DENISON MINES CORP.
Form 6-K
April 07, 2008

FORM 6-K
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Report of Foreign Private Issuer
Pursuant to Rule 13a-16 or 15d-16
of the Securities Exchange Act of 1934

Date: April 4, 2008
Commission File Number: 000-24443

Denison Mines Corp.
(Translation of registrant s name into English)
Atrium on Bay, 595 Bay Street, Suite 402, Toronto, Ontario M5G 2C2
(Address of principal executive offices)

Indicate by check mark whether the registrant files or will file annual reports under cover Form 20-F or Form 40-F.

Form 20-F o Form 40-F þ

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(1): o

Note: Regulation S-T Rule 101(b)(1) only permits the submission in paper of a Form 6-K if submitted solely to provide an attached annual report to security holders.

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(7): o

Note: Regulation S-T Rule 101(b)(7) only permits the submission in paper of a Form 6-K if submitted to furnish a report or other document that the registrant foreign private issuer must furnish and make public under the laws of the jurisdiction in which the registrant is incorporated, domiciled or legally organized (the registrant s home country), or under the rules of the home country exchange on which the registrant s securities are traded, as long as the report or other document is not a press release, is not required to be and has not been distributed to the registrant s security holders, and, if discussing a material event, has already been the subject of a Form 6-K submission or other Commission filing on EDGAR.

Indicate by check mark whether by furnishing the information contained in this Form, the registrant is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934.

Yes o No þ

If Yes is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b): 82-_________

Signatures

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: April 4, 2008

Denison Mines Corp.

/s/ Brenda Lazare
Brenda Lazare
Canadian Counsel and Corporate Secretary

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EXHIBIT INDEX

Exhibit Number	Description
1.	Management s Discussion and Analysis for the 12 months ended December 31, 2007 and
2.	Financial Results for the 12 months ended December 31, 2007

Exhibit 1

Denison Mines Corp.
Management s Discussion and Analysis
December 31, 2007

DENISON MINES CORP.
Management s Discussion and Analysis
Year Ended December 31, 2007
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INTRODUCTION

This Management s Discussion and Analysis (MD&A) of Denison Mines Corp. and its subsidiary companies and joint ventures (collectively, Denison or the Company) provides a detailed analysis of the Company s business and compares its financial results with those of the previous year. This MD&A is dated as of March 18, 2008 and should be read in conjunction with, and is qualified by, the Company s audited consolidated financial statements and related notes for the year ended December 31, 2007. The financial statements are prepared in accordance with generally accepted accounting principles in Canada with a discussion in Note 28 of the material differences between Canadian and United States generally accepted accounting principles and practices affecting the Company. All dollar amounts are expressed in U.S. dollars, unless otherwise noted.

Other continuous disclosure documents, including the Company s press releases, quarterly and annual reports, Annual Information Form and Form 40-F are available through its filings with the securities regulatory authorities in Canada at www.sedar.com and the United States at sec.gov/edgar.shtml

In August 2006, the Company changed its fiscal year end from September 30 to December 31 to align its reporting periods with that of its peers in the uranium industry. The Company elected to use a 15-month period ending December 31, 2006 for its audited consolidated financial statements as permitted under Canadian securities regulations. References to 2006 and 2005 refer to the 15-month period ended December 31, 2006 and year ended September 30, 2005. References to 2007 refer to the year ended December 31, 2007.

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This MD&A contains forward-looking statements , within the meaning of the United States Private Securities Litigation Reform Act of 1995 and similar Canadian legislation, concerning the business, operations and financial performance and condition of Denison.

Forward-looking statements include, but are not limited to, statements with respect to estimated production; the expected effects of possible corporate transactions and the development potential of Denison s properties; the future price of uranium, vanadium, nickel and cobalt; the estimation of mineral reserves and resources; the realization of mineral reserve estimates; the timing and amount of estimated future production; costs of production; capital expenditures; success of exploration activities; permitting timelines and permitting, mining or processing issues; currency exchange rate fluctuations; government regulation of mining operations; environmental risks; unanticipated reclamation expenses; title disputes or claims; and limitations on insurance coverage. Generally, these forward-looking statements can be identified by the use of forward-looking terminology such as plans, expects or does not expect, is expected, budget, scheduled, estimates, forecasts, intends, anticipates or does not anticipate or variations of such words and phrases or state that certain actions, events or results may, could, would, might or be taken, occur or be achieved.

Forward-looking statements are based on the opinions and estimates of management as of the date such statements are made, and they are subject to known and unknown risks, uncertainties and other factors that may cause the actual results, level of activity, performance or achievements of Denison to be materially different from those expressed or implied by such forward-looking statements, including but not limited to risks related to: unexpected events during construction, expansion and start-up; variations in ore grade, amount of material mined or milled; delay or failure to receive board or government approvals; timing and availability of external financing on acceptable terms; risks related to international operations; actual results of current exploration activities; actual results of current reclamation activities; conclusions of economic evaluations; changes in project parameters as plans continue to be refined; future prices of uranium, vanadium, nickel and cobalt; possible variations in ore reserves, grade or recovery rates; failure of plant, equipment or processes to operate as anticipated; accidents, labour disputes and other risks of the mining

industry; delays in the completion of development or construction activities and other factors listed under the heading Risk Factors in this MD&A. Although management of Denison has attempted to identify important factors that could cause actual results to differ materially from those contained in forward-looking statements, which only apply as of the date hereof, there may be other factors that cause results not to be as anticipated, estimated or intended.
There can be no assurance that such statements will prove to be accurate, as actual results and future events could differ materially from those anticipated in such statements. Accordingly, readers should not place undue reliance on forward-looking statements. Denison does not undertake to update any forward-looking statements that are included or incorporated by reference herein, except in accordance with applicable securities laws.

DENISON MINES CORP.
Management s Discussion and Analysis
Year Ended December 31, 2007
(Expressed in U.S. Dollars, Unless Otherwise Noted)

OVERVIEW

Denison, formerly International Uranium Corporation (IUC), was formed by articles of amalgamation effective May 9, 1997 pursuant to the Business Corporations Act (Ontario) (the OBCA). On December 1, 2006, IUC combined its business and operations with Denison Mines Inc. (DMI), by way of arrangement under the OBCA. Pursuant to the arrangement, all of the issued and outstanding shares of DMI were acquired in exchange for the Company s shares at a ratio of 2.88 common shares of the Company for each common share of DMI. Effective December 1, 2006, IUC s articles were amended to change its name to Denison Mines Corp. .

Denison is a reporting issuer in all of the Canadian provinces. Denison s common shares are listed on the Toronto Stock Exchange (the TSX) under the symbol DML and on the American Stock Exchange (the AMEX) under the symbol DNN .

Denison is a diversified, growth-oriented, intermediate uranium producer with active uranium mining projects in both the U.S. and Canada and development projects in Canada, Zambia and Mongolia. Denison expects production of between 3.6 to 6.0 million pounds of uranium oxide in concentrates (U_3O_8) by 2011. Denison s assets include an interest in 2 of the 4 licensed and operating conventional uranium mills in North America, with its 100% ownership of the White Mesa mill in Utah and its 22.5% ownership of the McClean Lake mill in Saskatchewan. Both mills are fully permitted and operating. The Company also produces vanadium as a co-product from some of its mines in Colorado and Utah. The Company is also in the business of recycling uranium-bearing waste materials, referred to as alternate feed materials , for the recovery of uranium, alone or in combination with other metals, at the Company s White Mesa mill.

Denison enjoys a global portfolio of world-class exploration projects, including properties in close proximity to the Company s mills in the Athabasca Basin in Saskatchewan and in the Colorado Plateau, Henry Mountains and Arizona Strip regions of the southwestern United States. Denison also has exploration and development properties in Mongolia, Zambia and, indirectly through its investments, in Australia.

Denison is the manager of Uranium Participation Corporation (UPC), a publicly traded company which invests in uranium oxide in concentrates and uranium hexafluoride. Denison is also engaged in mine decommissioning and environmental services through its Denison Environmental Services (DES) division.

The Uranium Industry

Commercial nuclear power generation began over 50 years ago and now generates as much global electricity as was produced in 1960 by all sources. The low operating cost of nuclear power generation and the increasing concern for the environment and climate change are driving a nuclear renaissance. China, India and Russia are proceeding with ambitious plans for new nuclear power plants. Many companies in the United States have filed applications for a combined construction and operating licence to build new nuclear reactors. Countries such as Egypt, United Arab Emirates, Thailand and Turkey are actively considering building nuclear power plants.

There are now 104 operating nuclear reactors in the United States and a total of 439 operating worldwide in 30 countries, representing a total world nuclear capacity of 372.1 gigawatts. A further 34 reactors with a capacity of 27.8 gigawatts are under construction in 12 countries and an additional 93 reactors (100.6 gigawatts) are planned. With the only significant commercial use for uranium being fuel for nuclear reactors, it follows that the nuclear renaissance will have a significant effect on future uranium demand.

Uranium Supply and Demand

The world s operating nuclear power reactors require approximately 180 million pounds of U_3O_8 per year. As nuclear power capacity increases, the uranium fuel requirement also increases and is estimated to rise to approximately 187 million pounds U_3O_8 by 2010 and approximately 212 million pounds U_3O_8 by 2015. Demand for uranium can be supplied through either primary production (newly mined uranium) or secondary sources (inventories, down blending of weapon grade material and reprocessing fuel rods). Secondary sources are of particular importance to the uranium industry when compared to other commodity markets.

Over the four-year period 2000-2003, annual global primary uranium production averaged 93.1 million pounds of uranium. In response to increasing uranium prices, worldwide uranium production rose to 104.6 million pounds in 2004 and to 108.1 million pounds in 2005; however, production decreased in 2006 to 102.5 million pounds as a result of problems at several production centres. 2007 production is estimated at 107 million pounds. Canada and Australia currently account for over 41% of the world s production. The United States production represented a little over 4.4%, or 4.7 million pounds of uranium in 2007. During the last decade, takeovers, mergers and closures have consolidated the uranium production industry. Based on preliminary 2007 production figures, seven companies

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accounted for over 88% of primary production while the six largest uranium mines produced over 56% of the aggregate global production.

Primary uranium production only supplies approximately 60% of the total annual requirements of nuclear power generators. The balance of requirements are met from secondary sources of supply, which include inventories held by producers and utilities, government inventories, uranium recycled from government stockpiles and uranium recycled from nuclear weapons. The recycling of highly enriched uranium (HEU) from former warheads in the Russian Federation is a unique subset of secondary supply. Surplus fissile military materials are converted in Russia from HEU into low enriched uranium (LEU) suitable for use in nuclear reactors. In February 1993, the United States and Russia entered into an agreement (the Russian HEU Agreement) which provided for the United States to purchase 500 metric tons of Russian HEU over a 20-year period. In April 1996, the USEC Privatization Act gave Russia and a three company consortium composed of Cameco Corporation (Cameco), AREVA Group (AREVA) and NUKEM, Inc., the authority to sell the natural uranium feed component (in the form of UF_6) derived from the LEU (the HEU Feed) in the United States over the 20-year period into the commercial U.S. uranium market under defined annual quotas. The USEC Privatization Act provides a framework for the introduction of this Russian HEU Feed into the U.S. commercial uranium market. Russia has been selling this HEU Feed through long-term supply agreements directly with U.S. utilities and the three companies.

