

FINAL TRANSCRIPT

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KAR - Q3 2011 KAR Auction Services Inc Earnings Conference Call

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PRESENTATION

Operator

(Operator Instructions). Good day, ladies and gentlemen and welcome to the Kar Auction Services Incorporated third quarter earnings conference call. Today's call is being recorded today's will be Jim Hallett, Chief Executive Officer of Kar Auction Services Inc. and Eric Loughmiller, Executive Vice President and Chief financial Officer of Kar Auction Services, Inc. I would like to turn the conference over to Mr. Loughmiller Please go ahead sir.

Eric Loughmiller - *KAR Auction Services Inc - EVP, CFO*

Thank you for joining us today for the KAR Auction Services third quarter earnings call. Today we will discuss the financial performance of Kar Auction Services for the period ended September 30, 2011. After concluding our commentary we will take questions from participants. We will make every effort to accommodate all of the questions within the hour we have scheduled today.

Before Jim kicks off our discussion, I would like to remind you that this conference call contains forward looking statements within the meaning of The Safe Harbor Provision of the Private Securities Litigation Reform Act of 1995. Investors are cautioned

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that such forward looking statements involve risk and uncertainties that may affect KAR's business prospects and result of operations and such risks are fully detailed in our SEC filings. Now I would like to turn the call over to Kar Auction Services CEO, Jim Hallett.

Jim Hallett - *KAR Auction Services Inc - CEO*

Great thank you Eric, good morning ladies and gentlemen and welcome to our third quarter discussion. Today I actually had Eric join me here in the Motor City I have been on the road this week with Thomas Caruso, President and CEO of ADESA, and Peter Kelly, President and CEO of OPENLANE doing customer visits across the Country and taking a time out to do this conference call and really there are two things I want to focus us on today.

I want to focus on our third quarter performance and then I want to give you update on OPENLANE, not only the acquisition, but the feedback from customers and employees as well. So with that, looking at the third quarter as they say give me the facts, third quarter EBITDA \$116 million year-to-date adjusted EBITDA \$375 million. And I would say that we are disappointed that the strong performances at Insurance Auto Auctions and at AFC, were not enough to offset the 15% volume decline at ADESA.

As a result we need to lower our 2011 adjusted EBITDA expectations from approximately \$500 million to approximately \$485 million to \$490 million. The volume outlook for ADESA, we expect that these industry headwinds will continue into 2012, and that 2012 institutional volumes are expected to be down from the 2011 levels.

However, we do anticipate future volume declines won't be as steep in the quarter-over-quarter going forward as what we experienced in the third quarter of 2011. And we are hopeful that our dealer consignment volumes will continue to improve and hopefully these volumes may offset the institutional volume declines.

I would also like to point out that with the merger of OPENLANE complete, we will begin reporting their volumes as part of ADESA in Q4. Virtual only auctions are not included in the industry data, though OPENLANES activity will be additional volume reported for our industry beginning in Q4 of 2011.

So despite the challenges, KAR continues to generate 45% gross margins, adjusted EBITDA margins of nearly 27% year-to-date and again, this is a result of the complimentary nature of our business model that we continued to talk about. Turning to OPENLANE, I have talked with you on a number of calls in the past that my major focus since becoming CEO of KAR in 2009 has been on technology for all of our business units.

And I think that the acquisition of OPENLANE really addresses a lot of the concerns that I have had over this period of time. OPENLANE at a high level expands our market capabilities. It gives us a toe hold into the virtual auction market.

That market is approximately 1 million vehicles. And we many think we can continue to grow in that space. We also believe that OPENLANE will be enabler to dealer to dealer trades and dealer to wholesaler market as well. If you add up the virtual sales, the wholesaler transactions and the dealer to dealer transactions, that opportunity is a 17 million unit opportunity.

Also, a I am very pleased with the Management Team that we have in place at OPENLANE, and really what we have been able to do is combine much of the existing Management Team in OPENLANE and then we have moved a number of ADESA Managers on to the OPENLANE team, to have the best of the best or as I would say field an all star team. Peter Kelly, the CEO of OPENLANE will be a direct report to me.

He will also be a member of the Senior Management team at KAR. And Peter got introduced, as they say, with a fire hose last week. He attended our Management meetings, he attended first Board Meeting, he also spoke at a Town Hall Meeting in Carmel, where we had over 500 employees at our Corporate Office where he introduced OPENLANE and the Management Team of OPENLANE. So he's well engaged as we get kicked off here.



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But I think it's very important, and I want to be very clear, that this is not just about OPENLANE, it's about the combination of OPENLANE with all of our physical auctions as well as all of our service offerings, and this will not only be a great benefit to ADESA and our other Companies at KAR, but it will also be a great benefit to OPENLANE as well. This becomes very powerful and gives us, what I have been referring to, as a end to end remarketing solution in the entire industry.

And just let me speak about that end to end solution and what that means. Not only does it give us a very strong presence in the physical space, and the very strong presence in the virtual or internet space, but it gives us all the services that a remarketter could possibly require. I would like to say that a remarketter could make one phone call and he would be able to satisfy any service that he would need.

So we are talking about vehicle logistics and transportation, reconditioning, financing, inspections, the ability to for dealers to self post, unmatched analytics available. Obviously, the repossession services that we provide, the guaranteed checks, guaranteed titles, this is really the customer value proposition that I speak about and I think this is the way that we are going to market as a full end to end solution for our customers. But the real key to this deal is going to be integration.

And as you know we closed on the October 3. The integration activities are in full force. It is our plan that OPENLANE will provide the platform for all ADESA E Business requirements.

And we would expect that we will be on a single platform by 2013, and coincidentally sometimes it's better to be lucky than good, I think from being on the road with all of our customers this week, our integration plan and the completion of that integration really matches up with our customers as their volumes will increase in 2013 going forward. So I think our timing has been good there.

Also within open OPENLANE, there are a couple other Companies that we should mention, as they have a transportation solution. They have a Company called Cars Arrive, which is a on line vehicle logistics platform. It's asset light. It's an internet tool that allows us to integrate and transport vehicles. And as a customer, as a dealer buys a car, there's really two things they want to know after they bought it.

