax benefits of $1,695 and $1,080, for the three months ended September 30, 2003 and 2004, respectively, and $4,496 and $3,505 for the nine months ended September 30, 2003 and 2004, respectively	(3,029)	(1,795)	(7,896)	(6,014)
Pro forma net income	$ 14,512	$ 17,486	$ 49,847	$ 65,444
Basic income (loss) per share:				
Net income as reported	$ 0.43	$ 0.47	$ 1.41	$ 1.73
Fair value compensation cost, net of tax benefit	(0.08)	(0.05)	(0.19)	(0.15)
Pro forma net income per share	$ 0.35	$ 0.42	$ 1.22	$ 1.58
Diluted income (loss) per share:				
Net income as reported	$ 0.41	$ 0.46	$ 1.37	$ 1.68
Fair value compensation cost, net of tax benefit	(0.07)	(0.05)	(0.19)	(0.14)
Pro forma net income per share	$ 0.34	$ 0.41	$ 1.18	$ 1.54

Cumulative Effect of a Change in Accounting Principle - The Emerging Issues Task Force ("EITF") of the FASB reached a consensus on Issue No. 02-16, "Accounting by a Customer for Certain Consideration Received from a Vendor." In accordance with Issue No. 02-16, which was effective January 1, 2003, payments received from manufacturers for floor plan assistance and certain types of advertising allowances should be recorded as a reduction of the cost of inventory and recognized as a reduction of cost of sales when the inventory is sold. The cumulative effect of the adoption of Issue No. 02-16 resulted in a decrease to net income of $5.6 million, net of income taxes of $3.3 million, for the nine month period ended September 30, 2003.

Reclassifications - Loss from operations and the sale of discontinued franchises for the three and nine month periods ended September 30, 2003 reflects reclassifications to (from) the prior year presentation to include additional franchises sold and terminated or identified for sale (retained for continuing operations) subsequent to September 30, 2003 which had not been (had been) classified as held for sale as of September 30, 2003.

Recent Accounting Pronouncements - In July 2003, the EITF reached a consensus on Issue No. 03-10, "Application of Issue No. 02-16 by Resellers to Sales Incentives Offered to Consumers by Manufacturers." Issue No. 03-10 requires certain consideration offered directly from manufacturers to consumers to be recorded as a reduction of cost of sales. Issue No. 03-10 was effective January 1, 2004. The adoption of Issue No. 03-10 had no effect on Sonic's consolidated operating results, financial position or cash flows.

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

In April 2004, the FASB staff finalized Position No. FAS 129-1, "Disclosure Requirements under FASB Statement No. 129, Disclosures of Information about Capital Structure, Relating to Contingently Convertible Securities" ("FSP FAS 129-1"). Sonic adopted FSP FAS 129-1 as of June 30, 2004. See Note 5.

In September 2004, the EITF reached a consensus on Issue No. 04-8, "Accounting Issues Related to Certain Features of Contingently Convertible Debt and the Effect on Diluted Earnings per Share." When finalized and ratified by the FASB, Issue No. 04-8 will require issuers of contingently convertible securities to include the dilutive effect of these securities in the calculation of dilutive weighted average shares outstanding regardless of whether conversion is likely. Issue No. 04-8 is expected to be effective starting with periods ending after December 15, 2004. Issue No. 04-8 also requires retroactive application to all prior periods for which contingently convertible securities were outstanding. Sonic has evaluated the provisions of Issue No. 04-8 as if Issue No. 04-8 were finalized and ratified by the FASB and has determined the impact on Sonic's consolidated diluted earnings per share using the "if-converted method" to be reductions of $ 0.03 and $ 0.01 for diluted net income per share for the nine month periods ended September 30, 2004 and 2003, respectively. The impact of Issue No. 04-8 was immaterial to diluted net income per share for both three month periods ended September 30, 2004 and 2003.

2. BUSINESS ACQUISITIONS AND DISPOSITIONS

Acquisitions:

During the first quarter of 2004, Sonic acquired two franchises located in Ontario, California (the "California Acquisitions") for an aggregate purchase price of approximately $58.6 million in cash, net of cash acquired, funded by cash from operations and borrowings under the revolving credit facility. During the second and third quarters of 2004, Sonic acquired eleven franchises under common control in Houston, Texas (the "Houston Acquisitions") for approximately $169.2 million, net of cash acquired. The Houston Acquisitions' purchase price was comprised of $135.4 million in cash from operations and borrowings under the revolving credit facility and the assumption of $33.8 million in debt, including premium of $7.3 million (see discussion regarding the assumed debt in Note 5). The unaudited consolidated balance sheet as of September 30, 2004 includes preliminary allocations of the purchase price of the California and Houston Acquisitions to the assets and liabilities acquired based on their estimated fair market values at the dates of acquisition and are subject to final adjustment. As a result of these allocations and adjustments for previously recorded acquisitions, Sonic has recorded the following:

- $19.0 million of intangible assets representing rights acquired under franchise agreements;
- $163.8 million of goodwill, all of which is expected to be tax deductible; and
- $(0.2) million adjustment of goodwill related to the final adjustment of purchase price allocations for prior year acquisitions.

The following unaudited pro forma financial information presents a summary of consolidated results of operations as if the Houston Acquisitions had occurred January 1, 2004 and at the beginning of the immediately preceding year, after giving effect to certain adjustments, including interest expense on acquisition debt and related income tax effects. The pro forma financial information does not give effect to adjustments relating to net reductions in floorplan interest expense resulting from renegotiated floorplan financing agreements or to reductions in salaries and fringe benefits of former owners or officers of acquired dealerships who have not been retained by Sonic or whose salaries have been adjusted pursuant to employment arrangements with Sonic. The pro forma results have been prepared for comparative purposes only and are not necessarily indicative of the results of operations that would have occurred had the acquisitions actually been completed at the beginning of the periods presented. The pro forma results are also not necessarily indicative of the results of future operations (dollars in thousands, except per share amounts).

	Nine Months Ended September 30,	
	2003	2004
Total revenues	$ 5,613,915	$ 5,725,202
Gross profit	851,132	873,526
Income before cumulative effect of change in accounting principle	64,411	72,935
Net income	58,725	72,935
Diluted net income per share	1.39	1.72

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Dispositions:

During the first nine months of 2004, Sonic completed seven franchise dispositions. These disposals generated cash of $32.5 million. These franchise dispositions resulted in a net loss of $0.7 million, which is included in discontinued operations in the accompanying unaudited condensed consolidated statements of income for the nine month period ended September 30, 2004. Sonic reduced goodwill by $26.3 million associated with these franchises.

In conjunction with the dispositions in the first nine months of 2004, Sonic has agreed to indemnify the buyers from certain liabilities and costs arising from operations or events that occurred prior to sale but which may or may not be known at the time of sale, including environmental liabilities and liabilities associated from the breach of representations or warranties made under the agreements. There was no additional liability associated with current year dispositions related to subleases. However, Sonic's maximum liability associated with general indemnifications increased by $42.0 million as a result of these dispositions. These indemnifications expire within a period of one to three years following the date of the sale. The estimated fair value of these indemnifications was not material.

In addition to the dispositions described above, as of September 30, 2004, Sonic had approved the sale of 12 dealerships, representing 19 franchises. These dealerships are generally franchises with unprofitable operations. The operating results of these franchises are included in discontinued operations on the accompanying unaudited condensed consolidated statements of income. Long lived assets to be disposed of in connection with franchises not yet sold, consisting primarily of property, equipment, goodwill and other intangible assets, totaled approximately $15.8 million at September 30, 2004 and have been classified in assets held for sale in the accompanying unaudited condensed consolidated balance sheet. Goodwill classified as assets held for sale totaled approximately $5.7 million and $11.2 million at September 30, 2004 and December 31, 2003, respectively. Other assets and liabilities to be disposed in connection with these dispositions include inventories and related notes payable - floor plan. Revenues associated with franchises classified as discontinued operations were $99.5 million and $335.4 million for the three and nine month periods ended September 30, 2004, respectively, and $150.7 million and $492.2 million for the three and nine month periods ended September 30, 2003, respectively. The pre-tax losses (before gains or losses on the sale of disposed franchises) associated with franchises classified as discontinued operations were $3.5 and $6.8 million for the three and nine month periods ended September 30, 2004, respectively, and $2.4 million and $10.8 million for the three and nine month periods ended September 30, 2003, respectively.

