LKQ CORP
Form 10-Q
October 29, 2010

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended September 30, 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: 000-50404

LKQ CORPORATION

(Exact name of registrant as specified in its charter)

DELAWARE	**36-4215970**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
120 NORTH LASALLE STREET, SUITE 3300, CHICAGO, IL	**60602**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code: (312) 621-1950

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

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

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

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

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

At October 22, 2010, the registrant had issued and outstanding an aggregate of 144,422,886 shares of Common Stock.

PART I

FINANCIAL INFORMATION

Item 1. Financial Statements.

LKQ CORPORATION AND SUBSIDIARIES

Unaudited Consolidated Condensed Balance Sheets

(In thousands, except share and per share data)

	September 30, 2010	December 31, 2009
Assets		
Current Assets:		
Cash and equivalents	$ 168,678	$ 108,906
Receivables, net	167,181	152,443
Inventory	444,617	385,686
Deferred income taxes	29,924	31,847
Prepaid income taxes		4,663
Prepaid expenses	11,100	9,603
Assets of discontinued operations		9,720
Total Current Assets	821,500	702,868
Property and Equipment, net	306,820	289,902
Intangible Assets:		
Goodwill	990,589	938,783
Other intangibles, net	64,708	67,239
Other Assets	21,832	21,329
Total Assets	$ 2,205,449	$ 2,020,121
Liabilities and Stockholders Equity		
Current Liabilities:		
Accounts payable	$ 70,413	$ 51,300
Accrued expenses:		
Accrued payroll-related liabilities	42,252	37,314
Self-insurance reserves	32,513	30,368
Other accrued expenses	25,992	26,345
Income taxes payable	1,713	
Deferred revenue	9,672	9,259
Current portion of long-term obligations	39,880	10,063
Liabilities of discontinued operations	2,857	3,832
Total Current Liabilities	225,292	168,481
Long-Term Obligations, Excluding Current Portion	557,589	592,982
Deferred Income Tax Liabilities	53,179	52,209
Other Noncurrent Liabilities	32,478	27,015
Commitments and Contingencies		
Stockholders Equity:		
	1,438	1,420

Common stock, $0.01 par value, 500,000,000 shares authorized, 143,788,606 and 142,004,797 shares issued and outstanding at September 30, 2010 and December 31, 2009, respectively		
Additional paid-in capital	841,747	815,952
Retained earnings	497,202	369,459
Accumulated other comprehensive loss	(3,476)	(7,397)
Total Stockholders Equity	1,336,911	1,179,434
Total Liabilities and Stockholders Equity	$ 2,205,449	$ 2,020,121

See notes to unaudited consolidated condensed financial statements.

LKQ CORPORATION AND SUBSIDIARIES

Unaudited Consolidated Condensed Statements of Income

(In thousands, except per share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	**2009**	**2010**	**2009**
Revenue	$ 607,621	$ 494,812	$ 1,795,818	$ 1,492,037
Cost of goods sold	346,197	269,708	989,838	817,114
Gross margin	261,424	225,104	805,980	674,923
Facility and warehouse expenses	56,991	48,337	170,125	145,101
Distribution expenses	51,783	45,604	154,140	132,608
Selling, general and administrative expenses	77,671	65,893	228,437	198,688
Restructuring expenses	223	852	593	1,910
Depreciation and amortization	9,549	8,373	27,940	24,893
Operating income	65,207	56,045	224,745	171,723
Other expense (income):				
Interest expense, net	7,186	7,780	21,617	23,082
Other income, net	(274)	(23)	(573)	(170)
Total other expense, net	6,912	7,757	21,044	22,912
Income from continuing operations before provision for income taxes	58,295	48,288	203,701	148,811
Provision for income taxes	22,394	18,147	77,911	58,197
Income from continuing operations	35,901	30,141	125,790	90,614
Discontinued operations:				
(Loss) income from discontinued operations, net of taxes		(986)	224	(298)
Gain on sale of discontinued operations, net of taxes			1,729	
(Loss) income from discontinued operations		(986)	1,953	(298)
Net income	$ 35,901	$ 29,155	$ 127,743	$ 90,316
Basic earnings per share [(a)]				
Income from continuing operations	$ 0.25	$ 0.21	$ 0.88	$ 0.65
(Loss) income from discontinued operations		(0.01)	0.01	(0.00)
Total	$ 0.25	$ 0.21	$ 0.89	$ 0.64
Diluted earnings per share [(a)]				
Income from continuing operations	$ 0.25	$ 0.21	$ 0.86	$ 0.63
(Loss) income from discontinued operations		(0.01)	0.01	(0.00)
Total	$ 0.25	$ 0.20	$ 0.88	$ 0.63

