LITHIA MOTORS INC
Form 10-Q
April 30, 2010
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2010

OR

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

For the transition period from______ to______

Commission file number: 001-14733

LITHIA MOTORS, INC.

(Exact name of registrant as specified in its charter)

Oregon	**93-0572810**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
360 E. Jackson Street, Medford, Oregon	**97501**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code: 541-776-6899

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

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

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

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨ (Do not check if a smaller reporting company)	Smaller reporting company	¨

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

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

Class A common stock without par value	**22,214,702**
Class B common stock without par value	**3,762,231**
(Class)	(Outstanding at April 30, 2010)

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LITHIA MOTORS, INC.

FORM 10-Q

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements

LITHIA MOTORS, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(In thousands)

(Unaudited)

	March 31, 2010	December 31, 2009
Assets		
Current Assets:		
Cash and cash equivalents	$ 11,421	$ 12,776
Contracts in transit	26,046	21,940
Trade receivables, net of allowance for doubtful accounts of $235 and $218	34,635	30,157
Inventories, net	360,025	328,726
Vehicles leased to others, current portion	7,638	7,384
Prepaid expenses and other	2,667	5,387
Assets held for sale	2,202	11,693
Total Current Assets	444,634	418,063
Land and buildings, net of accumulated depreciation of $27,334 and $25,495	323,194	326,625
Equipment and other, net of accumulated depreciation of $60,729 and $57,979	56,975	59,429
Other intangible assets, net of accumulated amortization of $100 and $93	42,639	42,496
Other non-current assets	8,584	7,752
Deferred income taxes	45,474	40,735
Total Assets	$ 921,500	$ 895,100
Liabilities and Stockholders' Equity		
Current Liabilities:		
Floorplan notes payable	$ 71,839	$ 68,907
Floorplan notes payable: non-trade	165,084	141,581
Current maturities of line of credit		24,000
Current maturities of other long-term debt	23,837	14,303
Trade payables	26,345	18,782
Accrued liabilities	55,032	47,518
Deferred income taxes	546	1,036
Liabilities related to assets held for sale	2,140	5,050
Total Current Liabilities	344,823	321,177
Real estate debt, less current maturities	231,285	230,265
Other long-term debt, less current maturities	2,763	2,800
Deferred revenue	19,067	17,981
Other long-term liabilities	15,084	15,839
Total Liabilities	613,022	588,062

Stockholders' Equity:		
Preferred stock no par value; authorized 15,000 shares; none outstanding		
Class A common stock no par value; authorized 100,000 shares; issued and outstanding 22,111 and 22,036	282,077	280,880
Class B common stock no par value; authorized 25,000 shares; issued and outstanding 3,762 and 3,762	468	468
Additional paid-in capital	9,955	10,501
Accumulated other comprehensive loss	(4,328)	(3,850)
Retained earnings	20,306	19,039
Total Stockholders' Equity	308,478	307,038
Total Liabilities and Stockholders' Equity	$ 921,500	$ 895,100

The accompanying notes are in integral part of these consolidated statements.

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LITHIA MOTORS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share amounts)

(Unaudited)

	Three months ended March 31, 2010	2009
Revenues:		
New vehicle sales	$ 217,447	$ 194,318
Used vehicle sales	160,688	126,230
Finance and insurance	14,740	13,646
Service, body and parts	69,696	73,878
Fleet and other	806	573
Total revenues	463,377	408,645
Cost of sales:		
New vehicle sales	198,913	177,470
Used vehicle sales	141,615	112,190
Service, body and parts	35,784	38,809
Fleet and other	451	214
Total cost of sales	376,763	328,683
Gross profit	86,614	79,962
Asset impairment charges	1,491	1,653
Selling, general and administrative	71,881	69,832
Depreciation buildings	1,581	1,228
Depreciation and amortization other	3,170	2,886
Operating income	8,491	4,363
Other income (expense):		
Floorplan interest expense	(2,783)	(2,929)
Other interest expense	(3,588)	(3,987)
Other income, net	66	1,165
Total other expense	(6,305)	(5,751)
Income (loss) from continuing operations before income taxes	2,186	(1,388)
Income tax (expense) benefit	(844)	615
Income (loss) from continuing operations, net of tax	1,342	(773)
Income (loss) from discontinued operations, net of tax	(75)	2,102
Net income	$ 1,267	$ 1,329
Basic income (loss) per share from continuing operations	$ 0.05	$ (0.04)
Basic income (loss) per share from discontinued operations	(0.00)	0.10
Basic net income per share	$ 0.05	$ 0.06

