KAR Holdings, Inc.
Form SP 15D2
March 27, 2008
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

SPECIAL FINANCIAL REPORT PURSUANT TO RULE 15d-2

OF THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED

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

For the fiscal year ended December 31, 2007

OR

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

Commission File Number: 333-148847

KAR Holdings, Inc.

(Exact name of Registrant as specified in its charter)

Delaware	**20-8744739**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

13085 Hamilton Crossing Boulevard

Carmel, Indiana 46032

(Address of principal executive offices, including zip code)

Registrant s telephone number, including area code: (800) 923-3725

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered pursuant to Section 12(g) of the Act: None

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

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company (as defined in Rule 12b-2 of the Exchange Act).

Large accelerated filer ¨ Accelerated filer ¨ Non-accelerated filer x Smaller reporting company ¨

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

As of June 30, 2007, there was no public trading market for the registrant s common stock and no shares of the registrant s common stock were held by non-affiliates of the registrant.

As of February 29, 2008, 10,686,316 shares of the registrant s common stock, par value $0.01 per share were outstanding.

Table of Contents

KAR Holdings, Inc.

Table of Contents

Special Financial Report Pursuant to Exchange Act Rule 15d-2

For the Fiscal Year Ended December 31, 2007

Table of Contents

EXPLANATORY NOTE

KAR Holdings, Inc. (KAR Holdings) was organized in the State of Delaware on November 9, 2006. The Company is a holding company organized for the purpose of consummating a merger with ADESA, Inc. and combining Insurance Auto Auctions, Inc. with ADESA. KAR Holdings had no operations prior to the merger transactions on April 20, 2007. A detailed description of the merger transactions is included in the Registration Statement on Form S-4 (Registration No. 333-148847) as well as in the financial statements included in this special financial report. A detailed description of KAR Holdings businesses is also included in the Registration Statement on Form S-4. KAR Holdings Registration Statement on Form S-4 was declared effective by the Securities and Exchange Commission (the SEC) on February 14, 2008.

Rule 15d-2 under the Securities Exchange Act of 1934, as amended, provides generally that if a company files a registration statement under the Securities Act of 1933, as amended, which does not contain certified financial statements for the company s last full fiscal year (or the life of the company if less than a full fiscal year), then the company must, within 90 days after the effective date of the registration statement, file a special report furnishing certified financial statements for the last full fiscal year or other period, as the case may be. Rule 15d-2 further provides that the special financial report is to be filed under cover of the facing sheet of the form appropriate for annual reports of the company.

KAR Holdings Registration Statement on Form S-4 did not contain the certified financial statements for the year ended December 31, 2007, the first fiscal year-end of KAR Holdings after the consummation of the merger transactions. Therefore, as required by Rule 15d-2, KAR Holdings is hereby filing such certified financial statements with the SEC under cover of the facing page of an Annual Report on Form 10-K.

CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this Special Financial Report pursuant to Rule 15d-2, the Company carried out an evaluation under the supervision and with the participation of the Company s management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company s disclosure controls and procedures. Based upon that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that the Company s disclosure controls and procedures were effective.

Changes in Internal Control over Financial Reporting

There has been no change in the Company s internal control over financial reporting during the quarter ended December 31, 2007, that has materially affected, or is reasonably likely to materially affect, the Company s internal control over financial reporting.

Table of Contents

MANAGEMENT S DISCUSSION AND ANALYSIS

OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward-Looking Statements

This report contains forward-looking statements which are subject to certain risks, trends and uncertainties. In particular, statements made in this report that are not historical facts (including, but not limited to, expectations, estimates, assumptions and projections regarding the industry, business, future operating results, potential acquisitions and anticipated cash requirements) may be forward-looking statements. Words such as anticipates, expects, intends, plans, believes, seeks, estimates, and similar expressions identify forward-looking statements. Such stater including statements regarding the Company s future growth; anticipated cost savings, revenue increases and capital expenditures; strategic initiatives such as selective relocations, greenfields and acquisitions; the Company s competitive position; and its continued investment in information technology are not guarantees of future performance and are subject to risks and uncertainties that could cause actual results to differ materially from the results projected, expressed or implied by these forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to:

- fluctuations in consumer demand for and in the supply of used, leased and salvage vehicles and the resulting impact on auction sales volumes and conversion rates;
- trends in new and used vehicle sales and incentives, including wholesale used vehicle pricing;
- economic conditions including fuel prices and Canadian exchange rate and interest rate fluctuations;
- trends in the vehicle remarketing industry;
- changes in the volume of vehicle production, including capacity reductions at the major original equipment manufacturers;
- the introduction of new competitors;
- laws, regulations and industry standards, including changes in regulations governing the sale of used vehicles, the processing of salvage vehicles and commercial lending activities;
- changes in the market value of vehicles auctioned, including changes in the actual cash value of salvage vehicles;
- competitive pricing pressures;
- costs associated with the acquisition of businesses or technologies;
- litigation developments;

- patent or other intellectual property infringement claims, which could have an impact on the business or operating results due to a disruption in business operations, the incurrence of significant costs and other factors;
- the Company s ability to successfully implement its business strategies or realize expected cost savings and revenue enhancements;
- the Company s ability to develop and implement information systems responsive to customer needs;
- business development activities, including acquisitions and integration of acquired businesses;
- weather;
- general business conditions; and
- other risks described from time to time.