And that's how much and how fast can I have it. And this is been very successful technology for OPENLANE. And it is our plan to integrate the Cars Arrive technology into our physical auctions at ADESA in fact Thomas Caruso has rolled out a pilot at seven ADESA auctions this week and we would hope that we would have Cars Arrive transportation fully integrated with the ADESA physical auctions in the coming year.

As well, we acquired a Company called Recovery Data Network, or as we say RDN. RDN is specialized provider for software or data solutions for banks and finance companies that have car loans. This allows them to track their repossession's with the agents and currently RDN has visibility into approximately 70% of all repossession's that take place in the United States, so we think this will be very powerful data and this data will allow us greater access to the repossession market going forward.

So with that we are excited about the integration. But I will say that it's not going to be over night. We expect that it will be somewhere in the order of 15 to 18 months.

And we are absolutely not going to rush it. We are much more focused on getting it right than we are in being in a hurry. And we will keep you posted on that integration as we go forward on future calls. So with that, I would like to now turn it over to Eric for a financial overview and then I would like to come back just before we go to Q&A and wrap up with some of my thoughts on how I see the Company and the industry going forward in 2012 and 2013, and so with that Eric.

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Eric Loughmiller - KAR Auction Services Inc - EVP, CFO

Thank you Jim. I will like to highlight just a few items in our performance for the quarter. First consolidated revenue was essentially flat. This reflects 16% growth in revenue in Insurance Auto Auctions, which was based on a 10% increase in volume sold.

And a 15% growth in revenue at AFC, which reflects a 13% increase in the number of loan transactions. Now, these strong performances though were not enough to offset the 10% decline in revenue at ADESA. That revenue at ADESA though reflects 15% decline in volume, so the good news is we were able to partially offset that decline in volume with some increases in revenue per unit sold. As Jim mentioned, the consolidated gross margin came in at 45%.

I believe this is a strong performance and reflects how we are running the business. We have been able to increase, especially at ADESA, the components of our cost structure that are variable, versus fixed, and maintain these strong margins. The SG&A for the quarter declined. This is primarily the result of a credit recorded in stock based compensation related to the profit interests held by Senior Management.

Credit reported in Q3 for this small group was \$13 million. Please keep in mind the variability of our stock based compensation only relates to profit interest held by members of the senior leadership team of KAR from 2007 LBO transaction and Insurance Auto Auctions from their 2005 LBO transaction. All other options are expensed based on the measurement at our IPO date in December of '09.

This amounted to approximately \$5 million of expense in Q3, so the next stock based compensation was a credit of \$8 million, taking those two components. Year to date adjusted EBITDA is about 1% ahead of the prior year. Our guidance of \$485 million \$490 million of adjusted EBITDA will result in 2% to 3% growth for the year once we achieve it. We are expecting OPENLANE to be break-even for Q4 in this forecast.

I would like to explain why we anticipate to improve our year-over-year growth in Q4. The most significant reason is the calendar. With our major holidays in December falling on Sunday we are picking up some key sale days in comparison to last year. We also have some increased volumes built up at Insurance Auto Auctions due to the weather on the east coast this year.

This will be positive for Q4 performance at IAAI, although we will off set some of this benefit with increased cost created by the extreme weather conditions, what we call cats or catastrophes in the insurance industry. Let me update a couple of other guidance items. We are not changing our guidance for net income per share, it remains at \$0.45 to \$0.50. This reflects the impact of the net credit and stock based compensation off setting the lower performance expectations of ADESA.

Adjusted net income per share is expected to be \$1.18 to \$1.20. Which is down slightly from our previous guidance. We are not changing our expectations for capital expenditures of approximately \$85 million or cash taxes of \$40 million to \$50 million. Next I will like to comment on the most compelling component of our consistent performance over the last five years.

Our strong cash flow generation. We continue to see consistently strong cash generated from our operations. Through three quarters of 2011 we have generated over \$200 million of cash from operations. This is real cash which was used to reduce our leverage at the time of our refinancing in May and also provided \$100 million of available cash which was used in the purchase of OPENLANE.

In terms of converting our adjusted EBITDA into free cash flow, our performance through Q3 is as follows. We had \$375 million of adjusted of EBITDA as we have mentioned. We spent \$64 million of our cash on capital expenditure. We have \$88 million in cash interest, I'm excluding the nonrecurring interest charge related to our Swap termination in May, which is reflected in our interest expense line item.

That was \$14.5 million. So \$88 million is our regular cash interest expense on the debt. And cash taxes of \$30 million for the first nine months. All of this adds up to \$193 million of free cash flow through September 30.



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That's the calculation many of us use to evaluate our EBITDA turning into cash. Of that keep in mind we reduced our cash interest expense in May with the refinancing, so our year-to-date cash interest is a little bit higher than our current run rate. Now I would like to provide a little more color on the expected synergies from the OPENLANE transaction. 2012 will be focused on integrating OPENLANE within KAR.

We will eliminate redundant functions and related cost primarily in administrative areas. We are expecting some revenue and cost reduction opportunities at ADESA as we integrate the Cars Arrive logistics model into the ADESA locations. We are integrating the dealer consignment efforts of OPENLANE and ADESA under the leadership of Tim Zierden, and this is expected to provide some cost benefits. We expect the cost and revenue synergies to aggregate \$8 million to \$12 million in 2012.

As we previously disclosed, this will result in 2012 adjusted EBITDA from OPENLANE and its related activities of \$20 million to \$25 million. The real opportunity for the integration of OPENLANE will be when we complete the integration of the technology. We will have an integrated offering for our customers. This will allow us to lower our IT Support costs and make changes in our prioritization of capital expenditures within IT.

We are in the early stages of IT integration and will provide more details as they are developed. However, I'll let you know we expect to begin seeing the operational benefits of this integration in the next four to six months, with the full benefits realized over the period Jim mentioned of 15 to 18 months.

The financial impact of the technology integration is not expected to be realized until 2013. We will share the expected impact of this technology integration in a future call when we have more details available to us. So now let me turn back to Jim for some final remarks.

