FINAL TRANSCRIPT

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the KAR Auction Services Incorporated Q3 2010 Quarter Earnings Conference Call. Today's call is being recorded.

Today's host will be Jim Hallett, Chief Executive Officer of KAR Auction Services, Incorporated, and Eric Loughmiller, Executive Vice President and Chief Financial Officer of KAR Auction Services, Incorporated.

I would now like to turn the call over to Mr. Eric 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, 2010. 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 may contain forward-looking statements. Such statements are subject to certain risks, trends and uncertainties that could cause actual results to differ materially from those projected, expressed or implied by such forward-looking statements.

Now I will turn the call over to Jim.

Jim Hallett - *KAR Auction Services, Inc. - CEO*

Great. Thanks, Eric, and good morning, ladies and gentlemen. And please allow me to add my welcome as well. I'm very excited to report on our third quarter. As well, I'm looking forward to discussing some of the strategic initiatives that we released last night.

First off, from a financial overview standpoint, very pleased to report that our revenues were up 4% for the quarter. Our gross profit increased 140 bps, taking us to 45.7%. And our adjusted EBITDA increased 6%, taking us to $121 million for the quarter.

For the full year 2010, we expect adjusted EBITDA to be approximately $470 million, which is very consistent with the guidance that we'd previously issued.

In taking a look at the business units and starting with ADESA, the story is much the same that we've been talking about for the last nine months. We would expect that industry volumes will remain tight, that the industry will fall below 9 million units sold in 2010. ADESA was down 6.7% on volumes in the third quarter. However, that did fare better than the industry. We expect that the industry will report that the industry is down in excess of 8% for the quarter. And we've continued to see traction with our dealer consignment initiative.

As you know, this is an initiative that we started talking about in the fourth quarter of 2009. And we've worked diligently on through 2010. And we're starting to see it gain traction and pay dividends. 35% of our cars sold in the quarter were dealer consignment cars, and that's been a nice increase for us.

We continue to remain focused on controlling our costs as well as growing our market share. Very encouraged with some of the news that's out about lease originations and the trends that we're seeing in leasing that I'll speak to more later in my commentary.

And as well, I would say that ADESA where we continue to be very focused on technology. We feel that we're improving our internet presence. And we definitely feel that we're winning our share of the virtual marketplace. And if you take a look at the last three quarters at ADESA, we have sold over 20% of our inventory each quarter during this year.

Taking a look at AFC, just a continued strong performance. On a year-over-year basis, we've seen growth in loan transactions. Revenue per loan transaction is up, as well as our average loan balances have increased. The credit stats are very favorable. We continue to be over 99% current with the portfolio, and that's been the story for most of the year at AFC. But I think the thing that's most impressive about AFC in the third quarter was that the adjusted EBITDA for the third quarter at AFC was almost a 50% increase to that of a year ago. So again, strong performance in AFC continues to deliver.

IAA, again, another very, very strong performance. And I think as we look at IAA, I think there's a number of factors that I would point to, not just the price of cars that are contributing to this performance at IAA. First and foremost, I continue to say that we very much believe in the hybrid methodology. We feel that the hybrid methodology, every time we offer a car physically, we offer that same car electronically. We feel it does attract more bidders. More bidders equals more bids. More bids equals higher proceeds for our sellers.

As well, we're feeling good about the buyer initiatives that we put in place over the last couple quarters, and no question, the strong used car values are continuing to pay dividends or to drive those proceeds as well as the solid commodity pricing and the miles driven are starting to return to more normalized levels.

So, all in all, good performance from IAA. I had the opportunity to attend the IAA insurance leadership summit last month, which was very well attended by our insurance customers. And I was impressed with the strong support that they have for our international buying initiatives.

As you know, we've spoken before that we have people on the ground traveling to many of these foreign markets to develop our buyer base. We're actually holding seminars. We're training buyers around the globe on how to use their technology. We're familiarizing them with currency issues and how to deal with logistics. And in fact, we've seen attendance exceed our expectations. And most recently, we've been in Africa, and I think now we have sold cars in excess of 120 countries during the last year. Our call center is able to communicate in 10 languages at IAA. And our website now communicates in 6 languages.

A couple new initiatives at Insurance Auto Auctions is we have released mobile technology for our buyers. This allows our buyers to view inventory and to purchase inventory directly from their mobile phones. And again, I think this is just an indication that we continue to grow and expand the level of service and convenience that we offer to our insurance customers.

A couple new -- not acquisitions, but a couple Greenfields and the relocation that I want to speak to at IAA. We have a new site that we've opened in Louisville, Kentucky. And as well, we've opened a new site in Fort Meyers, Florida. And we've relocated our site in San Diego to coexist with our existing whole car auction that's located in that market.

So with that, I'll move to a couple of these strategic initiatives that I talked about at KAR, and we announced that we plan to use $150 million to repay debt. We are seeking an amendment that Eric will discuss in detail in a few minutes. And we would expect that we would pay this debt down in the fourth quarter. And again, the paydown of this debt is very consistent with our strategy and our commitment to de-lever the Company.

We announced as well that we've done an acquisition of the Premier Auction Group, which includes six sites. As well, we've acquired -- taken on a lease for a whole car auction in Las Vegas.

And if I can just take a minute and maybe speak to these acquisitions a little bit, these six sites are smaller sites. They're primarily focused on dealer consignment and specialty sales. Typically, they're going to sell somewhere in the neighborhood of 5,000 to 10,000 vehicles on an annual basis. These are sites that we may have not looked at in the past. In fact, I would say they're not even in secondary markets. In many cases, they're in tertiary markets.

