

NowAuto Group, Inc.
Form 10-Q
February 22, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarter ended December 31, 2009
Commission file number 000-50709

NOWAUTO GROUP, INC.
(Exact name of small business issuer as specified in its charter)

Nevada 77-0594821
(State or other jurisdiction of (I.R.S. Employer
Incorporation or organization) Identification No.)

4240 East Elwood Street, Phoenix, Arizona 85040
(Address of principal executive offices) (Zip Code)
Registrant's Telephone Number: (480) 431-0015
Securities registered pursuant to Section 12(b) of the Act: None
Securities registered pursuant to Section 12(g) of the Act

COMMON STOCK
(Title of Class)

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

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

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

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

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

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

State the aggregate market value, based upon the closing bid price of the Common Stock as quoted on NASDAQ, of the voting stock held by non-affiliates of the registrant: \$184,661 as of February 16, 2010

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

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As of February 16, 2010 there were 9,383,046 shares, net of treasury shares, of common stock outstanding.

Item 1. Financial Statements

NowAuto Group, Inc
Condensed Consolidated Balance Sheets

	December 301 2009 (unaudited)	June 30, 2009 (audited)
Assets		
Current Assets		
Cash and Cash Equivalents	\$ 55,373	40,610
Investment in sales-type leases, net	4,280,796	3,578,326
Inventory	81,875	148,295
Prepaid Expenses	60,884	20,763
Equipment - net	49,101	69,882
Total Assets	\$ 4,528,029	3,857,876
Liabilities and Stockholders' Deficit		
Current Liabilities		
Accounts Payable	\$ 421,970	267,787
Line of Credit	11,471,100	9,996,319
Accrued Payroll	113,307	84,370
Other Liabilities	5,606	27,984
Total Liabilities	12,011,983	10,376,460
Stockholders' Deficit		
Common Stock, authorized 1,000,000,000 shares \$0.001 par value; Issued and Outstanding		
December 31, 2009 and June 30, 2009 - 9,843,046 shares issued;		
9,383,046 shares outstanding		
	9,843	9,843
Less Treasury Stock, 460,000 shares at cost	(27,499)	(27,499)
Paid in Capital	4,649,931	4,649,931
Accumulated Deficit	(12,116,229)	(11,150,859)
Total Stockholders' Deficit	(7,483,954)	(6,518,584)
Total Liabilities and Stockholders' Deficit	\$ 4,528,029	3,857,876

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

NowAuto Group, Inc
Condensed Consolidated Statements of Operations
(unaudited)

	3 Months Ended December 31, 2009 (Unaudited)	3 Months Ended December 31, 2008 As Restated	6 Months Ended December 31, 2009 (Unaudited)	6 Months Ended December 31, 2008 As Restated
Income				
Sales-type leases and other	\$ 1,185,780	\$ 1,123,178	2,332,012	\$ 1,954,902
Finance Income	295,761	238,472	576,156	512,974
Total revenue	1,481,541	1,361,650	2,908,168	2,467,876
Cost of Goods Sold				
Cost of Goods Sold	682,143	847,005	1,374,630	1,571,258
Gross Profit	799,398	514,645	1,533,538	896,618
Gross Margin	54.0%	37.8%	52.7%	36.3%
Expenses				
Selling and Financing Costs	603,614	525,790	1,121,553	997,682
General and Administrative	461,461	314,717	868,668	592,946
Loss from Operations	(265,677)	(325,862)	(456,683)	(694,010)
Interest Expense	256,991	221,352	508,687	444,029
Net Loss	\$ (522,668)	\$ (547,214)	(965,370)	\$ (1,138,039)
Basic and Diluted Loss per Share	\$ (0.06)	\$ (0.06)	\$ (0.10)	\$ (0.12)
Weighted Average Number of Common Shares Outstanding	9,383,046	9,402,046	9,383,046	9,423,046