Jim Hallett - KAR Auction Services Inc - CEO

Good, thank you, Eric. And just before we go to Q&A, I just want to take a moment and comment on why I remain very positive and optimistic about our Company and about the future of our industry going forward. There's no question that OPENLANE brings a lot of excitement to the party and I think that we all see the advantages of that.

But OPENLANE is only part of the reason for my optimism. When you think about it in Insurance Auto Auctions, they continue to excel as understanding the need of insurance and non insurance industry and that's been evidenced, witnessed by the 10% unit growth that they have seen in the third quarter, I think that speaks involves. AFC, AFC continues to use a very disciplined growth model and achieve strong profitable growth, while maintaining a portfolio that's 99% current.

There's no question we've talked about the pressure and the supply shortage at ADESA, but despite the declining revenues at ADESA, EBITDA margins remain robust and ADESA sales are now 45% dealer consignment. 45% of all the sales at ADESA are dealer sales, and this is initiative we first spoke to you about a couple years ago, and I'm very pleased with the way that initiative has been orchestrated and rolled out throughout the entire Company.

I think it's important to note that we don't believe we are finished in this area, and there's much progress that we feel that we can continue to gain with the dealer consignment initiative, and when you add the OPENLANE component in there, that even expands the opportunity and makes that whole initiative even more powerful. Eric mentioned that this business throws off a lot of cash.

Over \$200 million through September of this year, and we will continue to invest that cash and continue to generate strong returns. I would also say I'm very energized by what we are seeing with SAR, new cars numbers increase to increase. You know that's major driver of transactions for our business. Leasing continues to increase with all of our customers, for the most part we have talked with many of them this past week that I have told you about.

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2012 is upon us. And 2013 is right around the corner and I want to assure you that this Management Team is not sitting back and waiting. I would say that we are being very proactive in terms of how we are looking at businesses and how we expect those businesses to perform and how we expect to manage them going forward. At the start of the call, I told you that I was taking a time out here in Detroit.

I started on the west coast this week and have worked my way east with Caruso and Kelly and the customer meetings have really been, exceeded my expectations in terms of the feedback. Customers are very excited about what we have been able to do here. Complimentary of both ADESA and OPENLANE, but maybe even more complimentary about the combination of ADESA and OPENLANE together.

If I could just paraphrase in a few word or sentences what customers are saying, the feedback is, hey, this is a great fit within the industry. They are very high on the Management Team at OPENLANE and now the combination of Management Teams from ADESA and OPENLANE coming together to form that all star team that I talked about earlier. I'm excited again about the timing of the acquisition and how that matches up with the increases that we expect to come in 2013, and it coordinates with our lines with the integration plan that we have in mind.

Customers have indicated to us what their volume expectations are. And they have indicated to us how they expect to sell these cars going forward. And we are excited about that. Bottom line, the words that are getting tossed around are, this is a real game changer.

This is a real game changer for ADESA. It puts us in a very good position to handle what's coming at us, a real game changer for the Industry. And when you think about it, we have told you that we have a great physical footprint. We have a great internet platform and now we believe it's up to the market to decide how these vehicles get sold.

But if the internet is going to cannibalize what's going on with the physical, we want to make sure that we be are cannibalizing ourselves, and we believe we have the two platforms that allows us to bring this business through KAR. So with that, I'm going to turn it back to our operator and we will take Q&A.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). We will take our first question from Tony Cristello with BB&T of Capital Markets.

Tony Cristello - BB&T Capital Markets - Analyst

Good morning gentlemen.

Jim Hallett - KAR Auction Services Inc - CEO

Good morning Tony.

Tony Cristello - BB&T Capital Markets - Analyst

I guess the question I have is as we look at the ADESA side of the business today, do you think that this is sort of the trajectory we are going to see for the next few quarters. I mean you sort of adjusted the guidance down and it seems like this might have been worse than you expected and I guess what I'm wondering is could it continue to be worse than you possibly expect.

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Jim Hallett - KAR Auction Services Inc - CEO

Yeah, I would say to you that we think that the third quarter, as I mentioned earlier, we don't think the declines will be as steep going forward quarter over quarter. And we have had the opportunity to see October results, October results coming in, and I would say that we are seeing moderate improvement and we don't feel the declines will be as steep. Eric any thoughts on that.

Eric Loughmiller - KAR Auction Services Inc - EVP, CFO

No, Tony I mean Jim summed it up there, October was down year-over-year, but much less than what we experienced in the third quarter. We want everybody to hear that specific detail.

Tony Cristello - BB&T Capital Markets - Analyst

Okay. And then maybe if I could have one more question, when you look at what's going on at your other businesses, particularly IAA, it seems like the strength continues in spite of what has been a little bit of an easing on the pricing side. So what I want to understand is the dynamic if you see the seasonality along with an increase on volume, how quick do you see, or will you see, an impact on the pricing side of the business, or is what's going on the dynamics of the whole car still going to keep pricing relatively stable right now at IAA.

Eric Loughmiller - KAR Auction Services Inc - EVP, CFO

Well, Tony, that's a very good question. And predicting the future would help a whole lot of people in a lot of places. There seems to be no indication on the whole car side that there will be significant reductions in pricing.

Although there is some evidence of some moderation. You know, slight movement. And I'll just point to our third quarter result, we were up 16% in revenue, 10% in volume and roughly 6% on revenue per vehicle. Our revenue per vehicle is driven strictly by proceeds.

So I think in relative sense the pricing remains strong. There is a seasonality in the summer months, the types of cars and availability. There's also some impact as you get into some of the conditions in the north east that could impact what's happening in the salvage business relative to be abundance of flood cars from the hurricane's and things like that. All of that can impact the proceeds, but generally we are seeing what I would describe as overall strong pricing across the marketplace. I probably wouldn't get too caught up in the moderations that occur that are small changes, if that's fair for you.

Tony Cristello - BB&T Capital Markets - Analyst

No, that's very helpful. Thank you.

Jim Hallett - KAR Auction Services Inc - CEO

You're welcome.

Operator

We will take our next question from Gary Prestopino with Barrington Research.

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Gary Prestopino - Barrington Research - Analyst

Good morning everyone.

Eric Loughmiller - KAR Auction Services Inc - EVP, CFO

Good morning Gary.