Shares used in basic per share calculations		25,895		20,750
Diluted income (loss) per share from continuing operations	$	0.05	$	(0.04)
Diluted income (loss) per share from discontinued operations		(0.00)		0.10
Diluted net income per share	$	0.05	$	0.06
Shares used in diluted per share calculations		26,019		20,750

The accompanying notes are an integral part of these consolidated statements.

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LITHIA MOTORS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	Three months ended March 31, 2010	2009
Cash flows from operating activities:		
Net income	$ 1,267	$ 1,329
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Asset impairments	1,491	1,653
Depreciation and amortization	4,751	4,114
Depreciation and amortization within discontinued operations	2	214
Amortization of debt discount		48
Stock-based compensation	441	564
Gain on early extinguishment of debt		(1,086)
(Gain) loss on disposal of other assets	(300)	(747)
(Gain) loss from disposal activities within discontinued operations	17	(5,853)
Deferred income taxes	(5,264)	1,225
Excess tax deficits from share-based payment arrangements	329	77
(Increase) decrease, net of effect of divestitures:		
Trade receivables, net	(4,478)	5,374
Contracts in transit	(4,106)	4,210
Inventories	(24,330)	33,017
Vehicles leased to others	(569)	448
Prepaid expenses and other	2,332	17,916
Other non-current assets	(832)	434
Increase (decrease), net of effect of divestitures:		
Floorplan notes payable	4,163	(60,504)
Trade payables	7,563	607
Accrued liabilities	7,234	788
Other long-term liabilities and deferred revenue	(160)	11,898
Net cash provided by (used in) operating activities	(10,449)	15,726
Cash flows from investing activities:		
Capital expenditures:		
Non-financeable	(583)	(1,914)
Financeable	(206)	(7,131)
Proceeds from sale of other assets	2,144	5,551
Proceeds from sale of stores	421	11,642
Net cash provided by investing activities	1,776	8,148
Cash flows from financing activities:		
Borrowings (repayments) under floorplan notes payable: non-trade	20,615	(16,111)
Borrowings on lines of credit		15,000
Repayments on lines of credit	(24,000)	(26,000)
Principal payments on long-term debt, scheduled	(2,038)	(2,794)
Principal payments on long-term debt and capital leases, other	(13,361)	(19,476)
Proceeds from issuance of long-term debt	25,893	23,216
Proceeds from issuance of common stock	554	599

Repurchase of common stock		(16)		(1)
Excess tax deficits from share-based payment arrangements		(329)		(77)
Net cash provided by (used in) financing activities		7,318		(25,644)
Decrease in cash and cash equivalents		(1,355)		(1,770)
Cash and cash equivalents:				
Beginning of period		12,776		10,874
End of period	$	11,421	$	9,104
Supplemental disclosure of cash flow information:				
Cash paid during the period for interest	$	(6,392)	$	(8,789)
Cash refunded during the period for income taxes, net		1,180		17,891
Supplemental schedule of non-cash investing and financing activities:				
Floorplan debt paid in connection with store disposals	$		$	13,061

The accompanying notes are in integral part of these consolidated statements.

LITHIA MOTORS, INC. AND SUBSIDIARIES

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1. Interim Financial Statements

Basis of Presentation

These condensed consolidated financial statements contain unaudited information as of March 31, 2010 and for the three-month periods ended March 31, 2010 and 2009. The unaudited interim financial statements have been prepared pursuant to the rules and regulations for reporting on Form 10-Q. Accordingly, certain disclosures required by accounting principles generally accepted in the United States of America for annual financial statements are not included herein. In management s opinion, these unaudited financial statements include all adjustments necessary for a fair presentation of the information when read in conjunction with our 2009 audited consolidated financial statements and the related notes thereto. The financial information as of December 31, 2009 is derived from our 2009 Annual Report on Form 10-K. The interim condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and the notes thereto included in our 2009 Annual Report on Form 10-K. The results of operations for the interim periods presented are not necessarily indicative of the results to be expected for the full year.