And we feel it falls very much in line with our dealer consignment initiative. As we continue to drive dealer consignment to try and offset this downturn in the off-lease volumes, we feel that getting into these markets and getting closer to the independent dealers, this is a good initiative that will, again, continue to complement the initiatives that we have in place and continue to complement the volumes on the dealer consignment side.

As well, we think that we can leverage our technology into the Premier Auction Group, which will expand their service offerings to our customers, and it will be an opportunity for AFC to grow their portfolio at these sites as well.

With that, I'll take Vegas a little bit separately. One of these six sites is located in Vegas, and that site is primarily a specialty sale. It concentrates on boats and RVs and watercraft, that sort of thing, and we're going to continue to operate that specialty site there, but it was that site that really caused us to look further into the Vegas market, and we were able to acquire an ideal piece of property to open a full-blown whole car site for ADESA. And we are going to be opening a new car ADESA site in Vegas, a 45-acre site, 10 minutes, as we say, from the strip. And we think it's a great location. We think our customers are going to be excited about us being there. And the facility should be completed probably by the end of the first quarter, definitely up and operating early in the second quarter.

So with that, a lot of good news. I do have some additional commentary that I'll go into just before Q&A. But at this point in time, I'd like to turn it over to Eric Loughmiller, and Eric will walk us through the financials.

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

Thank you, Jim. First, let me state that I am very pleased with our third quarter performance.

Despite lower 2010 volumes as compared to the prior year in our ADESA and Insurance Auto Auction business segments, we were still able to grow revenue, improve our gross profit as a percent of revenue and increase adjusted EBITDA. We also had earnings per share in the third quarter of $0.19 compared to $0.08 for the prior year.

Our strong third-quarter performance is also seen in our continued strength in cash flows. Available cash at September 30, 2010, aggregated $322.2 million, up from $245.5 million at June 30, 2010.

Now, let me provide a little more color on the performance of each of our business segments. ADESA's performance in the third quarter continues to reflect the tight supply of vehicles at the wholesale auctions. ADESA revenue for the third quarter decreased $3 million to $267.4 million. Our units sold decreased 7% in the third quarter of 2007, as compared to the prior year. We believe our decrease in volumes is better than the volume declines experienced throughout the wholesale auction industry. We were able to offset substantially all of the volume decreases at ADESA through selected fee increases, improved ancillary services revenue, and a positive impact from the exchange rate for the Canadian dollar.

Gross profit for ADESA was 44.8% of revenue for the third quarter of 2010, compared to 46% in the prior year. We also have experienced a modest decrease in conversion rate to 64.2% for the third quarter of 2010, compared to 66.3% in the prior year.

Despite this small decrease, conversion rates remain significantly above historical levels. On a year-to-date basis, gross profit of 44.4% through three quarters of 2010 is slightly ahead of the 44.2% gross profit through the first 3 quarters of 2009.

Insurance Auto Auctions continued its strong2010 performance in the third quarter. Although units sold declined 4% in the third quarter as compared to 2009, IAA still had a 5% increase in revenue for the period. The increased revenue is representative of the continued strength in auction proceeds, which is directly related to the increase in average revenue per vehicle.

The third quarter is typically a lighter volume quarter in the salvage industry, and this year was no exception. We had a number of insurance providers with lower volumes this year compared to last. These were partially offset by other customers that experienced increases in volumes. We also experienced a modest decrease in non-insurance vehicles. This reflects the small increase in Q3 2009 volumes related to the Cash for Clunkers program, which obviously did not exist this year.

Gross profit at IAA was 39.1% of revenue for the third quarter of 2010 compared to 36.2% in the prior year. Contributing to the improved gross margin were the improved revenue per vehicle resulting from continued strength in the auction proceeds and lower tow costs, which reflect Insurance Auto Auctions efforts to reduce the average tow cost per vehicle sold. These increases were offset in part by -- the reductions in cost were offset in part by increased yard and auction costs throughout the chain.

Insurance Auto Auctions' SG&A costs declined in the third quarter of 2010 as compared to 2009. The primary driver of the decrease in SG&A is a reduction in stock-based compensation. The stock-based compensation expense recorded in the third quarter of 2009 was unusually high.

AFC continued its strong 2010 performance as well. The strong revenue growth through the third quarter reflects an increased number of loan transactions, improved revenue per loan transaction, and an increase in the average loan balance in the portfolio. We continue to experience exceptional credit quality throughout our AFC portfolio. This has led to extremely low loan loss expense in the third quarter. Our net provision for credit losses of $1.2 million for the third quarter of 2010 is lower than the net provision for credit losses of $4.8 million for the third quarter of 2009. I would like to remind you that the 2009 financial statements of AFC do not present this provision for credit losses in the same format as 2010 financial statements, where it was spread throughout the P&L in different line items.

Partially offsetting the increased revenue and related gross profit were increases in SG&A. The increased SG&A is primarily related to increased incentive and stock-based compensation for the AFC team.

The holding company had a significant decrease in net expense for the third quarter of 2010 as compared to 2009. This decrease is related to the timing of recording stock-based compensation expense in 2009. Approximately $15 million of stock-based compensation was recorded in the third quarter of 2009 compared to only $5 million in the third quarter of 2010.