Gary Prestopino - Barrington Research - Analyst

I checked the web site for the National Auto Auction Industry, I didn't see any data for Q3, do you have any data as to what the volumes were down in the industry.

Eric Loughmiller - KAR Auction Services Inc - EVP, CFO

You know Gary I haven't seen that yet. Okay. That's fine. Preliminary data they were down, and again there's preliminary data, it was down double digits, probably just slightly less than ours.

Gary Prestopino - Barrington Research - Analyst

Okay. And then in terms of the vehicles on the wholesale side, you are basically saying that going forward the magnitude of the declines won't be as much as they were over the last two quarters. Now, is that inclusive or exclusive of the what OPENLANE is going to add for you all.

Jim Hallett - KAR Auction Services Inc - CEO

Yeah, Gary that would be exclusive of what OPENLANE will add.

Gary Prestopino - Barrington Research - Analyst

So that's exclusive of what OPENLANE.

Jim Hallett - KAR Auction Services Inc - CEO

Yes.

Gary Prestopino - Barrington Research - Analyst

Okay great. And when you made the acquisition you said OPENLANE was going to do about 300,000 vehicles this year. Is that still a good number, and based on the fact that they are in, you know, maybe somewhat of a different industry with the virtual side, would you expect that to be up next year as well.

Jim Hallett - KAR Auction Services Inc - CEO

To answer your first question, yes, that's still a good number and your numbers are accurate and we do believe there is opportunity on the virtual side.

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Eric Loughmiller - *KAR Auction Services Inc - EVP, CFO*

Although I will add to that, a lot of the virtual business comes out of off lease and repossession's.

Gary Prestopino - *Barrington Research - Analyst*

Right.

Eric Loughmiller - *KAR Auction Services Inc - EVP, CFO*

They will not be immuned to the trends we are seeing as we going into 2012 with the off lease volumes. That's what we refer to, the institutional volumes are expected to be lower than '12 than '11, that would be true to their part of the market as well. Who knows how that would turn out, they could see some declines there as well.

Gary Prestopino - *Barrington Research - Analyst*

Okay. And then you talked about that they are in the virtual auction market as well as it enables dealer-to-dealer, and dealer-to-wholesaler, right now are the majority of what they are doing in the virtual auction market, and you have to transition that into dealer-to-dealer, dealer-to-wholesaler, or do they have a thriving business in there.

Jim Hallett - *KAR Auction Services Inc - CEO*

They are primarily, Gary, on the commercial space, but I will say that they have made very good progress in the dealer-to-dealer space, although it's still relatively a small portion of their business at this time. But again, this is an area that we think we have the opportunity to grow. One of the tools that we did not have was this dealer self posting activity.

And all of our competitors did have that. The ability to go to a dealer and allow him to image the car, do a condition report, and post it right from his facility, without that car ever having to go to auction, and this not only for the dealers, but it could be for the daily rental customers and others alike. So this is a whole new capability for us that we did not have in the past.

Gary Prestopino - *Barrington Research - Analyst*

So the dealer posts the car himself and it opens it up to the market including dealer-to-dealer, dealer-to-wholesaler. That's correct. Okay. All right.

Jim Hallett - *KAR Auction Services Inc - CEO*

Thank you.

Eric Loughmiller - *KAR Auction Services Inc - EVP, CFO*

Okay, thank you Gary.

Operator

And I will take our next question from Rick Nelson.

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Rick Nelson - *Stephens - Analyst*

Thank you, and good morning.

Jim Hallett - *KAR Auction Services Inc - CEO*

Good morning, Rick.

Eric Loughmiller - *KAR Auction Services Inc - EVP, CFO*

Hi Rick.

Rick Nelson - *Stephens - Analyst*

The 15% decline that you reported for ADESA volumes, can you break that down between the dealer consignment and the institutional business.

Eric Loughmiller - *KAR Auction Services Inc - EVP, CFO*

You know, I don't have that right in front of me Rick, but institutional was down. We are actually up year-over-year on dealer consignment.

Rick Nelson - *Stephens - Analyst*

Good. And the improvement that we are seeing here in October, is that happening on the dealer consignment or the institutional side of the business or both.

Jim Hallett - *KAR Auction Services Inc - CEO*

Actually Rick it's on both.

Rick Nelson - *Stephens - Analyst*

Got you. And what does this head wind of fewer off lease vehicles, when does that actually become tailwind for you.

Jim Hallett - *KAR Auction Services Inc - CEO*

You know, that's a good question and one that people are very much focused on. We think we will see the bottom of the trough sometime in late 2012, where some indication and a lot more feedback that we got this week, a lot more clarity that we got from our customers this week, that some customers are actually starting to see their volumes pick up on year-over-year basis, but we think it will come late in the year, possibly the fourth quarter.

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Rick Nelson - *Stephens - Analyst*

Got you. And are you seeing any indications of late given the Thailand floods and potential shortages again and on the new car supply that franchise dealers are increasingly going to focus on used cars, or once again I guess, and try to retail more wholesale last. Is that a growing head wind again.

Jim Hallett - *KAR Auction Services Inc - CEO*

Yeah, I think the floods in Thailand are a temporary thing. We spoke with the import manufacturers and the most it affected by that this week and they've given us their outlook on that. And so it's temporary. You know, you kind of get over the effects of the tsunami and then we are dealing with the floods in Thailand, but dealers are always going to, I think dealers have now become better merchandise of used vehicles.

They are always going to try to be focused on it trying to retail first. And I think it will be much of the same going forward.

Eric Loughmiller - *KAR Auction Services Inc - EVP, CFO*

And Rick, C&W's report on used car sales was put out, I think early this week, was pretty promising. I think it was 12% year-over-year growth for the month of October. And the strongest segment was franchise dealers, sooner or later they are going to run out of cars if they can't get the trades on the new cars and that's always good for the auction business.

Rick Nelson - *Stephens - Analyst*

Yeah, I saw that, thanks for picking up sequentially there from September to October and maybe that explains some of your improvement.

Jim Hallett - *KAR Auction Services Inc - CEO*

I think so.

Rick Nelson - *Stephens - Analyst*

Thanks a lot. And good luck.