Concentrations of Risk and Uncertainties Regarding Manufacturers

We purchase substantially all of our new vehicles and inventory from various manufacturers at the prevailing prices charged by auto makers to all franchised dealers. Our overall sales could be impacted by the auto manufacturers inability or unwillingness to supply the dealerships with an adequate supply of popular models.

We enter into agreements (Franchise Agreements) with the manufacturers. Each Franchise Agreement generally limits the location of the dealership and provides the auto manufacturer approval rights over changes in dealership management and ownership. The auto manufacturers are also entitled to terminate the Franchise Agreements if the dealerships are in material breach of the terms. Our ability to expand operations depends, in part, on obtaining consents of the manufacturers for the acquisition of additional dealerships.

We are subject to a concentration of risk in the event of financial distress, including potential reorganization or bankruptcy, of a major vehicle manufacturer. We purchase substantially all of our new vehicles from various manufacturers or distributors at the prevailing prices available to all franchised dealers. Our sales volume could be materially adversely impacted by the manufacturers or distributors inability to supply the stores with an adequate supply of vehicles and related financing. Our Chrysler, General Motors (GM) and Ford (collectively, the Domestic Manufacturers) stores represented approximately 28%, 18% and 6% of our new vehicle sales for the first three months of 2010, respectively, and approximately 31%, 17% and 5% for all of 2009, respectively.

We receive incentives and rebates from our manufacturers, including cash allowances, financing programs, discounts, holdbacks and other incentives. These incentives are recorded as receivables on our balance sheet until payment is received. Our financial condition could be materially adversely impacted by the manufacturers or distributors inability to continue to offer these incentives and rebates at substantially similar terms, or to pay our outstanding receivables. Total receivables from Domestic Manufacturers were $9.0 million and $7.2 million as of March 31, 2010 and December 31, 2009, respectively.

We currently have relationships with a number of manufacturers or their affiliated finance companies, including GMAC LLC, Daimler Financial, Toyota Financial Services, Ford Motor Credit Company, VW Credit, Inc., American Honda Finance Corporation, Nissan Motor Acceptance Corporation and BMW Financial Services NA, LLC. These companies provide new vehicle floorplan financing for their respective brands. GMAC LLC serves as the primary lenders for all other brands. At March 31, 2010,

GMAC was the floorplan provider on approximately 68.9% of the floorplan notes payable outstanding. Certain of these companies have incurred significant losses and are operating under financial constraints. Other companies may incur losses in the future or undergo funding limitations. As a result, credit that has typically been extended to us by the companies may be modified with terms unacceptable to us or revoked entirely. If these events were to occur, we may not be able to pay our floorplan debts or borrow sufficient funds to refinance the vehicles. Even if new financing were available, it may not be on terms acceptable to us.

Most manufacturers have experienced significant declines in sales due to the current economic recession. Many have disclosed substantial operating losses over the recent past. Two of these manufacturers, Chrysler and GM, filed a petition for Chapter 11 bankruptcy protection in the second quarter of 2009. Both succeeded in receiving approval for the transfer and sale of key operating assets into new companies with reduced debt, improved operating efficiencies, new ownership and resized operations.

In connection with its reorganization, the Chrysler entity emerging from bankruptcy protection (New Chrysler) assumed most Dealer Sales and Service (franchise) Agreements but elected to reject certain franchise agreements to reduce its dealer count. Two of our Chrysler stores (Omaha, NE Chrysler Jeep Dodge and Colorado Springs, CO Chrysler Jeep) were not assumed and those dealerships have ceased operations. Five of our existing Dodge dealerships were awarded additional franchises to sell either the Chrysler or Jeep brands, or both.