3. INVENTORIES

Inventories consist of the following:

	(Dollars in thousands)	
	December 31, 2003	September 30, 2004
New vehicles	$ 825,189	$ 756,609
Used vehicles	126,872	146,583
Parts and accessories	49,782	54,883
Other	45,066	56,951
Total	$1,046,909	$ 1,015,026

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SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

4. PROPERTY AND EQUIPMENT

Property and equipment consists of the following:

	(Dollars in thousands)	
	December 31, 2003	September 30, 2004
Land	$ 7,653	$ 7,208
Building and improvements	68,936	81,238
Office equipment and fixtures	35,061	43,270
Parts and service equipment	26,689	30,539
Company vehicles	8,050	9,021
Construction in progress	9,262	28,392
Total, at cost	155,651	199,668
Less accumulated depreciation	(30,295)	(38,887)
Property and equipment, net	$ 125,356	$ 160,781

In addition to the amounts shown above, Sonic incurred approximately $65.5 million in real estate and construction costs as of December 31, 2003 and $62.4 million as of September 30, 2004 on dealership facilities that are or were expected to be completed and sold within one year in sale-leaseback transactions. Accordingly, these costs are included in assets held for sale on the accompanying unaudited condensed consolidated balance sheets. Under the terms of the sale-leaseback transactions, Sonic sells the dealership facilities to unaffiliated third parties and enters into long-term operating leases on the dealership facilities. During the first nine months of 2004, Sonic sold dealership facilities with a carrying value of $23.2 million in sale-leaseback transactions. Gains and losses from these sale-leaseback transactions were not material.

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

5. LONG-TERM DEBT

Long-term debt consists of the following:

	(Dollars in thousands)	
	December 31, 2003	September 30, 2004
$550 million revolving credit facility bearing interest at 2.55 percentage points above LIBOR and maturing October 31, 2006, collateralized by all of Sonic's assets (1)	$ 285,523	$ 317,438
Senior Subordinated Notes bearing interest at 8.625%, maturing August 15, 2013	275,000	275,000
Convertible Senior Subordinated Notes bearing interest at 5.25%, maturing May 7, 2009	130,100	130,100
$50 million revolving construction line of credit with Toyota Credit bearing interest at 2.25 percentage points above LIBOR, maturing December 31, 2007, and collateralized by Sonic's guarantee and a lien on all of the borrowing subsidiaries' real estate and other assets (2)	4,568	—
$100 million revolving real estate acquisition line of credit with Toyota Credit bearing interest at 2.00 percentage points above LIBOR, maturing December 31, 2012, and collateralized by Sonic's guarantee and a lien on all of the borrowing subsidiaries' real estate and other assets (2)	5,470	—
Notes payable to a finance company bearing interest from 10.52% to 9.52% (with a weighted average of 10.19%), with combined monthly principal and interest payments of $325, maturing November 1, 2015 through September 1, 2016, and collateralized by letters of credit with a commercial bank (3)	—	26,090
Other notes payable (primarily equipment notes)	2,201	4,113
	$ 702,862	$ 752,741
Less unamortized discount, net of premiums	(6,420)	(1,243)
(Less) / plus fair value of variable interest rate swaps	(157)	294
Less current maturities	(1,387)	(3,984)
Long-term debt	$ 694,898	$ 747,808

(1) During the first quarter of 2004, the borrowing limit on the revolving credit facility was increased from $500.0 million to $550.0 million. In connection with this increase in the borrowing limit, two lenders were added to the revolving credit facility.

(2) Total combined borrowings under the construction and real estate lines of credit are limited to $100.0 million. During the second quarter of 2004, Sonic repaid the construction and real estate acquisition revolving lines of credit with cash on hand and advances on the $550 million revolving credit facility.

(3) Three notes payable were assumed in connection with the Houston Acquisitions during the second quarter of 2004 and were recorded at fair value using an interest rate of 5.35 % (see Note 2). The interest rate used to calculate the fair value was based on a quoted market price for notes with similar terms as of the date of assumption. As a result of calculating the fair value, a premium of $7.3 million was recorded which will be amortized over the lives of the notes payable.

Neither of the conversion features on the convertible senior subordinated notes (the "Convertibles") were satisfied during the nine months ended September 30, 2004. The Convertibles were not included in the calculation of diluted earnings per share for any periods presented in the accompanying unaudited condensed consolidated financial statements because of the substantive difference between the market price contingencies and the conversion price.

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During the second quarter of 2004, Sonic amended the current ratio and adjusted debt to EBITDA covenants (the "Amendment") under the $550.0 million revolving credit facility (the "Revolver"). Per the Amendment, Sonic will be in compliance with the required specified current ratio of greater than 1.23 if there is adequate availability on the Revolver which will, when added to Sonic's total current assets, make the current ratio greater than 1.23. Also per the Amendment, the Revolver availability used for the current ratio calculation is added to Sonic's debt for purposes of compliance with the required specified adjusted debt to EBITDA ratio of less than 2.25.

Sonic was in compliance with all financial convenants under the above credit facilities as of September 30, 2004.

6. PER SHARE DATA

The calculation of diluted net income per share considers the potential dilutive effect of options and shares under Sonic's stock compensation plans, and Class A common stock purchase warrants. The following table illustrates the dilutive effect of such items:

	(Shares in thousands) Three Months Ended September 30,		(Shares in thousands) Nine Months Ended September 30,	
	2003	2004	2003	2004
Basic weighted average number of common shares outstanding	40,926	41,349	40,858	41,328
Dilutive effect of stock options	2,094	815	1,428	1,111
Dilutive effect of warrants	2	—	2	—
Weighted average number of common shares outstanding, including effect of dilutive securities	43,022	42,164	42,288	42,439

In addition to the stock options included in the table above, options to purchase 1,115,000 shares and 1,896,000 shares of Class A common stock were outstanding during the nine month periods ended September 30, 2003 and 2004, respectively, but were not included in the computation of diluted net income per share because the options were antidilutive. The total amount of stock options outstanding at September 30, 2003 and 2004 were 6,879,000 and 6,260,000, respectively.

7. CONTINGENCIES

Sonic is involved, and will continue to be involved, in numerous legal proceedings arising in the ordinary course of business, including litigation with customers, employment related lawsuits, contractual disputes, class actions, purported class actions and actions brought by governmental authorities.

Several of Sonic's Texas dealership subsidiaries have been named in three class action lawsuits brought against the Texas Automobile Dealers Association ("TADA") and new vehicle dealerships in Texas that are members of the TADA. Approximately 630 Texas dealerships are named as defendants in two of the actions, and approximately 700 Texas dealerships are named as defendants in the other action. The three actions allege that since January 1994, Texas automobile dealerships have deceived customers with respect to a vehicle inventory tax and violated federal antitrust and other laws. In two of the actions, the Texas state court certified two classes of consumers on whose behalf the actions would proceed. The Texas Court of Appeals has affirmed the trial court's order of class certification in the state actions, and the Texas Supreme Court issued an order for the second time in September 2004 stating that it would not hear the merits of the defendant's appeal on class certification. The federal trial court conditionally certified a class of consumers in the federal antitrust case, but on appeal by the defendant dealerships, the U.S. Court of Appeals for the Fifth Circuit reversed the certification of the plaintiff class in October 2004 and remanded the case back to the federal trial court for further proceedings not inconsistent with the Fifth Circuit's ruling. The plaintiffs may appeal this ruling by the Fifth Circuit.

If the TADA matters are not settled, Sonic and its dealership subsidiaries intend to vigorously defend themselves and assert available defenses. In addition, Sonic may have rights of indemnification with respect to certain aspects of the TADA matters. However, an adverse resolution of the TADA matters may result in the payment of significant costs and damages, which could have a material adverse effect on Sonic's future results of operations and cash flows.

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In addition to the TADA matters described above, Sonic is involved in numerous other legal proceedings arising out of the conduct of Sonic's business. Sonic's management does not believe that the ultimate resolution of these legal proceedings will have a material adverse effect on the Company's business, financial condition, results of operations, cash flows or prospects. However, the results of these legal proceedings cannot be predicted with certainty, and an unfavorable resolution of one or more of these legal proceedings could have a material adverse effect on Sonic's business, financial condition, results of operations cash flows and prospects.

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

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

The following discussion and analysis of the results of operations and financial condition should be read in conjunction with the Sonic Automotive, Inc. and Subsidiaries Unaudited Consolidated Financial Statements and the related notes thereto appearing elsewhere in this report, as well as the audited financial statements and related notes and "Management's Discussion and Analysis of Financial Condition and Results of Operations" appearing in our Annual Report for the year ended December 31, 2003 on Form 10-K.

Overview

We are one of the largest automotive retailers in the United States. As of October 29, 2004 we owned dealership subsidiaries that operated 195 dealership franchises, representing 38 different brands of cars and light trucks at 156 locations, and 40 collision repair centers in 15 states. Our dealerships provide comprehensive services including sales of both new and used cars and light trucks, sales of replacement parts, performance of vehicle maintenance, warranty, paint and collision repair services, and arrangement of extended warranty contracts, financing and insurance for our customers. Our brand diversity allows us to offer a broad range of products at a wide range of prices from lower priced, or economy vehicles, to luxury vehicles. We believe that this diversity reduces the risk of changes in customer preferences, product supply shortages and aging products. In addition, although vehicle sales are cyclical and are affected by many factors, including general economic conditions, consumer confidence, levels of discretionary personal income, interest rates and available credit, our parts, service and collision repair services are not closely tied to vehicle sales and are not dependent upon near-term vehicle sales volume. As a result, we believe the diversity of these products and services reduces the risk of periodic economic downturns.