The Russian HEU Agreement terminates in 2013 and Russia has formally stated that it will not be renewed, as had once been anticipated. Additionally, as a result of the dramatic rise in uranium and enrichment prices of the past two years, Russia has notified all of the parties to the HEU Agreement that the previously agreed pricing can no longer stand. Discussions have begun to renegotiate the component prices among the parties and are expected to be completed later this year.

Based upon recent assessments of future secondary uranium supply, the uranium industry s scheduled uranium production forecast and expected nuclear generating capacity, there is a growing requirement for increased uranium production to meet the forecast needs of reactors world-wide. Based upon the most recent assessment of market trends published by The Ux Consulting Company LLC in their January 2008 edition of The Uranium Market Outlook , under Reference Case conditions, uranium production to support Western reactors will need to expand from its 2007 level of 107 million pounds, up to 152 million pounds in 2010 and reach 212 million pounds by 2015.

Uranium Prices

Most of the countries that use nuclear-generated electricity do not have a sufficient domestic uranium supply to fuel their nuclear power reactors, and their electric utilities secure most of their required uranium supply by entering into medium-term and long-term contracts with foreign uranium producers and other suppliers. These contracts usually provide for deliveries to begin one to three years after they are signed and to continue for several years thereafter. In awarding medium-term and long-term contracts, electric utilities consider, in addition to the commercial terms offered, the producer s or supplier s uranium reserves, record of performance and costs, all of which are important to the producer s or supplier s ability to fulfill long-term supply commitments. Under medium-term and long-term contracts, prices are established by a number of methods, including base prices adjusted by inflation indices, reference prices (generally spot price indicators but also long-term reference prices) and annual price negotiations. Contracts may also contain floor prices, ceiling prices, and other negotiated provisions which affect the amount paid by the buyer to the seller. Under these contracts the actual price mechanisms are usually confidential.

Electric utilities procure their remaining requirements through spot and near-term purchases from uranium producers and other suppliers, including other utilities holding excess inventory and governments.

Over the period from 1996 through 2004, annual spot market demand averaged just under 20 million pounds U_3O_8 or about 12% of the annual world consumption, but had jumped to about 35 million pounds in 2005 and 2006 as the rebuilding of utility inventories commenced, and investors and hedge funds entered the market as significant buyers. Spot market volume returned to its traditional level of approximately 20 million pounds in 2007.

Historically, spot prices have been more volatile than long-term contract prices. In December 2000, the spot price reached an all-time low of $7.10 per pound. The uranium price increased at a moderate rate reaching $14.50 per pound U_3O_8 by the end of 2003. The spot price increased steadily from that date reaching $72.00 by the end of 2006. A further market impact in October 2006 was the announcement of the flooding and indefinite postponement of the start up of the Cigar Lake mine in northern Saskatchewan. The Cigar Lake mine was scheduled to ramp up to an annual production rate of 18.0 million pounds by 2008. Producers were also active in the spot market, purchasing material to fill contractual demand, which they could not supply due to production issues at their respective operations. During the first half of 2007, the spot price continued its rapid rise reaching a peak of $136.00 in June 2007. At the end of June 2007, the spot price dropped $3.00, the first decline in the spot price since May of 2003. In the last half of the year, the spot price was very volatile, dropping to $75.00 in October, then rebounding to $95.00 in

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December. Prices have continued to be volatile in 2008. As of the date hereof, the uranium spot price is $74.00 per pound U_3O_8.

The long-term uranium price has undergone a similar increase over the past several years, but with significantly less volatility, rising from just under $11.00 per pound U_3O_8, at the end of 2002, to $95.00 per pound in May 2007. Since that time the long-term price has remained at $95.00 per pound U_3O_8. The long-term price rose due to increased demand from utilities as they placed more of their requirements under contract.

Future uranium prices will be influenced by increased demand from new reactors being constructed or planned in many parts of the world, as well as the amount of incremental supply made available to the market from the remaining excess inventories, HEU feed supplies, other stockpiles, and the availability of increased or new production from other uranium producers.

Competition

Uranium production is international in scope and is characterized by a relatively small number of companies operating in only a few countries. In 2007, four Western companies, Cameco, AREVA, Rio Tinto plc and BHP Billiton Limited produced approximately 58.4% of total world output. Most of the world s production was from Canada and Australia which produced a combined 41.6% of global uranium output in 2007. In 2006, Kazakhstan, Russia and Uzbekistan produced a combined 30.4% of worldwide uranium while supplying significant quantities of uranium into Western World markets. The Canadian uranium industry has in recent years been the leading world supplier, producing nearly 22.7% of the world supply.

Marketing Uranium

Denison markets its entire share of production from McClean Lake and Midwest jointly with AREVA Resources Canada Inc. (ARC) production from these properties through a joint marketing company, McClean Uranium Limited (MUL). MUL is incorporated in Saskatchewan and is owned 30% by Denison and 70% by ARC. Denison s production from the White Mesa mill is marketed directly by Denison. Agreements with AREVA provide for production to be allocated first to market related contracts with any surplus to be apportioned evenly over the legacy contracts. The lower price, base-escalated legacy contracts expire by the end of 2008.

The sale of Denison s uranium has traditionally been through long-term contracts and not on the spot market. These long-term, or legacy contracts have a variety of pricing methods, including fixed prices, base prices adjusted by inflation indices, changes in reference prices (spot price indicators or long-term contract reference prices) and annual price negotiations. Prices in the long-term market have normally been higher than those in the spot market at the time the contracts are entered into and are normally less volatile. However, when market prices are increasing rapidly, as has been the case over the last several years, prices received under some of the legacy contracts cannot match such market increases.

Delivery scheduling (or timing) under long-term contracts is at the discretion of the customer so may vary markedly from quarter to quarter.

Marketing of the White Mesa production, which is scheduled to begin in the second quarter of 2008, will concentrate on long-term contracts utilizing a variety of pricing mechanisms while retaining a portion of the production to be sold on the spot market to take advantage of opportunities in the current tight supply-demand situation.

The Vanadium Market

Vanadium is an essential alloying element for steels and titanium, and its chemical compounds are indispensable for many industrial and domestic products and processes. The principal uses for vanadium are: (i) carbon steels used for reinforcing bars; (ii) high strength, low alloy steels used in construction and pipelines; (iii) full alloy steels used in castings; (iv) tool steels used for high speed tools and wear resistant parts; (v) titanium alloys used for jet engine parts and air frames; and (vi) various chemicals used as catalysts.

Principal sources of vanadium are (i) titaniferous magnetites found in Russia, China, Australia and South Africa; (ii) sludges and fly ash from the refining and burning of U.S., Caribbean and Middle Eastern oils; and (iii) uranium co-product production from the Colorado Plateau. While produced and sold in a variety of ways, vanadium production figures and prices are typically reported in pounds of an intermediate product, vanadium pentoxide, or V_2O_5. The White Mesa mill is capable of producing three products, ammonium metavanadate (AMV) and vanadium pregnant liquor (VPL), both intermediate products, and vanadium pentoxide (flake, black flake, tech flake or V_2O_5). The majority of sales are as V_2O_5, with AMV and VPL produced and sold on a request basis only.

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In the United States, although vanadium is produced through processing petroleum residues, spent catalysts, utility ash, and vanadium bearing iron slag, the most significant source of production historically has been as a by-product of uranium production from ores in the Colorado Plateau District, accounting for more than half of historic U.S. production. Vanadium in these deposits typically occurs at an average ratio of five to six pounds of vanadium for every pound of uranium, and the financial benefit derived from the by-product sales have helped to make the mines in this area profitable in the past.

The market for vanadium has fluctuated greatly over the last 20 years. During the early 1980s, quoted prices were in the range of $3.00 per pound V_2O_5, but increased exports from China and Australia, coupled with the continued economic recession of the 1980s drove prices to as low as $1.30 per pound. Prices stabilized in the $2.00 $2.45 per pound range until perceived supply problems in 1988 caused by cancellation of contracts by China and rumours of South African production problems resulted in a price run-up to a high of nearly $12.00 per pound in February of 1989. This enticed new producers to construct additional capacity, and oversupply problems again depressed the price in the early 1990s to $2.00 per pound and below. Late in 1994, a reduction in supplies from Russia and China, coupled with concerns about the political climate in South Africa and a stronger steel market caused the price to climb to $4.50 per pound early in 1995. In the beginning of 1998, prices had climbed to a nine-year high of $7.00 caused by supply being unable to keep pace with record demand from steel and aerospace industries. However, during the second half of 1998, prices began to decline to $2.56 per pound by December 1998. This was due to sudden decreases in Far East steel production, along with suppliers from Russia and China selling available inventories at low prices in order to receive cash. Since that time, prices fell dramatically to a range of $1.20 to $1.50 per pound V_2O_5 due in part to the difficult economic conditions being experienced throughout the Pacific Rim and new sources of supply coming into the market. In the third quarter of 2003, vanadium prices started to increase because of increased steel consumption and the shutdown of an Australian primary producer. This trend continued through 2004. In 2005, demand from China resulted in a significant price run-up culminating in all time highs of $23.00 to $27.00 per pound V_2O_5. Subsequently, prices declined to a range of $8.00 to $10.00 per pound V_2O_5, at the end of 2005, due to the ramp-up of Chinese vanadium production. Prices continued to decline during 2006 to the $7.00 to $8.00 range and have remained in this range throughout 2007. In early 2008, vanadium prices increased significantly to $14.00 to $15.00 per pound due to power supply issues in South Africa. South Africa is a major supply source of vanadium, representing approximately 39% of the world s production.

World demand will continue to fluctuate in response to changes in steel production. However, the overall consumption is anticipated to increase as demand for stronger and lighter steels grows and the demand for titanium alloys for jet engine components increases with new aircraft orders throughout the world.

Marketing Vanadium

Prices for the products that are produced by the Company are generally based on weekly quotations published in Ryan s Notes or Platt s Metals Weekly. Historically, vanadium production from the White Mesa mill has been sold into the worldwide market both through traders, who take a 2% to 3% commission for their efforts and, to a lesser extent, through direct contacts with domestic converters and consumers. While priced in U.S. dollars per pound of V_2O_5, the product is typically sold by the container, which contains nominally 40,000 pounds of product packed in 55 gallon drums, each containing approximately 660 pounds of product.