One of the strengths of the car business model is our strong free cash flow generation from our diverse and complementary businesses. As I mentioned earlier, our available cash at September 30, 2010, is over $322 million. Our year-to-date capital expenditures aggregate $41.9 million. However, even though we're through 3 quarters of the year, I still expect our 2010 capital expenditures to total approximately $75 million.

I would also like to provide an update on our expectations for cash taxes. Previously, I have estimated our cash taxes to be approximately $20 million. While we continue to have minimal cash US taxes, we have seen an increase in our Canadian income taxes this year. Therefore, I'm updating our guidance, and I will expect cash taxes in 2010 to be approximately $40 million. This increase all relates to the increase in Canadian income taxes.

Now, let me give a few specifics about our efforts to amend the credit agreement to permit us to repay debt prior to year end. We have formally requested holders of term loan B and the revolving credit facility to approve the use of up to $75 million of our available cash to retire or redeem subordinated debt following a payment of at least $75 million on term loan B. We have not determined which subordinated debt will be retired if this is approved. However, the 8 ¾% senior notes are currently callable. We will provide more information as the amendment process concludes over the next couple of weeks.

If the amendment is not obtained, we will have the ability to repay debt in the first quarter of 2011 after completing the excess cash flow computation. Our excess cash flow sweep requires 50% of the excess cash flow to be used to repay term loan B. The retained excess cash flow or the other 50% may be used by the Company to retire or redeem subordinated debt. The actual amount of excess cash flow is defined in accordance with our credit agreement, cannot be determined until year end. But if we are successful in obtaining the requested amendment, we will receive credit against excess cash flow for any amounts repaid on debt prior to year end.

Our primary measure of performance at KAR is adjusted EBITDA. We have generated $372.3 million of adjusted EBITDA in the first 9 months of this year, a 14% increase over the $326.2 million generated in the first 9 months of 2009. With this performance in the first 9 months of 2010, we have reduced our net consolidated leverage ratio to 3.6 times. We continue to focus on achieving our leverage target of 3 times levered by the end of 2011.

As Jim mentioned, we are standing by our most recent guidance for 2010. In summary, we expect adjusted EBITDA of approximately $470 million. This will translate into earnings per share of $0.40 to $0.45 and adjusted earnings per share of $0.90 to $0.95. For a reconciliation of earnings per share to adjusted earnings per share, please review our press release that was issued last night.

I think that's enough of a history lesson. So let me turn it back to Jim for a few comments as we look forward.

Jim Hallett - *KAR Auction Services, Inc. - CEO*

Great. Thank you, Eric and just before we go to Q&A, maybe I can wrap up with some commentary. I think we all recognize that used car volumes are down, especially the institutional volumes and focused on the off lease being considerably down as we go into 2011 and beyond. And what we've seen over the last couple quarters is we've seen dealers choosing to try and retail as many of their trade-ins as they can with the tight market supply. They may be retailing cars that they would not normally try to retail. And we're not seeing those cars at transaction.

But on the other hand, let me reassure that the world does not end in 2011 and 2012. In fact, we are beginning to see some very positive trends. And earlier in my comments, I spoke about the return of leasing. Not only are the domestic getting--domestics getting back into leasing and getting back into leasing in a significant way, but the foreign manufacturers have gotten involved in leasing over the past couple years and they're staying in leasing and I would say that they're getting in leasing even in a more significant way. And the thing that excites me about some of the leasing that's going on is many of these leases are being reported as 24 and 36-month leases. And we can start to expect to see those maturities in late 2012 and certainly in 2013. As well I think most of you are familiar with the SAR reported for October. Pretty confident that that number will exceed 12 million units for the year. And there's some manufacturers that are thinking that we could get to as much as 12.5 million or 13 million units for 2011. Whether it's 12 million or 13 million, it's all good news for our industry. As you know, that's a major driver of our business. New car sales creating used car trades creating transactions at the auctions.

So with that, in the near term, we are very focused on cost containment. As I've said before, there's no finish line to our pride initiative. We're always looking for ways to contain our costs. We will continue to gain-- to focus on our market share gains. We do feel we are gaining market share. And I'll be very interested in seeing how those numbers shake out at the end of the year when all the numbers are compiled.

Aside from the Premier acquisition and the lease that we've taken on in Las Vegas, we will continue to look for additional acquisition opportunities going forward. So I would say to you that the long-term view is very positive. We are properly positioned for the rebound that we know is on the way. And I go back to much of Eric and I have been talking about for the last year and that's the diverse and the complementary nature of our businesses. When you think about the pressures at ADESA, that has really created a positive performance for Insurance Auto Auctions and for AFC. And we feel strongly committed that we're going to be able to generate 15% to 20% long-term growth in terms of adjusted EPS.

When you think about the third quarter performance, I believe that it truly demonstrates how this management team is able to function in a difficult market. This is a very veteran and very seasoned management team and I would say if there's one thing that we don't do, we don't panic. We find a way to work through it. And so, as we look forward to 2011 and 2012, I think we only have to take a look back at 2008 and 2009 to what we've been through. And I can't imagine conditions getting much tougher than what we've seen in the past. And I think that things only get better going forward.

So in closing, I would say to you that this is a very energized management team, very focused, very energetic and very enthusiastic about the opportunities and about the road that lays ahead. Believe me, we think this is a phenomenal company and we think that things will only continue to get better as we go forward.

So, with that, I'm going to turn it back to Rachelle, our operator. And we'll take some Q&A.