The following is a detail of our new vehicle revenues by brand for the three and nine month periods ended September 30, 2003 and 2004:

	Percentage of New Vehicle Revenues			
	Three Months Ended September 30,		Nine Months Ended September 30,	
	2003	2004	2003	2004
Brand (1)				
General Motors (2)	11.7%	13.4%	11.8%	12.3%
Honda	15.5%	12.3%	15.7%	12.7%
BMW	9.0%	12.2%	9.6%	11.3%
Cadillac	11.2%	11.1%	11.6%	11.7%
Toyota	14.0%	10.7%	12.9%	11.3%
Ford	10.4%	9.3%	11.5%	9.8%
Lexus	4.8%	5.6%	4.8%	5.9%
Volvo	4.4%	4.3%	4.0%	4.1%
Chrysler (3)	3.2%	3.0%	2.8%	3.1%
Mercedes	2.4%	2.7%	2.8%	3.0%
Nissan	2.7%	2.4%	2.6%	2.6%
Other (4)	6.1%	6.6%	5.5%	6.1%
Other Luxury (5)	4.6%	6.4%	4.4%	6.1%
Total	100.0%	100.0%	100.0%	100.0%

(1) In accordance with the provisions of SFAS No. 144, revenue data in 2003 reflects reclassifications from (to) the prior year presentation to include additional franchises sold and terminated or identified for sale (retained for continuing operations) subsequent to September 30, 2003 which had not been (had been) previously included in discontinued operations
(2) Includes Buick, Chevrolet, GMC, Oldsmobile, Saturn and Pontiac
(3) Includes Chrysler, Dodge and Jeep
(4) Includes Hino, Hyundai, Isuzu, KIA, Lincoln, Mercury, Minicooper, Mitsubishi, Scion, Subaru and Volkswagen
(5) Includes Acura, Audi, Hummer, Infiniti, Jaguar, Land Rover, Maybach, Morgan, Porsche, Rolls Royce and Saab

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We have accounted for all of our dealership acquisitions using the purchase method of accounting and, as a result, we do not include in our consolidated financial statements the results of operations of these dealerships prior to the date they were acquired. Our unaudited consolidated financial statements discussed below reflect the results of operations, financial position and cash flows of each of our dealerships acquired prior to September 30, 2004. As a result of the effects of our acquisitions and other potential factors in the future, the historical consolidated financial information described in "Management's Discussion and Analysis of Financial Condition and Results of Operations" is not necessarily indicative of the results of operations, financial position and cash flows that would have resulted had such acquisitions occurred at the beginning of the periods presented, nor is it indicative of future results of operations, financial position and cash flows.

Results of Operations

Revenues

Except where otherwise noted, the following discussions are on a same store basis.

New Vehicles:

	For the Three Months Ended				For the Nine Months Ended			
	9/30/2003	9/30/2004	Units or $ Change	% Change	9/30/2003	9/30/2004	Units or $ Change	% Change
New Vehicle Units								
Same Store	40,978	37,984	(2,994)	(7.3)%	113,890	107,078	(6,812)	(6.0)%
Acquisitions	455	3,174	2,719	597.6%	859	8,080	7,221	840.6%
Total As Reported	41,433	41,158	(275)	(0.7)%	114,749	115,158	409	0.4%
New Vehicle Revenues (in thousands)								
Same Store	$ 1,147,803	$ 1,101,400	$(46,403)	(4.0)%	$3,180,913	$3,099,432	$ (81,481)	(2.6)%
Acquisitions	9,845	108,268	98,423	999.7%	21,230	259,819	238,589	1123.8%
Total As Reported	$ 1,157,648	$ 1,209,668	$ 52,020	4.5%	$3,202,143	$3,359,251	$157,108	4.9%
New Vehicle Unit Price								
Same Store	$ 28,010	$ 28,996	$ 986	3.5%	$ 27,930	$ 28,946	$ 1,016	3.6%

New unit sales at our domestic dealerships increased slightly by 191 units, or 1.3%, for the quarter ended September 30, 2004, yet decreased by 1,301 units, or 2.9%, for the nine months compared to the same periods last year. Import new unit sales decreased for both the three and nine month periods ended September 30, 2004 compared to the same periods last year (3,185 units, or 12.4%, and 5,511 units, or 8.0%, respectively). Industry-wide domestic new unit sales were down for both the three and nine month periods ended September 30, 2004. Import sales in the industry declined slightly for the quarter ended September 30, 2004, but increased over the nine month period. We expect the retail environment for new vehicles to remain challenging for the remainder of 2004.

Toyota, Honda and Ford continued to be our most challenging brands in new vehicle unit sales for the three and nine month periods ended September 30, 2004. Our Toyota unit sales declined 24.0% for the quarter and 13.8% for the nine months ended September 30, 2004 due to increased competition in several of our locations and a decrease in new unit sales compared to extremely high volume sales in the prior year. Unit sales were also down at our Honda and Ford dealerships for both the three and nine month periods ended September 30, 2004 (15.9% and 14.1% for Honda, and 7.4% and 11.6% for Ford, respectively). Our Honda declines were primarily attributable to turnover in dealership management, increased competition in key markets, and high sales volumes in the prior year. Our Ford dealerships have experienced above average market declines and continued to show lower sales volumes in the third quarter. We believe this decline is in part attributed to stronger competition with General Motors dealerships that are offering attractive incentive packages. These declines were partially offset by increased new unit sales at several of our dealerships, the largest of which were GM (excluding Cadillac) (up 803 units, or 15.0%), BMW (up 181 units, or 6.4%) and Hyundai (up 106 units, or 13.6%) for the quarter ended September 30, 2004. Fleet sales drove the significant increase in unit sales at our GM (excluding Cadillac) dealerships. For the nine months ended September 30, 2004, Acura (up 227 units, or 18.3%), GM (excluding Cadillac) (up 797 units, or 5.2%) and BMW (up 552 units, or 6.8%) were our strongest performing brands.

Our top performing regions for the quarter ended September 30, 2004 were North Los Angeles (up 251 units, or 12.0%), Oklahoma (up 302 units, or 17.3%) and Alabama/Atlanta (up 139 units, or 5.1%). For the nine months ended September 30, 2004, our North Los Angeles and Birmingham/Tennessee regions showed significant improvement when compared to the same period last year (up

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
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794 units, or 14.9%, and 722 units, or 13.7%, respectively). Heavy concentrations of import and luxury brand dealerships in North Los Angeles and Birmingham/Tennessee contributed to these increases. Florida showed the greatest decline for the three and nine month periods ended September 30, 2004 compared to all other regions (down 768 units, or 22.8%, and 1,450 units, or 14.5%, respectively). This region was severely impacted by disruption caused by four hurricanes in the third quarter. Other underperforming regions for the quarter include our North Bay and Dallas regions. For the nine months ended September 30, 2004, significant unit declines were experienced in our Dallas and Ohio regions.

With the exception of GM, Honda and Volvo, all of our brands experienced increases in new unit sales price for the quarter ended September 30, 2004 as compared to the same period last year. For the nine month period, only Honda and Volvo showed a decreased selling price per new unit. Our total sales mix in 2004 shifted to a greater proportion of truck and sport-utility vehicle sales for the three and nine month periods ended September 30, 2004 compared to last year. This change in mix helped drive the overall increase in average price per unit.

Used Vehicles:

	For the Three Months Ended				For the Nine Months Ended			
	9/30/2003	9/30/2004	Units or $ Change	% Change	9/30/2003	9/30/2004	Units or $ Change	% Change
Used Vehicle Units								
Same Store	18,933	16,433	(2,500)	(13.2)%	53,840	48,401	(5,439)	(10.1)%
Acquisitions	207	1,418	1,211	585.0%	320	3,582	3,262	1019.4%
Total As Reported	19,140	17,851	(1,289)	(6.7)%	54,160	51,983	(2,177)	(4.0)%
Used Vehicle Revenues (in thousands)								
Same Store	$ 312,837	$ 281,023	$(31,814)	(10.2)%	$ 890,895	$ 825,374	$(65,521)	(7.4)%
Acquisitions	2,863	30,949	28,086	981.0%	4,676	69,982	65,306	1396.6%
Total As Reported	$ 315,700	$ 311,972	$ (3,728)	(1.2)%	$ 895,571	$ 895,356	$ (215)	(0.0)%
Used Vehicle Unit Price								
Same Store	$ 16,523	$ 17,101	$ 578	3.5%	$ 16,547	$ 17,053	$ 506	3.1%

The decline in used vehicle unit sales for the three and nine month periods ended September 30, 2004 was due partially to the continued strength of new vehicle incentives offered by manufacturers. We expect the retail environment for used vehicles to remain challenging to the extent new vehicle incentives remain high. Our Florida markets represented 15.2% of the quarter's decline due somewhat to disruption caused by the four hurricanes. Our San Diego and Houston markets represented 26.0% of the quarterly decline. Our Alabama/Atlanta and Birmingham/Tennessee regions had improved used unit sales because these regions have high concentrations of luxury dealerships which comprise the majority of certified pre-owned ("CPO") sales. CPO sales for both of these regions increased significantly for the three months ended September 30, 2004 as compared to the same period last year. For the nine months ended September 30, 2004, Florida, Ohio and Colorado represented 42.2% of the total decline.