Jim Hallett - *KAR Auction Services Inc - CEO*

You're welcome, thank you.

Eric Loughmiller - *KAR Auction Services Inc - EVP, CFO*

Thanks, Rick.

Operator

We will take our next question from Ryan Brinkman with Goldman Sachs.

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Ryan Brinkman - Goldman Sachs - Analyst

Hi, good morning.

Jim Hallett - KAR Auction Services Inc - CEO

Good morning, Ryan.

Ryan Brinkman - Goldman Sachs - Analyst

You know, I know you are looking forward to the return of these off lease volumes toward 2012 end and 2013, do you have an estimate, or care to guess publicly, regarding which quarter the core ADESA operation is likely to trough in terms of the number of vehicles auctioned.

Jim Hallett - KAR Auction Services Inc - CEO

Yeah as Eric said predictions or for gypsies. You I don't think I will want to predict when that takes place.

Ryan Brinkman - Goldman Sachs - Analyst

Okay then and I would just say that one strong part of your story right now is definitely the volume trend at IAA which comes despite the fairly negative trend at miles driven, can you talk about what is driving that result which in recent quarters has come also despite the drag from lost Allstate volumes, maybe you are better or fully cycling that this quarter, and I'm interested to know too if you think you are taking significant amounts of market share on salvage and if you are who do you think it's coming from mom and pops or TRA.

Jim Hallett - KAR Auction Services Inc - CEO

Yeah, I would say that the to growth the IAA is primarily coming from the of non insurance .

Eric Loughmiller - KAR Auction Services Inc - EVP, CFO

In this quarter.

Jim Hallett - KAR Auction Services Inc - CEO

Yes.

Eric Loughmiller - KAR Auction Services Inc - EVP, CFO

And let me add to that Ryan, this will be in our queue, but I think you've asked the right question. Non insurance, you know we have gotten a little more aggressive. We have taken title on more vehicles and in our queue you will see a disclosure about that. Not a significant number more, but slightly more so we have pointed that out and when our queue is filed we will give a little more detail on that.

To be honest. In the pricing environment we are in, there are alot of opportunities for everyone in our business, and while we talk about non insurance, our insurance business remains quite strong. And, you know you just happen to be in a quarter Q3

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where there are fewer accidents, the roads are in better shape, we aren't into any weather, we are holding our own, we are not losing ground there, I think we are doing well in the insurance segment. But in Q3, that was not a significant contributor to growth.

Ryan Brinkman - *Goldman Sachs - Analyst*

Still encouraging, thank you. Can you talk about how you think OPENLANE is benefit you from rental car channel diversion perspective. I think they have strong relationship with Avis, Budget and perhaps others.

Jim Hallett - *KAR Auction Services Inc - CEO*

Yes, OPENLANE has strong relationships with the customers that you mentioned, with the daily rental companies. And we are currently selling cars for those rental companies. We would expect that with the combination, there is more of an opportunity for us to do more of that business. And going back to that self posting capability that I spoke about earlier with the dealers, we will actually be able to image and post cars that are still driving around earning rent for these companies. These cars can be posted for sale while they are still in their inventory and we see that as a growing opportunity and OPENLANE has demonstrated their capability to be able to handle this business.

Ryan Brinkman - *Goldman Sachs - Analyst*

Great. And my last question is just a housekeeping item. You know your share accounts have been pretty steady, yet it looks like it picked up 2.1 million during the quarter, is that right and what had would be it contribute of attribute to..

Jim Hallett - *KAR Auction Services Inc - CEO*

It is correct that it went up but that was because in Q2 as a result of refinancing and all though costs we had a net loss, therefore you do not dilute the share count. Year to date through Q2 the shares were 137.6 , so it was really just the exclusion of the of dilution for options. So a pretty good number to use now would be in the neighborhood of 137.5 to 138. But it was really just the impact of the accounting rules on whether your dilute the shares on a quarter with a loss, that's why the share count in second quarter was lower.

Ryan Brinkman - *Goldman Sachs - Analyst*

Got you. Thank you..

Operator

And we will take our next question from John Murphy with Bank of America Merrill Lynch.

John Murphy - *Bank of America Merrill Lynch - Analyst*

Good morning guys.

Jim Hallett - *KAR Auction Services Inc - CEO*

Good morning John.



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John Murphy - Bank of America Merrill Lynch - Analyst

Just wanted to ask a question on the ADESA side that you guys didn't talk about too much on the conversion rate side, the 57% was relatively low, I'm curious, is that a mixed impact from dealer consignment, it seems a little odd given the pricing was so strong and the conversion rate was light relative to where it's been in the last couple years.

Jim Hallett - KAR Auction Services Inc - CEO

Yes, John that is attributed to the mix. As you know, we are selling a much higher number of dealer vehicles in as we have talked about in the past dealer consignment does not convert at the same level as the commercial inventory.

John Murphy - Bank of America Merrill Lynch - Analyst

And then a I'll follow on to that, revenue per vehicle sold increasing, is that result of fees being picked up on your schedules or is that really also just a function of dealers being on both side of the equation in your mix.

Jim Hallett - KAR Auction Services Inc - CEO

John, good question. It's actually a combination of two things, in our mix we are seeing a little bit of a lift on ancillary services due to the types of institutional cars even though there's fewer, and then we have had fee increases combined with the increased dealer mix gets you the as we call it the two legged fee because the sell fee is higher on many dealer cars than it would be on institutional car, but there's also some miner fee increases as well on the rate schedules.

John Murphy - Bank of America Merrill Lynch - Analyst

Got you. On the AFC side you guys are doing great job of growing loan transactions there. Are you, who are you taking share from, you know is this initiative there to, you know, go to these Manheim auctions and work that business. I know you guys have always been doing that. What's going on with the growth there, because it's far out stripping what you are doing with the volume on your ADESA side.

Jim Hallett - KAR Auction Services Inc - CEO

You know, I think what's going on there is we are getting credit for our ability to increase our capacity. So we are a very dependable floor plan provider, where the competition in that space is generally pretty tight on it's available capital and maybe seen as risk. You can't really highlight because when you borrow for a car John and you pay it off, you don't like, it's not like credit card where you transfer balances.