GM undertook a similar process in its reorganization, and selected certain dealerships within its network for termination. The terminated dealerships were offered agreements winding down their operations with a final termination no later than October 2010. The GM closure list was not made public, and each terminated dealership signed a non-disclosure agreement with respect to its closure. We received franchise agreement modification documents that terminate all operations at three locations, terminate Cadillac franchises at two Chevrolet/Cadillac stores, and terminate heavy truck franchises at two Chevrolet franchises. We have also received notification that our one Saturn franchise would not be continued by GM, and we terminated the franchise in December 2009.

Federal legislation was passed in December 2009 which provides terminated Chrysler dealers and GM dealers who have closed or have signed wind-down letters, the opportunity to pursue reinstatements through an arbitration proceeding. The legislation provides that the arbitrator, under the auspices of the American Arbitration Association, shall balance the economic interest of the covered dealership, the economic interest of the manufacturer and the economic interest of the public at large and shall decide, based upon that balancing, whether or not the covered dealership should be reinstated in the dealer network.

We filed notice of arbitration with respect to our previous Colorado Springs, CO Chrysler Jeep store; however, we withdrew the notice in the first quarter of 2010. We also filed notice of arbitration with respect to three GM stores. We continue to negotiate with GM for the full reinstatement of these stores.

As a result of this legislation, it is possible that we could lose the recently awarded additional brands at the five Chrysler stores or have competing points reinstated in these markets. Further, such reinstatements could add additional costs and burdens on the reorganized manufacturers, reducing their competitiveness. We are unable to predict the ultimate financial impact on our business, if any.

As evidenced by the recent bankruptcy proceedings of both Chrysler and GM, state dealer laws do not afford continued protection from manufacturer terminations or non-renewal of franchise agreements under federal bankruptcy laws. While we do not believe additional bankruptcy filings are probable, no assurances can be given that a manufacturer will not seek protection under bankruptcy laws, or that, in this event, they will not seek to terminate franchise rights held by us.

While New Chrysler and GM have both emerged from bankruptcy protection and completed their reorganizations, and much of the near-term risk to the viability of the suppliers has been mitigated, the future remains uncertain. The success of the reorganizations and Chrysler s integration with Fiat S.p.A., are unknown. The future financial condition of GM and New Chrysler, and their ability to provide products that result in sales and profits consistent with historical results is at risk. Resizing operations could negatively impact the volume of vehicles produced and made available to dealers. Shortages in inventory for any manufacturer as a result of production delays, recalls or other factors could also have a negative impact on our sales volumes and financial results. As such, no assurances can be given that our financial condition, results of operations and cash flows will not be adversely impacted in the future.

Note 2. Inventories

Inventories are valued at the lower of market value or cost, using a pooled approach for vehicles and the specific identification method for parts. The cost of new and used vehicle inventories includes the cost of any equipment added, reconditioning and transportation. Inventories consisted of the following (in thousands):

	March 31, 2010	December 31, 2009
New and program vehicles	$ 264,259	$ 238,814
Used vehicles	75,157	70,819
Parts and accessories	20,609	19,093
	$ 360,025	$ 328,726

Note 3. Credit Facility Amendment

In January 2010, we executed the eighth amendment to our Credit Facility, which increased the amount allowable for letters of credit to $2.0 million. In February 2010, we executed the ninth amendment to our Credit Facility, which altered the definition of vehicle equity in the agreement to allow more vehicles to be included in the borrowing base calculation.

We had $0 and $24.0 million outstanding on our Credit Facility as of March 31, 2010 and December 31, 2009, respectively. The Credit Facility matures in October 2010.

Note 4. Contingencies

Litigation

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

Phillips/Allen/Aripe Cases

On November 25, 2003, Aimee Phillips filed a lawsuit in the U.S. District Court for the District of Oregon (Case No. 03-3109-HO) against Lithia Motors, Inc. and two of its wholly-owned subsidiaries alleging violations of state and federal RICO laws, the Oregon Unfair Trade Practices Act (UTPA) and common law fraud. Ms. Phillips seeks damages, attorney s fees and injunctive relief. Ms. Phillips complaint stems from her purchase of a Toyota Tacoma pick-up truck on July 6, 2002. On May 14, 2004, we filed an answer to Ms. Phillips Complaint. This case was consolidated with the Allen case described below and has a similar current procedural status.