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SELECTED ANNUAL FINANCIAL INFORMATION

The following selected financial information was obtained directly from or calculated using the Company s consolidated financial statements for the year ended December 31, 2007, for the 15 months ended December 31, 2006 and for the year ended September 30, 2005.

(in thousands)	3 Months ended Dec. 31, 2007	Year ended Dec. 31, 2007	15 Months ended Dec. 31, 2006	Year ended Sept. 30 2005
Results of Operations:				
Total revenues	$ 36,825	$76,764	$ 9,722	$ 131
Net income (loss)	23,542	47,244	(16,998)	(11,450)
Basic earnings (loss) per share	0.12	0.25	(0.18)	(0.14)
Diluted earnings (loss) per share	0.12	0.24	(0.18)	(0.14)

	As at Dec. 31, 2007	As at Dec. 31, 2006	As at Sept. 30, 2005
Financial Position:			
Working capital	$ 75,915	$ 93,743	$ 4,244
Long-term investments	20,507	16,600	3,814
Property, plant and equipment	727,823	403,571	6,767
Total assets	1,001,581	659,348	34,214
Total long-term liabilities	$ 175,081	$123,244	$ 13,444

RESULTS OF OPERATIONS

General

The Company recorded net income of $47,244,000 ($0.25 per share) for 2007 compared with a net loss of $16,998,000 ($0.18 per share) for 2006.

Revenues totaled $76,764,000 for 2007 compared with $9,722,000 for 2006. Expenses totaled $83,771,000 for 2007 compared with $33,816,000 for 2006. Net other income totaled $41,627,000 for 2007 compared with $7,399,000 for 2006.

Revenues

Uranium sales revenues for the fourth quarter were $34,173,000. Sales from U.S. production were 250,000 pounds U_3O_8 at an average price of $89.84 per pound. Sales of Canadian production were 150,000 pounds U_3O_8 at an average price of $74.37 per pound. Amortization of the fair value increment related to the DMI sales contracts totaled $906,000 for the quarter. Reported revenue is also impacted by the effect of foreign currency transactions.

Uranium sales revenues for the year were $65,125,000. Sales from U.S. production were 325,000 pounds U_3O_8 at an average price of $99.11 per pound. Sales of Canadian production were 420,000 pounds U_3O_8 at an average price of

$74.91 per pound. Uranium sales revenue also includes amortization of the fair value increment related to long-term sales contracts from the acquisition of DMI in the amount of $2,418,000.

Uranium sales revenue in the 2006 period totaled $7,575,000 for the net sale of 109,400 pounds U_3O_8 from Canadian production at an average sales price of $55.76 per pound and from amortization of the fair value increment related to the long-term sales contracts of DMI in the amount of $1,475,000. Revenue in 2006 represents only one month activity post acquisition of DMI.

Denison currently markets its uranium from the McClean Lake joint venture jointly with ARC. Denison share of current contracts sales volumes is set out in the table below:

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Current Contracted Sales Volumes
(pounds U_3O_8 x 1000)

(in thousands)	2008	2009	Pricing
Market Related	590	440	80% to 85% of Spot
Legacy Base Escalated	220	0	\$20.00 to \$26.00
Legacy Market Related	140	0	96% of Spot

Notes:
It is anticipated that the joint marketing of Canadian uranium production will cease at the end of 2008 except for the market related category above. Future long-term sales agreements for the Company s uranium inventory and production are expected to be primarily under market related contracts with appropriate floor prices. In March 2007, one such contract was completed for the sale of 17% of the White Mesa mill production commencing in 2008 up to 6.5 million pounds with a minimum of 250,000 pounds in 2008 increasing to a minimum of 1 million pounds by 2011. The sales price is 95% of the published long-term price for the month prior to delivery with a floor price of \$45.00. No other new sales contracts are in place at this time.
During 2007, the Company continued to receive alternate feed materials at the White Mesa mill. Alternate feed materials, usually classified as waste products by the processing facilities that generate these materials, contain uranium that can be recovered as an environmentally preferable alternative to direct disposal. The Company received a fee for a majority of its alternate feed materials once they are delivered to the mill. In addition to the recycling fees, the Company will retain any uranium recovered from these materials, which can be sold in subsequent periods, at which time the revenue from the sales will be recorded. Also during 2007, the Company continued to receive high-grade alternate feed materials under its existing contract with Cameco Corporation. The Company does not receive a recycling fee for these types of material; however, the Company is able to retain all of the proceeds received from the sale of the uranium produced.
During the year, the Company completed a processing campaign of alternate feed materials on which a processing fee is paid. Processing and by-product disposal revenue totaled \$2,526,000 compared to \$1,492,000 in 2006.
Revenue from the environmental services division was \$4,723,000 compared to \$221,000 in 2006. Revenue from the management contract with Uranium Participation Corporation was \$4,390,000 compared to \$430,000 in 2006. Both of these revenue sources were acquired in the DMI transaction that was effective December 1, 2006. Therefore 2006 revenues represent only one month.

Operating Expenses

Milling and Mining Expenses

The McClean Lake joint venture produced 738,000 pounds U_3O_8 for the three months and 1,907,000 pounds U_3O_8 for the year ended December 31, 2007. Denison s 22.5% share of production totaled 166,000 and 429,000 pounds respectively.
Unit production cash costs in Canada are driven primarily by production volumes as the majority of costs do not vary with volume. These fixed costs for the McClean operations total approximately Cdn\$46 million per year so as production volumes increase, the cost per pound decreases. Reagent costs are in addition to this cost as are amortization depletion and depreciation costs. Production by the joint venture in 2008 is expected to be 3.2 million pounds U_3O_8.

The Midwest deposit is currently scheduled to commence production in mid-2011 and production is planned to be processed at a rate of about 8-9 million pounds per year. The processing of Cigar Lake ore, expected to ramp up to over 7.7 million pounds of mill output per year, was scheduled to commence in early 2008 until delayed by the flooding of the Cigar Lake mine in late 2006. The timing of commencement of production of Cigar Lake ore is in 2011 at the earliest. The McClean Lake mill expansion required to receive and process ore from Cigar Lake, which was funded by the Cigar Lake joint venture, is substantially complete. The McClean joint venture will have the benefit of the Cigar Lake expansion until it is utilized for processing Cigar Lake ore. Denison has no ownership interest in the Cigar Lake joint venture.

Production at the White Mesa mill from alternate feed milling was 254,000 pounds U_3O_8. The Company will continue to process alternate feed materials in the first quarter 2008

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Sales Royalties and Capital Taxes
Sales royalties and capital taxes totaled $2,301,000 for the year compared with $420,000 in 2006. This difference is due to the inclusion of the operation of DMI for only one month in 2006. Denison pays a Saskatchewan basic uranium royalty of 4% of gross uranium sales after receiving the benefit of a 1% Saskatchewan resource credit. Denison also pays Saskatchewan capital taxes based on the greater of 3.3% of gross uranium sales and capital tax otherwise computed under the Saskatchewan Corporation Capital Tax Act. For uranium production after July 1, 2007, the factor applied to gross uranium sales for Saskatchewan capital tax purposes will be reduced to 3.1% with further reductions scheduled in 2008. The Saskatchewan government also imposes a tiered royalty which ranges from 6% to 15% of gross uranium sales after recovery of mill and mine capital allowances which approximate capital costs. Denison has sufficient mill and mine capital and expansion allowances available or anticipated to shelter it from the tiered royalty at current uranium prices for at least 2008.

MINERAL PROPERTY EXPLORATION
Denison is engaged in uranium exploration, as both operator and non-operator of joint ventures and as operator of its own properties in Canada, the U.S. and Mongolia. For the three months ended December 31, 2007 exploration expenditures totaled $4,049,000 and totaled $20,963,000 for the year ended December 31, 2007 as compared to $3,370,000 and $14,790,000 for the three and fifteen months ended December 31, 2006.

A majority of the exploration expenditures during the period were spent in the Athabasca Basin region of northern Saskatchewan. Denison is engaged in uranium exploration on advanced projects in this region of Canada as part of the ARC operated McClean and Midwest joint ventures. A significant discovery, termed the Midwest A deposit (formerly the Mae Zone) and located 3 km northeast of the proposed Midwest open pit, was drilled this past winter. Denison is also participating in a total of 33 other exploration projects concentrating in the productive southeast margin of the Athabasca Basin. Denison is operator of two mid-stage projects, the Moore Lake and the Wheeler River joint ventures, included in this portfolio. Denison s share of exploration spending on its Canadian properties totaled $3,239,000 of which $3,036,000 was expensed in the statement of operations for the three months ended December 31, 2007 and totaled $17,445,000 of which $16,638,000 was expensed in the statement of operations for the year ended December 31, 2007.

Exploration expenditures of $1,000,000 for the three month period and $4,048,000 for the year ended December 31, 2007 were spent in Mongolia on the Company s joint venture and 100% owned properties. The Company has a 70% interest in the Gurvan Saihan Joint Venture (GSJV) in Mongolia. The other parties to the joint venture are the Mongolian government as to 15% and Geologorazvedka, a Russian government entity, as to 15%. Additional expenditures for development of the GSJV s Hairhan uranium deposits have also been incurred. Development work includes extensive resource delineation drilling, hydrological drilling, plant design and environmental studies.

The remaining expenditures of $13,000 for the three-month period and $277,000 for the year were spent on the Company s other properties.

General and Administrative
General and administrative expenses were $3,871,000 for the three months and $13,469,000 for the year ended December 31, 2007 compared with $7,286,000 and $11,379,000 for the three and fifteen months ended December 31, 2006. The increase was primarily the result of the inclusion of Denison Mines Inc. (DMI) effective December 1, 2006, a ramping up of the Company s operations, the acquisition and implementation of new information systems and an increase in public company expenses due to additional compliance costs. General and administrative expenses consist primarily of payroll and related expenses for personnel, contract and professional services and other overhead expenditures.

Other Income and Expenses

Other income (expense) totaled $4,284,000 for the three months and $41,627,000 for the year ended December 31, 2007 compared with $4,652,000 and $7,399,000 for the three and fifteen month periods ended December 31, 2006. The net other income in the quarter and for the year is primarily due to the disposition of portfolio investments.

Income Taxes

The Company has provided for a current tax expense of $3,141,000 and for a future tax recovery of $15,765,000. The future tax recovery results primarily from a decline in expected future income tax rates.