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

NowAuto Group, Inc
Condensed Consolidated Changes in Stockholders' Deficit

	Shares	Amount	Paid in Capital	Treasury Stock	Accumulated Deficit	Total Equity
Balance June 30, 2008	9,843,046	\$ 9,843	\$ 4,649,931	\$ (12,500)	\$ (8,919,328)	\$ (4,272,054)
Stock repurchase, 60,000 shares				(14,999)		(14,999)
Net Loss					(2,231,531)	(2,231,531)
Balance June 30, 2009	9,843,046	9,843	4,649,931	(27,499)	(11,150,859)	(6,518,584)
Net Loss (Unaudited)					(965,370)	(965,370)
Balance September 30, 2009 (Unaudited)	9,843,046	\$ 9,843	\$ 4,649,931	\$ (27,499)	\$ (12,116,229)	\$ (7,483,954)

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

NowAuto Group, Inc
Condensed Consolidated Statements of Cash Flows

	6 Months Ended December 31, 2009	6 Months Ended December 31, 2008 (As restated)
Operating Activities		
Net Loss	\$ (965,370)	\$ (1,138,039)
Adjustments to reconcile Net Loss to Net Cash used in Operating Activities		
Significant Non-Cash Transactions		
Depreciation/Amortization Expense	10,795	5,951
Loss on disposal of fixed assets	14,691	39,933
Interest expense capitalized into principal	508,687	443,930
Provision for uncollectible receivables	(230,974)	43,266
Changes in assets and liabilities		
Investment in sales-type leases	(471,496)	(479,752)
Inventory	66,420	302,322
Prepaid expenses	(40,121)	22,907
Accounts payable	154,183	(91,486)
Other liabilities	6,559	(2,918)
	18,744	284,153
Net cash used in operating activities	(946,626)	(853,886)
Investing Activities		
Purchase of Fixed Assets	(4,705)	(29,973)
Net Cash provided by (used in) Investing Activities	(4,705)	(29,973)
Financing Activities		
Proceeds from line of credit	2,755,335	2,053,291
Principal payments on line of credit	(1,789,241)	(1,143,586)
Purchase in Treasury Stock	-	(11,000)
Net cash provided by Financing Activities	966,094	898,705
Net Increase in Cash	14,763	14,846
Cash, Beginning of Period	40,610	32,508
Cash, End of Period	\$ 55,373	\$ 47,354
Supplemental Information:		
Period interest	\$ -	\$ 99

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Income Taxes paid	\$	-	\$	-
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The accompanying notes are an integral part of these condensed consolidated financial statements.

Condensed Notes to Consolidated Financial Statements

Note 1. Nature of Operations and Significant Accounting Policies

Nature of Operations

NowAuto Group, Inc primarily leases vehicles in the Buy Here, Pay Here industry through the use of sales-type leases. Our customers are individuals with sub-prime credit histories. We currently operate primarily in the Phoenix, Arizona Metropolitan area.

NowAuto Group, Inc was originally formed as WH Holdings, Inc., a Nevada Corporation, on August 19, 1998. On June 8, 2004 the name was changed to Automotive Capital Group, Inc. and again changed on August 31, 2004 to NowAuto, Inc. NowAuto, Inc. was purchased by Global-E Investments, Inc. on July 22, 2005. Global-E Investments was a non-operating public shell. The stockholders of NowAuto, Inc. became the majority owners of Global-E Investments and as such, the transaction has been accounted for as a recapitalization of NowAuto, Inc. As such, all financial statements presented are the activity of NowAuto, Inc. Global-E Investments subsequently changed their name to NowAuto Group, Inc.

The Company also has a subsidiary, NavicomGPS, Inc. that was involved in the sales and installation of global positioning systems. However, this subsidiary has been largely inactive since approximately June of 2007.

General

The accompanying condensed consolidated balance sheet as of June 30, 2009, which has been derived from audited financial statements and the unaudited interim condensed financial statements as of December 31, 2009 have been prepared in accordance with generally accepted accounting principles for interim financial information and in accordance with the instructions to Form 10-Q in Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by the accounting principles generally accepted in the United States for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three months ended December 31, 2009 are not necessarily indicative of the results that may be expected for the year ending June 30, 2010. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's annual report on Form 10-K for the year ended June 30, 2009.