Despite the decline in used unit volumes, the average used selling price per unit increased for both the three and nine month periods ended September 30, 2004 compared to the same periods last year. The increased average price per unit was attributable to an increase in CPO sales as a percentage of total used vehicle sales for both the quarter and nine months ended September 30, 2004.

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Wholesale Vehicles:

	For the Three Months Ended		Units or $ Change	% Change	For the Nine Months Ended		Units or $ Change	% Change
	9/30/2003	9/30/2004			9/30/2003	9/30/2004		
Wholesale Vehicle Units								
Same Store	15,570	14,652	(918)	(5.9)%	41,495	41,373	(122)	(0.3)%
Acquisitions	611	1,758	1,147	187.7%	1,479	4,435	2,956	199.9%
Total As Reported	16,181	16,410	229	1.4%	42,974	45,808	2,834	6.6%
Wholesale Vehicle Revenues (in thousands)								
Same Store	$ 108,329	$ 115,002	$ 6,673	6.2%	$ 296,191	$ 326,987	$30,796	10.4%
Acquisitions	7,451	24,478	17,027	228.5%	18,600	53,748	35,148	189.0%
Total As Reported	$ 115,780	$ 139,480	$23,700	20.5%	$ 314,791	$ 380,735	$65,944	20.9%
Wholesale Unit Price								
Same Store	$ 6,958	$ 7,849	$ 891	12.8%	$ 7,138	$ 7,903	$ 765	10.7%

Total same store wholesale vehicle unit sales decreased for both the three and nine month periods ended September 30, 2004 (down 918 units, or 5.9%, and 122 units, or 0.3%, respectively). Consistent with industry prices, our wholesale unit prices increased by 12.8% and 10.7% for the three and nine months periods ended September 30, 2004, respectively.

For the three months ended September 30, 2004, our GM (excluding Cadillac), Honda and Cadillac dealerships experienced decreases in wholesale unit sales (down 19.0%, 13.3% and 15.7%, respectively). GM (excluding Cadillac), Cadillac and Ford experienced similar decreases in wholesale unit sales for the nine months ended September 30, 2004. These decreases were somewhat offset by increases at several of our import dealerships (BMW, Audi, Honda and Volvo).

Parts, Service and Collision Repair ("Fixed Operations"):

	For the Three Months Ended		$ Change	% Change	For the Nine Months Ended		$ Change	% Change
	9/30/2003	9/30/2004			9/30/2003	9/30/2004		
Fixed Operations Revenue (in thousands)								
Same Store	$ 243,123	$ 238,783	$ (4,340)	(1.8)%	$ 699,558	$ 704,107	$ 4,549	0.7%
Acquisitions	1,976	30,766	28,790	1457.0%	4,589	69,016	64,427	1403.9%
Total As Reported	$ 245,099	$ 269,549	$24,450	10.0%	$ 704,147	$ 773,123	$68,976	9.8%

For the quarter ended September 30, 2004, both parts and service revenues decreased and collision repair revenues were flat. Parts revenue also decreased for the nine months ended September 30, 2004, which was partially offset by an increase in service revenues. Collision repair revenues were flat for the three and nine months ended September 30, 2004 despite the negative impact of the hurricanes on our Alabama/Atlanta region. Large declines in wholesale parts sales were somewhat offset by increases in warranty parts revenues for the three and nine month periods ended September 30, 2004 compared to the same periods last year. For the quarter ended September 30, 2004, service revenues declined due to decreases in customer pay partially offset by an increase in warranty revenues. For the nine months ended September 30, 2004, service revenues increased due to increased warranty service revenues and customer pay.

The largest declines in Fixed Operations revenue for the quarter ended September 30, 2004 were at our GM (excluding Cadillac) (down $3.5 million, or 8.3%), Ford (down $3.3 million, or 14.7%) and Honda (down $2.1 million, or 6.2%) dealerships. Our Ford dealerships continued to experience a decline in wholesale parts revenues due to a manufacturer owned wholesale parts operation in Houston. For the nine month period ended September 30, 2004, warranty revenues generated the majority of the overall increase, partially offset by decreases in both customer pay and wholesale parts revenues. Quick lube revenues were also up for the nine months ended September 30, 2004 ($4.1 million, or 56.3%).

Our BMW dealerships were the strongest performers with an increase of $11.7 million, or 15.2%, in Fixed Operations for the nine months ended September 30, 2004 compared to the same period last year. Our BMW and Honda dealerships showed significant

increases in warranty revenues for the nine months ended September 30, 2004 compared to the same period last year. Increased volume at our BMW dealerships contributed to greater warranty revenues as regular maintenance is covered by the manufacturer's warranty. Recalls on two Honda models contributed to the increase in warranty revenues at our Honda dealerships. We experienced significant declines at our Ford and GM (excluding Cadillac) dealerships for the nine month period ended September 30, 2004 ($8.9 million, or 13.3%, and $6.2 million, or 5.2%, respectively).

Finance and Insurance:

	For the Three Months Ended				For the Nine Months Ended			
	9/30/2003	9/30/2004	$ Change	% Change	9/30/2003	9/30/2004	$ Change	% Change
Finance & Insurance Revenue (in thousands)								
Same Store	$ 52,198	$ 47,098	$(5,100)	(9.8)%	$ 147,529	$ 131,572	$(15,957)	(10.8)%
Acquisitions	1,182	5,205	4,023	340.4%	2,954	12,975	10,021	339.2%
Total As Reported	$ 53,380	$ 52,303	$(1,077)	(2.0)%	$ 150,483	$ 144,547	$ (5,936)	(3.9)%
Total F&I per Unit								
Same Store, Excluding Fleet Units	$ 898	$ 922	$ 24	2.7%	$ 922	$ 906	$ (16)	(1.7)%

Total same store finance and insurance revenues decreased $5.1 million, or 9.8%, and $16.0 million, or 10.8%, for the three and nine month periods ended September 30, 2004, respectively. Sales volume declines in both new and used vehicles were responsible for 94.1% of the decline in finance and insurance revenues for the quarter and 67.1% of the finance and insurance decline for the nine months ended September 30, 2004 as compared to the same periods last year.

Gross Profit and Gross Margins

Overall same store gross profit as a percentage of revenues ("gross margin") decreased from 14.9% to 14.8% for the quarter and remained flat at 15.3% for the nine months ended September 30, 2004 compared to the same periods last year. For the three months ended September 30, 2004, the new vehicle gross margin decreased 10 bps and the used vehicle gross margin decreased 20 bps, which was partially offset by an increase of 40 bps in the Fixed Operations gross margin. Compared to the first six months of 2004, our overall new vehicle gross margin was down 40 bps and our overall used vehicle margin was down 70 bps. This sequential decline in new vehicle gross margin was caused by pricing pressure stemming from excess inventories industry-wide. We expect new vehicle pricing pressure to continue to the extent the manufacturers do not reduce production in the fourth quarter. The sequential decline in the overall used vehicle gross margin was primarily caused by the same trends in new vehicle incentives discussed above under used vehicle revenues. Although wholesale unit sales were down, increased wholesale revenues and unit prices for both the three and nine month periods ended September 30, 2004 contributed to a favorable decrease in wholesale losses (down 20 bps and 60 bps, respectively). Revenue mix also contributed to the decline in overall gross margin for the three months ended September 30, 2004. Increases in Fixed Operations and wholesale revenues as a percentage of total revenues were offset by decreases in the higher margin yielding used vehicle and finance and insurance revenues (down 10.2% and 9.8%, respectively) for the three months ended September 30, 2004.

Selling, General and Administrative Expenses ("SG&A")

SG&A expenses increased $18.8 million, or 8.5%, and $37.2 million, or 5.8%, during the quarter and year to date periods ended September 30, 2004, respectively, due to the impact of acquisitions, hurricane damage and disruption costs, hailstorm physical damage, Sarbanes-Oxley compliance expenses and legal costs which were partially offset by same store declines. Acquisitions added $28.6 million and $59.7 million to SG&A expenses for the quarter and year to date periods, respectively. SG&A expenses at same store dealerships decreased $9.9 million and $22.4 million for the three and nine month periods, respectively, as compared to 2003.

As a percentage of gross profits, same store SG&A expenses increased slightly to 76.7% in the third quarter of 2004 from 76.2% in the third quarter of 2003 primarily due to the reduction in vehicle sales volumes. On a year to date basis, same store SG&A expenses as a percentage of gross profits decreased to 75.8% in 2004 from 76.6% in 2003 primarily due to reductions in spending. In both the quarter and year to date periods, decreases were attributable to advertising, compensation and other fixed expenses which were somewhat offset by increases in other variable expenses.

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Advertising expenses continued to decline compared to the prior year periods as a result of the centralization of advertising expenditures that began in early 2004. On a same store basis, advertising expenses in the third quarter of 2004 declined $2.7 million, or 15.2% compared to the third quarter of 2003. On a year to date basis, advertising declined $6.0 million, or 12.7%. We expect this favorable trend in advertising to continue in the fourth quarter.