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Outlook for 2008
Mining and Production
Canada
Mining at the Sue E pit at McClean Lake in northern Saskatchewan is expected to be completed early in the second quarter of 2008. Stripping of the Sue B overburden was completed in 2007. Mining of the Sue B deposit, which contains approximately 1.4 million pounds U_3O_8, will follow completion of Sue E.
U_3O_8 production at McClean Lake in 2008 is expected to be 3.2 million pounds of which Denison s share is 720,000 pounds.
United States
Four mines are operating on the Colorado Plateau with production from the Sunday, Pandora, Topaz and West Sunday mines running at about 350 tons per day. At the Tony M mine within the Henry Mountains Complex, located in Utah, operational permits have been received and production from this mine is underway and will ramp up to 300 tons per day in the second quarter of 2008 eventually climbing to 450 tons per day by year end. Production from these mines is being hauled to Denison s White Mesa mill and is currently being stockpiled. At December 31, 2007, a total of 85,000 tons had been shipped to the mill. The Company expects to have approximately 160,000 tons of material stockpiled before conventional ore production commences in May of 2008. Mine development work has begun at the Company s Arizona 1 mine on the Arizona Strip located in northeastern Arizona. Ore production from this mine is anticipated by mid-2008.
The White Mesa mill refurbishment program is now scheduled to be completed by the end of April, 2008. The short delay is due to a number of factors including, abnormal snow fall, equipment deliveries, contractor availability and difficulties in completing the alternate feed processing. The $21 million program includes modifications and upgrading of the mill process equipment, upgrading the entire mill process control system, and relining of tailings cell 4A. Once relining of cell 4A is completed, the company will apply for an operating permit which is expected to be received by July 2008.
Due to the short delay in commencing the milling of conventional ore and the scheduling of ore feeds, we now expect to produce 1.4 to 1.7 million pounds U_3O_8 and 3 to 4 million pounds V_2O_5 during 2008. The drop in uranium production is impacted primarily by the delay in processing of the Arizona 1 ore to late in the year. This has pushed uranium production from the fourth quarter 2008 to the first quarter of 2009.
Sales
The Company expects to sell 1.8-1.9 million pounds of U_3O_8 in 2008 including 1.1-1.2 million pounds from U.S. production. It also anticipates selling 3 million pounds of vanadium. Vanadium prices are quite volatile but have recently risen to a level of $14 to $15 per pound V_2O_5 from an average of $7.00 to $8.00 per pound in 2007. Most of Denison s sales of uranium and vanadium from U.S. production will occur in the third and fourth quarters of the year.
Exploration
Athabasca Basin
In the Athabasca Basin, Denison is participating in 35 exploration projects, primarily located in the southeast part of the Basin and within trucking distance of all the three operating mills in the area. The physical properties of the basement rocks underlying the sandstone Basin, not the sandstone, determine the economic potential of any property. Denison, together with a subsidiary of AREVA and Cameco Corporation, now control the majority of the highly favourable basements rocks in the prolific southeastern sector of the Basin.
Denison is participating in 14 drill programs during the current winter season in the Basin. Denison is operator on the Wheeler River, Park Creek, North Wedge, Bell Lake, and Moore Lake Joint Ventures. In addition, Denison is drilling

on the 100% owned Bachman-Crawford Lakes, Jasper Lake, Stevenson River and Ahenakew projects. JNR Resources Inc. is operator of the Pendleton Lake JV, where four holes totalling 500 metres will be drilled, and the Lazy Edward Bay project where 3,500 metres in 20 holes are targeted. Near the McClean Mill, joint venture partner ARC is operator of the Midwest, Wolly and McClean projects, where 72 holes totalling 17,800 metres in aggregate are planned.

On Denison s operated and non-operated projects, a total of approximately 34,000 metres of drilling is planned this winter. The Company s projects in the Basin represent a good balance of grass roots, mid-stage, and developed projects. Other than 11,600 metres dedicated to drilling advanced targets on the Midwest property, almost all holes

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are focussed on well prepared targets in high potential areas not yet at the development stage. Denison strives to achieve a budget total of 80% devoted to drilling.

In addition to these major drill campaigns, Denison is carrying out a number of different geophysical surveys to identify targets for future drill programs. Approximately 750 line kilometres of airborne geophysical surveys are being flown over two properties as an initial screening tool. Denison is also carrying out a large number of ground geophysical surveys on ten properties, where over 200 line kilometres of Fixed Loop or Moving Loop Time Domain EM surveys, 317 line kilometres of Horizontal Loop Electromagnetics and over 160 line kilometres of DC Resistivity surveys will be completed during the 2008 winter season. Over 675 line kilometres of ground magnetic surveys will also be carried out in conjunction with the above.

Denison s exploration spending in 2008 in the Athabasca Basin is expected to total $15,300,000.

Southwest United States

Denison is planning on spending $2,000,000 on its 2008 U.S. exploration program. The program will be focussed on exploring near its existing operations on the Colorado Plateau. The program is projected to entail an estimated 149,000 feet (45,000 metres) of drilling.

Mongolia

In Mongolia, Denison is committing to a substantial increase in work compared to previous years. The work in 2007 was successful in confirming and enhancing the potential of the two advanced properties and several exploration projects while downgrading several reconnaissance projects.

Denison s plans for 2008 involve over 85,000 metres of drilling. All drill and logging contracts have been signed and are in place for this work. On the GSJV Hairhan project, development drilling will be aimed at upgrading resources from inferred to indicated, and to test high potential areas for additional resources. Several basinal depressions (one over 200 kilometres long) will be evaluated. A major hydrological drilling program will also be undertaken at Hairhan in preparation for ISR pilot plant commercial testwork slated for 2009.

Zambia

Denison commenced field work in the last quarter of 2007, and is planning an intensive program of both reverse circulation and diamond drilling totalling 47,000 metres of drilling in support of its advanced work. A budget of over $20,000,000 is slated to upgrade resources, carry out a metallurgical pilot plant program and complete the feasibility study in support of taking an anticipated production decision in 2009. The Mutanga project has two deposits drill defined to date Mutanga and Dibwe where the drilling efforts are focussed on upgrading and expanding the resources of both deposits.

SUMMARY OF QUARTERLY FINANCIAL RESULTS

(in thousands)	**2007 Q4**	**2007 Q3**	**2007 Q2**	**2007 Q1**
Total revenues	$36,825	$ 9,411	$18,809	$11,719
Net income (loss)	23,542	(11,721)	40,489	(5,066)
Basic and diluted earnings (loss) per share	0.12	(0.06)	0.21	(0.03)

(in thousands)	2006 Q5	2006 Q4	2006 Q3	2006 Q2	2006 Q1

Total revenues	8,322	$ 1	$ 2	$ 666	$ 731
Net income (loss)	(2,407)	(6,368)	(2,886)	(2,474)	(2,863)
Basic and diluted earnings (loss) per share	(0.02)	(0.06)	(0.03)	(0.03)	(0.04)

LIQUIDITY AND CAPITAL RESOURCES

Cash and cash equivalents were $19,680,000 at December 31, 2007 compared with $69,127,000 at December 31, 2006. The decrease of $49,447,000 was due primarily to the acquisition of OmegaCorp Limited (OmegaCorp) using net cash of $158,583,000 offset by net cash proceeds of $107,265,000 received from the issuance of common

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shares through private placements and exercise of warrants and stock options. In addition, the Company raised $52,870,000 from the sale of long-term investments and expended $59,578,000 for property, plant and equipment.

Net cash used in operating activities was $23,084,000 during 2007 compared with $27,494,000 during 2006. Net cash used in operating activities are comprised of net income for the period, adjusted for non-cash items and for changes in working capital items. Significant changes in working capital items during 2007 include increases of $28,443,000 (2006: $7,175,000) in trade and other receivables and $9,468,000 (2006: $4,414,000) in inventories. The increase in trade and other receivables during 2007 is primarily the result of uranium sales in December. The increase in inventories during 2007 consists primarily of the increase in ore in stockpile at December 31, 2007.

Net cash used in investing activities was $158,469,000 during 2007 compared with net cash provided of $45,752,000 during 2006. The decrease was due primarily to the acquisition of OmegaCorp using net cash of $158,583,000, expenditures on property, plant and equipment of $59,578,000 offset by proceeds from the sale of long-term investments of $52,870,000 and a decrease in notes receivable of $9,778,000.

During 2007, the Company completed two significant equity financings for total gross proceeds of $105,419,000 (Cdn$123,876,000). On January 9, 2007, the Company completed a private placement of 9,010,700 common shares at a price of Cdn$11.75 per share for gross proceeds of $89,847,000 (Cdn$105,876,000). On April 2, 2007, the Company completed a private placement of 1,104,295 flow-through common shares at a price of Cdn$16.30 per share for gross proceeds of $15,572,000 (Cdn$18,000,000) to fund eligible Canadian exploration expenditures. Net proceeds from these private placement financings totaled $102,151,000.

In total, these sources and uses of cash resulted in a net cash outflow of $49,447,000 during 2007 compared with a net cash inflow of $63,016,000 during 2006.

Subsequent to the year end, the Company put in place a Cdn$25,000,000 uncommitted secured revolving credit facility with the Bank of Nova Scotia. It is secured by the assets of Denison Mines Inc. Management is confident that the Company s future cash flows and additional financing available to it will be sufficient to allow it to carry out its operational and development plans.

OFF-BALANCE SHEET ARRANGEMENTS

The Company does not have any off-balance sheet arrangements.

TRANSACTIONS WITH RELATED PARTIES

The Company is a party to a management services agreement with UPC. Under the terms of the agreement, the Company will receive the following fees from UPC: a) a commission of 1.5% of the gross value of any purchases or sales of U_3O_8 and UF_6 completed at the request of the Board of Directors of UPC; b) a minimum annual management fee of Cdn$400,000 (plus reasonable out-of-pocket expenses) plus an additional fee of 0.3% per annum based upon UPC s net asset value between Cdn$100,000,000 and Cdn$200,000,000 and 0.2% per annum based upon UPC s net asset value in excess of Cdn$200,000,000; c) a fee of Cdn$200,000 upon the completion of each equity financing where proceeds to UPC exceed Cdn$20,000,000; d) a fee of Cdn$200,000 for each transaction or arrangement (other than the purchase or sale of U_3O_8 and UF_6) of business where the gross value of such transaction exceeds Cdn$20,000,000 (an initiative); and e) an annual fee up to a maximum of Cdn$200,000, at the discretion of the Board of Directors of UPC, for on-going maintenance or work associated with an initiative. In accordance with the management services agreement, all uranium investments owned by UPC are held in accounts with conversion facilities in the name of Denison Mines Inc. as manager for and on behalf of UPC.

The Company was also a party to a temporary revolving credit facility agreement with UPC (not to exceed Cdn$15,000,000). The credit facility terminated on the earlier of repayment or May 10, 2007 and was collateralized by the uranium investments of UPC. Interest under the credit facility was based upon Canadian bank prime plus 1%. Standby fees also applied at a rate of 1% of the committed facility amount. As at December 31, 2006, UPC had drawn

Cdn$11,000,000 under the facility. The temporary facility was fully repaid and cancelled on April 10, 2007.
In June 2007, the Company sold 75,000 pounds of U_3O_8 to UPC at a price of $130.00 per pound for total consideration of $9,750,000.