Weighted average common shares outstanding:				
Basic	143,258	140,746	142,769	140,257
Diluted	145,798	144,047	145,470	143,669

(a) The sum of the individual earnings per share amounts may not equal the total due to rounding.

See notes to unaudited consolidated condensed financial statements.

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LKQ CORPORATION AND SUBSIDIARIES

Unaudited Consolidated Condensed Statements of Cash Flows

(In thousands)

	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 127,743	$ 90,316
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	30,389	27,931
Stock-based compensation expense	7,713	5,457
Deferred income taxes	(788)	2,663
Excess tax benefit from share-based payments	(9,375)	(5,744)
Gain on sale of discontinued operations	(2,744)	
Other	791	3,873
Changes in operating assets and liabilities, net of effects from acquisitions and divestitures:		
Receivables	(1,433)	18,671
Inventory	(43,818)	(24,302)
Prepaid income taxes/income taxes payable	14,566	19,887
Accounts payable	11,307	(12,722)
Other operating assets and liabilities	10,212	9,434
Net cash provided by operating activities	144,563	135,464
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment	(36,982)	(28,993)
Proceeds from sales of property and equipment	977	952
Proceeds from sale of businesses, net of cash sold	11,992	
Cash used in acquisitions, net of cash acquired	(70,281)	(18,580)
Net cash used in investing activities	(94,294)	(46,621)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from exercise of stock options	8,725	4,986
Excess tax benefit from share-based payments	9,375	5,744
Repayments of long-term debt	(8,824)	(16,212)
Borrowings under line of credit		2,310
Net cash provided by (used in) financing activities	9,276	(3,172)
Effect of exchange rate changes on cash and equivalents	227	1,267
Net increase in cash and equivalents	59,772	86,938
Cash and equivalents, beginning of period	108,906	79,067
Cash and equivalents, end of period	$ 168,678	$ 166,005
Supplemental disclosure of cash flow information:		
Notes issued in connection with business acquisitions	$ 2,432	$ 1,129
Cash paid for income taxes, net of refunds	65,709	34,450
Cash paid for interest	20,927	22,235

Property and equipment purchases not yet paid	611	598

See notes to unaudited consolidated condensed financial statements.

LKQ CORPORATION AND SUBSIDIARIES

Unaudited Consolidated Condensed Statements of Stockholders Equity and Other Comprehensive Income

(In thousands)

	Common Stock				Accumulated	
	Shares Issued	Amount	Additional Paid-In Capital	Retained Earnings	Other Comprehensive Loss	Total Stockholders Equity
BALANCE, December 31, 2009	142,005	$ 1,420	$ 815,952	$ 369,459	$ (7,397)	$ 1,179,434
Net income				127,743		127,743
Net reduction of unrealized loss on fair value of interest rate swap agreements, net of tax of $1,655					2,943	2,943
Foreign currency translation					978	978
Total comprehensive income						131,664
Stock issued as director compensation	11		218			218
Stock-based compensation expense			7,495			7,495
Exercise of stock options	1,773	18	8,707			8,725
Excess tax benefit from share-based payments			9,375			9,375
BALANCE, September 30, 2010	143,789	$ 1,438	$ 841,747	$ 497,202	$ (3,476)	$ 1,336,911

See notes to unaudited consolidated condensed financial statements.

LKQ CORPORATION AND SUBSIDIARIES

Notes to Unaudited Consolidated Condensed Financial Statements

Note 1. Interim Financial Statements

The unaudited financial statements presented in this report represent the consolidation of LKQ Corporation, a Delaware corporation, and its subsidiaries. LKQ Corporation is a holding company and all operations are conducted by subsidiaries. When the terms the Company, we, us, or our are used in this document, those terms refer to LKQ Corporation and its consolidated subsidiaries.