Principles of Consolidation

The consolidated financial statements include the accounts of NowAuto Group, Inc. and our subsidiary, NavicomGPS, Inc. All significant inter-company accounts and transactions have been eliminated.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the period. Actual results could differ from those estimates. Material estimates that are susceptible to significant change in the near term include, but are not limited to, the determination of the allowance for doubtful accounts, the realization of deferred financing revenue, and the carrying value of inventory.

Concentration of Risk

We originate our contracts and provide financing in connection with the sale and/or lease of substantially all of our vehicles. Although we attempt to mitigate our exposure to credit risk through the use of employment checks, reference checks, proof of residence, and other procedures, failure of the customers to make scheduled payments under their lease contracts could have a material near term impact on our results of operations and financial condition. In addition, all of our financing is provided through our revolving credit agreement which is held by one privately controlled venture capital fund.

Periodically, we maintain cash in financial institutions in excess of the amounts insured by the federal government.

Cash Equivalents

We consider all highly liquid instruments purchased with maturities of three months or less to be cash equivalents.

Inventory

Inventory consists of used vehicles and is valued at the lower of cost or market on a specific identification basis. Vehicles purchased at auction, or wholesale, are typically recorded at their purchase price. Repossessed vehicles are recorded at the lesser of their original cash value or their fair value, which is determined based upon the approximate wholesale value. Vehicle reconditioning costs are capitalized as a component of inventory. The cost of used vehicles sold is determined using the specific identification method.

Equipment

Property and equipment are stated at cost. Expenditures for additions, renewals and improvements are capitalized. Costs of repairs and maintenance are expensed as incurred. Leasehold improvements are amortized over the shorter of the estimated life of the improvement or the lease period. The lease period includes the primary lease term plus any extensions that are reasonably assured. Depreciation is computed principally using the straight-line method generally over the following estimated useful lives:

Furniture, fixtures and equipment	3 to 7 years
Leasehold improvements	Length of the lease, typically 1 to 3 years

Property and equipment are reviewed for impairment whenever events or changes in circumstances indicate the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying values of the impaired assets exceed the fair value of such assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

Sales Tax

We pay sales taxes to local and state governmental agencies on vehicles sold and leased. For lease agreements, sales tax is paid when funds are received from the customer. Therefore, a liability is recorded for sales tax purposes in the period the lease is paid, and remitted as they are collected. For sales contracts, calculations for sales taxes are made on an accrual basis. Vehicle repossessions are allowed as a deduction from taxable sales in the month of repossession. Customers often make their down payments in periodic increments over a period of four to six weeks. We do not report the sales for tax purposes until the down payments are fully paid. This is compliant with industry standards and with most state and local tax codes.

Income Taxes

Income taxes are accounted for under the asset and liability method. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates expected to apply in the years in which these temporary differences are expected to be recovered or settled. Deferred tax assets are reduced by a valuation allowance when in the opinion of management; it is more likely than not that some portion or all of the deferred tax assets will not be realized.

The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Interest and penalties associated with unrecognized tax benefits are classified as additional income taxes in the statement of income.

The Company's policy is to recognize interest accrued related to unrecognized tax benefits in interest expense and penalties in operating expenses.

We have adopted the provisions of Accounting Standards Codification 740-10. As of December 31, 2009, we had no liabilities, included on the consolidated balance sheets, associated with uncertain tax positions.

Revenue Recognition

Sales-type leases

The Company's financing agreements are classified as sales-type leases pursuant to the provisions of Accounting Standards Codification - 840, Accounting for Leases. As such, revenues representing the sales price of the vehicles are recognized as income upon inception of the lease, with the resulting gross profit from the sales included in operations. Lease terms are typically for a period of 36 to 39 months with either monthly or bi-monthly payments.