Many of these risk factors are outside of the Company s control, and as such, they involve risks which are not currently known that could cause actual results to differ materially from those discussed or implied herein. The forward-looking statements in this document are made as of the date on which they are made and the Company does not undertake to update its forward-looking statements.

Table of Contents

The Company s future growth depends on a variety of factors, including its ability to increase vehicle sold volumes and loan transaction volumes, acquire additional auctions, manage expansion, relocation and integration of acquisitions, control costs in its operations, introduce fee increases, expand its product and service offerings, including information systems development, and retain its executive officers and key employees. Certain initiatives that management considers important to the Company s long-term success include substantial capital investment in e-business, information technology, facility relocations and expansions, as well as operating initiatives designed to enhance overall efficiencies, have significant risks associated with their execution, and could take several years to yield any direct monetary benefits. Accordingly, the Company cannot predict whether its growth strategy will be successful. In addition, the Company cannot predict what portion of overall sales will be conducted through online auctions or other redistribution methods in the future and what impact this may have on its auction business.

Merger Transactions

On December 22, 2006, KAR Holdings II, LLC (KAR LLC) entered into a definitive merger agreement to acquire ADESA, Inc. (together with its subsidiaries, ADESA). The merger occurred on April 20, 2007 and as part of the agreement, Insurance Auto Auctions, Inc., a leading provider of automotive salvage auction and claims processing services in the United States, was contributed to KAR LLC. Both ADESA and Insurance Auto Auctions, Inc. (together with its subsidiaries, IAAI) became wholly owned subsidiaries of KAR Holdings, Inc. (KAR Holdings) which is owned by KAR LLC. KAR Holdings is the accounting acquirer, and the assets and liabilities of both ADESA and IAAI were recorded at fair value.

The following transactions occurred in connection with the merger:

- Approximately 90.8 million shares of ADESA s outstanding common stock converted into the right to receive $27.85 per share in cash;

- Approximately 3.4 million outstanding options to purchase shares of ADESA s common stock were cancelled in exchange for payments in cash of $27.85 per underlying share, less the applicable option exercise price, resulting in net proceeds to holders of $18.6 million;

- Approximately 0.3 million outstanding restricted stock and restricted stock units of ADESA vested immediately and were paid out in cash of $27.85 per unit;

- Affiliates of Kelso Investment Associates VII, L.P., GS Capital Partners VI, L.P., ValueAct Capital Master Fund, L.P. and Parthenon Investors II, L.P. (the Equity Sponsors) and management contributed to KAR Holdings approximately $1.1 billion in equity, consisting of approximately $790.0 million in cash and ADESA, Inc. stock (ADESA, Inc. stock contributed by one of the Equity Sponsors had a fair value of $65.4 million and was recorded at its carryover basis of $32.1 million) and approximately $272.4 million of equity interest in IAAI;

- KAR Holdings entered into new senior secured credit facilities, comprised of a $1,565.0 million term loan facility and a $300.0 million revolving credit facility. Existing and certain future domestic subsidiaries, subject to certain exceptions, guarantee such credit facilities;

- KAR Holdings issued $150.0 million Floating Rate Senior Notes due May 1, 2014, $450.0 million 8 $^{3}/4$% Senior Notes due May 1, 2014 and $425.0 million 10% Senior Subordinated Notes due May 1, 2015.

Use of Proceeds

The net proceeds from the equity sponsors and financings were used to: (a) fund the cash consideration payable to ADESA stockholders, ADESA option holders and ADESA restricted stock and restricted stock unit holders under the merger agreements; (b) repay the outstanding principal and accrued interest under ADESA s existing credit facility and notes as of the closing of the merger; (c) repay the outstanding principal and accrued interest under IAAI s existing credit facility and notes as of the closing of the merger; (d) pay related transaction fees and expenses;

and (e) contribute IAAI s equity at fair value.