Same store compensation expense made up 55.5% and 56.4% of total SG&A expenses in the quarter and year to date periods, respectively, down from 56.9% and 57.7% in the same periods in 2003. Compensation expense declined $8.6 million, or 7.1%, and $20.8 million, or 5.9%, in the quarter and year to date periods, respectively. On both a quarterly and year to date basis, the decline in compensation was due primarily to the decreases in unit volume. Total compensation as a percentage of gross profits decreased to 42.6% on a quarterly basis, from 43.4% in 2003, and also improved on a year to date basis declining to 42.8% from 44.2% in the prior year. Contributing to this decrease was the standardization of pay plans which began in the first quarter of 2004.

The improvements in all of these areas were offset slightly by increases in other expenses of $2.0 million, or 4.5%, and $4.1 million, or 3.2%, in the quarter and year to date periods, respectively. During the quarter and nine months ended September 30, 2004, bad debt, employee benefits, delivery and credit card expense increases were partially offset by lower training and general operating costs.

Depreciation and Amortization

Depreciation and amortization expense increased over the three and nine month periods by $1.2 million and $4.4 million, respectively, due to acquisitions, the completion of leasehold improvement projects and other general capital expenditures.

Floor Plan Interest Expense

The weighted average floor plan interest rate incurred by continuing dealerships was 2.79% for the quarter ended September 30, 2004, compared to 2.49% for the quarter ended September 30, 2003, which increased interest expense by approximately $0.6 million. The average floor plan balance from continuing dealerships increased to $925.1 million during the third quarter of 2004 from $737.3 million during the third quarter of 2003, resulting in increased interest expense of approximately $1.3 million. Approximately $65.9 million of the increase in the average floor plan balance was due to additional dealerships we acquired subsequent to September 30, 2003. The remaining increase in the floor plan balance was due to inventory optimization efforts.

The weighted average floor plan interest rate incurred by continuing dealerships was 2.70% for the nine months ended September 30, 2004, compared to 2.84% for the nine months ended September 30, 2003, which reduced interest expense by approximately $0.7 million. This decrease in expense was offset by an increase in floor plan balances. The average floor plan balance from continuing dealerships increased to $937.7 million during the first nine months of 2004 from $728.9 million during the first nine months of 2003, resulting in an interest expense increase of approximately $4.2 million. Approximately $39.4 million of the increase in the average floor plan balance was due to additional dealerships we acquired subsequent to September 30, 2003. The remaining increase in the floor plan balance was due to inventory optimization efforts.

Our floor plan expenses are substantially offset by amounts received from manufacturers in the form of floor plan assistance. These payments are credited against our cost of sales upon the sale of the vehicle. During the quarter and nine months ended September 30, 2004, respectively, the amounts we recognized from floor plan assistance exceeded our floor plan interest expense by approximately $2.5 million and $9.2 million, respectively. In the three and nine month periods ended September 30, 2003, floor plan assistance exceeded floor plan interest expense by approximately $5.6 million and $11.9 million, respectively.

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Interest Expense, Other

Changes in interest expense, other in 2004 compared to 2003 are summarized in the table below:

	For the Three Months Ended September 30, 2004	Nine Months Ended September 30, 2004
	Increase/(decrease) (in millions)	Increase/(decrease) (in millions)
Interest rates –		
• Changes in the average interest rate on the Revolving Credit Facility from 3.96% to 4.10% and from 4.80% to 3.95% for the three and nine months ended September 30, 2004, respectively	$ 0.2	$ (1.4)
• Refinancing $182.4 million of the 11% Senior Subordinated Notes with $200.0 million of 8.625% Senior Subordinated Notes in Q3 2003	(0.6)	(2.0)
Debt balances –		
• Higher average balance on the Revolving Credit Facility	0.9	1.4
• Issuance of an additional $75.0 million of 8.625% Senior Subordinated Notes in Q4 2003	1.6	4.8
• Double carry of the 11% Senior Subordinated Notes and the 8.625% Senior Subordinated Notes during the 30-day call period in Q3 2003	(1.2)	(1.2)
Other factors –		
• Decrease in capitalized interest in first quarter 2004	—	0.2
• Incremental interest savings (expense) related to floating to fixed interest rate swaps	(0.2)	0.1
• Incremental interest savings related to fixed to floating interest rate swaps	(0.9)	(3.5)
• Increase in interest income	(0.7)	(1.9)
• Increase in other interest	0.3	0.8
	$ (0.6)	$ (2.7)

Other Income / Expense, Net

Other expense decreased by $14.0 million and $13.9 million for the three and nine month periods ended September 30, 2004, respectively, as compared to the same periods in 2003 due to costs associated with the repurchase of our 11% senior subordinated notes due 2008 on August 12, 2003.

Liquidity and Capital Resources

We require cash to finance acquisition and fund debt service and working capital requirements. We rely on cash flows from operations, borrowings under our various credit facilities and offerings of debt and equity securities to meet these requirements.

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

Floor Plan Facilities

The weighted average interest rate for our floor plan facilities was 2.81% and 2.52% for the three months ended September 30, 2004 and 2003, respectively, and 2.71% and 2.84% for the nine months ended September 30, 2004 and 2003, respectively. Our floor plan interest expense is substantially offset by amounts received from manufacturers, in the form of floor plan assistance. In the third quarter of 2004, we received approximately $9.6 million in manufacturer assistance, and $29.8 million of assistance in the first nine months of 2004, which resulted in an effective borrowing rate under our floor plan facilities for both periods of 0%. Interest payments under each of our floor plan facilities are due monthly, and we are generally not required to make principal repayments prior to the sale of the vehicles. We were in compliance with all restrictive covenants as of September 30, 2004.

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Long-Term Debt and Credit Facilities

The Revolving Credit Facility: In the first quarter of 2004, we added two lenders to our Revolving Credit Facility and increased our borrowing limit by $50.0 million. At September 30, 2004 our Revolving Credit Facility had a borrowing limit of $550.0 million, subject to a borrowing base calculated on the basis of our receivables, inventory and equipment and a pledge of certain additional collateral by one of our affiliates (the borrowing base and availability were approximately $550.0 million and $174.6 million at September 30, 2004, respectively). The amount available to be borrowed under the Revolving Credit Facility is reduced on a dollar-for-dollar basis by the cumulative face amount of outstanding letters of credit. At September 30, 2004, we had $58.0 million in letters of credit outstanding.

8.625% Senior Subordinated Notes: On August 12, 2003, we issued $200.0 million in aggregate principal amount of 8.625% senior subordinated notes due 2013 (the "8.625% Notes"). The net proceeds, before expenses, of approximately $194.3 million together with an advance from Revolving Credit Facility, were used to redeem all of the 11% senior subordinated notes due 2008. On November 19, 2003 we issued an additional $75.0 million in aggregate principal amount of the 8.625% Notes. The net proceeds, before expenses, were approximately $78.9 million, and were used to pay down our Revolving Credit Facility.

Notes Payable to a Finance Company: Three notes payable totaling $26.6 million in aggregate principal were assumed with the purchase of franchises during the second quarter of 2004 (the "Assumed Notes"). The Assumed Notes bear interest rates from 10.52% to 9.52% (with a weighted average of 10.19%), have a combined monthly principal and interest payment of $0.3 million, mature November 1, 2015 through September 1, 2016 and are collateralized by letters of credit with a commercial bank. We recorded the Assumed Notes at fair value using an interest rate of 5.35%. The interest rate used to calculate the fair value was based on a quoted market price for notes with similar terms as of the date of assumption. As a result of calculating the fair value, a premium of $7.3 million was recorded that will be amortized over the lives of the Assumed Notes.

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

At September 30, 2004, the outstanding balance and availability on our long-term debt and credit facilities were as follows (in thousands):

	Interest Rate (1)	Outstanding Balance	Additional Borrowing Availability
Revolving Credit Facility (matures October 2006)	LIBOR + 2.55%	$ 317,438	$ 174,557
Senior Subordinated Notes (mature August 2013)	8.625%	$ 275,000	$ —
Convertible Senior Subordinated Notes (mature May 2009) (2)	5.25%	$ 130,100	$ —
Mortgage Facility:			
Construction Loan (matures December 2007)	LIBOR + 2.25%	$ —	$ 50,000(3)
Permanent Loan (matures December 2012)	LIBOR + 2.00%	$ —	$ 100,000(3)
Notes Payable to a Finance Company (mature November 2015 through September 2016)	10.19%(4)	$ 26,090	$ —

(1) Six-month LIBOR was 2.20% at September 30, 2004.
(2) Notes were not convertible at any time during the nine months ended September 30, 2004.
(3) Total combined borrowings under the Construction and Permanent Loans are limited to $100,000. Borrowings were repaid during the nine months ended September 30, 2004. We do not currently intend to borrow on the Construction and Permanent Loans in the future.
(4) Weighted average rate.

We were in compliance with all of the restrictive and financial covenants under all our long-term debt and credit facilities as of September 30, 2004.

Dealership Acquisitions and Dispositions

In the first nine months of 2004, we acquired 13 franchises for an aggregate purchase price of $227.8 million in cash, net of cash acquired, comprised of $194.0 million in cash from operations and by borrowings under the Revolving Credit Facility and the assumption of $33.8 million in debt, including premium of $7.3 million. The total purchase price for these acquisitions was based on our internally determined valuation of the franchises and their assets. During the first nine months of 2004, we completed seven planned franchise dispositions. These disposals generated cash of $32.5 million.