The portion of revenues representing the difference between the gross investment in the lease (the sum of the minimum lease payments and the guaranteed residual value) and the sum of the present value of the two components is recorded as deferred revenue and amortized over the lease term. This deferred revenue represents the effective interest rate on the sales-type lease and ranges from approximately 19% to 29% per annum.

For the three months ended December 31, 2009 and 2008, amortization of deferred revenue totaled \$295,761 and \$238,472, respectively. For the six months ended December 31, 2009 and 2008, the total is \$576,156 and \$512,974 respectively.

Taxes assessed by governmental authorities that are directly imposed on revenue-producing transactions between the Company and its customers (which may include, but are not limited to, sales, use, value added and some excise taxes) are excluded from revenues.

Lessees are responsible for all taxes, insurance, and maintenance costs.

Repossessions

If the lessee ceases making payments pursuant to the lease terms and the decision is made by the Company to repossess the vehicle the lease is considered terminated. In such an event, the remaining balance of the lease is removed from the Investment in Sales-Type Leases, the repossessed vehicle is recorded as inventory at the lower of its original cost or its fair value at wholesale, and any resulting adjustment is charged to income during the period.

Advertising Costs

Advertising costs are expensed as incurred and consist principally of radio, television and print media marketing costs. Advertising costs amounted to \$17,414 and \$13,742 for the quarters ended December 31, 2009 and 2008, respectively. For the six months ended December 31, 2009 and 2008, the total is \$40,190 and \$44,469 respectively.

Loss per Share

The loss per share (“EPS”) is presented in accordance with the provisions of Accounting Standards Codification - 260. Basic EPS is calculated by dividing the income or loss available to common shareholders by the weighted average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock. Basic and diluted EPS were the same for fiscal 2009 and 2008, as the Company had losses from operations during both years and therefore the effect of all potential common stock equivalents is antidilutive (reduces loss per share). There were no warrants or options outstanding as of December 31, 2009.

Stock Option Plans

As of December 31, 2009 we had no employee stock ownership plan.

Allowance for Delinquent Leases

Provisions for losses on leases in default are charged to operations in amounts sufficient to maintain the allowance for delinquent leases at a level considered adequate to cover probable credit losses.

The Company established the allowance for delinquent leases based on the determination of the amount of probable credit losses inherent in the finance receivables as of the reporting date. The Company reviews charge-off experience factors, delinquency reports, historical collection rates, estimates of the value of the underlying collateral, economic trends, such as unemployment rates, industry standards and other information in order to make the necessary judgments as to probable credit losses. Assumptions regarding probable credit losses and loss confirmation periods are reviewed periodically and may be impacted by actual performance of finance receivables and changes in any of the factors discussed above.

Note 2. Non-Classified Balance Sheet

We are a finance company, originating and financing all of our own leasing contracts. These contracts are 36 to 39 months in length. Therefore, our balance sheet is presented on a non-classified basis.

Note 3. Investment in Sales-Type Leases – net

The Company's leasing operations consist principally of leasing vehicles under sales-type leases expiring in various years to 2012. Following is a summary of the components of the Company's net investment in sales-type leases:

	December 31, 2009 (Unaudited)	June 30, 2009
Total Minimum Lease Payment to be Received	\$ 7,063,921	\$ 6,447,089
Residual Value	348,700	260,050
Lease Carrying Value	7,412,621	6,707,139
Less: Allowance for Uncollectible Amounts	(1,256,927)	(1,487,901)
Less: Unearned Income	(1,874,898)	(1,640,912)
Net Investment in Sales-Type Leases	\$ 4,280,796	\$ 3,578,326

A schedule of future minimum lease payments for each of the next three years is as follows:

Years Ending	December 31,	
	2009	June 30, 2009
	(Unaudited)	
2010	\$ 3,995,796	\$ 3,610,370
2011	1,695,341	1,547,301
2012	1,412,784	1,289,418
Total	7,063,921	6,447,089

Note 4. Property and Equipment

A summary of equipment and accumulated depreciation is as follows:

	December 31,	
	2009	June 30, 2009
	(Unaudited)	
Furniture, fixtures and equipment	\$ 45,558	\$ 31,740
Leasehold improvements	3,448	27,323
Computers and miscellaneous	47,321	47,964
	96,327	107,027
Less: accumulated depreciation	(47,226)	(37,145)
	\$ 49,101	\$ 69,882

Note 5. Income Taxes

The significant components of the Company's deferred tax assets are as follows:

	December 31,	June 30,
	2009	2009
	(Unaudited)	
Deferred tax assets		
Net operating losses carryforward	\$ 3,640,000	\$ 3,257,000
Less: valuation allowance	(3,640,000)	(3,257,000)
Deferred tax assets	\$ -	\$ -

At December 31, 2009, the Company has incurred accumulated net operating losses totaling approximately 9,100,000, which are available to reduce federal and state taxable income in future years.

Note 6. Contract Financing

As of December 31, 2009 the Company had a revolving credit agreement with a private equity fund. The credit agreement is secured by the lease contracts it agrees to fund, as well as the underlying vehicle. The monies advanced under the line of credit are based upon the contract price and vary per contract, at the discretion of the lender. Substantially all the sales-type lease contracts financed require our customers to make their monthly payments directly to the finance company via ACH (automatic account withdrawal). The Company retains ownership of the contracts and is active in the collection of delinquent accounts from the contracts. The line of credit matures and renews annually on February 6th. At inception, March 31, 2006, our credit limit was \$3,000,000. This limit has been

expanded by the lender to its current \$12,000,000 limit. The interest rate is at the prime lending rate plus 6% (9.25% at December 31, 2009).

The revolving credit agreement has two debt covenants. The Company must maintain a tangible net worth of at least \$2,000,000 and a leverage ratio that total liabilities cannot exceed four times the tangible net worth. As of December 31, 2009 we are not in compliance with either of these covenants, however we have a strong relationship with our lender and do not anticipate any problems as a result.

Note 7. The Effect of Recently Issued Accounting Standards

Recent Accounting Pronouncements

The company does not expect the adoption of any accounting pronouncements issued since those disclosed in the company's annual report on Form 10-K for the year ended June 30, 2009 to have a significant impact on the company's results of operations, financial position or cash flow.

Note 8. Going Concern

The accompanying financial statements have been prepared assuming that we will continue as a going concern. We sustained a material loss in the year ended June 30, 2005. This loss continued through June 30, 2009. This raises substantial doubt about our ability to continue as a going concern. The financial statements do not include any adjustments that might result from this uncertainty.

Since that initial loss, great efforts have been made to improve our profitability. Margins on cars sold have increased. Costs, especially overhead, have been reduced. Head count is kept to a minimum. Accountability has been greatly enhanced by development of qualified Accounting staff and the implementation of an enterprise-wide and fully integrated software system. The Company has been and continues to develop the financing function whose focus includes, but is not limited to improved stability scoring and credit approval process, improvement of the total portfolio aging, and reduction of account losses. On the date of this report, the corporate office and Service Department relocated to the same facility. This new facility greatly enhances the Service Department's efficiency and capacity and gives upper management closer oversight of operations.

A detailed discussion of management's plans for dealing with this issue is in the Company's annual report of Form 10-K for the year ended June 30, 2009.

Note 9. Subsequent Events

Subsequent events have been evaluated and disclosed through the date of this filing, which is the date these consolidated financial statements were issued.

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

The following discussion should be read in conjunction with the Company's consolidated financial statements and notes thereto appearing elsewhere in this report.