On April 28, 2004, Robert Allen and 29 other plaintiffs (Allen Plaintiffs) filed a lawsuit in the U.S. District Court for the District of Oregon (Case No. 04-3032-HO) against Lithia Motors, Inc. and three of its wholly-owned subsidiaries alleging violations of state and federal RICO laws, the Oregon UTPA and common law fraud. The Allen Plaintiffs seek damages, attorney s fees and injunctive relief. The Allen Plaintiffs Complaint stems from vehicle purchases made at Lithia stores between July 2000 and April 2001. On August 27, 2004, we filed a Motion to Dismiss the Complaint. On May 26, 2005, the

Court entered an Order granting Defendants Motion to Dismiss plaintiffs state and federal RICO claims with prejudice. The Court declined to exercise supplemental jurisdiction over plaintiffs UTPA and fraud claims. Plaintiffs filed a Motion to Reconsider the dismissal Order. On August 23, 2005, the Court granted Plaintiffs Motion for Reconsideration and permitted the filing of a Second Amended Complaint (SAC). On September 21, 2005, the Allen Plaintiffs, along with Ms. Phillips, filed the SAC. In this complaint, the Allen plaintiffs seek actual damages that total less than $500,000, trebled, approximately $3.0 million in mental distress claims, trebled, punitive damages of $15.0 million, attorney s fees and injunctive relief. The SAC added as defendants certain officers and employees of Lithia. In addition, the SAC added a claim for relief based on the Truth in Lending Act (TILA). On November 14, 2005 we filed a second Motion to Dismiss the Complaint and a Motion to Compel Arbitration. In two subsequent rulings, the Court has dismissed all claims except those under Oregon s Unfair Trade Practices Act and a single fraud claim for a named individual. We believe the actions of the court have significantly narrowed the claims and potential damages sought by the plaintiffs. Discovery is completed and a resolution of the case is expected by the end of 2010.

On September 23, 2005, Maria Anabel Aripe and 19 other plaintiffs (Aripe Plaintiffs) filed a lawsuit in the U.S. District Court for the District of Oregon (Case No. 05-3083-HO) against Lithia Motors, Inc., 12 of its wholly-owned subsidiaries and certain officers and employees of Lithia, alleging violations of state and federal RICO laws, the Oregon UTPA, common law fraud and TILA. The Aripe Plaintiffs seek actual damages of less than $600,000, trebled, approximately $3.7 million in mental distress claims, trebled, punitive damages of $12.6 million, attorney s fees and injunctive relief. The Aripe Plaintiffs Complaint stems from vehicle purchases made at Lithia stores between May 2001 and August 2005 and is substantially similar to the allegations made in the Allen case. On July 27, 2009, we filed a Motion to Dismiss all claims with the Arbitrators hearing the dispute. On September 30, 2009, the Chief Arbitrator issued an Order acknowledging the voluntary withdrawal of the federal RICO claims by the Plaintiff and dismissed the claim for emotional distress damages. Further motions are pending, but the most significant monetary exposures have been removed from the case.

Alaska Service and Parts Advisors and Managers Overtime Suit

On March 22, 2006, seven former employees in Alaska brought suit against Lithia (Dunham, et al. v. Lithia Support Services, et al., 3AN-06-6338 Civil, Superior Court for the State of Alaska) seeking overtime wages, additional liquidated damages and attorney s fees. The complaint was later amended to include a total of 11 named plaintiffs. The court ordered the dispute to arbitration. In February 2008, the arbitrator granted the plaintiffs request to establish a class of plaintiffs consisting of all present and former service and parts department employees totaling approximately 150 individuals who were paid on a commission basis. We have filed a motion requesting reconsideration of this class certification, but the arbitrator died before issuing his opinion. The reconsideration sought a ruling whether these employees or some of these employees are exempt from the applicable state law that provides for the payment of overtime under certain circumstances. The replacement arbitrator has now been appointed and recently ruled to remove all service and parts managers from the case. A class action opt-out notice was mailed to the service and parts employees in October 2009. No arbitration date has been set.