We have prepared the accompanying unaudited consolidated condensed financial statements pursuant to the rules and regulations of the Securities and Exchange Commission (SEC) applicable to interim financial statements. Accordingly, certain information related to our significant accounting policies and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted. These unaudited consolidated condensed financial statements reflect, in the opinion of management, all material adjustments (which include only normal recurring adjustments) necessary to fairly state, in all material respects, our financial position, results of operations and cash flows for the periods presented.

Operating results for interim periods are not necessarily indicative of the results that can be expected for any subsequent interim period or for a full year. These interim financial statements should be read in conjunction with our audited consolidated financial statements and notes thereto included in our most recent Annual Report on Form 10-K for the year ended December 31, 2009 filed with the SEC on February 26, 2010.

As described in Note 3, Discontinued Operations, during the fourth quarter of 2009, we sold, agreed to sell or closed certain of our self service facilities. These facilities qualified for treatment as discontinued operations. The financial results and assets and liabilities of these facilities are segregated from our continuing operations and presented as discontinued operations in the unaudited consolidated condensed balance sheets and unaudited consolidated condensed statements of income for all periods presented.

Note 2. Financial Statement Information

Revenue Recognition

The majority of our revenue is derived from the sale of recycled and aftermarket products. Revenue is recognized when the products are shipped or picked up by customers and title has transferred, subject to an allowance for estimated returns, discounts and allowances that we estimate based upon historical information. We have recorded a reserve for estimated returns, discounts and allowances of approximately $15.3 million and $15.8 million at September 30, 2010 and December 31, 2009, respectively. We present taxes assessed by governmental authorities collected from customers on a net basis. Therefore, the taxes are excluded from revenue and are shown as a liability on our unaudited consolidated condensed balance sheets until remitted. Revenue from the sale of separately-priced extended warranty contracts is reported as deferred revenue and recognized ratably over the term of the contracts or three years in the case of lifetime warranties.

Receivables

We have recorded a reserve for uncollectible accounts of approximately $6.9 million and $6.5 million at September 30, 2010 and December 31, 2009, respectively.

Inventory

Inventory consists of the following (in thousands):

	September 30, 2010	December 31, 2009
Salvage products	$ 197,438	$ 152,438
Aftermarket and refurbished products	240,186	226,299
Core facilities inventory	6,993	6,949

	$ 444,617	$ 385,686

LKQ CORPORATION AND SUBSIDIARIES

Notes to Unaudited Consolidated Condensed Financial Statements (Continued)

Intangibles

Intangible assets consist primarily of goodwill (the cost of purchased businesses in excess of the fair value of the identifiable net assets acquired), and other specifically identifiable intangible assets, including the Keystone trade name, covenants not to compete and trademarks.

The change in the carrying amount of goodwill during the nine months ended September 30, 2010 is as follows (in thousands):

Balance as of December 31, 2009	$ 938,783
Business acquisitions	50,759
Exchange rate effects	1,047
Balance as of September 30, 2010	$ 990,589

Other intangible assets totaled approximately $64.7 million and $67.2 million, net of accumulated amortization of $12.3 million and $9.2 million, at September 30, 2010 and December 31, 2009, respectively. Amortization expense was approximately $3.1 million for each of the nine month periods ended September 30, 2010 and 2009. Estimated annual amortization expense is approximately $4.0 million for each of the years 2010 through 2014.

Depreciation Expense

Included in cost of goods sold on the unaudited consolidated condensed statements of income is depreciation expense associated with refurbishing and smelting operations.

Warranty Reserve

Some of our mechanical products are sold with a standard six-month warranty against defects. We record the estimated warranty costs at the time of sale using historical warranty claim information to project future warranty claims activity and related expenses. The changes in the warranty reserve during the nine months ended September 30, 2010 were as follows (in thousands):

Balance as of December 31, 2009	$ 604
Warranty expense	6,085
Warranty claims	(5,767)
Balance as of September 30, 2010	$ 922

For an additional fee, we also sell extended warranty contracts for certain mechanical products. The expense related to extended warranty claims is recognized when the claim is made.