Forward-looking Information

The Private Securities Litigation Reform Act of 1995 provides a "safe harbor" for certain forward-looking statements. Certain information included in this Quarterly Report on Form 10-Q contains, and other materials filed or to be filed by the Company with the Securities and Exchange Commission (as well as information included in oral statements or other written statements made or to be made by the Company or its management) contain or will contain, forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, and Section 27A of the Securities Act of 1933, as amended. The words "believe," "expect," "anticipate," "estimate," "project" and similar expressions identify forward-looking statements, which speak only as of the date the statement was made. The Company undertakes no obligation to publicly update or revise any forward-looking statements. Such forward-looking statements are based upon management's current plans or expectations and are subject to a number of uncertainties and risks that could significantly affect current plans, anticipated actions and the Company's future financial conditions and results. As a consequence, actual results may differ materially from those expressed in any forward-looking statements made by or on behalf of the Company as a result of various factors. Any forward-looking statements are made pursuant to the Private Securities Litigation Reform Act of 1995 and, as such, speak only as of the date made.

Overview

Since 2004, NowAuto Group, Inc., a Nevada corporation (the "Company") is a publicly held retailer focused on the "Buy Here/Pay Here" segment of the used vehicle market. The Company generally sells 1999 and newer model-year used vehicles and provides financing for substantially all of its customers. Many of the Company's customers have limited financial resources and would not qualify for conventional financing as a result of limited credit histories or past credit problems. As of December 31, 2009 the Company had three stores, all of which are located in the State of Arizona.

The market for used vehicle sales in the United States is significant. Used vehicle retail sales typically occur through franchised new vehicle dealerships that sell used vehicles, or independent used vehicle dealerships. The Company operates in the "Buy Here/Pay Here" segment of the independent used vehicle sales and finance market. Buy Here/Pay Here dealers sell and finance used vehicles to individuals with limited credit histories or past credit problems. Buy Here/Pay Here dealers typically offer their customers certain advantages over more traditional financing sources, such as broader and more flexible credit terms, attractive payment terms, including scheduling payments on a weekly or bi-weekly basis to coincide with a customer's payday, and the ability to make payments in person, an important feature to individuals who may not have checking accounts. In turn, interest rates on vehicle loans provided by the Company are generally higher than those offered to individuals who purchase from other new or used vehicle dealers or who have better credit histories.

The Company's primary focus is on sales and collections. The Company is responsible for its own collections through its internal collection department with supervisory involvement of the corporate office. In the past year the Company implemented new and stricter underwriting criteria at the store level. In addition the Company implemented stricter contract criteria, which in the short term, resulted in higher repossessions and charge-off accounts. In addition, credit losses are also imparted, to some degree, by economic conditions in the markets in which the Company serves. In recent months, adverse economic conditions have had a negative impact on collection results. While the Company

believes the most significant factor affecting credit losses is the proper execution (or lack therefore) of its business practices, the Company also believes that current economic conditions have had a negative impact on its operations and results.

Hiring, training and retaining qualified personnel are critical to the Company's success. The number of trained managers the Company has at its disposal will limit the rate at which the Company adds new stores. Excessive turnover, particularly at the store manager level, could impact the Company's ability to add new stores. The Company expects to continue to invest in the development of its workforce.

Three Months and Six Months Ended December 31, 2009 vs. Three Months and Six Months Ended December 31, 2008

Total revenue for the quarter ended December 31, 2009 was \$1,481,541 versus revenue of \$1,361,650 for the quarter ended December 31, 2008. Total revenue for the six months ended December 31, 2009 and 2008 totaled \$2,908,168 and \$2,467,876 respectively. For the three month ended December 31, 2009 and 2008, average sales price per unit declined from approximately \$9,700 to \$7,600 while volume increased only 2%. The Company has been able to purchase units at significantly better prices and therefore are able to offer a lower sales price. Our customer base has increased due to the current economy increasing volume in prior periods. However, the seasonal downturn has kept volume constant.

The Company's gross profit as a percentage of sales during the quarter ending December 31, 2009 was 54.7% vs. 37.8% for the quarter ended December 31, 2008. There are two reasons for the increase. The first is better capture and recovery of costs in the sales price. Account losses during the quarter ending December 31, 2009 have declined from previous quarters thus increasing interest earnings on active accounts.