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

Rachelle, before you start, I made a mistake in my notes. I want to correct something. Our adjusted earnings per share guidance hasn't changed. It's $0.92 to $0.97. I apologize. My notes were wrong and it's my mistake. But we have not changed that. It's $0.92 to $0.97. Now Rachelle, back to you.

QUESTIONS AND ANSWERS

Operator

Thank you. (OPERATOR INSTRUCTIONS) And our first question will come from Chris Ceraso with Credit Suisse.

Chris Ceraso - *Credit Suisse - Analyst*

Thanks. Good morning.

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

Morning, Chris.

Chris Ceraso - *Credit Suisse - Analyst*

So, Eric, let's just pick up where you left off with regard to your comment about the guidance. Is your intention to be nudging people lower on the fourth quarter, if I back into what the implied Q4 guidance is relative to what you've done through nine months versus your full year? It's a fair amount lower than the consensus. Is this just you not changing it or are you trying to signal that something is getting more difficult relative to the run rate that we've seen? I know seasonally Q4 is softer, but aside from that.

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

Well Chris, we give annual guidance. And what I'd like to say is we don't have anything material to update the annual guidance. But we are not signaling any concerns about the fourth quarter. We really feel good about our business. It's a tough environment as Jim mentioned. But please what we're telling you is we're just not updating our annual guidance.

Chris Ceraso - *Credit Suisse - Analyst*

Okay. If we could maybe just consider a scenario for 2011 where off-lease units are down 20%. If you've got a different number that you're thinking about, I'd be interested to hear that. How would your auction volumes fare relative to 2010? Do you think you can make up for that fully with dealer units? Do you think you'll do better than the industry? Worse than the industry? How are you envisioning 2011 in terms of dealing with the slide in off-lease units?

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

Yes, Chris, I think I mentioned that we think in large part that we can make up for the loss that we're going to see in the off-lease segment. Primarily, we think we're going to do that through our dealer consignment growth. And we've certainly seen that well into 2010 and we expect that that will only continue to grow through 2011.

And another area that I touched on that we haven't talked much about in the past is our specialty division. And our specialty division has grown significantly over the course of the last year and a half. And this includes, as I mentioned, RVs, boats, water craft, motorcycles, Sea-Doo's, snowmobiles, whatever you can think of. That division is growing as well. And with the acquisition that we talked about, not only do we pick up more dealer consignment and more opportunity to sell dealer consignment, but we also picked up a couple significant specialty sales which we think will complement our existing specialty sales as well. So long answer, but yes we think for the most part we can make up much of that decline.

Chris Ceraso - *Credit Suisse - Analyst*

And is there a US sales rate, Jim, in 2011 that we need to see at a minimum for that to happen? In other words, if it-- if we run at 12 even instead of 13, is that enough or is it-- it doesn't matter within that range?

Jim Hallett - *KAR Auction Services, Inc. - CEO*

I think the trend is in our favor. Obviously, we feel-- I think the marketplace feels very confident. I read something this morning that they feel that this year may even end at 12.6 with we would say is a little optimistic. But we think that's trending up. And anything that gets you 12 and above I think is going to be good news.

Chris Ceraso - *Credit Suisse - Analyst*

Okay, thank you.

Jim Hallett - *KAR Auction Services, Inc. - CEO*

You're welcome.

Operator

And next we'll move to John Murphy with Bank of America, Merrill Lynch.

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

Morning, guys. How are you?

Jim Hallett - *KAR Auction Services, Inc. - CEO*

Good, thank you.

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

Just a question on dealers first. It sounds like there's a bit of a pressure as dealers are holding on to vehicles they would have wholesaled previously and retailing them. But at the same time, on the flip side, we're hearing from dealers that they're coming to auctions to source more vehicles. So I'm just wondering as we think of the net of those two impacts from dealers focusing more on the used car business, really how that's impacting the business? Cause it seems like it's good and bad at the same time.

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

John, that's interesting. That is good and bad, you're absolutely correct. They may not be taking their trades back to auction, but they're also paying up to get inventory, which is high used car values. While that's not the best situation at all times for ADESA, it works out very well at Insurance Auto Auctions and AFC. And you hit the nail on the head. They're having to buy that inventory to keep their lots full. And what Jim just mentioned about the SAR, we can't wait till these new car dealers become new car dealers again instead of used car dealers. Cause then those trades will come back to the auction.

Jim Hallett - *KAR Auction Services, Inc. - CEO*

Yes, I think they're-- they're really stretching to sell inventory right now than under normal circumstances they would not be retailing. So the SAR will take care of a lot of our pain.

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

Got you. Then a question on the acquisitions. And Jim you mentioned that they were generally smaller sites than you operate normally. I was just wondering as we think about how you ramp up the sites over time, is there the possibility as you put your systems in place to ramp up volume, take advantage of economies of scale and if these sites could grow over time? Or do you think they can be as profitable as your other sites at these smaller levels just cause they're higher margin dealer business? Just trying to understand how these smaller sites, the economies will really work versus your other sites?

Jim Hallett - *KAR Auction Services, Inc. - CEO*

Yes, well I think it's all of the above. But let me talk a little bit about it. First of all, we absolutely expect that we can have organic growth just with the ADESA shingle. And our presence there we feel that brand does attract more dealers. We feel that we can definitely grow our technology and our internet offerings from those locations, which probably-- well I can say not probably which don't have those facilities or those resources in place today. And then I think we can grow other areas of our business. That specialty business that I talked about, we can grow that. And it gives us six more dots on the map that dealers can get to. And in some cases, there may even be some commercial business in the local market that we may be able to handle for some of our large national consignors right there in the local market without having to transport it out.