Stock-Based Compensation

The fair value of stock options has been estimated using the Black-Scholes option-pricing model. The following table summarizes the assumptions used to compute the weighted average fair value of options granted during the respective periods:

	Nine Months Ended September 30, 2010	2009
Expected life (in years)	6.4	6.3
Risk-free interest rate	3.17%	1.84%
Volatility	43.9%	44.6%
Dividend yield	0%	0%
Weighted average fair value of options granted	$ 9.54	$ 5.50

Estimated forfeitures When estimating forfeitures, we consider voluntary and involuntary termination behavior as well as analysis of historical forfeitures. For options granted in 2010, a forfeiture rate of 8.0% has been used in calculating the stock-based compensation expense for employee option grants, while a forfeiture rate of 0% has been used in calculating the stock-based compensation expense for executive officer option grants.

LKQ CORPORATION AND SUBSIDIARIES

Notes to Unaudited Consolidated Condensed Financial Statements (Continued)

The components of pre-tax stock-based compensation expense are as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Stock options	$ 2,298	$ 1,624	$ 6,812	$ 4,696
Restricted stock	230	183	683	544
Stock issued to non-employee directors	73	72	218	217
Total stock-based compensation expense	$ 2,601	$ 1,879	$ 7,713	$ 5,457

The following table sets forth the total stock-based compensation expense included in the accompanying unaudited consolidated condensed statements of income (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Cost of goods sold	$ 73	$ 13	$ 216	$ 36
Facility and warehouse expenses	541	688	1,608	1,992
Selling, general and administrative expenses	1,987	1,178	5,889	3,429
	2,601	1,879	7,713	5,457
Income tax benefit	(1,023)	(738)	(3,032)	(2,145)
Total stock-based compensation expense, net of tax	$ 1,578	$ 1,141	$ 4,681	$ 3,312

We have not capitalized any stock-based compensation costs during either of the nine month periods ended September 30, 2010 or 2009. As of September 30, 2010, unrecognized compensation expense related to unvested stock options and restricted stock is expected to be recognized as follows (in thousands):

	Stock Options	Restricted Stock	Total
Remainder of 2010	$ 2,300	$ 230	$ 2,530
2011	8,376	913	9,289
2012	7,048	913	7,961
2013	4,789	208	4,997
2014	3,146	139	3,285
2015	79		79
Total unrecognized compensation expense	$ 25,738	$ 2,403	$ 28,141

Fair Value of Financial Instruments

We are required to disclose the fair value for any financial instruments carried at cost on the balance sheet.

Our debt is reflected on the balance sheet at cost. Based on current market conditions, our interest rate margins are below the rate available in the market, which causes the fair value of our debt to fall below the carrying value. The fair value of our term loans (see Note 5, Long-Term Obligations) is approximately $576 million at September 30, 2010, as compared to the carrying value of $589 million. We estimated the fair value of our term loans by calculating the upfront cash payment a market participant would require to assume our obligations. The upfront cash payment, excluding any issuance costs, is the amount that a market participant would be able to lend at September 30, 2010 to an entity with a credit rating similar to ours and achieve sufficient cash inflows to cover the scheduled cash outflows under our term loans. The carrying amounts of our cash and equivalents, net trade receivables and accounts payable approximate fair value.

We apply the market and income approaches to value our financial assets and liabilities, which include the cash surrender value of life insurance, deferred compensation liabilities and interest rate swaps. Required fair value disclosures are included in Note 7, Fair Value Measurements.

LKQ CORPORATION AND SUBSIDIARIES

Notes to Unaudited Consolidated Condensed Financial Statements (Continued)

Segments

We are organized into three operating segments, composed of wholesale recycled and aftermarket products, self service retail products, and recycled heavy-duty truck products. These segments are aggregated into one reportable segment because they possess similar economic characteristics and have common products and services, customers and methods of distribution.