Sale-Leaseback Transactions

In an effort to generate additional cash flow, we typically seek to structure our operations to minimize the ownership of real property. As a result, dealership facilities either constructed by us or obtained in acquisitions are typically sold to third parties in sale-leaseback transactions. The resulting operating leases generally have initial terms of 10-15 years and include a series of five-year renewal options. We have no continuing obligations under these arrangements other than lease payments. During the first nine months of 2004, we sold $23.2 million in dealership facilities in sale-leaseback transactions.

Capital Expenditures

Our capital expenditures include the construction of new dealerships and collision repair centers, building improvements and equipment purchased for use in our dealerships. Capital expenditures in the first nine months of 2004 were approximately $73.3 million, of which approximately $53.2 million related to the construction of new dealerships and collision repair centers. Once completed, these new dealership facilities and collision repair centers are generally sold in sale-leaseback transactions. Capital expenditures incurred during the first nine months of 2004 expected to be sold within a year in sale-leaseback transactions were $46.5

million. We do not expect any significant gains or losses from these sales. As of September 30, 2004, commitments for facilities construction projects totaled approximately $23.1 million. We expect $14.4 million of this amount to be financed through future sale-leaseback transactions.

Stock Repurchase Program

As of September 30, 2004, our Board of Directors authorized us to expend up to $185.0 million to repurchase shares of our Class A common stock or redeem securities convertible into Class A common stock. In the first nine months of 2004, we repurchased 951,500 shares for approximately $20.9 million which was partially offset by proceeds received from the exercise of stock options under stock compensation plans of $13.7 million. As of October 29, 2004, we had $32.8 million remaining under our Board authorization.

Dividends

Our Board of Directors approved a quarterly cash dividend of $0.12 per share for shareholders of record on September 15, 2004, which was paid on October 15, 2004. On October 21, 2004, our Board of Directors approved a quarterly cash dividend of $0.12 per share for stockholders of record on December 15, 2004, which will be paid on January 15, 2005.

Cash Flows

For the nine months ended September 30, 2004, net cash provided by operating activities was approximately $119.8 million, which was driven primarily by net income adjusted for non-cash items such as depreciation, amortization and gains on disposals of assets and, to a lesser extent, changes in working capital accounts. Cash used in investing activities in the first nine months of 2004 was $202.5 million, the majority of which related to dealership acquisitions and capital expenditures on property and equipment which was partially offset by proceeds received from dealership dispositions and the sales of property and equipment in sale-leaseback transactions. In the first nine months of 2004, net cash provided by financing activities was $0.6 million and related primarily to repurchases of Class A common stock of $20.9 million and dividends paid of $12.4 million, which was offset by the exercise of shares under stock compensation plans of $13.7 million and net borrowings on revolving credit facilities of $21.9 million.

Future Liquidity Outlook

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

Seasonality

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

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES

Item 3: Quantitative and Qualitative Disclosures About Market Risk.

Interest Rate Risk. Our variable rate notes payable–floor plan, revolving credit facility borrowings and other variable rate notes expose us to risks caused by fluctuations in the underlying interest rates. The total outstanding balance of such instruments was approximately $1.2 billion at September 30, 2004 and approximately $1.1 billion at September 30, 2003. A change of 100 basis points in the underlying interest rate would have caused a change in interest expense of approximately $8.8 million in the first nine months of 2004 and approximately $7.3 million in the first nine months of 2003. Of the total change in interest expense, approximately $6.3 million in the first nine months of 2004 and approximately $5.9 million in first nine months of 2003 would have resulted from notes payable–floor plan.

Our exposure to notes payable–floor plan is mitigated by floor plan assistance payments received from manufacturers that are generally based on rates similar to those incurred under our floor plan financing arrangements. These payments are capitalized as inventory and charged against cost of sales when the associated inventory is sold. During the nine months ended September 30, 2004 and 2003, the amounts we received from manufacturer floor plan assistance exceeded our floor plan interest expense by approximately $9.2 million and $11.1 million, respectively. As a result, the effective rate incurred under our floor plan financing arrangements was reduced to 0% after considering these incentives. A change of 100 basis points in the underlying interest rate would have caused an estimated change in floor plan assistance of approximately $5.2 million in the first nine months of 2004.

In addition to our variable rate debt, we also have lease agreements on a portion of our dealership facilities where the monthly lease payment fluctuates based on LIBOR interest rates. Many of our lease agreements have interest rate floors whereby our lease expense would not fluctuate significantly in periods when LIBOR is relatively low.

In order to reduce our exposure to market risks from fluctuations in interest rates, we have two separate interest rate swap agreements (the “Fixed Swaps”) to effectively convert a portion of the LIBOR-based variable rate debt to a fixed rate. The Fixed Swaps each have a notional principal amount of $100.0 million and mature on October 31, 2004 and September 6, 2006. Incremental interest expense incurred (the difference between interest received and interest paid) as a result of the Fixed Swaps was $4.5 million and $4.4 million for the nine month periods ended September 30, 2004 and 2003, respectively. The Fixed Swaps have been designated and qualify as cash flow hedges and, as a result, changes in the fair value of the Fixed Swaps have been recorded in other comprehensive loss, net of related income taxes, in the statement of stockholders’ equity with offsetting amounts in other accrued and long-term liabilities. In addition, we have five separate interest rate swaps totaling $150.0 million (collectively, the “Variable Swaps”) to effectively convert a portion of our fixed rate debt to a LIBOR-based variable rate debt. The Variable Swaps expire on August 15, 2013 and have been designated and qualify as fair value hedges and, as a result, changes in the fair value of the Variable Swaps have been recorded against the associated fixed rate long-term debt with offsetting amounts recorded as a derivative liability within other long term liabilities. Incremental interest expense savings as a result of the Variable Swaps was $3.5 million for the nine month period ended September 30, 2004.

Item 4: Controls and Procedures.

Our management, under the supervision and with the participation of our principal executive officer and principal financial officer, evaluated the effectiveness of 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 principal executive officer and principal financial officer have concluded that our disclosure controls and procedures were effective as of the end of the period covered by this Quarterly Report on Form 10-Q. There were no changes in our internal control over financial reporting during the past fiscal quarter that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES

PART II – OTHER INFORMATION

Item 1: Legal Proceedings.

We are involved, and expect to continue to be involved, in numerous legal proceedings arising in the ordinary course of our business, including litigation with customers, employment related lawsuits, contractual disputes, class actions, purported class actions and actions brought by governmental authorities.

Several of our Texas dealership subsidiaries have been named in three class action lawsuits against the Texas Automobile Dealers Association ("TADA") and new vehicle dealerships in Texas that are members of the TADA. Approximately 630 Texas dealerships are named as defendants in two of the actions, and approximately 700 dealerships are named as defendants in the other action. The three actions allege that since 1994, Texas automobile dealerships have deceived customers with respect to a vehicle inventory tax and violated federal antitrust and other laws. In April 2002, in two actions, the Texas state court certified two classes of consumers on whose behalf the actions would proceed. The Texas Court of Appeals has affirmed the trial court's order of class certification in the state actions, and the Texas Supreme Court issued an order for the second time in September 2004 stating that it would not hear the merits of the defendant's appeal on class certification. The federal trial court conditionally certified a class of consumers in the federal antitrust case, but on appeal by the defendant dealerships, the U.S. Court of Appeals for the Fifth Circuit reversed the certification of the plaintiff class in October 2004 and remanded the case back to the federal trial court for further proceedings not inconsistent with the Fifth Circuit's ruling. The plaintiffs may appeal this ruling by the Fifth Circuit.

If the TADA matters are not settled, Sonic and its dealership subsidiaries intend to vigorously defend themselves and assert available defenses. In addition, Sonic may have rights of indemnification with respect to certain aspects of the TADA matters. However, an adverse resolution of the TADA matters may result in the payment of significant costs and damages, which could have a material adverse effect on Sonic's future results of operations and cash flows.

In addition to the TADA matters described above, we are also involved in numerous other legal proceedings arising out of the conduct of our business. We do not believe that the ultimate resolution of these legal proceedings will have a material adverse effect on our business, financial condition, results of operations, cash flows or prospects. However, the results of these legal proceedings cannot be predicted with certainty, and an unfavorable resolution of one or more of these legal proceedings could have a material adverse effect on our business, financial condition, results of operations, cash flows and prospects.

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SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES

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

Issuer Repurchases of Equity Securities

The following table sets forth information about the shares of Class A Common Stock we repurchased during the fiscal quarter ended September 30, 2004.

	Total Number of Shares Purchased (1)	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (2)	Approximate Dollar Value of Shares That May Yet Be Purchased Under the Plans or Programs
	(Amounts in Thousands, Except Per Share Amounts)			
July 2004	**280**	**$ 19.74**	**280**	**$ 32,838**
August 2004	**0**	**0**	**0**	**32,838**
September 2004	**0**	**0**	**0**	**32,838**
Total	**280**	**$ 19.74**	**280**	**$ 32,838**

(1) All shares repurchased were part of publicly announced share repurchase programs

(2) Our publicly announced Class A Common Stock repurchase authorizations occurred as follows:

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

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES

Item 6: Exhibits.