We intend to vigorously defend all matters noted above, and to assert available defenses. We cannot make an estimate of the likelihood of negative judgment in any of these cases at this time. The ultimate resolution of the above noted cases is not expected to result in any significant settlement amounts. However, the results of these matters cannot be predicted with certainty, and an unfavorable resolution of one or more of these matters could have a material adverse effect on our results of operations, financial condition or cash flows.

Note 5. Comprehensive Income

Comprehensive income for the three-month periods ended March 31, 2010 and 2009 included the change in the fair value of cash flow hedging instruments that are reflected in stockholders equity, net of tax, instead of net income . The following table sets forth the calculation of comprehensive income (in thousands):

	Three Months Ended March 31,	
	2010	2009
Net income	$ 1,267	$ 1,329
Cash flow hedges:		
Derivative gain (loss), net of tax effect of $294 and $(483), respectively	(478)	831
Comprehensive income	$ 789	$ 2,160

Note 6. 2003 Stock Incentive Plan

At our 2010 Annual Meeting of Shareholders in April 2010, our shareholders amended and restated the 2003 Stock Incentive Plan (the 2003 Plan), increasing the number of shares issuable by 600,000 shares to 2,800,000 shares.

Note 7. Reclassifications

The results of operations of stores classified as discontinued operations have been presented on a comparable basis for all periods presented in the accompanying consolidated statements of operations. See also Note 13.

Note 8. Earnings (Loss) Per Share

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

Except with respect to voting rights, the rights of the holders of our Class A and Class B common stock are identical. Our Articles of Incorporation require that the Class A and Class B common stock must share equally in any dividends, liquidation proceeds or other distribution with respect to our common stock and the Articles of Incorporation can only be amended by a vote of the shareholders. Additionally, Oregon law provides that amendments to our Articles of Incorporation, which would have the effect of adversely altering the rights, powers or preferences of a given class of stock, must be approved by the class of stock adversely affected by the proposed amendment. As a result, the undistributed earnings for each year are allocated based on the contractual participation rights of the Class A and Class B common shares as if the earnings for the year had been distributed. As the liquidation and dividend rights are identical, the undistributed earnings are allocated on a proportionate basis. Further, as we assume the conversion of Class B common stock in the computation of the diluted net income per share of Class A common stock, the undistributed earnings are equal to net income for that computation.

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Following is a reconciliation of the income (loss) from continuing operations and weighted average shares used for our basic earnings per share (EPS) and diluted EPS for the three months ended March 31, 2010 and 2009 (in thousands, except per share amounts):

Three Months Ended March 31,	2010		2009	
Basic EPS	**Class A**	**Class B**	**Class A**	**Class B**
Numerator:				
Income (loss) from continuing operations applicable to common stockholders	$ 1,147	$ 195	$ (633)	$ (140)
Distributed income applicable to common stockholders				
Basic undistributed (loss) income from continuing operations applicable to common stockholders	$ 1,147	$ 195	$ (633)	$ (140)
Denominator:				
Weighted average number of shares outstanding used to calculate basic income per share	22,133	3,762	16,988	3,762
Basic distributed income per share applicable to common stockholders	$	$	$	$
Basic undistributed income (loss) per share applicable to common stockholders	0.05	0.05	(0.04)	(0.04)
Basic income (loss) per share applicable to common stockholders	$ 0.05	0.05	$ (0.04)	$ (0.04)

Three Months Ended March 31,	2010		2009	
Diluted EPS	**Class A**	**Class B**	**Class A**	**Class B**
Numerator:				
Distributed income applicable to common stockholders	$	$	$	$
Reallocation of distributed income as a result of conversion of dilutive stock options				
Reallocation of distributed income due to conversion of Class B to Class A common shares outstanding				
Diluted distributed income applicable to common stockholders	$	$	$	$
Undistributed income (loss) from continuing operations applicable to common stockholders	$ 1,147	$ 195	$ (633)	$ (140)
Reallocation of undistributed income as a result of conversion of dilutive stock options	1	(1)		
Reallocation of undistributed income (loss) due to conversion of Class B to Class A	194		(140)	
Diluted undistributed income (loss) from continuing operations applicable to common stockholders	$ 1,342	$ 194	$ (773)	$ (140)