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The following transactions were incurred with UPC for the periods noted:

(in thousands)	2007	2006 [(1)]
Revenue		
Uranium sales	$ 9,750	$
Management fees (including expenses)	2,301	94
Commission fees on purchase and sale of uranium	2,089	336
Other income		
Loan interest under credit facility	202	57
Standby fee under credit facility	9	3
Total fees earned from UPC	$14,351	$490

(1) Reflects fees earned for the one month period of December 2006 only.

At December 31, 2007, accounts receivable includes $377,000 due from UPC with respect to the fees indicated above.

During 2007, the Company had the following additional related party transactions:

a) Sold 16,562,500 shares of Fortress Minerals Corp. (Fortress) to a company associated with the Chairman of the Company for gross proceeds of approximately Cdn$20,703,000;

b) incurred management and administrative service fees of $251,000 (2006: $237,000) with a company owned by the Chairman of the Company which provides corporate development, office premises, secretarial and other services in Vancouver at a rate of Cdn$18,000 per month plus expenses. At December 31, 2007, an amount of $9,000 (2006: $100,000) was due to this company; and

c) provided executive and administrative services to Fortress and charged an aggregate of $69,000 (2006: $112,000) for such services. At December 31, 2007, no amount (2006: $31,000) was due from Fortress relating to this agreement.

OUTSTANDING SHARE DATA

At March 18, 2008, there were 189,780,035 common shares issued and outstanding, 8,409,155 stock options outstanding to purchase a total of 8,409,155 common shares and 3,321,151 warrants outstanding to purchase a total of 9,564,914 common shares, for a total of 207,754,104 common shares on a fully-diluted basis.

CONTROLS AND PROCEDURES

The Company carried out an evaluation, under the supervision and with the participation of its management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company s disclosure controls and procedures (as defined in the Exchange Act Rule 13a-15(e)) as of the end of the period covered by this report. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company s disclosure controls and procedures are effective.

The Company s management is responsible for establishing and maintaining an adequate system of internal control over financial reporting. Management conducted an evaluation of the effectiveness of internal control over financial reporting based on the *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, management concluded that the Company s internal control over financial reporting was effective as of December 31, 2007. Management s assessment of the effectiveness of the Company s internal control over financial reporting as of December 31, 2007 excluded the operations of OmegaCorp, which was acquired by the Company effective August 1, 2007. OmegaCorp is a wholly-owned subsidiary of the Company. OmegaCorp total assets represented approximately 23% of the book value of consolidated total assets of the Company for the period ended December 31, 2007. Companies are allowed to exclude acquisitions from their assessment of internal control over financial reporting during the first year of an acquisition while integrating the acquired company under guidelines established by the SEC.

There has not been any change in the Company s internal control over financial reporting that occurred during the Company s fourth fiscal quarter of 2007 that has materially affected, or is reasonably likely to materially affect, the Company s internal control over financial reporting.

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CRITICAL ACCOUNTING ESTIMATES

The preparation of the Company s consolidated financial statements in conformity with generally accepted accounting principles in Canada requires management to make judgments with respect to certain estimates and assumptions. These estimates and assumptions, based on management s best judgment, affect the reported amounts of certain assets and liabilities, including disclosure of contingent liabilities. On an ongoing basis, management re-evaluates its estimates and assumptions. Actual amounts, however, could differ significantly from those based on such estimates and assumptions.

Significant areas critical in understanding the judgments that are involved in the preparation of the Company s consolidated financial statements and the uncertainties inherent within them include the following:

Depletion and Amortization of Property, Plant and Equipment

Depletion and amortization of property, plant and equipment used in production is calculated on a straight line basis or a unit of production basis as appropriate. The unit of production method allocates the cost of an asset to production cost based on current period production in proportion to total anticipated production from the facility. Mining costs are amortized based on total estimated uranium in the ore body. Mill facility costs to be amortized are reduced by estimated residual values. In certain instances, residual values are established based upon estimated toll milling fees to be received. If Denison s estimated amounts to be received from toll milling prove to be significantly different from estimates or its reserves and resource estimates are different from actual (in the case where unit of production amortization is used), there could be a material adjustment to the amounts of depreciation and amortization to be recorded in the future.

Impairment of Long-Lived Assets

The Company s long-lived assets consist of plant and equipment, mineral properties, intangible assets and goodwill. At the end of each accounting period, the Company reviews the carrying value of its long-lived assets based on a number of factors. Capitalized mineral property expenditures, these factors include analysis of net recoverable amounts, permitting considerations and current economics. Should an impairment be determined, the Company would write-down the recorded value of the long-lived asset to fair value.

Asset Retirement Obligations

Denison follows CICA Handbook section 3110, Asset Retirement Obligations, which requires that the fair value of the full decommissioning cost of an asset be capitalized as part of property, plant and equipment when the asset is initially constructed. In subsequent periods, Denison then is required to recognize interest on the liability, to amortize the capital costs in a rational and systematic manner, and to adjust the carrying value of the asset and liability for changes in estimates of the amount or timing of underlying future cash flows. Denison has accrued, in accordance with CICA Handbook Section 3110, its best estimate of the ongoing reclamation liability in connection with the decommissioned Elliot Lake mine site and is currently accruing its best estimate of its share of the cost to decommission its other mining and milling properties. The costs of decommissioning are subject to inflation and to government regulations, which are subject to change and often not known until mining is substantially complete. A significant change in either may materially change the amount of the reclamation liability accrual.

Stock-Based Compensation

Denison has recorded stock based compensation expense in accordance with the CICA handbook section 3870, using the Black-Scholes option pricing model, based on its best estimate of the expected life of the options, the expected volatility factor of the share price, a risk-free rate of return and expected dividend yield. The use of different assumptions regarding these factors could have a significant impact on the amount of stock-based compensation expense charged to income over time. Changes in these estimates will only apply to future grants of options and the amounts amortized over the vesting period of existing options should not change as a result.

Retiree Benefit Obligation

Denison has assumed an obligation to pay certain and limited retiree medical and dental benefits and life insurance as set out in a plan to a group of former employees. Denison has made certain assumptions and will retain an actuary at least once every three years to estimate the anticipated costs related to this benefit plan. The actual cost to Denison of this plan will be influenced by changes in health care practices and actuarial factors. While the plan contains certain limits, changes in assumptions could affect earnings.

CHANGES IN ACCOUNTING POLICIES

Effective December 1, 2006, the Company adopted the expensing of exploration expenditures on mineral properties not sufficiently advanced to identify their development potential. Previously, the Company had been capitalizing such exploration expenditures as incurred which is permitted under Canadian GAAP, provided that these exploration

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expenditures have the characteristics of property, plant and equipment and that capitalization is appropriate under the circumstances.

The primary purpose of this change in accounting policy is to align the accounting treatment of exploration expenditures on mineral properties not sufficiently advanced to identify their development potential, with those of the Company s producing peers in the resource industry.

The Company has adopted this change in accounting policy on a retrospective basis with restatement of the comparative periods presented. This change has also been applied to the Company s recognition of its investment in Fortress Minerals Corp.

The Company adopted the following new accounting standards effective January 1, 2007:

a) CICA Handbook Section 1530: Comprehensive Income establishes standards for reporting comprehensive income, defined as a change in value of net assets that is not due to owner activities, by introducing a new requirement to temporarily present certain gains and losses outside of net income. The impact of this new standard is discussed below in c);

b) CICA Handbook Section 3251: Equity establishes standards for the presentation of equity and changes in equity during the reporting period. The adoption of this new standard by the Company did not have a material impact;p;

	$1.10		
Basic net income per common share	$ 1.57	$ 1.26	$ 1.14
Income before extraordinary item per diluted common share	$ 1.31	$ 1.16	$ 1.01
Net income per diluted common share	$ 1.31	$ 1.02	$ 1.04
Shares used in computing basic per share data	23,147	20,207	21,950
Shares used in computing diluted per	34,196	29,415	26,526

share data

See Notes to Consolidated Financial Statements.

UNITED AUTO GROUP, INC.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY AND

COMPREHENSIVE INCOME (LOSS)

	Class A Convertible Preferred Stock		Class B Convertible Preferred Stock		Voting and Non-voting Common Stock				Accumulated Other		
	Issued Shares	Amount	Issued Shares	Amount	Issued Shares	Amount	Additional Paid-in Capital	Retained Earnings (Deficit)	Comprehensive Income (Loss)	Total Stockholders Equity	Comprehensive Income (Loss)
						(Dollars in thousands)					
Balances, December 31, 1998					20,738,384	$ 2	$ 352,591	$ (10,943)	$	$ 341,650	$
Issuance of stock for acquisitions					1,261,327		(13,960)			(13,960)	
Repurchase of common stock					(118,000)		(992)			(992)	
Issuance of preferred stock and warrants	7,904		397				76,679			76,679	
Net income								27,488		27,488	
Balances, December 31, 1999	7,904		397		21,881,711	2	414,318	16,545		430,865	
Issuance of common stock					2,981,011		26,950			26,950	
Repurchase of common stock					(2,872,856)		(26,176)			(26,176)	
Payment in kind dividends	438		124				5,074	(5,074)			
Net income								30,031		30,031	
Balances, December 31, 2000	8,342		521		21,989,866	2	420,166	41,502		461,670	
Issuance of common stock					1,593,869		19,041			19,041	
Exercise of options					343,588		4,781			4,781	
Repurchase of common stock					(387,092)		(5,790)			(5,790)	
Payment in kind dividends	452		128				7,113	(7,113)			
Payment of preferred stock dividends								(384)		(384)	
Fair value of interest rate swap agreement									(7,205)	(7,205)	(7,205)
Foreign currency translation									(1,175)	(1,175)	(1,175)
Net income								44,745		44,745	44,745
Balances, December 31, 2001	8,794		649		23,540,231	$ 2	$ 445,311	$ 78,750	$ (8,380)	$ 515,683	$ 36,365

See Notes to Consolidated Financial Statements.

UNITED AUTO GROUP, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended December 31,		
	2001	**2000**	**1999**
		(Dollars in thousands)	
Operating Activities:			
Net income	$ 44,745	$ 30,031	$ 27,488
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	33,625	24,174	19,131
Deferred income taxes	12,546	10,897	10,007
Minority interests	815	512	722
Extraordinary item		5,613	
Non-cash compensation expense			2,250
Changes in operating assets and liabilities:			
Accounts receivable	(56,420)	(33,144)	(11,090)
Inventories	158,164	(67,942)	(73,687)
Floor plan notes payable	(124,777)	69,186	59,371
Accounts payable and accrued expenses	18,079	24,478	2,690
Other	(14,338)	(11,969)	13,526
Net cash provided by operating activities	72,439	51,836	50,408
Investing Activities:			
Purchase of equipment and improvements	(83,394)	(37,384)	(22,161)
Dealership acquisitions, net of cash acquired	(138,389)	(197,148)	(28,251)
Net cash used in investing activities	(221,783)	(234,532)	(50,412)
Financing Activities:			
Proceeds from borrowings of long-term debt	289,407	339,449	65,000
Payments of long-term debt and capital leases	(155,092)	(159,863)	(159,147)
Proceeds from issuance of common stock, preferred stock and warrants	18,822	16,852	76,679
Repurchase of common stock	(5,790)	(26,176)	(992)
Deferred financing costs			(227)
Net cash provided by (used in) financing activities	147,347	170,262	(18,687)
Net decrease in cash and cash equivalents	(1,997)	(12,434)	(18,691)
Cash and cash equivalents, beginning of year	7,413	19,847	38,538
Cash and cash equivalents, end of year	$ 5,416	$ 7,413	$ 19,847

See Notes to Consolidated Financial Statements.