Table of Contents

Significant Items Affecting Comparability

The merger transactions resulted in a new basis of accounting under Statement of Financial Accounting Standards (SFAS) No. 141, *Business Combinations*. This change creates many differences between reporting for KAR Holdings post merger, as successor, and ADESA and IAAI independently pre-merger. The ADESA and IAAI financial data for periods ending on or prior to April 19, 2007, generally will not be comparable to the successor financial data for periods after that date. The merger resulted in KAR Holdings having an entirely new capital structure, which results in significant differences between ADESA and IAAI pre-merger and KAR Holdings post-merger in the stockholders equity sections of the financial statements. In addition, the successor incurred debt issuance costs and $2,590 million of debt in connection with the merger. The $662.6 million of debt related to ADESA s and IAAI s credit facilities and notes was paid off in connection with the merger and contribution ($318.0 million for ADESA and $344.6 million for IAAI). As a result, interest expense, debt and debt issuance costs are not comparable between the pre-merger and the post-merger companies. Certain adjustments have been made to increase or decrease the carrying amount of assets and liabilities as a result of preliminary estimates and certain reasonable assumptions, which, in certain instances, has resulted in changes to amortization and depreciation expense amounts. The final valuations are not yet complete; as such, the allocation of purchase price has not been completed and further adjustments to the preliminary allocations may be made in subsequent periods.

Executive Overview

Business

KAR Holdings is the only auction services provider in North America with leading market positions in both the whole car auction and salvage auction markets. The business is divided into three reportable business segments that are integral parts of the vehicle redistribution industry: ADESA Auctions, Insurance Auto Auctions, Inc. (IAAI) and Automotive Finance Corporation (AFC). The ADESA Auctions segment consists primarily of ADESA s used vehicle auctions and is the second largest used vehicle auction network in North America with 59 ADESA sites. ADESA Auctions also provide services such as inbound and outbound logistics, reconditioning, vehicle inspection and certification, titling and administrative services.

The IAAI segment consists of salvage vehicle auctions and related services in North America and is the second largest provider with 145 sites. The salvage auctions facilitate the redistribution of damaged vehicles that are designated as total losses by insurance companies, recovered stolen vehicles for which an insurance settlement with the vehicle owner has already been made and older model vehicles donated to charity or sold by dealers in salvage auctions. The salvage auction business specializes in providing services such as inbound and outbound logistics, inspections, evaluations, titling and settlement administrative services.

The AFC segment is primarily engaged in the business of providing short-term, inventory-secured financing, known as floorplan financing, to independent used vehicle dealers. AFC conducts business at 91 loan production offices in the U.S. and Canada.

The holding company is maintained separately from the three reportable segments and includes expenses associated with the corporate office, such as salaries, benefits, and travel costs for the corporate management team, certain human resources, information technology and accounting costs, and incremental insurance, treasury, legal and risk management costs. Holding company interest includes the interest incurred on the corporate debt structure. Costs incurred at the holding company are not allocated to the three business segments.

The Company believes it is well positioned in both the used vehicle auction and salvage auction industries which have demonstrated long-term stability. The Company is one of the top three players in most markets in which it operates in an industry with high barriers (facilities, technology and expertise) to entry. ADESA and IAAI are able to serve the diverse and multi-faceted needs of customers through the wide range of services offered at their facilities. The Company s business model consistently generates substantial operating cash flow, which can be used to fund growth initiatives with minimal inventory risk.

Table of Contents

Industry Outlook and Trends

The decline in retail used vehicle sales experienced in 2006 persisted throughout 2007 as well. Retail used vehicle sales were down approximately 3% for the year ended December 31, 2007 as compared with the same period in 2006. This decline has continued to impact demand and used vehicle auction volumes. The Company believes that the weak retail used vehicle market is the result of several factors including used cars being priced high relative to new discounted vehicles, slow economic growth, negative equity on longer term used vehicle loans and vehicle longevity. In addition, new vehicle sales also experienced a decline of approximately 2.5% for the year ended December 31, 2007 compared with the year ended December 31, 2006. A decline in new vehicle sales generally results in a reduction in trade-in volumes and auction volumes. Capacity reductions at the major U.S. OEMs are expected to impact the industry and may result in reduced program vehicles and rental fleet sales. While off-lease vehicles declined in 2006, lease penetration rates have been modestly increasing since 2004 and the Company estimates that industry off-lease auction volumes increased in 2007 and expects industry off-lease auction volumes to continue to increase in 2008.

Wholesale used vehicle prices were up in December 2007 and averaged $9,739 as compared with $9,686 in December 2006, according to ADESA Analytical Services monthly analysis of Wholesale Used Vehicle Prices by Vehicle Model Class.

Salvage vehicle supplies were fairly strong throughout the industry in 2007. The Company believes increased complexity in vehicles contributed to a larger number of insurance claims resulting in a total loss. The percentage of claims resulting in total losses continues at an all-time-high level. In addition, flooding in several markets throughout 2007 has added incremental units.

Seasonality

The volume of vehicles sold at the Company s auctions generally fluctuates from quarter to quarter. This seasonality is affected by several factors including weather, the timing of used vehicles available for sale from selling customers, the availability and quality of salvage vehicles, holidays, and the seasonality of the retail market for used vehicles, which affect the demand side of the auction industry. Used vehicle auction volumes tend to decline during prolonged periods of winter weather conditions. In addition, mild weather conditions and decreases in traffic volume can each lead to a decline in the available supply of salvage vehicles because fewer traffic accidents occur, resulting in fewer damaged vehicles overall. As a result, revenues and operating expenses related to volume will fluctuate accordingly on a quarterly basis. The fourth calendar quarter typically experiences lower used vehicle auction volume as well as additional costs associated with the holidays and winter weather.