The following table sets forth our revenue by product category within our reportable segment (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Recycled and related products and services	$ 228,797	$ 180,482	$ 658,179	$ 548,040
Aftermarket, other new and refurbished products	291,607	257,670	894,251	799,953
Other	87,217	56,660	243,388	144,044
	$ 607,621	$ 494,812	$ 1,795,818	$ 1,492,037

Revenue from other sources includes scrap sales, bulk sales to mechanical remanufacturers, and sales of aluminum ingots and sows.

Note 3. Discontinued Operations

On October 1, 2009, we sold to Schnitzer Steel Industries, Inc. (SSI) four self service retail facilities in Oregon and Washington and certain business assets related to two self service facilities in Northern California and a self service facility in Portland, Oregon for $17.5 million, net of cash sold. We recognized a gain on the sale of approximately $2.5 million, net of tax, in our fourth quarter 2009 results. Goodwill totaling $9.9 million was included in the cost basis of net assets disposed when determining the gain on sale. In the fourth quarter of 2009, we closed the two self service facilities in Northern California and converted the self service operation in Portland to a wholesale recycling business.

On January 15, 2010, we also sold to SSI two self service retail facilities in Dallas, Texas for $12.0 million. We recognized a gain on the sale of approximately $1.7 million, net of tax, in our first quarter 2010 results. Goodwill totaling $6.7 million was included in the cost basis of net assets disposed when determining the gain on sale.

The self service facilities that we sold or closed are reported as discontinued operations for all periods presented. We reported these facilities in discontinued operations because the cash flows derived from the facilities were eliminated as a result of the sales or closures and we will not have continuing involvement in these facilities. A summary of the assets and liabilities applicable to discontinued operations included in the unaudited consolidated condensed balance sheets as of September 30, 2010 and December 31, 2009 is as follows (in thousands):

	September 30, 2010	December 31, 2009
Inventory	$	$ 1,152
Other current assets		307
Property and equipment, net		1,553
Goodwill		6,708
Total assets	$	$ 9,720
Accounts payable and accrued liabilities	$ 2,857	$ 3,832

Total liabilities	$ 2,857	$ 3,832

As of September 30, 2010, approximately $2.9 million of accrued restructuring expenses remained in liabilities of discontinued operations on our unaudited consolidated condensed balance sheets for the excess lease payments (net of estimated sublease income), and facility closure costs related to the two closed self service facilities in Northern California. The excess lease payments are expected to be paid over the remaining term of the leases through 2018.

LKQ CORPORATION AND SUBSIDIARIES

Notes to Unaudited Consolidated Condensed Financial Statements (Continued)

Results of operations for the discontinued operations for the three and nine months ended September 30, 2010 and 2009 are as follows (in thousands):

	Three Months Ended September 30, 2010	Three Months Ended September 30, 2009	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009
Revenue	$	$ 7,335	$ 686	$ 20,853
(Loss) income before income tax (benefit) provision		(1,565)	355	(473)
Income tax (benefit) provision		(579)	131	(175)
(Loss) income from discontinued operations, net of taxes, before gain on sale of discontinued operations		(986)	224	(298)
Gain on sale of discontinued operations, net of taxes of $1,015			1,729	
(Loss) income from discontinued operations, net of taxes	$	$ (986)	$ 1,953	$ (298)

Note 4. Equity Incentive Plans

We have two stock-based compensation plans, the LKQ Corporation 1998 Equity Incentive Plan (the Equity Incentive Plan) and the Stock Option and Compensation Plan for Non-Employee Directors (the Director Plan). Under the Equity Incentive Plan, both qualified and nonqualified stock options, stock appreciation rights, restricted stock, performance shares and performance units may be granted.

Stock options expire 10 years from the date they are granted. Most of the options granted under the Equity Incentive Plan vest over a period of five years. Options granted under the Director Plan vest six months after the date of grant. We expect to issue new shares of common stock to cover future stock option exercises.