So it's really who has the most stable deal at the time. But it's it not a competitive fee environment, I think our availability of capital has been a big plus and the discipline in the marketplace that our AFC team has shown to consistently perform, all of that combined to what we are doing. So yeah, the service element and our competition particularly our large competitor that has a captive that you named, that we don't use name too often, they probably are more focused on financing cars acquired at their auctions where we have really never put restriction on our customers as to where they buy their cars.

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John Murphy - Bank of America Merrill Lynch - Analyst

Lastly big picture question for you Jim. As you think about the recovery in the SAR, do you think there's the potential that as that recovers we get a better churn in the secondary market, being the used car market that you play in, and that could be a very significant, potentially complete offset, to the pressure you are expecting to continue on the institutional side next year.

Jim Hallett - KAR Auction Services Inc - CEO

I would certainly hope that it would offset some of those volumes, yes.

John Murphy - Bank of America Merrill Lynch - Analyst

Okay, but I mean would you venture a guess that pretty significant recovery even a recovery that we have seen late this year could offset the pressure on institutional or is the institutional pressure going to overwhelm it and we see some volume declines next year I'm trying to gauge the plus or minus.

Jim Hallett - KAR Auction Services Inc - CEO

John all we have been able to get to is the declines in our view and these were in our comments. We think will not be at the pace we experienced in the third quarter. You know, we aren't going to get into specific predicts on volume quite yet. You know, we are still working throughout the year ends. We will probably have more commentary in our next call when we give you some insights into what we are seeing for 2012.

John Murphy - Bank of America Merrill Lynch - Analyst

Great thank you very much guys.

Jim Hallett - KAR Auction Services Inc - CEO

Thank you.

Operator

We will take our next question from Craig Kennison from Robert W. Baird.

Craig Kennison - Robert W. Baird - Analyst

Good morning, thanks for taking my questions.

Jim Hallett - KAR Auction Services Inc - CEO

Good morning, Craig.

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Craig Kennison - *Robert W. Baird - Analyst*

Given the discussion already on this call around 2013, when you are going to be on the better side of the OPENLANE integration and some of these off lease trends, I am curious if you would comment on any opportunities outside of North America that your acquisition of OPENLANE would create for you.

Jim Hallett - *KAR Auction Services Inc - CEO*

Yeah, I think that our primary focus is getting this integration and getting it right here in North America. But there's no question that we know there are opportunities outside North America. And I've spoken in the past that we are very familiar with the opportunities and who the targets would be. They are certainly familiar with us.

I would say we are well known to each other. Our relationships are good. And I think it's a matter of time as to first things first. Let's take care of business at home and then possibly look at opportunities where we could leverage this technology around the globe.

Craig Kennison - *Robert W. Baird - Analyst*

Thank you, and with respect to the integration, are there any major fee differences between OPENLANE and ADESA that you will need to reconcile and present to you an opportunity or a problem as you do so.

Jim Hallett - *KAR Auction Services Inc - CEO*

You know, Craig, what I would comment on is there are virtual only auctions so their fee is structure is designed around less services as we provide as ancillary services at the auction. But there's not significant differences in terms of auction fees as it relates to the type of sale. If your do apples to apples, physical versus OPENLANE, they would be very comparable.

Craig Kennison - *Robert W. Baird - Analyst*

Thanks, and Eric you may have commented on this earlier in the call, will we see OPENLANE metrics stand alone or will they be imbedded within ADESA .

Jim Hallett - *KAR Auction Services Inc - CEO*

OPENLANE will be reported as part of the ADESA segment. With that said in order, because they haven't been included in the volume numbers of industry, or at ADESA, will we will be able to give you some data to help you understand what the impact of the acquisition is, compared to what's happening kind of in the core industry that we have been talking about for the last several years. But we will not be reporting OPENLANE separately.

Craig Kennison - *Robert W. Baird - Analyst*

Thank you.

Jim Hallett - *KAR Auction Services Inc - CEO*

You're welcome .

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Operator

We will go next to Scott Ciccarelli with RBC Capital Markets.

Scott Ciccarelli - RBC Capital Markets - Analyst

This is Patrick.

Jim Hallett - KAR Auction Services Inc - CEO

Good morning Scott.

Scott Ciccarelli - RBC Capital Markets - Analyst

Thanks for taking my questions. I guess my first question is just around AFC and OPENLANE, I was just sort of wondering what kind of financing opportunities were available at OPENLANE previously, and what you see there as you move AFC financing into your OPENLANE business.

Jim Hallett - KAR Auction Services Inc - CEO

Yeah, AFC has existing relationship with OPENLANE that has been in place for some time now, but we feel now with the integration and with the focus that we put on the consolidated entity, we feel that there will be increased opportunity for OPENLANE just because of the nature of all the relationships coming together.

Eric Loughmiller - KAR Auction Services Inc - EVP, CFO

Scott, the other thing is remember now that customer basis buying there, we can market directly to them, where before it was kind of pushed to us, so we can be a little more forward about the ability to use AFC as part of the OPENLANE transaction.

Scott Ciccarelli - RBC Capital Markets - Analyst

Thanks, and then I guess, within the whole car auction business, you have seen growth in dealer consignment despite dealers selling their own inventory to supplement the drop in new and used car sales. I guess looking forward you expect some of the dealers to move back to the more traditional businesses allowing for you to capture this part of the market or do you expect them to remain in the market.

Jim Hallett - KAR Auction Services Inc - CEO

I would very much expect that they will remain in the market and, you know, I think that, I think in many cases dealers have discovered that the auction is even more critical to how they manage their inventory and how they manage their supply and how they maximize their proceeds. And there may have been some good habits that have been learned through this period of time.

Scott Ciccarelli - RBC Capital Markets - Analyst

Okay thank you for taking my questions, guys.

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Jim Hallett - KAR Auction Services Inc - CEO

You're welcome.

Eric Loughmiller - KAR Auction Services Inc - EVP, CFO

Thanks Scott.

Operator

We will take our next question from Bill Armstrong with CL King and Associates.

Bill Armstrong - CL King & Associates - Analyst

Good morning, Jim and Eric.

Jim Hallett - KAR Auction Services Inc - CEO

Good morning Bill.