Results of Operations

The Company s revenue is derived from auction fees and related services at its whole car and salvage auction facilities and dealer financing fees and net interest income at AFC. Although auction revenues primarily include the auction services and related fees, the Company s related receivables and payables include the value of the vehicles sold. AFC s net revenue consists primarily of securitization income and interest and fee income less provisions for credit losses. Securitization income is primarily comprised of the gain on sale of finance receivables sold, but also includes servicing income, discount accretion, and any change in the fair value of the retained interest in finance receivables sold. Operating expenses for the Company consist of cost of services, selling, general and administrative expenses and depreciation and amortization. Cost of services is composed of payroll and related costs, subcontract services, supplies, insurance, property taxes, utilities, maintenance and lease expense related to the auction sites and loan offices. Cost of services excludes depreciation and amortization. Selling, general and administrative expenses are composed of indirect payroll and related costs, sales and marketing, information technology services and professional fees.

Table of Contents

Prior to April 19, 2007, ADESA, Inc. s operations were grouped into three operating segments: used vehicle auctions, Impact salvage auctions and AFC. These three operating segments were aggregated into two reportable business segments: Auction Services Group (used vehicle auctions and Impact salvage auctions) and Dealer Services Group (AFC and related businesses). Prior to April 19, 2007, IAAI operated in a single business segment. Concurrent with the merger transaction, KAR Holdings established three reportable business segments: ADESA Auctions, IAAI and AFC. ADESA s Impact salvage auctions operating segment was combined with IAAI. For comparative purposes, ADESA Impact s results of operations are included in the IAAI segment for all periods presented below. These reportable segments offer different services, have distinct suppliers and buyers of vehicles and are managed separately based on the fundamental differences in their operations.

Operating Results Summary for the Year Ended December 31, 2007

The following unaudited pro forma condensed results of operations for the year ended December 31, 2007 are based on ADESA and IAAI s financial statements for the periods from January 1, 2007 to April 19, 2007 and KAR Holding s financial statements for the period from January 1, 2007 to December 31, 2007, appearing elsewhere in this special financial report, as adjusted to combine the financial statements of ADESA Impact and IAAI on a historical basis and to illustrate the estimated pro forma effects of the merger transactions as if they had occurred on January 1, 2006. KAR Holdings had no operations during the period of January 1, 2007 to April 19, 2007.

The merger transactions described in Merger Transactions, were completed on April 20, 2007. Pro forma adjustments have been made to the historical combined statements of income for the years ended December 31, 2007 and 2006 as if the merger transactions had been completed on January 1, 2006.

The unaudited pro forma adjustments are based upon available information and certain assumptions that the Company believes are reasonable under the circumstances. The unaudited pro forma condensed results are presented for informational purposes only. The unaudited pro forma condensed results do not purport to represent what KAR Holdings results of operations would have been had the merger transactions actually occurred on the dates indicated and they do not purport to project KAR Holdings results of operations for any future period.

The unaudited pro forma condensed combined results of operations should be read in conjunction with the information contained in the financial statements and related notes thereto, appearing elsewhere in this special financial report. The pro forma adjustments inherent in the segments results presented below include: pro forma interest expense resulting from the new capital structure; pro forma depreciation and amortization expense resulting from the new basis of property and equipment and intangible assets; adjustments to selling, general and administrative expenses for the annual sponsor advisory fees; and adjustment to write up the finance receivables acquired to fair value. In addition, certain human resources and information technology costs that ADESA had historically allocated to its segments and certain professional fees historically recorded at the segments were reclassified to the holding company for all periods presented. Transaction expenses, representing legal and professional fees as well as accelerated incentive compensation costs, were also removed from 2007 operating results.

Table of Contents

Overview of Pro Forma Results of KAR Holdings for the Years Ended December 31, 2007 and 2006

	Pro Forma Year Ended December 31,	
(In millions)	2007	2006
Revenues		
ADESA Auction Services	**$ 965.5**	$ 853.8
IAAI Salvage Services	**482.5**	438.1
AFC	**143.0**	141.8
Total revenues	**1,591.0**	1,433.7
Cost of services*	**891.2**	799.6
Gross profit*	**699.8**	634.1
Selling, general and administrative	**348.2**	305.1
Depreciation and amortization	**181.2**	181.2
Loss related to flood		3.5
Operating profit	**170.4**	144.3
Interest expense	**232.4**	232.4
Other (income) expense	**(9.7)**	(4.2)
Income (loss) from continuing operations before income taxes	**(52.3)**	(83.9)
Income taxes	**(4.7)**	(16.1)
Income (loss) from continuing operations	**($47.6)**	($67.8)

* Exclusive of depreciation and amortization

For the year ended December 31, 2007, the Company had pro forma revenue of $1,591.0 million compared with pro forma revenue of $1,433.7 million for the year ended December 31, 2006, an increase of 11%. Included in the pro forma results for the year ended December 31, 2006, was a $2.7 million pretax charge related to the correction of certain unreconciled balance sheet differences concealed by a former employee at ADESA s Kitchener, Ontario, auction facility. In addition, the results for the year ended December 31, 2006 included a $3.5 million loss related to the flood at IAAI s Grand Prairie, Texas facility. The flood loss consisted of a loss of vehicles and fixed assets as well as costs to clean up the facility.