UNITED AUTO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, Except Per Share Amounts)

1. Organization and Summary of Significant Accounting Policies

United Auto Group, Inc. (UAG or the Company) is engaged in the sale of new and used motor vehicles and related products and services, including vehicle service, parts and collision repair, finance and insurance products and other aftermarket products. The Company operates dealerships under franchise agreements with a number of automotive manufacturers. In accordance with the individual franchise agreements, each dealership is subject to certain rights and restrictions typical of the industry. The ability of the manufacturers to influence the operations of the dealerships, or the loss of a franchise agreement, could have a negative impact on the Company s operating results.

Principles of Consolidation

The consolidated financial statements include all majority-owned subsidiaries. All intercompany accounts and transactions among the consolidated subsidiaries have been eliminated.

Cash and Cash Equivalents

Cash and cash equivalents include all highly-liquid investments that have an original maturity of three months or less at the date of purchase.

Fair Value of Financial Instruments

Financial instruments consist of cash and cash equivalents, accounts receivable, accounts payable, debt, including floor plan notes payable, and interest rate swaps used to hedge future cash flows. The carrying amount of all significant financial instruments, except the interest rate swaps, approximates fair value due either to length of maturity or the existence of variable interest rates that approximate prevailing market rates. The net fair value of the interest rate swaps, based on discounted cash flows, is approximately $12,752.

Revenue Recognition

The Company records revenue when vehicles are delivered to customers, when vehicle service work is performed and when parts are delivered.

The Company arranges financing for customers through various financial institutions and receives a commission from the lender equal to the difference between the interest rates charged to customers over the predetermined interest rates set by the financing institution. The Company also receives commissions from the sale of various insurance contracts to customers. The Company may be assessed a chargeback fee in the event of early cancellation of a loan or insurance contract by the customer. Finance and insurance commission revenue is recorded net of estimated chargebacks at the time the related contract is placed with the financial institution.

The Company also receives commissions from the sale of non-recourse third party extended service contracts to customers. Under these contracts the applicable manufacturer or third party warranty company is directly liable for all warranties provided within the contract. Commission revenue from the sale of these third party extended service contracts is recorded net of estimated chargebacks at the time of sale.

Inventory Valuation

Inventories are stated at the lower of cost or market. Cost for new and used vehicle inventories is determined using the specific identification method. Cost for parts, accessories and other inventories is based on factory list prices.

UNITED AUTO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Property and Equipment

Property and equipment are recorded at cost and depreciated over estimated useful lives, primarily using the straight-line method. Useful lives for purposes of computing depreciation for assets, other than equipment under capital lease and leasehold improvements, are between 5 and 10 years. Leasehold improvements and equipment under capital lease are depreciated over the shorter of the term of the lease or the estimated useful life of the asset.

Expenditures relating to recurring repair and maintenance are expensed as incurred. Expenditures that increase the useful life or substantially increase the serviceability of an existing asset are capitalized. When equipment is sold or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts, and any resulting gain or loss is reflected in income.

Income Taxes

Income taxes are provided in accordance with Statement of Financial Accounting Standards No. 109, Accounting for Income Taxes (SFAS 109). Deferred tax assets or liabilities are computed based upon the difference between financial reporting and tax bases of assets and liabilities using enacted tax rates. A valuation allowance is provided when it is more likely than not that taxable income will not be sufficient to fully realize deferred tax assets.

Intangible Assets

Intangible assets of $784,149, consisting primarily of excess of cost over the fair value of net assets acquired in purchase business combinations, are being amortized on a straight-line basis over periods not exceeding 40 years. Accumulated amortization at December 31, 2001 amounted to $68,780. Amortization expense for the years ended December 31, 2001, 2000 and 1999 was $19,705, $15,408 and $12,996, respectively.

Impairment of Long-Lived Assets

The carrying value of long-lived assets, including intangibles, is reviewed if the facts and circumstances, such as significant declines in revenues, earnings or cash flows or material adverse changes in the business climate, indicate that they may be impaired. The Company performs its review by comparing the carrying amounts of long-lived assets to the estimated undiscounted cash flows relating to such assets. If any impairment in the value of the long-lived assets is indicated, the carrying value of the long-lived assets is adjusted to reflect such impairment based on the discounted cash flows or the fair value of the impaired assets.

Defined Contribution Plans

The Company sponsors a number of defined contribution plans covering a significant majority of the Company s employees. Company contributions to such plans are discretionary and are typically based on the level of compensation and contributions by plan participants. The Company incurred expense of $1,575, $1,389 and $1,315 relating to such plans during the years ended December 31, 2001, 2000 and 1999, respectively.

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 amounts of assets and liabilities, the disclosure 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

UNITED AUTO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

could differ from those estimates. The accounts requiring the use of significant estimates include accounts receivable, inventories, income taxes, intangible assets and certain reserves.

Advertising

Advertising costs are expensed as incurred. The Company incurred advertising costs of $60,952, $51,248 and $43,165 during the years ended December 31, 2001, 2000 and 1999, respectively.

Net Income Per Common Share

Income available to common stockholders used in the computation of basic earnings per share data was computed based on net income, as adjusted to reflect dividends accrued relating to outstanding preferred stock. Basic earnings per share data was computed based on the weighted average number of common shares outstanding. Diluted earnings per share data was computed based on the weighted average number of common shares outstanding, adjusted for the dilutive effect of stock options, preferred stock and warrants.

	Year Ended December 31,		
	2001	**2000**	**1999**
Weighted average number of common shares outstanding	23,147	20,207	21,950
Effect of stock options, preferred stock and warrants	11,049	9,208	4,576
Weighted average number of common shares outstanding, including effect of dilutive securities	34,196	29,415	26,526

Segment Reporting

The Company follows the provisions of Statement of Financial Accounting Standards No. 131, Disclosures About Segments of an Enterprise and Related Information, which establishes standards for reporting information about a Company s operating segments. The Company operates in one reportable segment.

Derivative Instruments

Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities, as amended and interpreted (SFAS No. 133) establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. Under SFAS 133, all derivatives, whether designated in hedging relationships or not, are required to be recorded on the balance sheet at fair value. SFAS 133 defines requirements for designation and documentation of hedging relationships, as well as ongoing effectiveness assessments, which must be met in order to qualify for hedge accounting. For a derivative that does not qualify as a hedge, changes in fair value would be recorded in earnings immediately. If the derivative is designated in a fair-value hedge, the changes in the fair value of the derivative and the hedged item are recorded in earnings. If the derivative is designated in a cash-flow hedge, effective changes in the fair value of the derivative are recorded in other comprehensive income and recorded in the income statement when the hedged item affects earnings. Changes in the fair value of the derivative attributable to hedge ineffectiveness are recorded in earnings immediately. The Company adopted SFAS 133 on January 1, 2001 and recorded $10,187 as a cumulative transition adjustment (reducing other comprehensive income) relating to an interest rate swap (cash-flow hedge) the Company entered into prior to the adoption of SFAS 133. Pursuant to SFAS 133, the cumulative transition adjustment will be amortized and reflected as floorplan interest expense over the remaining life of the interest rate swap.

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UNITED AUTO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Reclassification

In order to maintain consistency and comparability of financial information between periods presented, certain reclassifications have been made to the prior year financial statements to conform to the current year presentation.

2. Business Combinations

During 2001 and 2000, the Company completed a number of acquisitions. Each of these acquisitions has been accounted for using the purchase method of accounting. As a result, the Company s financial statements include the results of operations of the acquired dealerships from the date of acquisition.

During 2001, the Company acquired 13 automobile dealership franchises. The aggregate consideration paid in connection with such acquisitions amounted to $138,900, consisting of approximately $128,350 in cash, the issuance of 289,243 shares of the Company s $0.0001 par value voting common stock (Common Stock) and $5,550 of seller financed promissory notes. The consolidated balance sheets include preliminary allocations of the purchase price relating to these acquisitions, which are subject to final adjustment. Such allocations resulted in recording approximately $134,383 of intangibles. In addition, the Company made an equity investment in a dealership group for approximately $8,000 in cash. During 2000, the Company acquired 35 automobile dealership franchises. The aggregate consideration paid in connection with such acquisitions amounted to $225,623, consisting of approximately $204,975 in cash, the issuance of 841,476 shares of Common Stock and $10,550 of seller financed promissory notes.

In connection with one of the acquisitions consummated during 2001, the Company agreed to make a contingent payment in cash to the extent the Common Stock issued in connection with the acquisition has a market value of less than $17.29 per share during specified future periods. The Company also has obligations with respect to past acquisitions totaling approximately $32,000 over the next four years. In addition, the Company agreed to make a contingent payment in cash to the extent the Common Stock issued in connection with an acquisition completed in 2000 has a market value of less than $12.00 per share during specified future periods.

During 2000, the Company paid $6,147 in cash in final settlement of its obligation with respect to a guarantee relating to 375,404 shares of Common Stock issued in connection with an acquisition that took place prior to 1998.

Pro Forma Results of Operations (Unaudited)

The following unaudited consolidated pro forma results of operations of the Company for the years ended December 31, 2001 and 2000 give effect to acquisitions consummated during 2001 and 2000 as if they had occurred on January 1, 2000.

	December 31,	
	2001	**2000**
Revenues	$6,359,384	$5,790,858
Income before minority interests and income taxes	87,618	75,922
Net income	48,691	42,187
Net income per diluted common share	1.41	1.39

UNITED AUTO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

3. Inventories

Inventories consisted of the following:

	December 31, 2001	December 31, 2000
New vehicles	$490,445	$564,159
Used vehicles	111,253	136,980
Parts, accessories and other	39,702	36,803
Total Inventories	$641,400	$737,942

4. Property and Equipment

Property and equipment consisted of the following:

	December 31, 2001	December 31, 2000
Furniture, fixtures and equipment	$ 77,006	$ 58,069
Equipment under capital lease	823	3,806
Buildings and leasehold improvements	142,698	69,357
Total	220,527	131,232
Less: Accumulated depreciation and amortization	35,075	24,147
Property and equipment, net	$185,452	$107,085

Depreciation and amortization expense for the years ended December 31, 2001, 2000 and 1999 was $13,920, $8,766 and $6,135, respectively. Accumulated amortization at December 31, 2001 and 2000 on equipment under capital lease, included in accumulated depreciation and amortization above, amounted to $347 and $1,629, respectively.