Bill Armstrong - CL King & Associates - Analyst

Earlier you mentioned that about 45% of ADESA sales are dealer consignment, is that a third quarter number.

Jim Hallett - KAR Auction Services Inc - CEO

Yes that's a third quarter number.

Bill Armstrong - CL King & Associates - Analyst

Okay. Does your remaining guidance for the year, you know, to what extent is the strong SAR that we have seen September and October play into your guidance in terms of helping dealer consignment volume.

Eric Loughmiller - KAR Auction Services Inc - EVP, CFO

You know, Bill, to be honest, the SAR from our perspective for the year is kind of ending up where we thought it would, somewhere between 12.5 and 13 and the monthly variations. We probably don't spend as much time focused on. So we have not adjusted our expectations at all as a result of September and October if new car sales being a little bit higher. There seems to be other pressures that might influence us in the fourth quarter.

Bill Armstrong - CL King & Associates - Analyst

Okay. And thinking about 2012 internally what is your outlook for the SAR for 2012.

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Eric Loughmiller - *KAR Auction Services Inc - EVP, CFO*

You know what Tom Contos has really talked about is steadily increasing SAR over a period of time and I think Jim that's where we are, right. We don't have a number but we think it will be above 2011 and we are not looking at any production levels that would indicate it would be big jump, it will be more like incremental gains as we have continued the SAR on slow moderate recovery.

Bill Armstrong - *CL King & Associates - Analyst*

Got it. And then ADESA SG&A expense seems to be pretty well under control. Can you break out the variable, versus fixed components of SG&A for ADESA, what the percentages are.

Eric Loughmiller - *KAR Auction Services Inc - EVP, CFO*

You know I have given the guidance before that we are about 40% fixed 60%, variable but because ADESA own's more property than IAA, IAA leases substantially all of their property, probably like 35% at ADESA and maybe a little above 40% at IAA because of the occupancy cost, I consider a fixed component.. So although I think we have made further improvements relative to, we have outsourced some functions in the shops and in the reconditioning centers, we might have made a little improvement, I haven't updated that number, maybe I will do that towards year end, but I have always believed around 35%, we might be it slightly less than that right now.

Bill Armstrong - *CL King & Associates - Analyst*

Got it. Okay thank you.

Jim Hallett - *KAR Auction Services Inc - CEO*

You are welcome.

Operator

And we will take our next question from Chris Ceraso with Credit Suisse.

Chris Ceraso - *Credit Suisse - Analyst*

Good morning.

Jim Hallett - *KAR Auction Services Inc - CEO*

Good morning he is Chris.

Chris Ceraso - *Credit Suisse - Analyst*

So just to check because we have heard about this from some of the other companies, the adjustment that you had in stock comp in the quarter where it ended up being a credit, is that because the price of your stock was down in Q3.

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Jim Hallett - KAR Auction Services Inc - CEO

Yes, Chris and it only applies to the profit interests, not to the larger number of options or larger number of people that have smaller grants throughout our work force. Those are not impacted by the stock price. That's a fixed measurement. So it's the top six executives at KAR, and I think there are 7 at IAA from the '05 transaction, that are accounted for in the liability method, which means any move in stock up or down has direct impact on our P&L.

Chris Ceraso - Credit Suisse - Analyst

So is that is likely to flip to an expense in Q4 but you pull this out of both your earnings and EBITDA guidance any way, right.

Jim Hallett - KAR Auction Services Inc - CEO

On the adjusted yes. It's out of adjusted EBITDA, it's out of adjusted earning per share, but not GAAP earnings per share, which is why the GAAP earnings per share didn't change.

Chris Ceraso - Credit Suisse - Analyst

Ford I believe, mentioned something recently on sales call that not only were off lease units down but the percentage of lessees that were keeping their vehicle was up quite a bit, further reducing the flow through of off lease vehicles, is that something you can validate, have you seen that and have you taken into account that change in the number of people keeping their vehicles in your expectations for Q4 and for next year.

Jim Hallett - KAR Auction Services Inc - CEO

I would say that although we don't have any exact data on this, I know from our if customers anecdotally, there's no question that more cars are being kept at termination, either by the consumer or by the dealer that originated the lease. So yes, that would be accurate statement.

Eric Loughmiller - KAR Auction Services Inc - EVP, CFO

Chris I will go even further, we believe again from what we are hearing, that's a major factor as to why the declines in Q2 and Q3 for us on the volumes were greater than what we expected going into the year. Because we have good visibility on the number of cars coming back from leases, what we don't have is good visibility on what do they do with them when they turn them in relative to remarketing.

Chris Ceraso - Credit Suisse - Analyst

Right, so have you taken that into account as you have thought about Q4 so you don't get surprised to the down side again.

Eric Loughmiller - KAR Auction Services Inc - EVP, CFO

Well, we have been responding to it all along. I'm referring back to our expectations at the beginning of the year, but yes we have taken that into account as a major factor as to why we provided updated guidance today.



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Chris Ceraso - *Credit Suisse - Analyst*

Right, okay. And then just lastly, I'm sorry, if I didn't quite get this, but can you just explain again what Cars Arrive is about.

Jim Hallett - *KAR Auction Services Inc - CEO*

Yeah, Cars Arrive is a transportation solution, basically they have many created software that allows for us to aggregate and dispatch vehicles to be transported in a most efficient way with the use of technology. And to elaborate on that a little bit is all of the vehicles that are bought by customers, that the customer asking for shipping, they are able to instantly provide them with a price to move that car from zip to zip and then all those cars are posted in a pool, the transporters go in, there are 30,000 or 40,000 trucks that go in and actually bid on that move they build their own loads and very high percentage of these vehicles, I'm thinking like in the order of 80% to 85% of these vehicles, are bid on and self distributed without us ever having to being involved in it, it's all through technology.

So these cars, if obviously if a transporter is moving in this direction and there's a car going in that direction he goes in and bids on it and draws it down himself. So what we have been able to do is OPENLANE has been very successful with providing that. Number one, it makes it very easy for the dealer when he can buy the car and he can instantly see how much it is to ship that car and they can also guarantee him how many days it's going to take for that car to arrive.