During the quarter ended December 31, 2009 the Company experienced a slight increase in bad accounts of approximately 5% from the previous year. However, bad debt losses for the six months ended December 31, 2009 improved 20% from the previous year and is still below normal. The Company believes the improvement in bad debt losses is due to, among other things, stricter underwriting criteria and improved collection practices. While the Company believes that proper execution (or lack thereof) of its business practices is the most significant factor affecting credit losses, the Company also believes that general economic conditions, including but not limited to rising unemployment and troubled credit markets adversely affect collection efforts and may result in higher than normal account losses for the foreseeable future. General and Administrative expenses as a percentage of revenue for the three months ended December 31, 2009 increased over the prior year to 31.3% of revenue due primarily to increased costs for labor, health insurance, and professional fees.

Total operating expenses were 71.9% of total revenues for the quarter ended December 31, 2009 versus 61.7% for the quarter ended December 31, 2008. Most of the change is due to increased labor cost including increased staff as well as health insurance and professional fees as stated previously.

Financial Condition

The following sets forth the major balance sheet accounts of the Company as of the dates specified.

	December 31, 2009 (Unaudited)	June 30, 2009
Investments in Sale-type leases, net	\$ 4,280,796	\$ 3,578,326
Inventory	81,875	148,295
Equipment	49,101	69,882
Accounts Payable	421,970	267,787

Liquidity and Capital Resources

The Company's liabilities exceeded its assets by approximately \$7,500,000 as of December 31, 2009. The deterioration in our financial condition was primarily the result of our net loss during the operating period.

Cash and cash equivalents at December 31, 2009 were approximately \$55,000. Our investment in sales-type leases increased by approximately \$702,000 during the six months ended December 31, 2009. As our contract terms are 36 to 39 months, we will be collecting on our investment in these leases over the next several years. Inventory of vehicles on December 31, 2009 was approximately \$82,000 versus \$148,000 on June 30, 2009, a decrease of \$66,000. The decrease is due to increases in sales and the Company's position of not using a floor plan to carry extra inventory.

Net cash used in investing activities during the current period was approximately \$5,000, compared to net cash used in investing activities in the six months ended December 31, 2008 of \$30,000. The current period decrease was primarily due to a reduction in the purchase of office equipment. Net cash provided by financing activities during the six months ended December 31, 2009 was approximately \$966,000 versus approximately \$899,000 for the six months ended December 31, 2008. This activity is a result of the revolving credit agreement.

At December 31, 2009, the Company had approximately a \$11.5 million line of credit balance under a \$12 million line of credit agreement with a privately held, independent finance company. Interest rate on the line of credit agreement is at prime plus 6% (9.25% at December 31, 2009). The line of credit agreement has two covenants (see Note 6 to the accompanying financial statements), neither of which the Company is in compliance with as of December 31, 2009. However, management believes they have a positive relationship with the independent finance company and does not expect any collection activity as a result of these defaults. The original line of credit with the lender at its inception in 2006 was \$3,000,000 and the lender has periodically and consistently increased the limit as the need arose.

Considering the Company's current working capital position management estimates that the current cash position will not be adequate to meet cash requirements for the next twelve months and that additional draws will need to be made against the line of credit to fund operations. Subsequent to December 31, 2009, the Company has been allowed to take additional draws under the revolving credit agreement. We anticipate that we will be able to continue to draw on this credit facility as the need arises until such time as we are able to generate sufficient cash flow from operations to be self sufficient and commence repaying the debt.

Although management cannot assure that future operations will be profitable, or that additional debt and/or equity financing will be available, we believe our current cash balance, together with additional debt financing, may provide adequate capital resources to maintain operations for the next year. If additional working capital is required during fiscal 2010 and not obtained through additional debt, equity capital or operations, it could adversely affect future operations. Management has historically been successful in obtaining financing and has demonstrated the ability to implement a number of cost-cutting initiatives to reduce working capital needs. Accordingly, the condensed consolidated financial statements contained in Item 1 of this Form 10-Q have been prepared assuming the Company will continue to operate and do not include any adjustments that might be necessary if the Company is unable to continue as a going concern. As a result, the Company's independent registered public accountants issued a going concern opinion on the consolidated financial statements of the Company for the year ended June 30, 2009.