Pro Forma ADESA Auctions Results

	Pro Forma Year Ended December 31,	
(In millions)	2007	2006
ADESA Auction Services revenue	**$ 965.5**	$ 853.8
Cost of services*	**541.5**	468.6
Gross profit*	**424.0**	385.2
Selling, general and administrative	**200.5**	179.9
Depreciation and amortization	**92.5**	92.5

Operating profit	**$ 131.0**	$ 112.8

* Exclusive of depreciation and amortization

7

Table of Contents

Revenue

Revenue from ADESA Auctions increased $111.7 million, or 13%, to $965.5 million for the year ended December 31, 2007, compared with $853.8 million for the year ended December 31, 2006. The 13% increase in revenue was a result of an 8% increase in revenue per vehicle sold for the year ended December 31, 2007 compared with the year ended December 31, 2006, and a 5% increase in the number of vehicles sold.

An 8% increase in revenue per vehicle sold resulted in increased auctions revenue of approximately $71.5 million. The increase in revenue per vehicle sold was primarily attributable to an increase in ancillary services such as transportation and other services. These factors resulted in increased ADESA Auctions revenue of approximately $37.8 million. The higher transportation and other ancillary services revenues also resulted in corresponding increases in cost of services. Incremental fee income related to selective fee increases and higher wholesale used vehicle values resulted in increased ADESA Auctions revenue of approximately $20.8 million. Fluctuations in the Canadian exchange rate increased revenue by approximately $12.9 million for the year ended December 31, 2007 compared with the year ended December 31, 2006.

While the number of retail used vehicles sold in North America decreased, the total number of wholesale vehicles sold at ADESA Auctions increased 5% in the year ended December 31, 2007 compared with year ended December 31, 2006, resulting in an increase in ADESA Auctions revenue of approximately $40.2 million.

The used vehicle conversion percentage, calculated as the number of vehicles sold as a percentage of the number of vehicles entered for sale at the Company s used vehicle auctions, was 60.0% for the year ended December 31, 2007 compared with 60.4% for the year ended December 31, 2006.

Gross Profit

For the year ended December 31, 2007, gross profit in the ADESA Auctions segment increased $38.8 million, or 10%, to $424.0 million. The 13% increase in revenues was the leading factor increasing gross profit for the ADESA Auctions segment, despite an increase in cost of services on both a dollar and percentage of revenues basis. Increases in transportation costs (which includes fuel costs) and other ancillary services costs was a leading driver of the $35.3 million increase in cost of services for the ADESA Auctions segment. Cost of services also increased due to the costs associated with handling additional used vehicles entered for sale at the Company s used vehicle auctions for the year ended December 31, 2007 compared with the year ended December 31, 2006. Fluctuations in the Canadian exchange rate increased cost of services at the ADESA Auctions segment by approximately $7.4 million.

Selling, General and Administrative

Selling, general and administrative expenses for the ADESA Auctions segment increased $20.6 million, or 11%, to $200.5 million for the year ended December 31, 2007 compared with the prior year, primarily due to increases in compensation and related employee benefit costs, consulting and travel costs related to process improvement initiatives, marketing costs and costs at acquired sites. These increases were partially offset by a $2.7 million pretax charge in 2006 related to unreconciled balance sheet differences concealed by a former employee at ADESA s Kitchener, Ontario, auction facility.

Table of Contents

Pro Forma Insurance Auto Auctions, Inc. (IAAI   ) Results

(In millions)	Pro Forma Year Ended December 31, 2007	2006
IAAI Salvage Services revenue	**$ 482.5**	$ 438.1
Cost of services*	**317.9**	302.6
Gross profit*	**164.6**	135.5
Selling, general and administrative	**67.4**	53.6
Depreciation and amortization	**57.3**	57.3
Loss related to flood		3.5
Operating profit	**$ 39.9**	$ 21.1

* Exclusive of depreciation and amortization

Revenue

Revenue from IAAI increased $44.4 million, or 10%, to $482.5 million for the year ended December 31, 2007, compared with $438.1 million for the year ended December 31, 2006. The increase in revenue was a result of an 18% increase in salvage vehicles sold during the year ended December 31, 2007. The increase in salvage vehicles sold was primarily a result of volumes provided by acquisitions and greenfields in addition to growth in vehicles sold on a same-store basis. The increase in revenue was partially offset by reduced proceeds from units sold under purchase agreements with customers. For purchase agreement vehicles, the gross sales price of the vehicle is recognized as revenue. Vehicles sold under purchase agreements represented less than 4% of total vehicles sold.