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

Got you and then just another question. You had mentioned international visits and touching base with international customers. I was just wondering, in Insurance Auto Auctions and then also in ADESA, how much of your sales volume is going on the overseas that you can tell either from physical bidders or online bidders? Just trying to gage what-- how that's changing over time and where it stands right now?

Jim Hallett - *KAR Auction Services, Inc. - CEO*

Yes, and I'll ask Eric to chip in here as well, but I believe most recently we would say that 30% of our inventory at Insurance Auto Auctions is being sold outside of Canada and United States. Largest ones obviously being Mexico and then in Eastern Europe and South America. In the ADESA whole car side, much lesser extent but we're seeing more and more brokers and international buyers certainly buying whole cars and shipping them to some of these foreign marketplaces.

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

John, let me point out. At IAA, what makes this difficult-- we believe the cars leave the US. They're often acquired by US brokers on behalf of foreign buyers. So it's an approximation at 30%. You know what? But what we do know is it's been fairly consistent in-- around that 30% number this year.

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

Got you. And then Eric, just one last question, what's your minimum cash balance? You guys talked about it before. Just what is it now you think?

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

I've always said John that I'm comfortable. We've got a revolver but we like to keep a minimum of $50 million. I mean again if you look at the daily working capital needs that could come up from a sale. And that hasn't changed. As we've grown, we see efficiencies. It's still probably around $50 million would be the minimum cash balance you'd want to keep. But again, if it fell below that with given an undrawn revolver, I'd be comfortable as well.

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

Great. Thank you very much, guys.

Jim Hallett - *KAR Auction Services, Inc. - CEO*

You're welcome, John.

Operator

And next we'll move on to Gary Prestopino with Barrington Research.

Gary Prestopino - *Barrington Research - Analyst*

Hey, good morning, everyone.

Jim Hallett - *KAR Auction Services, Inc. - CEO*

Morning, Gary.

Gary Prestopino - *Barrington Research - Analyst*

Jim, you gave some statistics on the dealer cars this quarter, 35%. What was it last year?

Jim Hallett - *KAR Auction Services, Inc. - CEO*

For the quarter or overall?

Gary Prestopino - *Barrington Research - Analyst*

For the quarter.

Jim Hallett - *KAR Auction Services, Inc. - CEO*

It was about 32%.

Gary Prestopino - *Barrington Research - Analyst*

Okay, that's fine. And then getting back to these auctions that you've purchased in Vegas. You said they do between 5,000 and 10,000 cars each. That's a pretty wide range, 30,000 to 60,000 cars. Could you maybe truncate it a little bit more for us?

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

Gary, this is Eric. Let me answer that. We don't want to give too much detail for this-- for our acquisition but I would just tell you they vary in size, but overall, they're within that range. It's not a large transaction. It's just not a large transaction but we wanted to give you a flavor for it. And I would expect the volumes to be below 50,000 units somewhere.

Gary Prestopino - *Barrington Research - Analyst*

Okay, that's fine. And then in terms of this new site that you're opening in Vegas on the wholesale side, this is not a replacement site, this is a Greenfield, correct?

Jim Hallett - *KAR Auction Services, Inc. - CEO*

Yes, this is a Greenfield.

Gary Prestopino - *Barrington Research - Analyst*

So, how long does that take you to get that fully loaded up to speed? And I would assume it would be somewhat of a drag on 2010 results. Is that a correct assumption?

Jim Hallett - *KAR Auction Services, Inc. - CEO*

Well, I think that-- first of all I think that in the case of Greenfields, in the past we've always said we'd like to think that these Greenfields can be cash flow positive in 12 to 18 months. But in the case of Vegas, we feel very optimistic about Vegas, just based on the feedback we've gotten from our customers. In fact, we're going to start marshalling cars there, I think we announced in our press release, we're going to start marshalling cars there for a major customer almost immediately because the ground is prepared, the fence and security are in place, and we're getting ready to go. So we feel that Vegas will certainly be cash flow positive quicker than what a typical Greenfield would be just because of the amount of momentum that we have going in from customers who have indicated they're willing to support us in that marketplace.

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

And Jim mentioned in his commentary, Gary, that the Vegas site for Premier is primarily specialty. However, they had developed some traction in the used car market that we're able to take their momentum and carry on as well. So this might be a little quicker.

Gary Prestopino - *Barrington Research - Analyst*

Reconstructed in terms of the facilities and whatever there?

Jim Hallett - *KAR Auction Services, Inc. - CEO*

Gary, it was it was almost considered almost a gift from a heaven. This facility was completely fenced, completely paved and actually the steel structures were up for another business and we were able to take the steel that was already erected and just convert it into auction buildings and body shops and reconditioning centers. And very quickly that lease has just gotten signed here in the last few weeks and we're telling you that we're going to be operational come the start of the second quarter. So--

Gary Prestopino - *Barrington Research - Analyst*

That's great news. And then lastly, Eric, in terms of this-- what you're trying to pay down $150 million in debt, I mean why can't you do more if you've got $380 million on the balance sheet and you're generating pretty significant free cash flow, at least by my estimates? Is that just a minimum number or is that just what you're going to do?