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Denominator:				
Weighted average number of shares outstanding used to calculate basic income per share	22,133	3,762	16,988	3,762
Weighted average number of shares from stock options	124			
Conversion of Class B to Class A common shares outstanding	3,762		3,762	
Weighted average number of shares outstanding used to calculate diluted income per share	26,019	3,762	20,750	3,762
Diluted distributed income per share applicable to common stockholders	$	$	$	$
Diluted undistributed income (loss) per share applicable to common stockholders	0.05	0.05	(0.04)	(0.04)
Diluted income (loss) per share available to common stockholders	$ 0.05	$ 0.05	$ (0.04)	$ (0.04)

Three Months Ended March 31,	**2010**		**2009**	
Diluted EPS	**Class A**	**Class B**	**Class A**	**Class B**
Antidilutive Securities				
2 7/8% convertible senior subordinated notes			1,177	
Shares issuable pursuant to stock options not included since they were antidilutive	734		1,858	

Note 9. Asset Impairment Charges

Long-lived assets classified as held and used and definite-lived intangible assets are reviewed for impairment whenever events or circumstances indicate that the carrying amount of assets may not be recoverable. If estimated future undiscounted net cash flows are not sufficient to recover the carrying value of the assets, an impairment charge is recorded for the amount by which the carrying value of the asset exceeds its fair value.

In the first quarter of 2010, due to changes in specific facts and circumstances on three properties held for future development, we tested certain long-lived assets for recoverability. As a result of the test, we recorded an impairment of $1.5 million as a component of asset impairment charges on our Consolidated Statements of Operations mainly related to a property for which a preliminary agreement to sell was entered into in March 2010. See also Note 12.

Note 10. Stock-Based Compensation

In the first quarter of 2010, we issued restricted stock units covering 309,000 shares of our Class A common stock to certain employees. The restricted stock units are not participating and fully vest on the fourth anniversary of the grant date. Total estimated compensation expense to be recognized over the vesting period related to these stock-based awards, calculated using a fair value methodology, is $1.5 million, of which approximately $0.3 million will be recognized in 2010.

Note 11. Derivative Instruments

We enter into interest rate swaps to manage the variability of our interest rate exposure, thus fixing a portion of our interest expense in a rising or falling rate environment. We do not enter into derivative instruments for any purpose other than to manage interest rate exposure of the 1-month LIBOR benchmark. That is, we do not engage in interest rate speculation using derivative instruments.

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

At March 31, 2010 and December 31, 2009, the net fair value of all of our agreements totaled a loss of $7.7 million and $6.9 million, respectively, which was recorded on our balance sheet as a component of accrued liabilities and other long-term liabilities. The estimated amount expected to be reclassified into earnings within the next twelve months was $2.8 million at March 31, 2010.

As of March 31, 2010, we had outstanding the following interest rate swaps with U.S. Bank Dealer Commercial Services:

- effective June 16, 2006 a ten year, $25 million interest rate swap at a fixed rate of 5.587% per annum, variable rate adjusted on the 1st and 16th of each month;
- effective January 26, 2008 a five year, $25 million interest rate swap at a fixed rate of 4.495% per annum, variable rate adjusted on the 26th of each month;
- effective May 1, 2008 a five year, $25 million interest rate swap at a fixed rate of 3.495% per annum, variable rate adjusted on the 1st and 16th of each month; and
- effective May 1, 2008 a five year, $25 million interest rate swap at a fixed rate of 3.495% per annum, variable rate adjusted on the 1st and 16th of each month.

We receive interest on all of the interest rate swaps at the one-month LIBOR rate. The one-month LIBOR rate at March 31, 2010 was 0.2486% per annum as reported in the Wall Street Journal.

The fair value of our derivative instruments was included in our balance sheet as follows:

Balance Sheet Information

(in thousands)	**Fair Value of Asset Derivatives**		**Fair Value of Liability Derivatives**	
Derivatives Designated as Hedging Instruments	**Location in Balance Sheet**	**March 31, 2010**	**Location in Balance Sheet**	**March 31, 2010**
Interest Rate Swap Contracts	Prepaid expenses and other	$	Accrued liabilities	$ 2,020
	Other non-current assets		Other long-term liabilities	5,703