A summary of transactions in our stock-based compensation plans for the nine months ended September 30, 2010 is as follows:

		Restricted Shares		Stock Options	
	Restricted Shares and Options Available For Grant	Number Outstanding	Weighted Average Grant Date Fair Value	Number Outstanding	Weighted Average Exercise Price
Balance, December 31, 2009	3,642,803	202,000	$ 19.00	9,329,407	$ 8.81
Granted	(1,711,533)			1,711,533	19.95
Exercised				(1,773,005)	4.92
Restricted shares vested		(43,000)	19.07		
Cancelled	116,275			(116,275)	16.00
Balance, September 30, 2010	2,047,545	159,000	$ 18.98	9,151,660	$ 11.56

The following table summarizes information about outstanding and exercisable stock options at September 30, 2010:

	Outstanding	Exercisable
Range of Exercise Prices		

	Shares	Weighted Average Remaining Contractual Life (Yrs)	Weighted Average Exercise Price	Shares	Weighted Average Remaining Contractual Life (Yrs)	Weighted Average Exercise Price
$0.75 5.00	2,808,535	3.4	$ 3.71	2,808,535	3.4	$ 3.71
5.01 10.00	745,160	5.2	9.39	661,700	5.2	9.34
10.01 15.00	2,564,290	7.5	11.30	1,123,570	7.0	10.91
15.01 20.00	3,003,675	8.4	19.56	807,948	7.7	19.27
20.01 +	30,000	7.6	21.61	12,150	7.6	21.60
	9,151,660	6.4	$ 11.56	5,413,903	5.0	$ 8.26

At September 30, 2010, a total of 9,030,657 options with an average exercise price of $11.47 and a weighted average remaining contractual life of 6.3 years were exercisable or expected to vest.

LKQ CORPORATION AND SUBSIDIARIES

Notes to Unaudited Consolidated Condensed Financial Statements (Continued)

The aggregate intrinsic value (market value of stock less option exercise price) of outstanding, expected to vest and exercisable stock options at September 30, 2010 was $84.6 million, $84.2 million and $67.9 million, respectively. The aggregate intrinsic value represents the total pre-tax intrinsic value, based on our closing stock price of $20.80 on September 30, 2010. This amount changes based upon the fair market value of our common stock. There were 1,773,005 stock options exercised during the nine months ended September 30, 2010 with an intrinsic value of $27.0 million. There were 1,240,471 stock options exercised during the nine months ended September 30, 2009 with an intrinsic value of $15.9 million.

The total grant-date fair value of options that vested during the nine months ended September 30, 2010 was approximately $7.6 million. The fair value of restricted shares that vested during the nine months ended September 30, 2010 was approximately $0.9 million.

Note 5. Long-Term Obligations

Long-Term Obligations consist of the following (in thousands):

	September 30, 2010	December 31, 2009
Senior secured debt financing facility:		
Term loans payable	$ 588,995	$ 595,716
Revolving credit facility		
Notes payable to individuals through August 2019, interest at 2.0% to 8.0%	8,474	7,329
	597,469	603,045
Less current maturities	(39,880)	(10,063)
	$ 557,589	$ 592,982

We obtained a senior secured debt financing facility from Lehman Brothers Inc. and Deutsche Bank Securities, Inc. on October 12, 2007, which was amended on October 26, 2007 and was further amended on October 27, 2009 (as further amended, the Credit Agreement). The Credit Agreement matures on October 12, 2013 and includes a $610 million term loan, a $40 million Canadian currency term loan, an $85 million U.S. dollar revolving credit facility, and a $15 million dual currency revolving facility for drawings of either U.S. dollars or Canadian dollars. The Credit Agreement also provides for (i) the issuance of letters of credit of up to $35 million in U.S. dollars and up to $10 million in either U.S. or Canadian dollars and (ii) the opportunity for us to add additional term loan facilities and/or increase the $100 million revolving credit facility s commitments, provided that such additions or increases do not exceed $150 million in the aggregate and provided further that no existing lender is required to make its pro rata share of any such additions or increases without its consent. Amounts under each term loan facility are due and payable in quarterly installments of increasing amounts that began in the first quarter of 2008, with the balance payable in full on October 12, 2013. Amounts due under each revolving credit facility will be due and payable on October 12, 2013. We are also required to prepay the term loan facilities with certain amounts generated by the sale of assets under certain circumstances, the incurrence of certain debt, and the receipt of certain insurance and condemnation proceeds, in each case, to the extent of the proceeds of such event, and with up to 50% of our excess cash flow, with the amount of such excess cash flow determined based upon our total leverage ratio.