Gross Profit

For the year ended December 31, 2007, gross profit at IAAI increased to $164.6 million, or 34% of revenue, compared with $135.5 million, or 31% of revenue, for the year ended December 31, 2006. Cost of services increased 5% due to increases related to acquisitions and greenfields, as well as costs associated with the increased volumes; however, cost of services increased at a lower rate than revenues. IAAI has negotiated a number of tow contracts in the current year resulting in lower tow costs per vehicle towed. In addition, the Company has reduced its auction yard costs due to the elimination of costs associated with Hurricane Katrina related vehicles.

Selling, General and Administrative

Selling, general and administrative expenses at IAAI increased $13.8 million, or 26%, to $67.4 million for the year ended December 31, 2007, compared with $53.6 million for the year ended December 31, 2006. The increase in selling, general and administrative expenses was primarily attributable to integration costs associated with the integration of ADESA Impact into IAAI and an increase in stock compensation expense. The integration costs represent travel, consulting costs, outside labor and retention agreements.

Table of Contents

Pro Forma Automotive Finance Corporation (AFC) Results

(In millions except volumes and per loan amounts)	Pro Forma Year Ended December 31, 2007	2006
AFC revenue		
Securitization income	**$ 74.1**	$ 74.2
Interest and fee income	**67.1**	67.0
Other revenue	**2.4**	0.8
Provision for credit losses	**(0.6)**	(0.2)
Total AFC revenue	**143.0**	141.8
Cost of services*	**31.8**	28.4
Gross profit*	**111.2**	113.4
Selling, general and administrative	**16.2**	16.5
Depreciation and amortization	**25.4**	25.4
Operating profit	**$ 69.6**	$ 71.5
Loan transactions	**1,205,865**	1,151,702
Revenue per loan transaction	**$ 119**	$ 123

* Exclusive of depreciation and amortization

Revenue

For the year ended December 31, 2007, AFC pro forma revenue increased $1.2 million, or 1%, to $143.0 million, compared with $141.8 million for the year ended December 31, 2006. A 5% increase in the number of loan transactions was offset by a 3% decrease in revenue per loan transaction for the year ended December 31, 2007, compared with the same period in 2006. The increase in loan transactions to 1,205,865 for the year ended December 31, 2007 was primarily the result of an increase in floorplan utilization by AFC s existing dealer base.

Revenue per loan transaction, which includes both loans paid off and loans curtailed, decreased $4, or 3%, primarily as a result of decreases in net interest rate spread and an increase in the provision for credit losses for both loans held and sold partially offset by increases in the average portfolio duration and the average values of vehicles floored.

Gross Profit

For the year ended December 31, 2007, gross profit for the AFC segment decreased $2.2 million, or 2%, to $111.2 million as a result of the 12% increase in cost of services partially offset by the $1.2 million increase in revenue. Cost of services increased as a result of increased professional fees, compensation and related employee benefit cost increases, increased expenses associated with lot checks and processing additional loan transactions.

Selling, General and Administrative Expenses

Selling, general and administrative expenses at AFC decreased $0.3 million, or 2%, for the year ended December 31, 2007 compared with the year ended December 31, 2006. The decrease is primarily the result of decreases in compensation costs.

Table of Contents

Pro Forma Holding Company Results

(In millions)	Pro Forma Year Ended December 31, 2007	2006
Selling, general and administrative	**$ 64.1**	$ 55.1
Depreciation and amortization	**6.0**	6.0
Operating profit (loss)	**($70.1)**	($61.1)

Selling, General and Administrative Expenses

For the year ended December 31, 2007, selling, general and administrative expenses at the holding company increased $9.0 million, or 16%, to $64.1 million, primarily due to increases in compensation and related employee benefit costs as well as professional and consulting fees.

LIQUIDITY AND CAPITAL RESOURCES

The Company believes that the significant indicators of liquidity for its business are cash on hand, cash flow from operations, working capital and amounts available under its credit facility. The Company s principal sources of liquidity consist of cash generated by operations and borrowings under its revolving credit facility.

The indentures governing the notes and the agreement governing the Company s senior secured credit facilities contain various provisions that limit the Company s ability and the ability of its restricted subsidiaries, including ADESA and IAAI, to, among other things:

- incur additional debt;
- provide guarantees in respect of obligations of other persons;
- issue redeemable stock and preferred stock;
- pay dividends or distributions or redeem or repurchase capital stock;
- prepay, redeem or purchase debt;
- make loans, investments and capital expenditures;
- incur liens;
- create restrictions on dividends or other payments by the Company s restricted subsidiaries;

enter into certain transactions with affiliates;

sell assets and capital stock of the Company s subsidiaries; and

consolidate or merge with or into, or sell substantially all of the Company s assets to, another person.