5. Floor Plan Notes Payable

The Company finances the majority of its new and a portion of its used vehicle inventory under revolving floor plan financing arrangements with various lenders. The Company makes monthly interest payments on the amount financed, but is not required to make loan principal repayments prior to the sale of new and used vehicles. Outstanding borrowings under floor plan financing arrangements amounted to $620,014 and $689,687 as of December 31, 2001 and 2000, respectively. The floor plan agreements grant a security interest in substantially all of the assets of the Company s dealership subsidiaries, and require repayment after a vehicle s sale. Interest rates on the floor plan agreements are variable and increase or decrease based on movements in prime or LIBOR borrowing rates. Floor plan interest expense for the years ended December 31, 2001, 2000 and 1999 was $42,430, $44,406 and $28,676, respectively. The weighted average interest rate on floor plan borrowings was 5.60%, 7.92% and 7.33% for the years ended December 31, 2001, 2000 and 1999, respectively.

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UNITED AUTO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

6. Long-Term Debt

Long-term debt consisted of the following:

	December 31,	
	2001	**2000**
Credit Agreement Revolving Loans, weighted average interest 6.25% and 8.39% at December 31, 2001 and 2000, respectively	$380,500	$204,595
Credit Agreement Term Loans, weighted average interest 7.25% and 9.20% at December 31, 2001 and 2000, respectively	161,000	186,000
Seller financed promissory notes payable through 2002, weighted average interest 7.63% and 6.60% at December 31, 2001 and 2000, respectively	6,634	15,492
Term loans, weighted average interest 6.12% and 6.95% at December 31, 2001 and 2000, respectively	3,435	5,433
11% Series A and B Senior Subordinated Notes due 2007	3,650	3,650
Capitalized lease obligations	823	4,007
Total long-term debt	556,042	419,177
Less: Current portion	4,202	41,456
Net long-term debt	$551,840	$377,721

Scheduled maturities of long-term debt for each of the next five years and thereafter are as follows:

2002	$ 4,202
2003	26,753
2004	1,404
2005	25,995
2006	791
2007 and thereafter	496,897
Total long-term debt	$556,042

The Company s Credit Agreement, dated as of August 3, 1999, as amended and restated (the Credit Agreement), provides for up to $770,000 in revolving loans to be used for acquisitions, working capital, the repurchase of common stock and general corporate purposes, as well as a $50,000 standby letter of credit facility. In addition, the Credit Agreement provided for up to $186,000 to be used to repurchase the Company s 11% Senior Subordinated Notes due 2007 (the New Notes). Pursuant to the terms of the Credit Agreement, the Company repaid $25,000 in 2001, resulting in a permanent reduction in the term loans under the Credit Agreement relating to the refinancing of the New Notes. Loans under the Credit Agreement bear interest between LIBOR plus 2.00% and LIBOR plus 3.00%. Outstanding letters of credit under the Credit Agreement as of December 31, 2001 amounted to $27,824. The Credit Agreement replaced the Company s previous bank borrowing facility, which was terminated upon the effective date of the Credit Agreement. The Company incurred an extraordinary charge during 1999 of $494 ($0.02 per diluted share), net of income taxes of $396, resulting from the write-off of unamortized deferred financing costs relating to the Company s previous bank borrowing facility.

The Credit Agreement is fully and unconditionally guaranteed on a joint and several basis by the Company s domestic automotive dealership subsidiaries and contains a number of significant covenants that, among other things, restrict the ability of the Company to dispose of assets, incur additional indebtedness, repay other indebtedness, create liens on assets, make investments or acquisitions and engage in mergers or

UNITED AUTO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

consolidations. In addition, the Company is required to comply with specified ratios and tests, including debt to equity and minimum working capital covenants. The Credit Agreement also contains typical events of default including change of control and non-payment of obligations. Substantially all of the Company s assets are subject to security interests granted to lenders under the Credit Agreement.

In October 2001, we entered into swap agreements of approximately four years duration pursuant to which a notional $400,000 of our floating rate debt was exchanged for fixed rate debt. The fixed rate interest to be paid by us is based on LIBOR and amounts to approximately 4.23%. During 2000, we entered into a swap agreement of five years duration pursuant to which a notional $200,000 of our floating rate debt was exchanged for fixed rate debt for five years. The fixed rate interest to be paid by us is based on LIBOR and amounts to approximately 7.15%. The swaps have been designated as cash flow hedges of future interest payments of the Company s LIBOR based borrowings. The swaps have been designated as hedges of the Company s floor plan borrowings and Credit Agreement.

During 1997, the Company issued $200,000 aggregate principal amount of New Notes. The indentures governing the New Notes require the Company to comply with specified debt service coverage ratio levels in order to incur incremental indebtedness. Such indentures also limit the Company s ability to pay dividends based on a formula which takes into account, among other things, the Company s consolidated net income, and contain other covenants which restrict the Company s ability to purchase capital stock, incur liens, sell assets and enter into other transactions. The indentures governing the New Notes further require the Company to offer to purchase all of the then outstanding New Notes at a purchase price in cash equal to 101% of their principal amount in the event of a change in control, as defined. During 2000, the beneficial interest of Penske Capital Partners and certain affiliated entities exceeded 40%, which, pursuant to the indentures, was deemed to be a change in control. As a result, the Company made an offer to purchase the outstanding New Notes. The tender resulted in the repurchase and retirement of $147,350 face value of New Notes. The Company recorded a $3,969 loss ($0.14 per diluted share), net of $3,118 of tax, relating to the redemption premium paid for the New Notes and the write-off of unamortized deferred financing costs. During 1999, the Company repurchased and retired $49,000 of the New Notes. As a result, the Company recorded an extraordinary gain of $1,226 ($0.04 per diluted share), net of $1,001 of tax. The New Notes are fully and unconditionally guaranteed on a joint and several basis by the Company s auto dealership subsidiaries.

As noted, the Credit Agreement and the New Notes are fully and unconditionally guaranteed on a joint and several basis by the Company s domestic automotive dealership subsidiaries (the Note Guarantors). Separate financial information of the Note Guarantors has been omitted because the Company is a holding company with no independent operations.

UNITED AUTO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

7. Operating Lease Obligations

The Company leases its dealership facilities and corporate offices under non-cancelable operating lease agreements with expiration dates through 2026, including all option periods available to the Company.

Minimum future rental payments required under non-cancelable operating leases in effect as of December 31, 2001 follow:

2002	$ 59,323
2003	58,328
2004	58,048
2005	56,570
2006	54,656
2007 and thereafter	465,574
	$752,499

Rent expense for the years ended December 31, 2001, 2000 and 1999 amounted to $47,693, $35,113 and $29,493, respectively. A number of the dealership leases are with former owners who continue to operate the dealerships as employees of the Company or with other affiliated entities. Of the total rental payments, $12,954, $5,575 and $8,466, respectively, were made to related parties during 2001, 2000, and 1999, respectively.

8. Related Party Transactions

As discussed in Note 7, the Company is the tenant under a number of non-cancelable lease agreements with employees of the Company and certain other affiliated entities. The terms of the leases with the former owners were negotiated prior to acquisition and the Company believes all such leases are on terms no less favorable to the Company than would be obtained through arm s-length negotiations with unaffiliated third parties. The Company is also a tenant under a number of non-cancelable lease agreements with Automotive Group Realty, LLC (AGR). AGR is a wholly-owned subsidiary of Penske Corporation. The Company paid AGR $5,753 and $1,260 under such lease agreements during the years ended December 31, 2001 and 2000, respectively. In addition, the Company sold AGR real property and improvements for $20,870 and $23,365 during 2001 and 2000, respectively, which were subsequently leased by AGR to the Company. The sale of each parcel of property was valued at a price which was either independently confirmed by a third party appraiser, or at the price at which the Company purchased the property from an independent third party. The Company believes that the terms of these transactions are no less favorable than the terms available from unaffiliated third parties negotiated on an arm s length basis.

The Company is party to operating agreements with Roger S. Penske, Jr., the son of Roger S. Penske, the Company s Chairman and Chief Executive Officer, reflecting (a) the ownership by Mr. Penske, Jr. of 10% of HBL, LLC and the ownership by the Company of the remaining 90% of HBL, LLC and (b) the ownership by Mr. Penske, Jr. of 4.7% of United Auto do Brasil, Ltda. and by the Company of 90.6% of United Auto do Brasil, Ltda. In 2000, the Company contributed approximately $3,571 for its 90.6% interest in United Auto do Brasil, Ltda. and Mr. Penske, Jr. contributed approximately $185 for his 4.7% interest in United Auto do Brasil, Ltda. In 2001, Mr. Penske, Jr. contributed approximately $7,229 for his 10% interest in HBL, LLC and the Company contributed $65,064 for its 90% interest in HBL, LLC. Prior to December 31, 2001, Mr. Penske, Jr. owned 20% of UAG Cerritos, LLC. On December 31, 2001, the Company purchased Mr. Penske Jr. s 20% interest in UAG Cerritos, LLC for $1,838. From time to time, the Company provides these subsidiaries with working capital and other debt financing at costs that are comparable to the costs charged by the Company to its other subsidiaries.

UNITED AUTO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

In prior years, the Company entered into management agreements at certain dealerships for which the closing of the acquisition of such dealerships awaited final manufacturer approval. Pursuant to such management agreements, the Company was paid a monthly fee for managing all aspects of the dealerships operations. Aggregate income relating to such management fees of $2,571 for the year ended December 31, 1999 has been included in other income (expense), net in the accompanying consolidated statement of operations.

From time to time, the Company pays and/or receives fees from Penske Corporation and its affiliates for services rendered in the normal course of business, including rents paid to AGR. These transactions reflect the provider s cost or an amount mutually agreed upon by both parties. It is the Company s belief that the payments relating to these transactions are on terms at least as favorable as those which could be obtained from an unrelated third party. Aggregate payments relating to such transactions amounted to $9,798, $3,721 and $311 for the years ended December 31, 2001, 2000 and 1999, respectively.

From time to time, the Company paid and/or received fees from Trace International Holdings, Inc. and its affiliates for services rendered in the normal course of business. The Company no longer engages in such transactions. These transactions reflected the provider s cost or an amount mutually agreed upon by both parties. It is the Company s belief that the payments relating to these transactions were on terms at least as favorable as those which would have been obtained from an unrelated third party. Aggregate payments relating to such transactions amounted to $131 for the year ended December 31, 1999.