(a) Exhibits:

Exhibit No.	Description
31.1	Certification of Mr. E. Lee Wyatt, Jr. pursuant to Rule 13a – 14 (a).
31.2	Certification of Mr. O. Bruton Smith pursuant to Rule 13a – 14 (a).
32.1	Certification of Mr. E. Lee Wyatt, Jr. pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Mr. O. Bruton Smith pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
99.1	Risk Factors.

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES

Forward Looking Statements

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

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

These forward-looking statements are based on our current estimates and assumptions and involve various risks and uncertainties. As a result, you are cautioned that these forward looking statements are not guarantees of future performance, and that actual results could differ materially from those projected in these forward looking statements. Factors which may cause actual results to differ materially from our projections include those risks described in Exhibit 99.1 to this quarterly report on Form 10-Q and elsewhere in this report, as well as:

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

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES

EXHIBIT INDEX

Exhibit No.	Description
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99.1	Risk Factors.

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES

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.

SONIC AUTOMOTIVE, INC.

Date: November 3, 2004	By:	/s/ O. Bruton Smith
		O. Bruton Smith *Chairman and Chief Executive Officer*
Date: November 3, 2004	By:	/s/ E. Lee Wyatt, Jr.
		E. Lee Wyatt, Jr. *Executive Vice President, Treasurer and Chief Financial Officer* *(Principal Financial and Accounting Officer)*

Exhibit 31.1

CERTIFICATION

I, E. Lee Wyatt, Jr., certify that:

1. I have reviewed this quarterly report on Form 10-Q of Sonic Automotive, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
   (b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   (c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 3, 2004

By: /s/ E. Lee Wyatt, Jr.

E. Lee Wyatt, Jr.
Executive Vice President, Chief Financial Officer
and Treasurer

Exhibit 31.2

CERTIFICATION

I, O. Bruton Smith, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Sonic Automotive, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
   (b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   (c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 3, 2004

By: /s/ O. Bruton Smith

O. Bruton Smith,
Chairman and Chief Executive Officer

Exhibit 32.1

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Sonic Automotive, Inc. (the "Company") on Form 10-Q for the period ending September 30, 2004 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, E. Lee Wyatt, Jr., Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

(1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ E. Lee Wyatt, Jr.

E. Lee Wyatt, Jr.
Executive Vice President,
Chief Financial Officer and Treasurer

November 3, 2004

Exhibit 32.2

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Sonic Automotive, Inc. (the "Company") on Form 10-Q for the period ending September 30, 2004 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, O. Bruton Smith, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

(1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ O. Bruton Smith

O. Bruton Smith
Chairman and Chief Executive Officer

November 3, 2004

EXHIBIT 99.1

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES

RISK FACTORS

Risks Related to Our Indebtedness

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

As of September 30, 2004, our total outstanding indebtedness was approximately $1.676.9 million, including the following:

- $317.4 million under a revolving credit facility;
- $925.4 million under standardized secured inventory floor plan facilities;
- $127.4 million in $5\frac{1}{4}\%$ convertible senior subordinated notes due 2009 representing $130.1 million in aggregate principal amount outstanding less unamortized discount of approximately $2.7 million;
- $271.9 million in $8\frac{5}{8}\%$ senior subordinated notes due 2013 representing $275.0 million in aggregate principal amount outstanding less unamortized net discount of approximately $3.1 million; and
- $34.8 million of other secured debt, representing $30.2 million in aggregate principal amount plus unamortized premium of approximately $4.6 million.

As of September 30, 2004, we had approximately $174.6 million available for additional borrowings under a revolving credit facility. We also had approximately $100.0 million available under a construction/mortgage credit facility for real estate acquisitions and new dealership construction. We also have significant additional capacity under the floor plan facilities. In addition, the indentures relating to our senior subordinated notes, convertible senior subordinated notes and other debt instruments allow us to incur additional indebtedness, including secured indebtedness.

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

- our ability to obtain additional financing for acquisitions, capital expenditures, working capital or general corporate purposes may be impaired in the future;
- a substantial portion of our current cash flow from operations must be dedicated to the payment of principal and interest on our indebtedness, thereby reducing the funds available to us for our operations and other purposes;
- some of our borrowings are and will continue to be at variable rates of interest, which exposes us to the risk of increasing interest rates;
- the indebtedness outstanding under our revolving credit facility and floor plan facilities are secured by a pledge of substantially all the assets of our dealerships; and
- we may be substantially more leveraged than some of our competitors, which may place us at a relative competitive disadvantage and make us more vulnerable to changing market conditions and regulations.

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

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

Our revolving credit facility, floor plan facilities and the indenture governing our senior subordinated notes contain numerous financial and operating covenants. A breach of any of these covenants could result in a default under the applicable agreement or indenture. If a default were to occur, we may be unable to adequately finance our operations and the value of our common stock would be materially adversely affected. In addition, a default under one agreement or indenture could result in a default and acceleration of our repayment obligations under the other agreements or indentures, including the indentures governing our outstanding convertible senior subordinated notes and our $8\frac{5}{8}\%$ senior subordinated notes, under the cross default provisions in those agreements or indentures. If a cross default were to occur, we may not be able to pay our debts or borrow sufficient funds to refinance them. Even if new financing were available, it may not be on terms acceptable to us. As a result of this risk, we could be forced to take actions that we otherwise would not take, or not take actions that we otherwise might take, in order to comply with the covenants in these agreements and indentures.

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

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

Risks Related to Our Relationships with Vehicle Manufacturers

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

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

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

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

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

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

- customer rebates or below market financing on new vehicles;
- dealer incentives on new vehicles;
- warranties on new and used vehicles; and
- sponsorship of used vehicle sales by authorized new vehicle dealers.

Manufacturers are currently offering very favorable incentives to potential customers. A reduction or discontinuation of a manufacturer's incentive programs may materially adversely affect our profitability.

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

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

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

During the first nine months of 2004, approximately 69.1% of our new vehicle revenue was derived from the sale of new vehicles manufactured by Ford, Honda, General Motors (including Cadillac), BMW and Toyota. Our success depends to a great extent on these manufacturers':

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

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

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

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

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

Manufacturers' restrictions on acquisitions could limit our future growth.

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

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

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

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

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

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

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

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

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

In addition, these laws restrict the ability of automobile manufacturers to directly enter the retail market in the future. If manufacturers obtain the ability to directly retail vehicles and do so in our markets, such competition could have a material adverse effect on us.

Risks Related to Our Acquisition Strategy

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

Our future operating results depend on our ability to integrate the operations of recently acquired dealerships, as well as dealerships we acquire in the future, with our existing operations. In particular, we need to integrate our management information systems, procedures and organizational structures, which can be difficult. Our growth strategy has focused on the pursuit of strategic acquisitions that either expand or complement our business. We acquired eleven dealerships in 2000, twelve in 2001, thirty-one in 2002, thirteen in 2003 and thirteen in the nine months ended September 30, 2004.

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

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

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

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

The automobile retailing industry is considered a mature industry in which minimal growth is expected in total unit sales. Accordingly, our ability to generate higher revenue and earnings in future periods depends in large part on our ability to acquire additional dealerships, manage geographic expansion, control costs in our operations and consolidate both past and future dealership

acquisitions into our existing operations. In pursuing a strategy of acquiring other dealerships, we face risks commonly encountered with growth through acquisitions. These risks include, but are not limited to:

- incurring significantly higher capital expenditures and operating expenses;
- failing to assimilate the operations and personnel of acquired dealerships;
- entering new markets with which we are unfamiliar;
- potential undiscovered liabilities and operational difficulties at acquired dealerships;
- disrupting our ongoing business;
- diverting our limited management resources;
- failing to maintain uniform standards, controls and policies;
- impairing relationships with employees, manufacturers and customers as a result of changes in management;
- increased expenses for accounting and computer systems, as well as integration difficulties;
- failure to obtain a manufacturer's consent to the acquisition of one or more of its dealership franchises or renew the franchise agreement on terms acceptable to us; and
- incorrectly valuing entities to be acquired.

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

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

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

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

Substantially all the assets of our dealerships are pledged to secure our floor plan indebtedness and the indebtedness under the revolving credit facility. In addition, substantially all the real property and assets of our subsidiaries that are constructing new dealerships are pledged under our construction/mortgage facility with Toyota Credit. These pledges may impede our ability to borrow from other sources. Moreover, because Toyota Credit is associated with Toyota Motor Sales, U.S.A., Inc., any deterioration of our relationship with one could adversely affect our relationship with the other. The same is true of our relationships with Chrysler, GM and Ford and the floor plan financing divisions of each of these manufacturers.

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

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

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

- our financial capabilities;
- our stock price; and
- the availability of skilled employees to manage the acquired companies.

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

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

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

Our obligations under the revolving credit facility are secured with a pledge of shares of common stock of Speedway Motorsports, Inc., a publicly traded owner and operator of automobile racing facilities. These shares of Speedway Motorsports common stock are beneficially owned by Sonic Financial Corporation, an entity controlled by Mr. Smith. Presently, the $550.0 million borrowing limit of the revolving credit facility is subject to a borrowing base calculation that is based, in part, on the value of the Speedway Motorsports shares pledged by Sonic Financial. Consequently, a withdrawal of this pledge by Sonic Financial or a significant decrease in the value of Speedway Motorsports common stock could reduce the amount we can currently borrow under the revolving credit facility.