As of September 30, 2010, there were no borrowings against our revolving credit facility of $100 million. Availability on the revolving credit facility is reduced by outstanding letters of credit. At September 30, 2010, there were $20.1 million of outstanding letters of credit and thus availability on the revolving credit facility totaled approximately $79.9 million.

The Credit Agreement contains customary representations and warranties, and contains customary covenants that restrict our ability to, among other things (i) incur liens, (ii) incur any indebtedness (including guarantees or other contingent obligations), and (iii) engage in mergers and consolidations. The Credit Agreement also requires us to meet certain financial covenants, the most restrictive of which is the required senior secured debt ratio. We were in compliance with all restrictive covenants as of September 30, 2010 and December 31, 2009.

Borrowings under the Credit Agreement accrue interest at variable rates, which depend on the type (U.S. dollar or Canadian dollar) and duration of the borrowing, plus an applicable margin rate. The weighted-average interest rates, including the effect of interest rate swap agreements and excluding the amortization of debt issuance costs, on borrowings outstanding against our senior secured credit facility at September 30, 2010 and December 31, 2009 were 4.40% and 4.53%, respectively. Borrowings against the senior secured credit facility totaled $589.0 million and $595.7 million at September 30, 2010 and December 31, 2009, respectively, of which $37.4 million and $7.5 million are classified as current maturities, respectively.

LKQ CORPORATION AND SUBSIDIARIES

Notes to Unaudited Consolidated Condensed Financial Statements (Continued)

Note 6. Derivative Instruments and Hedging Activities

We are exposed to market risks, including the effect of changes in interest rates, foreign currency exchange rates and commodity prices. Under our current policies, we use derivatives to manage our exposure to variable interest rates on our Credit Agreement, but we do not attempt to hedge our foreign currency and commodity price risks. We do not hold or issue derivatives for trading purposes.

At September 30, 2010, we had interest rate swap agreements in place to hedge a portion of the variable interest rate risk on our variable rate term loans, with the objective of minimizing the impact of interest rate fluctuations and stabilizing cash flows. Beginning on the effective dates of the interest rate swap agreements, on a monthly basis through the maturity date, we have paid and will pay the fixed interest rate and have received and will receive payment at a variable rate of interest based on the London InterBank Offered Rate (LIBOR) on the notional amount. The interest rate swap agreements qualify as cash flow hedges, and we have elected to apply hedge accounting for these swap agreements. As a result, the effective portion of changes in the fair value of the interest rate swap agreements is recorded in Other Comprehensive Income and is reclassified to earnings when the underlying interest payment has an impact on earnings. The ineffective portion of changes in the fair value of the interest rate swap agreements is reported in interest expense.

The following table summarizes the terms of our interest rate swap agreements as of September 30, 2010:

Notional Amount	Effective Date	Maturity Date	Fixed Interest Rate*
$200,000,000	April 14, 2008	April 14, 2011	4.99%
$250,000,000	September 15, 2008	October 14, 2010	4.88%
$250,000,000	October 14, 2010	October 14, 2015	3.81%
$100,000,000	April 14, 2011	October 14, 2013	3.34%

* Includes applicable margin of 2.25% per annum currently in effect under the Credit Agreement

As of September 30, 2010, the fair market value of these contracts was a liability of $5.6 million and was included in Other Accrued Expenses ($3.3 million) and Other Noncurrent Liabilities ($2.3 million) on our unaudited consolidated condensed balance sheet. As of December 31, 2009, the fair market value of the interest rate swap contracts was a liability of $10.2 million and was included in Other Accrued Expenses ($5.0 million) and Other Noncurrent Liabilities ($5.2 million) on our unaudited consolidated condensed balance sheet.

During the nine months ended September 30, 2010 and 2009, we recognized a $2.5 million loss (net of tax) and $4.4 million loss (net of tax), respectively, on derivatives in Other Comprehensive Income. Approximately $5.4 million of losses (net of tax) were reclassified to interest expense from Accumulated Other Comprehensive Loss during each of the nine month periods ended September 30, 2010 and 2009. As of September 30, 2010, we estimate that $2.4 million of net derivative losses (net of tax) included in Accumulated Other Comprehensive Loss will be reclassified into interest expense within the next 12 months. There was no hedge ineffectiveness for the nine months ended September 30, 2010 and 2009.