The Company has previously agreed to enter into an operating agreement with Lucio A. Noto, a director of the Company, which provides that an entity in which Mr. Noto has an interest will own 20% of UAG Connecticut, LLC. The Company will own the remaining 80% of UAG Connecticut, LLC. The Company purchased the operating assets (excluding real property) of UAG Connecticut, LLC in October 2000 for approximately $26,789. Mr. Noto s entity will pay approximately $5,358 for its 20% interest in UAG Connecticut, LLC, which represents 20% of the consideration paid by the Company inclusive of assets acquired and goodwill paid. The payment will be made as follows: $1,184 upon closing and the remaining $4,174 in quarterly payments over twenty years at an interest rate equal to LIBOR plus 2.25%. The payments due will be offset from permitted periodic cash distributions to Mr. Noto s entity by UAG Connecticut, LLC. The transaction is subject to approval by the manufacturers.

UNITED AUTO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

9. Stock Compensation Plans

The Company s Board of Directors and stockholders adopted a Stock Option Plan pursuant to which all full-time employees of the Company and its subsidiaries and affiliates are eligible to receive stock options. During 2001, the Company granted options to purchase 466,000 shares of Common Stock at the fair market value of the Common Stock on the grant date. Options granted under the Stock Option Plan have a ten year life and typically vest on a pro-rata basis over three or five years. As of December 31, 2001, the aggregate number of shares of Common Stock for which stock options may be granted under the Stock Option Plan is 3,000,838. As of December 31, 2001, 581,080 shares of Common Stock were available for the grant of options under the Stock Option Plan. Presented below is a summary of the status of stock options held by eligible employees during 2001, 2000 and 1999:

	2001		2000		1999	
Stock Options	**Shares**	**Weighted Average Exercise Price**	**Shares**	**Weighted Average Exercise Price**	**Shares**	**Weighted Average Exercise Price**
Options outstanding at beginning of year	2,020,147	$13.63	1,431,794	$15.16	1,227,390	$18.06
Granted	466,000	9.78	588,353	9.89	332,790	7.23
Exercised	268,588	11.14				
Forfeited	401,815	18.96			128,386	20.25
Options outstanding at end of year	1,815,744	$11.82	2,020,147	$13.63	1,431,794	$15.16

The following table summarizes the status of stock options outstanding and exercisable at January 1, 2002:

Range of Exercise Prices	Stock Options Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Stock Options Exercisable	Weighted Average Exercise Price
$7 to $13	1,243,055	7.97	$ 9.21	353,154	$ 9.10
13 to 30	572,689	6.50	17.49	407,587	17.54
	1,815,744			760,741	

The Company has adopted the disclosure only provisions of Financial Accounting Standards Board Statement of Financial Accounting Standards No. 123, *Accounting for Stock Based Compensation* (SFAS 123). Had the Company elected to recognize compensation expense for stock options based on the fair value at the grant dates of awards, income before extraordinary item and income before extraordinary item per diluted common share would have been as follows (unaudited):

Year Ended December 31,		
2001	**2000**	**1999**

Income before extraordinary item	$42,754	$32,032	$24,516
Income before extraordinary item per diluted common share	1.25	1.09	0.92

The weighted average fair value of the Company s stock options was calculated using the Black-Scholes option-pricing model with the following weighted-average assumptions used for grants: no dividend yield; expected volatility of 38.5% in 2001, 40.3% in 2000 and 49.7% in 1999; risk-free interest rate of 5.5% in 2001, 7.75% in 2000 and 8.00% in 1999; and expected lives of five years. The weighted average fair value of options granted during the years ended December 31, 2001, 2000 and 1999 is $4.15, $4.67 and $3.85 per share, respectively.

UNITED AUTO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

In connection with the Securities Purchase Agreement, the Company issued 800,000 options during 1999 to purchase Common Stock with an exercise price of $10.00 per share. The Company recorded $2,250 in compensation expense during 1999 relating to the issuance of such options.

10. Stockholders Equity

In September 2001, the Company announced that its Board of Directors authorized the repurchase of up to three million shares of the Company s outstanding stock. Pursuant to such authorization, the Company repurchased 387,092 shares during 2001 through open market purchases and negotiated transactions at an aggregate cost of $5,790. During 2000 and 1999, the Company completed the repurchase of 2,990,856 shares through open market purchases and negotiated transactions at an aggregate cost of $27,168.

In February 2001, we issued 1,302,326 shares of voting common stock to Mitsui & Co., Ltd. and Mitsui & Co. (U.S.A.), Inc. in a private placement for $10.75 per share (the Mitsui Transaction). Aggregate proceeds, amounting to $14.0 million, were used to reduce debt.

In December 2000, the Company issued 2,139,535 shares of Common Stock to Penske Corporation in a private placement for $10.75 per share. Aggregate proceeds, amounting to $23,000, were used to reduce debt. In addition, the Company s Third Restated Certificate of Incorporation was amended to increase the number of authorized shares of Common Stock from 40,000,000 shares to 80,000,000 shares in December 2000.

The shares of Series A preferred stock and Series B preferred stock entitle International Motor Cars Group I, L.L.C. and International Motor Cars Group II, L.L.C. (collectively, the PCP Entities) to dividends at a rate of 6.5% per year. The dividends were payable in kind for the first two years after issuance and are currently payable in cash. The Series A preferred stock is convertible into an aggregate of 8,794,171 shares of common stock and the Series B preferred stock is convertible into an aggregate of 648,588 shares of non-voting common stock (in each case, after giving effect to payable in kind dividends). We are entitled under some circumstances to redeem the preferred stock after May 3, 2002, for an amount per share equal to the liquidation preference. The liquidation preference is currently $10,000 per share plus accrued and unpaid dividends. Actual cash dividends payable relating to dividends earned during fiscal 2001 in connection with the preferred stock totaled $3.1 million. Beginning in fiscal 2002, the aggregate annual cash dividends payable by us are expected to total $6.1 million. Funding for such dividends is expected to come from cash flow from operations and working capital borrowings under our credit agreement.

The warrants, as originally issued to the PCP Entities, were exercisable at a price of $12.50 per share until February 3, 2002, and $15.50 per share thereafter until May 2, 2004. Pursuant to the anti-dilution provisions of the warrants and as a result of the sale of equity to Mitsui & Co. in 2001, (a) the number of warrants to purchase common stock was increased from 3,898,665 shares to 3,915,580 shares, (b) the number of warrants to purchase non-voting common stock was increased from 1,101,335 shares to 1,106,113 shares, and (c) the warrant exercise price was lowered from $12.50 to $12.45. On February 1, 2002, the PCP Entities exercised the warrants in full and paid us the full exercise price of $62.5 million. The proceeds of the warrant exercise will be used for general working capital purposes which may include acquisitions. Pending such use, the proceeds will be used to pay down indebtedness.

UNITED AUTO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

11. Income Taxes

The income tax provision relating to income from continuing operations consisted of the following:

	Year Ended December 31,		
	2001	2000	1999
Current:			
Federal	$16,990	$11,950	$ 7,091
State and local	5,535	3,269	3,352
Foreign	4	442	964
Total current	22,529	15,661	11,407
Deferred:			
Federal	10,214	9,397	9,085
State and local	2,080	1,255	517
Foreign	252	245	405
Total deferred	12,546	10,897	10,007
Income tax provision before extraordinary item	$35,075	$26,558	$21,414

The income tax provision varied from the U.S. federal statutory income tax rate due to the following:

	Year Ended December 31,		
	2001	2000	1999
Income tax provision at the federal statutory rate of 35%	$28,222	$21,374	$17,096
State and local income taxes, net of federal benefit	4,950	2,941	2,516
Non-deductible amortization of goodwill	2,393	1,864	1,330
Other	(490)	379	472
Income tax provision relating to continuing operations	$35,075	$26,558	$21,414

The components of deferred tax assets and liabilities at December 31, 2001 and 2000 were as follows:

	2001	2000
Deferred Tax Assets		
Accrued liabilities	$ 8,056	$ 7,567
Derivative instruments	5,547	
Net operating loss carryforwards	1,162	2,565

Capital loss carryforwards	41	3,031
Other	1,491	3,020
Total deferred tax assets	16,297	16,183
Valuation allowance		(1,490)
Net deferred tax assets	16,297	14,693

UNITED AUTO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	2001	2000
Deferred Tax Liabilities		
Depreciation and amortization	(29,915)	(19,021)
Partnership investments	(16,439)	(17,440)
Total deferred tax liabilities	(46,354)	(36,461)
Net deferred tax liabilities	$(30,057)	$(21,768)

At December 31, 2001, the Company has $35,691 of state net operating loss carryforwards that expire at various dates through 2021.

12. Supplemental Cash Flow Information

The following table presents supplementary cash flow information:

	2001	2000	1999
Cash paid interest	$81,385	$77,560	$57,073
Cash paid income taxes	25,481	14,149	9,587
Non-cash financing and investing activities:			
Dealership acquisition costs financed by issuance of stock	5,000	10,098	
Dealership acquisition cost financed by long-term debt	5,550	10,550	1,500

13. Summary of Quarterly Financial Data (Unaudited)

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
2001				
Total revenues	$1,394,976	$1,615,183	$1,595,783	$1,614,721
Gross profit	191,790	218,996	221,099	219,273
Net income	6,570	13,405	13,488	11,282
Net income per diluted common share	$ 0.21	$ 0.40	$ 0.38	$ 0.32

	First Quarter	Second Quarter(1)	Third Quarter	Fourth Quarter
2000				
Total revenues	$1,110,767	$1,204,149	$1,331,173	$1,237,900
Gross profit	152,113	166,780	182,613	176,451
Net income	5,640	7,095	11,179	6,117
Net income per diluted common share	$ 0.19	$ 0.24	$ 0.40	$ 0.21

(1) As discussed in Note 6, the Company recorded a $3,969 extraordinary loss in the second quarter of 2000.

The per share amounts are calculated independently for each of the quarters presented. The sum of the quarters may not equal the full year per share amounts.

14. Subsequent Event

In February 2002, the PCP Entities exercised the Warrants for $62,520. As a result, the Company issued 3,915,580 shares of Common Stock and 1,106,113 shares of Non-Voting Common Stock. In March 2002, the Company completed the sale of 3,000,000 shares of voting common stock to the public for $22.00 per share and issued $300.0 million of Senior Subordinated Notes due 2012. The notes bear interest at 9.625% per annum. Net proceeds of $416.4 million from these transactions was used to repay indebtedness under the Company s credit agreement.

Item 7.

c. Exhibits

Exhibit 23.1 Consent of Deloitte & Touche LLP

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

Dated:	May 10, 2002		UNITED AUTO GROUP, INC.
		By:	/s/ Robert H. Kurnick, Jr.
			ROBERT H. KURNICK, JR.
		Its:	EXECUTIVE VICE PRESIDENT

Index to Exhibits

Exhibit No.	Description
23.1	Consent of Deloitte & Touche LLP