(Dollars in millions)	**December 31, 2007**	**December 31, 2006 (1)**
Cash and cash equivalents	**$ 204.1**	$ 209.7
Restricted cash	**$ 16.9**	$ 7.8
Working capital	**$ 442.1**	$ 375.1
Amounts available under credit facility	**$ 282.5**	$ 295.0
Cash flow from operations	**$ 96.8**	$ 207.8

(1) Working capital statistics for the year ended December 31, 2006 represent ADESA and IAAI combined to make comparative to statistics for the year ended December 31, 2007.

11

Table of Contents

Working Capital

A substantial amount of the Company s working capital is generated from the payments received for services provided. The majority of the Company s working capital needs are short-term in nature, usually less than a week in duration. Due to the decentralized nature of the business, payments for services are received at each auction and loan production office. Most of the financial institutions place a temporary hold on the availability of the funds deposited that can range anywhere from one to three business days, resulting in cash in the Company s accounts and on its balance sheet that is unavailable for use until it is made available by the various financial institutions. Over the years, the Company has increased the amount of funds that are available for immediate use and is actively working on initiatives that will continue to decrease the time between the deposit of and the availability of funds received from customers. There are outstanding checks (book overdrafts) to sellers and vendors included in current liabilities. Because the majority of these outstanding checks for operations in the U.S. are drawn upon bank accounts at financial institutions other than the financial institutions that hold the unavailable cash, the Company cannot offset the cash and the outstanding checks on its balance sheet.

AFC offers short-term inventory-secured financing, also known as floorplan financing, to used vehicle dealers. Financing is primarily provided for terms of 30 to 60 days. AFC principally generates its funding through the sale of its U.S. dollar denominated receivables. For further discussion of AFC s securitization arrangements, see Off-Balance Sheet Arrangements .

Credit Facilities

KAR Holdings has a $300 million revolving line of credit as part of the Company s $1,865 million senior credit facility, from which nothing was drawn during 2007. There were related outstanding letters of credit totaling approximately $17.5 million at December 31, 2007, which reduce the amount available under the senior credit facility. The Company s Canadian operations had letters of credit outstanding totaling approximately $2.5 million at December 31, 2007, which do not impact amounts available under the KAR Holdings credit facility.

On April 20, 2007, the Company entered into a $1,865 million senior credit facility, pursuant to the terms and conditions of a credit agreement (the Credit Agreement) with Bear Stearns Corporate Lending Inc., as administrative agent, and a syndicate of lenders. The Credit Agreement has a six and one-half year term that expires on October 19, 2013. Under the terms of the Credit Agreement, the lenders committed to provide advances and letters of credit in an aggregate amount of up to $1,865 million subject to certain conditions. Borrowings under the Credit Agreement may be used to finance working capital, capital expenditures and acquisitions permitted under the Credit Agreement and for other corporate purposes.

The Credit Agreement provides for a six and one-half year $1,565 million term loan and a six year $300 million revolving credit facility. The term loan will be repaid in quarterly installments at an amount of 0.25% of the initial term loan, with the remaining principal balance due on October 19, 2013. The revolving credit facility may be used for loans, and up to $75 million may be used for letters of credit. The revolving loans may be borrowed, repaid and reborrowed until April 19, 2013, at which time all revolving amounts borrowed must be repaid.

The revolving credit facility bears interest at a rate equal to LIBOR plus a margin ranging from 150 basis points to 225 basis points depending on the Company s total leverage ratio. Although it had no borrowings outstanding at December 31, 2007, KAR s revolving credit facility margin based on its leverage ratio was 225 basis points. The revolving credit facility also provides for both overnight and swingline borrowings at a rate of prime plus a margin ranging from 50 basis points to 125 basis points. At December 31, 2007 the applicable margin was 125 basis points. The term loan facility bears interest at a rate equal to LIBOR plus a margin of either 200 basis points or 225 basis points depending on the Company s total leverage ratio and ratings received from Moody s and Standard and Poor s. As of December 31, 2007, KAR s term loan facility margin was 225 basis points.

Table of Contents

The Credit Agreement contains certain restrictive loan covenants, including, among others, financial covenants requiring a maximum consolidated senior secured leverage ratio, provided there are revolving commitments outstanding, and covenants limiting KAR s ability to incur indebtedness, grant liens, make acquisitions, be acquired, dispose of assets, pay dividends, make capital expenditures and make investments. The leverage ratio covenants are based on consolidated Adjusted EBITDA which is EBITDA (earnings before interest expense, income taxes, depreciation and amortization) adjusted to exclude among other things (a) gains and losses from asset sales; (b) unrealized foreign currency translation gains and losses in respect of indebtedness; (c) certain non-recurring gains and losses; (d) stock option expense; (e) certain other noncash amounts included in the determination of net income; (f) management, monitoring, consulting and advisory fees paid to the equity sponsors; (g) charges and revenue reductions resulting from purchase accounting; (h) unrealized gains and losses on hedge agreements; (i) minority interest expense; (j) expenses associated with the consolidation of salvage operations; (k) consulting expenses incurred for cost reduction, operating restructuring and business improvement efforts; (l) expenses realized upon the termination of employees and the termination or cancellation of leases, software licenses or other contracts in connection with the operational restructuring and business improvement efforts; and (m) expenses incurred in connection with permitted acquisitions.