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

Risks Related to the Automotive Retail Industry

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

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

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

This competition is increasing as these products are now being marketed and sold over the Internet.

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

Our franchise agreements do not grant us the exclusive right to sell a manufacturer’s product within a given geographic area. Our revenues or profitability could be materially adversely affected if any of our manufacturers award franchises to others in the same markets where we operate or if existing franchised dealers increase their market share in our markets.

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

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

Our business is heavily dependent on consumer demand and preferences. Our revenues will be materially and adversely affected if there is a severe or sustained downturn in overall levels of consumer spending. Retail vehicle sales are cyclical and historically have experienced periodic downturns characterized by oversupply and weak demand. These cycles are often dependent on general economic conditions and consumer confidence, as well as the level of discretionary personal income and credit availability. The economic outlook appears uncertain in the aftermath of the terrorist attacks in the U.S. on September 11, 2001, the subsequent war on terrorism and other geopolitical conflicts. Future recessions may have a material adverse effect on our retail business, particularly sales of new and used automobiles. In addition, severe or sustained increases in gasoline prices may lead to a reduction in automobile purchases or a shift in buying patterns from luxury and sport utility vehicle models (which typically provide high margins to retailers) to smaller, more economical vehicles (which typically have lower margins).

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

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

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

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

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

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

General Risks Related to Investing in Our Securities

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

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

- “going private” transaction;
- disposition of substantially all of our assets;
- transfer resulting in a change in the nature of our business; or

- merger or consolidation in which current holders of common stock would own less than 50% of the common stock following such transaction.

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

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

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

In 2001, the Florida Attorney General's Office notified two of our wholly-owned dealership subsidiaries located in Florida that it was investigating whether the manner in which finance and insurance products were sold to certain customers of these two dealerships violated Chapter 501 of the Florida Statutes. In April 2002, the Florida Department of Financial Services informed the same two dealership subsidiaries that it had also initiated an investigation into whether the same conduct that was the subject of the Attorney General's investigation violated certain provisions of Florida's insurance code.

In April 2003, the two dealership subsidiaries entered into agreements with the Florida Department of Financial Services that provided that the Department would resolve its investigation of the two dealerships following the dealerships' completion of a specified refund program. Under the refund program specified by the agreement, certain customers who purchased specified finance and insurance products from the two dealerships between March 30, 1998 and March 31, 2002 were provided the opportunity to apply for refunds from the two dealerships for the purchase of those finance and insurance products. Customers determined to be entitled to a refund pursuant to the program received the refund after executing a written general release of claims against the dealership. The Florida Attorney General's office, being aware of the above refund program, also entered into an agreement with the two dealerships in April 2003 to conclude its investigation of those dealerships. The refund program has now been completed, and in October 2004, the Department of Financial Services announced the conclusion of its investigation of these two dealerships. Because our company had established appropriate reserves related to the refund program in prior years, the refund program has had no impact on the Company's reported financial results for 2004.

Additionally, several private civil actions have been filed against these dealership subsidiaries stating allegations similar to those underlying the original investigations by the Florida Attorney General's Office and the Department of Insurance. One private civil action filed against one of the dealership subsidiaries purports to represent a class of customers as potential plaintiffs, although no motion for class certification has been filed. Another private civil action has been filed against Sonic Automotive, Inc., which purports to represent a class of customers of all of our Florida dealership subsidiaries. The plaintiffs filed a motion for class certification in this proceeding in October 2003, but we are vigorously opposing this motion and the Florida court has not yet ruled on the motion.

In September of 2002, the Los Angeles County District Attorney's office served a search warrant on one of our wholly-owned dealership subsidiaries located in Los Angeles County relating to alleged deceptive practices of the dealership's finance and insurance department. Our dealership is cooperating with the District Attorney in its investigation. No charges have been filed and no proceedings have been instituted to date by the District Attorney. A private civil action has also been filed against the dealership stating allegations similar to those underlying the District Attorney's investigation. The plaintiffs in this private civil action purport to represent a class of customers as potential plaintiffs, although no motion for class certification has been filed.

In December 2003, the North Carolina Attorney General's office notified us that it had initiated an inquiry into the sales practices of our North Carolina dealerships following a negative media report on our company. We are cooperating with the North Carolina Attorney General's office in its inquiry. No charges have been filed and no proceedings have been instituted to date by the North Carolina Attorney General's Office.

Because the respective investigations by the Los Angeles County District Attorney's Office and North Carolina Attorney General's Office are continuing and have not resulted in formal charges to date, and because the private civil actions described above are also in the early stages of litigation, we cannot assure you as to the outcomes of these proceedings. We intend to vigorously defend ourselves and assert available defenses with respect to each of the foregoing matters, and do not believe that the ultimate resolution of these matters will have a material adverse affect on our business, results of operations, financial condition, cash flows or prospects.

Furthermore, several of our Texas dealership subsidiaries have been named in three class action lawsuits brought against the Texas Automobile Dealers Association ("TADA") and new vehicle dealerships in Texas that are members of the TADA.

Approximately 630 Texas dealerships are named as defendants in two of the actions, and approximately 700 Texas dealerships are named as defendants in the other action. The three actions allege that since January 1994, Texas automobile dealerships have deceived customers with respect to a vehicle inventory tax and violated federal antitrust and other laws. In April 2002, in two actions the Texas state court certified two classes of consumers on whose behalf the actions would proceed. The Texas Court of Appeals has affirmed the trial court's order of class certification in the state actions, and the Texas Supreme Court issued an order for the second time in September 2004 stating that it would not hear the merits of the defendant's appeal on class certification. The federal trial court conditionally certified a class of consumers in the federal antitrust case, but on appeal by the defendant dealerships, the U.S. Court of Appeals for the Fifth Circuit reversed the certification of the plaintiff class in October 2004 and remanded the case back to the federal trial court for further proceedings not inconsistent with the Fifth Circuit's ruling. The plaintiffs may appeal this ruling by the Fifth Circuit.

If the TADA matters are not settled, Sonic and its dealership subsidiaries intend to vigorously defend themselves and assert available defenses. In addition, Sonic may have rights of indemnification with respect to certain aspects of the TADA matters. However, an adverse resolution of the TADA matters may result in the payment of significant costs and damages, which could have a material adverse effect on Sonic's future results of operations and cash flows.

Finally, we are involved, and expect to continue to be involved, in numerous other legal proceedings arising out of the conduct of our business, including litigation with customers, employment related lawsuits, contractual disputes, class actions, purported class actions and actions brought by governmental authorities. The results of these matters cannot be predicted with certainty, and an unfavorable resolution of one or more of these matters, including the matters specifically discussed above, could have a material adverse effect on our business, financial condition, results of operations, cash flows and prospects.

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

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

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

Our performance is subject to local economic, competitive and other conditions prevailing in geographic areas where we operate. For example, our current results of operations depend substantially on general economic conditions and consumer spending habits in the Southeast and in our Northern California and Houston markets. Sales in our Northern California and Houston markets represented approximately 15.5 % and 13.0%, respectively of our sales for the nine months ended September 30, 2004. We may not be able to expand geographically and any geographic expansion may not adequately insulate us from the adverse effects of local or regional economic conditions.

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

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

On April 27, 2004, we filed a Current Report on Form 8-K with the Securities Exchange Commission announcing that Mr. Theodore M. Wright had resigned as Sonic's President on April 26, 2004, and announcing that Mr. Jeffrey C. Rachor had been appointed as President of Sonic on that same day. In addition to serving as President, Mr. Rachor will continue to serve as our Chief Operating Officer. We do not anticipate that Mr. Wright's resignation from our company will have a material adverse effect on our results of operations.

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

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

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

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

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

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

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

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

Pursuant to applicable accounting pronouncements, we test goodwill for impairment annually or more frequently if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. We describe the process for testing goodwill more thoroughly in our Annual Report on Form 10-K under the heading “Management’s Discussion and Analysis of Financial Condition and Results of Operations - Use of Estimates and Critical Accounting Policies.” If we determine that the amount of our goodwill is impaired at any point in time, we will be required to reduce goodwill on our balance sheet. A reduction in the amount of goodwill on our balance sheet will require us to record a non-cash impairment charge against our earnings for the period in which the impairment of goodwill occurred. This would have a material adverse impact on our earnings for that period.

Poor performance in one or more of our geographic divisions could constitute an event or change in circumstances for purposes of determining whether the fair value of our goodwill has been reduced below the carrying amount. We would therefore be required to test our goodwill for impairment. As of September 30, 2004, our balance sheet reflected a carrying amount of approximately $1,057.5 million in goodwill (including amounts classified as assets held for sale), which was allocated between four geographic reporting units. If the goodwill in any of our reporting units is impaired, we will record a significant non-cash impairment charge that would very likely have a material adverse effect on our earnings for the period in which the impairment of goodwill occurred.