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

That is what we're going to do. Given the announcement of Premier and Jim telling you that we're open to other opportunities, we feel that's the right amount of debt to repay right now and keep-- cash is king and we want to keep cash on that balance sheet so that we can move quickly if opportunities arise.

Gary Prestopino - *Barrington Research - Analyst*

Okay, thanks guys.

Jim Hallett - *KAR Auction Services, Inc. - CEO*

Thank you, Gary.

Operator

And Rick Nelson with Stephens Investment Bank will have our next question.

Nathan Mendez - *Stephens Investment Bank - Analyst*

Hi, good morning, guys. This is actually Nathan Mendez in for Rick. I wanted to talk about the revenue per vehicle at ADESA. You saw a nice uptick during the quarter. Can you help us understand how much of that is ancillary revenues versus increased fees on the buyer/seller side? And then more specifically, what trends are you seeing on that-- in that part of the business?

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

Yes, Nathan, we have seen an increase in ancillary revenues and our Q we would expect to file later today will give you a little bit of detail on that. And it's several things but the ancillary services have been down. Most of our fee increase as year to date have been a result of auction fee increases put in place late last year and early this year. And as we start to see these cars needing to be differentiated in the marketplace, we hope to see continued use of ancillary services. In terms of allocating the dollar amounts, we don't really need to give the detail. In the Q, you'll see it tonight. I will give a heads up though. There was about $4.5 million that relates to increases in fees at ADESA. $5.7 million relates to increases in ancillary services. And just over $3 million was the currency exchange. You'll see those numbers tonight.

Jim Hallett - *KAR Auction Services, Inc. - CEO*

And Nathan the other thing that I would add to Eric's comments is that although we don't speak to specific customers, we have grown a large account which is a heavy user of our ancillary services. And I think that has continued to improve as well, Eric.

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

Yes.

Nathan Mendez - *Stephens Investment Bank - Analyst*

And then just kind of taking off on that a little bit, with used in such high demand now, have you started or I mean I guess what are you seeing in terms of the sellers using those ancillaries or less likely to use those ancillary services? I guess if they feel the need, less of a need to dress up the car? Is that something that you're seeing still?

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

I think the dealer wants to get that car turned as quickly as he can. And he may forego some of the light reconditioning. But I don't think we've seen a significant change on the dealer side.

Jim Hallett - *KAR Auction Services, Inc. - CEO*

No, not on the dealer. We do no the institutional side though. As we start to see the OEMs become-- all year they've been talking about their sales activity. To the extent that the OEMs are bringing cars to the auction, they tend to be bigger users of ancillary services. So and again they've been kind of troughed at the bottom and so that's a contributor. You have to look within the mix of institutional vehicles, Nathan, and again I'm optimistic that we'll continue to see this. The other thing is when you're in a highly competitive environment, no matter what the prices are, you're going to tend to want to present that car in the best possible way. So I wouldn't tell you that-- as high prices stay steady for a while, you'll see our sellers focus on is there something I can to differentiate the car so that mine is the one that gets the premium. So we'll see how that turns out.

Nathan Mendez - *Stephens Investment Bank - Analyst*

And then one more question, if I can. On the conversion rate, saw it drop a bit in the third quarter. I think we saw the same thing last quarter. Can you talk about the drivers of that? And you said it's going to continue towards more normalized trends. Can you talk about where you see it normalizing and over what period of time?

Jim Hallett - *KAR Auction Services, Inc. - CEO*

Yes, I think the drop that you've seen is just seasonal. People are starting to think a little bit more about Santa Claus. And I think it's a trend that we see during the fourth quarter. Usually that conversion rate will drop down. And we'll see it ramp right back up come the new year.

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

And Nathan, one thing that many have focused on is last year's conversion rate. Go back to 2008 and in the third quarter historically would have had a high 50-- actually would have been typically below 60%. So we're off of an unusually aggressive conversion rate that was experienced in the third quarter of 2009. We're very happy with 64%. It's very high for the third quarter.

Nathan Mendez - *Stephens Investment Bank - Analyst*

Thanks for that and good luck with the quarter.

Jim Hallett - *KAR Auction Services, Inc. - CEO*

Great. Thank you.

Operator

And we'll move on Scot Ciccarelli with RBC Capital Markets.

Scot Ciccarelli - *RBC Capital Markets - Analyst*

Hey guys, Scot Ciccarelli.

Jim Hallett - *KAR Auction Services, Inc. - CEO*

Good morning.

Scot Ciccarelli - *RBC Capital Markets - Analyst*

I guess the first question is when we look at the ADESA volume, what percent of your units are off lease at this point? And what percent is dealer consignment?

Jim Hallett - *KAR Auction Services, Inc. - CEO*

We told you we're just over 35% dealer consignment. And Scott we've never disclosed off lease as a specific component. But the 65% of institutional volume, off lease is one of the major contributors to those volumes as well as repos, factory, and the fleet, the de-fleeting that that the private fleets do.

Scot Ciccarelli - *RBC Capital Markets - Analyst*

If we are thinking in just kind of very rough terms, is it half of the institutional volume?

Jim Hallett - *KAR Auction Services, Inc. - CEO*

We can't give away all of our competitive intelligence. So really don't want to go there. We just want to say, Scot, that 65% of our business is commercial business and a significant portion of that is the lease business. I think-- other than that I don't think we want to go further than that at this point.

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

And Scot, there is some industry data out there for the whole industry that's updated annually. There's some 2009 data, I don't have it in front of me so I don't want to try to remember it. But there is some data on that for the industry.