And now if you think about that, Cars Arrive has been doing that for OPENLANE in their market place has been in that 300,000 to 350,000 volume and now if you think about bringing that into ADESA, where you have approximately 2 million vehicles moving in and out, this really expands the opportunity there and that's the opportunity that we see.

Chris Ceraso - *Credit Suisse - Analyst*

Okay. Thank you very much.

Eric Loughmiller - *KAR Auction Services Inc - EVP, CFO*

And Chris, let me add, I just want to be clear, Cars Arrive and RDN were owned by OPENLANE. You know we have talked about acquiring, them they were part of the OPENLANE.

Chris Ceraso - *Credit Suisse - Analyst*

Got it.

Operator

And we will take our next question from Eli Halliwell with DE Shaw.

Eli Halliwell - *DE Shaw - Analyst*

Hi guys, good morning. I just had three quick questions. One is on the volume that you guys got as IAAI. It looked like it took a big jump in Q3 and I was wondering if you can help explain that.



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Jim Hallett - *KAR Auction Services Inc - CEO*

Yes, I think I said earlier that you know it's primarily the non insurance vehicles that we were able to attract to IAA.

Eric Loughmiller - *KAR Auction Services Inc - EVP, CFO*

Yep and we did acquire, and you will get the numbers on this we did acquire title to more cars than we have in the past because of the opportunities in the market place and again it's still not a significant number, but it was up from what we passed so we have given that in our it queue that disclosure which will go out in the next day or so, probably today I hope.

Eli Halliwell - *DE Shaw - Analyst*

That's the trend we can sort of count on continuing that you are having more robust than historical growth in that category, the non insurance vehicles.

Eric Loughmiller - *KAR Auction Services Inc - EVP, CFO*

Yes. I think it's a focus of the industry, not just IAA and I think we are having success because of the relationships that we have through ADESA to be honest. Jim maybe tell them about VRD as a components vehicle remarketing it division as a part of that.

Jim Hallett - *KAR Auction Services Inc - CEO*

Yeah, we have talked in the past about VRD. And VRD is a program to attract some of the lower end whole cars and also some of the of damaged cars from our whole car customers that had historically been going through whole car auctions. Now we are able to give them the choice of should that car go to a salvage auction, is that where the best buying audience is, or should that vehicle go to whole car auction.

And again because much our footprint and because of the complimentary companies, we are able to offer that service and many of our whole car customers are now taking advantage of that, and that continues to grow and we see more and more whole car customers sending cars to the salvage auction, primarily damaged cars and some of the low end cars that are going there as well.

Eric Loughmiller - *KAR Auction Services Inc - EVP, CFO*

With all that said, I would like to reiterate about 85% of our Insurance Auto Auctions business is still with the insurance industry, so that is still the focus and they are doing very well within that segment as well.

Eli Halliwell - *DE Shaw - Analyst*

Got it, thank you.

Second question was on the SG&A, I know you have been through it a couple times with the stock account thing, what I have a hard time understanding is the underlying level of spending at the corporate level, if I take the SG&A you report and subtract the division SG&A's I get a number of like \$4 million in this quarter, which I understand has an if offset against it. But what's the underlying SG&A spending level that we can look at going forward. How much of an offset was there.



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Jim Hallett - *KAR Auction Services Inc - CEO*

Again I will give you an approximate number but we said our goal for this year was keep that holding company number flat year-over-year on adjusted EBITDA basis and magnitude of it is about \$60 million these are rough numbers, \$15 million per quarter. That's what you're looking for isn't it.

Eli Halliwell - *DE Shaw - Analyst*

Yes, that's perfect. Okay great. And then the last question, you mentioned earlier that you said you are implying positive guidance for growth in Q4 based on a change in the calendar and I guess maybe some good momentum at IAAI, it's a big jump though from trend in the last two quarters can you help us understand that a little bit better so we can get a better sense for that quarter.

Eric Loughmiller - *KAR Auction Services Inc - EVP, CFO*

Yeah, I'll just clarify. I even, with it December 25th and January 1st being Sunday, the legal holidays are Mondays. And last year the legal holidays were Fridays. If I were to tell you the strongest auction days are Wednesday, Thursday and Friday.

I mean every week, so you are you are picking up two strong auction days, that last year were holidays, and then on top of that the day before a holiday is often, just having the 23rd and the 30th is fortuitous from an auction scheduling perspective. And with the strong market, I mean part of that is our expectations are built upon the strength of the market. Our customers are wanting their cars continuing to be sold.

Where some years if the pricing were softer they may say I will wait until January. There is a lot of that going in our favor. And then again, unfortunately in my business I have to become very anal about minutia, you look at how many Wednesdays you have, it's a good month for us across all of our business so that's the number of auction days.

Then you hit on the other one, I mean, the hurricanes, you know, the land based hurricanes I'm now calling them. But the hurricanes that crawled over land, you know, you build up that inventory, we have pretty good visibility into that and you will see strong salvage volumes, I would expect in the industry, but as specially at IAA in the fourth quarter that are also something that came out of what we saw in the September, I think it was September when all those hurricanes hit ground and it takes a while to process them.

Eli Halliwell - *DE Shaw - Analyst*

Great so then.

Eric Loughmiller - *KAR Auction Services Inc - EVP, CFO*

Is on a strong run, again we have included all that that's why I took the time to explain it because, you know, somebody might ask. It's not optimism that things are turning around. It, you know, over the macro of our businesses.

Eli Halliwell - *DE Shaw - Analyst*

Got it.

Operator

We will now turn the call over to Jim Hallett for closing remarks.

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Jim Hallett - *KAR Auction Services Inc - CEO*

No, I would just say thank you very much we appreciate you being on and appreciate your continued interest. You know, we are not without challenge on the whole car side, but again as I mentioned in my comments there's much to be optimistic about. And you know we think about how fast a year goes by, 2012 is going to come it's going to go and we are going to get to 2013 and with all the things that we have addressed we feel good about the future outlook of the business and the Company and are very positive and very focused on going forward, so with that I want to thank you for being on the call today and appreciate your interest and we will look forward to talking to you on the next quarter

Operator

That concludes today's conference, thank you for your participation

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