Critical Accounting Policies

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires us to make estimates and assumptions in determining the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from our estimates. We believe the most significant estimates made in the preparation of the accompanying consolidated financial statements relates to the determination of our allowance for doubtful accounts, which is discussed below, as well as our revenue recognition policy as it relates to sales-type leases, and the carrying value of our inventory.

We maintain an allowance for doubtful accounts on an aggregate basis at a level we considers sufficient to cover estimated losses in the collection of our finance receivables. This reserve is currently accrued at 33% of revenue that results from financed sales or leases. The rate is periodically reviewed by management and changed to reflect current operations. Although it is at least reasonably possible that events or circumstances could occur in the future that are not presently foreseen which could cause actual credit losses to be materially different from the recorded allowance for credit losses, we believe that we have given appropriate consideration to all factors and have made reasonable assumptions in determining the allowance for doubtful accounts.

The SEC suggests that all registrants list their most “critical accounting policies” in Management’s Discussion and Analysis. A critical accounting policy is one which is both important to the portrayal of the Company’s financial condition and results and requires management’s most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain. Management has identified the critical accounting policies presented above as those accounting policies that affect its more significant judgments and estimates in the preparation of its consolidated financial statements. The Company’s Board of Directors has reviewed and approved the critical accounting policies identified.

Off-Balance Sheet Arrangements

As of December 31, 2009, we did not have any relationship with unconsolidated entities or financial partnerships, which other companies have established for the purpose of facilitating off-balance sheet arrangements as defined in Item 303(c)(2) of SEC Regulation S-B. Therefore, we are not materially exposed to any financing, liquidity, market or credit risk that could arise if we had engaged in such relationships.

Recent Accounting Pronouncements

Recent accounting pronouncements are more fully addressed in Note 7 to the accompanying financial statements.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Not applicable, as the Company is a smaller reporting company.

Item 4T. Controls and Procedures

(a) EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES

The Company carried out, under the supervision and with the participation of the Company’s management, including the Company’s Chief Executive Officer and the Company’s Chief Financial Officer, an evaluation of the effectiveness of the design and operation of the Company’s disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities and Exchange Act of 1934, as amended). Based on their evaluation, the Company’s Chief Executive Officer and its Chief Financial Officer concluded that, the Company’s disclosure controls and procedures were not effective as of the end of the period covered by this report, because of the material weakness identified as of June 30, 2009. Notwithstanding the existence of the material weakness identified as of June 30, 2009, management has concluded that the consolidated financial statements in this Form 10-Q fairly present, in all material respects, the Company’s financial position, results of operations and cash flows for the periods and dates presented.

(b) CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING

There were no changes in our internal control over financial reporting that occurred during our last fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

The Company is continuing the process of developing and implementing a remediation plan to address the material weaknesses as described above, as more fully discussed in the Form 10-K filing for the year ended June 30, 2009.

PART II – OTHER INFORMATION

Item 1. Legal Proceedings

As of December 31, 2009 the Company is not involved in any legal proceedings other than standard collection activities deemed to be in the normal course of business.

Item 1a. Risk Factors

No additional significant risk factors have been identified beyond those discussed in the Form 10-K filing for the year ended June 30, 2009.

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

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Submission of Matters to a Vote of Security Holders

None.

Item 5. Other Information

None.

Exhibits

3.1. Consent of Independent Registered Public Accounting Firm

31.1. Rule 13a-14(a) certification

31.2. Rule 13a-14(a) certification

32.1. Rule Section 1350 certification

SIGNATURES

In accordance with Section 13 or 15(d) of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

NOW AUTO GROUP, INC.

Date: 2/19/10 By: /s/ Scott Miller,
Scott Miller,
Chief Executive Officer

NOW AUTO GROUP, INC.

Date: 2/19/10 By: /s/ Faith Forbis
Faith Forbis
Chief Financial Officer, Principle Accounting Officer