Note 7. Fair Value Measurements

Effective January 1, 2010, we adopted a newly issued accounting standard which clarifies existing disclosure requirements related to the level of disaggregation of fair value measurements for each class of assets and liabilities and requires additional disclosures about inputs and valuation techniques used to measure fair value for both recurring and nonrecurring Level 2 and Level 3 measurements. As this newly issued accounting standard only requires enhanced disclosure, the adoption of this standard did not impact our financial position or results of operations.

The tables below present information about our assets and liabilities that are measured at fair value on a recurring basis and indicate the fair value hierarchy of the valuation techniques we utilized to determine such fair value. The tiers in the fair value hierarchy include: Level 1, defined as observable inputs such as quoted market prices in active markets; Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and Level 3, defined as unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions.

LKQ CORPORATION AND SUBSIDIARIES

Notes to Unaudited Consolidated Condensed Financial Statements (Continued)

We use the market and income approaches to value our financial assets and liabilities, and there were no changes in valuation techniques during the nine months ended September 30, 2010. Our Level 2 assets and liabilities are valued using inputs from third parties and market observable data. We obtain valuation data for the cash surrender value of life insurance and deferred compensation liabilities from third party sources, which determine the net asset values for our accounts using quoted market prices, investment allocations and reportable trades. We value the interest rate swaps using a third party valuation model that performs a discounted cash flow analysis based on the terms of the contracts and market observable inputs such as LIBOR and forward interest rates. The following tables present information about our financial assets and liabilities measured at fair value on a recurring basis as of September 30, 2010 and December 31, 2009 (in thousands):

	Balance as of September 30, 2010	Fair Value Measurements as of September 30, 2010		
		Level 1	Level 2	Level 3
Assets:				
Cash surrender value of life insurance	$ 9,539	$	$ 9,539	$
Total Assets	$ 9,539	$	$ 9,539	$
Liabilities:				
Deferred compensation liabilities	$ 9,690	$	$ 9,690	$
Interest rate swaps	5,615		5,615	
Total Liabilities	$ 15,305	$	$ 15,305	$

	Balance as of December 31, 2009	Fair Value Measurements as of December 31, 2009		
		Level 1	Level 2	Level 3
Assets:				
Cash surrender value of life insurance	$ 7,323	$	$ 7,323	$
Total Assets	$ 7,323	$	$ 7,323	$
Liabilities:				
Deferred compensation liabilities	$ 7,902	$	$ 7,902	$
Interest rate swaps	10,213		10,213	
Total Liabilities	$ 18,115	$	$ 18,115	$

The cash surrender value of life insurance and deferred compensation liabilities are included in other assets and other noncurrent liabilities, respectively, on our unaudited consolidated condensed balance sheets.

Note 8. Commitments and Contingencies

Operating Leases

We are obligated under noncancelable operating leases for corporate office space, warehouse and distribution facilities, trucks and certain equipment. The future minimum lease commitments under these leases at September 30, 2010 are as follows (in thousands):

Three months ending December 31, 2010	$ 15,416
Years ending December 31:	
2011	53,729
2012	44,943
2013	38,682
2014	28,630
2015	20,043
Thereafter	56,488
Future Minimum Lease Payments	$ 257,931

Litigation and Related Contingencies

We have certain contingencies resulting from litigation, claims and other commitments and are subject to a variety of environmental and pollution control laws and regulations incident to the ordinary course of business. We currently expect that the resolution of such contingencies will not materially affect our financial position, results of operations or cash flows.

LKQ CORPORATION AND SUBSIDIARIES

Notes to Unaudited Consolidated Condensed Financial Statements (Continued)

Note 9. Earnings Per Share

The following chart sets forth the computation of earnings per share (in thousands, except per share amounts):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	**2009**	**2010**	**2009**
Income from continuing operations	$ 35,901	$ 30,141	$ 125,790	$ 90,614
Denominator for basic earnings per share-				
Weighted- average shares outstanding	143,258	140,746	142,769	140,257
Effect of dilutive securities:				