Scot Ciccarelli - *RBC Capital Markets - Analyst*

Okay. And can you guys estimate the impact from-- I know you don't like to talk about specific customers, but the unit volume was down a little bit in the salvage segment this quarter, can you kind of give us a bracket in terms of what the loss of Allstate? Everyone kind of knows you lost that business. It's been coming off pretty quickly. How much did that impact the numbers during the quarter?

Jim Hallett - *KAR Auction Services, Inc. - CEO*

Well, again, we'll try and give you some color. We're not going to speak specifically to that one account. There's no question it had an impact, but we did sell Allstate vehicles through the third quarter and we'll continue to see Allstate vehicles probably through the end of the year. And it'll probably take till the first quarter of January for all those vehicles to clear. But we-- that volume loss, you have some customers that are just down as a result of total claims. And on the other hand, you have some customers that are up with us. So, it's kind of just the mix of any-- it's kind of a mix but did it impact us? Yes it did impact us. To what degree? I'm not sure if I could quantify that. Eric?

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

Right. Scot, and there's seasonal impact. As we look across, Scot, all the insurance providers, there's a number of them where there's no call it change in contractual relationship that had declines as a result of just fewer claims. So that was an impact during the quarter.

Scot Ciccarelli - *RBC Capital Markets - Analyst*

Okay, and then the last question is on the AFC side, obviously you guys have seen a pretty big acceleration there. How are you thinking about the business going forward in terms of kind of providing financing? Does your appetite continue to increase? What's the right way to think about that business at this stage?

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

Well, Scot, it's interesting. Here we are talking about declining wholesale used car volumes at auction with a growing portfolio that's growing based upon basically additional loan transaction. And I think that reflects that back in 2008 and 2009, AFC took their medicine. Did a really nice job of getting the portfolio aligned but created capacity. So we're optimistic. I mean there's some seasonality, the fourth quarter. The third quarter historically in the finance business is when some people put some inventory on. And the portfolio growth occurs. In the fourth quarter, you probably see more steady state. I don't think we continue this level of growth. But having capacity, having such high credit quality, there's still room for AFC to grow. So we're optimistic as we have a long-term view of that business.

Scot Ciccarelli - *RBC Capital Markets - Analyst*

Got it. Thanks a lot, guys.

Jim Hallett - *KAR Auction Services, Inc. - CEO*

You're very welcome.

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

Thanks, Scot.

Operator

And we'll move on to Ryan Brinkman with Goldman Sachs.

Ryan Brinkman - *Goldman Sachs - Analyst*

Could you help us in terms of thinking about the relative possibility of the new specialty auctions versus traditional whole car auctions? I think in the past year or maybe others have spoken about how RV sales, for example, could be somewhat less attractive, given that the vehicles take up more space at your whole car sites? And do the economics change given that these are dedicated specialty sites?

Jim Hallett - *KAR Auction Services, Inc. - CEO*

Well, there's no question they do take up more space, especially when you're dealing with larger boats and RVs and things of that nature. But on the other hand, I would also say to you that there is opportunity for increased revenues on those vehicles as well. So, we're happy to have them and we'll figure out a way to park them.

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

And Ryan, one of the advantages to the specialty business that Jim alluded to is until the Premier acquisition, we've been able to run these specialty sales on our car sites. And maybe we couldn't have done that at the end of 2008, even though wholesale auction volumes were down, inventory was way up. And we were out of parking space. But right now, we're able to accommodate both the specialty business and the used car business. And incrementally not incurring additional land cost to accommodate that business.

Ryan Brinkman - *Goldman Sachs - Analyst*

Okay, great, that makes a lot sense. You've noted about-- you've noted the positive volume performance at ADESA versus the industry and that's fairly impressive. I was hoping you could talk a little bit about the competitive dynamics on the salvage side where industry data for whatever reason, it seems somewhat harder to come by. And given your confidence in the hybrid selling model you've released several press releases about that and talked about on your calls. And then with your overseas buyer initiatives that you talked about today, have you started to see any market share gains at IAA like at whole car or if not, do you think it would be reasonable to assume that you could realize some in the future?

Jim Hallett - *KAR Auction Services, Inc. - CEO*

I would say first off, you're right. We don't have a resource that is able to provide us with market data like on the whole car side at the National Auto Auction Association. But other than that--

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

And Ryan at the same time, we have felt very good about our place in the competitive marketplace. But during the IPO, we told you there's not a lot of opportunity for increasing market share unless we can find new sources of vehicles at the salvage auction.

The insurance companies kind of balance things out over time. And it's not necessarily a market share gain. We got winds and we've got movements around the insurance business and we're comfortable with that. What we're really focused on is the non-insurance vehicles is the chance to really increase the size of the market and perhaps gain share in that manner.

Ryan Brinkman - *Goldman Sachs - Analyst*

I see. Thanks a lot.

Jim Hallett - *KAR Auction Services, Inc. - CEO*

You're welcome.

Operator

And we'll move on to Justin Boisseau from Gates Capital Management.

Jeff Gates - *Gates Capital Management - Analyst*

Yes, it's actually Jeff Gates. I have a couple questions. First of all, on the accounts receivable from AFC, what-- just remind me what your current capacity is for collateralization and kind of how you're thinking of the size of that portfolio in today's market, where you're ultimately going with that, number one? Number two, I'm just wondering what the capital costs are for Las Vegas? And three, can you talk about the acquisition landscape and what the pipeline might look like and the valuations that you're seeing out there in the marketplace?

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

Okay, Jeff, let me handle the first two and then I think Jim will give you some flavor on the third one. We have a $450 million securitization in the US and $75 million in Canada. That's the current capacity. And those facilities extend through April of 2012. And we're very comfortable in the near term with the growth that we can accommodate what we're seeing in the business. And we have a great relationship with our lenders and we have a great performance in the portfolio right now. So we're comfortable as we get closer to that, the maturity or the expiration date that we'll be able to right size this based on how the business looks at that time. So we're very comfortable with the capacity. And we still have additional capacity within the existing facilities for growth in the near term.

Jeff Gates - *Gates Capital Management - Analyst*

Plus the $700 million portfolio, where do you see that going over the next year or two?

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

Again, it's hard to predict where it will go, but we see the opportunity for it to grow is all I'll say, Jeff. And again, that number again, it's at a peak probably in October. There's some seasonality to it. But we think the general trend will be to grow. And part of that is actually we're-- there's not as much competition as there was during the boom of 2005, '06, and '07 where local banks and others were getting into this business. I mean there's a limited supply of capital to the independent used car dealers and that's our primary focus. So there is growth opportunity but there's no number I'm going to be able to give you today. It just should be steady growth. And we do actually look at disciplined growth as the theme there.

In terms of the Las Vegas site, again, Jim gave you some flavor as to the condition of the site. So the capital costs are less than we've incurred in previous new sites. But again, it's something we can handle within the $75 million guidance we've given you this year. And as we look forward, it's not going to have a material impact increase in our long-term spend in CapEx next year from our perspective. So, we can handle it within the current parameters that we've given the public.

Jim Hallett - *KAR Auction Services, Inc. - CEO*

And also, Eric I would just add that for the record that the current land values in Vegas were very attractive for us being able to enter that market. I think we're able to enter that market surprisingly less than what it would have been just a year or two ago.

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

And Jeff, there might be some confusion. We're using a lease. We are not acquiring the land outright. So our cost is really just the improvements.

Jim Hallett - *KAR Auction Services, Inc. - CEO*

And Jeff, in terms of additional acquisition opportunities, there are numerous opportunities that are available. The sellers know who we are and we certainly know who they are. We have continuous ongoing conversations. And I think that we may have even opened up some more opportunities based on our strategy to take on some of these smaller markets. So, I would say that we will continue to look for those opportunities and as they make sense from a strategic standpoint and from a geographic standpoint, we will continue to act upon.

Operator

And our final question will come from Craig Kennison with Robert W. Baird.

Craig Kennison - *Robert W. Baird - Analyst*

Thanks for taking my questions. Most have been answered but wanted to follow up on the salvage market where you did have a competitor take a large client. Did you see that lead to any discounting or any other clients looking for a national contract? Or is that looking more like a one-off?

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

Craig that continues. That whole situation we have not seen the industry move in that direction. So with that said though, you do know over the past five years, we've seen a lot of pressure to move the fees from the seller to the buyer. We're not seeing any big moves on that any longer. So I don't see it as significant discounting from the seller perspective right now. At the same time, you've got to be competitive. You've got to control your costs. And that's where we focus our attention in the business. So, we're not seeing significant pressure on the pricing side. And we all know that if that starts to occur, everybody loses in the industry. I mean, again, we've got a market we're serving there.

Jim Hallett - *KAR Auction Services, Inc. - CEO*

And the other thing, Craig, I'd mention is more so in the salvage business, even compared to the whole car business, I think the insurance companies really look for balance and market share and it's what Eric spoke to earlier. There really isn't that much movement in market share. And the insurance companies like to keep the balance where is on the whole car side you could see more dramatic swings than just in terms of percentage of market share.

Craig Kennison - *Robert W. Baird - Analyst*

And then finally you mentioned your long-term plans to grow earnings per share approximately 15% to 20%. Fortunately, you're in a very steady business with predictable revenue streams, but certainly the top line isn't growing that fast. Where do you see that opportunity in the income statement driving that kind of EPS performance? Thanks.

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

Well, you're absolutely right, Craig. In our model, there's not one lever we're focused on, not top line but for example, taking gross profit up a 140 bps in this environment is what supports it. The ability to generate such strong cash to repay debt and reduce our interest expense is a contributor. And then once again, you look at the SG&A, ignore the anomaly of last year's stock-based comp versus this year's, we're able to control that SG&A such that even though it's only a 4% increase year over year in revenue, we get a lot of that through to our profitability and operating income and ultimately earnings per share. So, again, it's kind of an interesting business where we-- I'll go back to our theme. We have a complementary model. And despite the fact you see pressure on the top line in our largest segment, which is ADESA, we see the performance on the other parts of our business. And at the same time, able to really control costs, really drive a higher gross profit. And so I think, again, we look at all the levers. And they're available to us and Jim's comments are appropriate. We're not dependent on one single component of our income statement to generate that growth.

Craig Kennison - *Robert W. Baird - Analyst*

Thank you.

Jim Hallett - *KAR Auction Services, Inc. - CEO*

Thank you.

Operator

And that will conclude the question and answer session. I will turn the call back over to Mr. Loughmiller for any additional or closing remarks.

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

Thank you, Rachelle, and we thank everyone for attending today and appreciate your support.

Operator

And that will conclude today's call. We thank you for your participation.