The covenants contained within the senior credit facility are critical to an investor s understanding of the Company s financial liquidity, as the violation of these covenants could cause a default and lenders could elect to declare all amounts borrowed due and payable. In addition, the indentures governing the Company s notes contain certain financial and operational restrictions on paying dividends and other distributions, making certain acquisitions or investments, incurring indebtedness, granting liens and selling assets. These financial covenants affect the Company s operating flexibility by, among other things, restricting its ability to incur expenses and indebtedness that could be used to grow the business, as well as to fund general corporate purposes. The Company was in compliance with the covenants at December 31, 2007.

On December 31, 2007, $1,557.2 million was outstanding on the term loan and there were no borrowings on the revolving credit facility. The Company believes its sources of liquidity from its cash and cash equivalents on hand, working capital, cash provided by operating activities, and availability under its senior credit facility are sufficient to meet its short and long-term operating needs for the foreseeable future. In addition, the Company believes the previously mentioned sources of liquidity will be sufficient to fund the Company s capital requirements and debt service payments for the next twelve months.

EBITDA and Adjusted EBITDA

EBITDA and Adjusted EBITDA, as presented herein, are supplemental measures of the Company s performance that are not required by, or presented in accordance with, generally accepted accounting principles in the United States (GAAP). They are not measurements of the Company s financial performance under GAAP and should not be considered as alternatives to revenues, net income (loss) or any other performance measures derived in accordance with GAAP or as alternatives to cash flow from operating activities as measures of the Company s liquidity.

EBITDA is defined as net income (loss), plus interest expense net of interest income, income tax provision (benefit), depreciation and amortization. The Company calculates Adjusted EBITDA by adjusting EBITDA for the items of income and expense and expected incremental revenue and cost savings described above in the discussion of certain restrictive loan covenants under Liquidity and Capital Resources Working Capital Credit Facilities . Management believes that the inclusion of supplementary adjustments to EBITDA applied in presenting Adjusted EBITDA is appropriate to provide additional information to investors about one of the principal internal measures of performance used by the Company. Management uses the Adjusted EBITDA measure to evaluate the performance of the Company and to evaluate results relative to incentive compensation targets. Adjusted EBITDA per the Credit Agreement adds the pro forma impact of recent acquisitions and the pro forma cost savings per the credit agreement to Adjusted EBITDA. This measure is used by the Company s

Table of Contents

creditors in assessing debt covenant compliance and management believes its inclusion is appropriate to provide additional information to investors about certain covenants required pursuant to the Company s senior secured credit facility and the notes. EBITDA, Adjusted EBITDA and Adjusted EBITDA per the Credit Agreement measures have limitations as analytical tools, and should not be considered in isolation, or as a substitute for analysis of the results as reported under GAAP. These measures may not be comparable to similarly titled measures reported by other companies.

Certain of the Company s loan covenant calculations require financial results for the most recent four consecutive fiscal quarters, with combined results for ADESA and IAAI prior to the merger. The calculation of Adjusted EBITDA (per the Credit Agreement) for the last twelve months ended December 31, 2007, presented below, includes a pro forma adjustment for anticipated cost savings related to the merger totaling $10.5 million net of realized cost savings. The adjustment relates to anticipated costs savings for redundant selling, general and administrative costs for the salvage operations. The following table reconciles EBITDA, Adjusted EBITDA and Adjusted EBITDA per the Credit Agreement to net income (loss) for the periods presented:

	Three Months Ended				**Year Ended**
(In millions)	**March 31, 2007**	**June 30, 2007**	**September 30, 2007**	**December 31, 2007**	**December 31, 2007**
Net income (loss)	$38.4	($7.3)	($8.6)	($34.3)	($11.8)
Add back: discontinued operations	0.1				0.1
Income (loss) from continuing operations	38.5	(7.3)	(8.6)	(34.3)	(11.7)
Add back:					
Income taxes	24.6	4.6	3.7	(16.5)	16.4
Interest expense, net of interest income	13.3	46.6	56.3	56.0	172.2
Depreciation and amortization	18.8	32.2	39.6	59.8	150.4
EBITDA	95.2	76.1	91.0	65.0	327.3
Nonrecurring charges	1.2	5.7	4.9	12.4	24.2
Nonrecurring transaction charges	2.4	22.4			24.8
Noncash charges	5.2	1.0	0.9	9.5	16.6
Advisory services	0.1	0.8	0.9	0.8	2.6
Adjusted EBITDA	104.1	106.0	97.7	87.7	395.5
Pro forma impact of recent acquisitions	1.5	1.7	1.5		4.7
Pro forma cost savings per the credit agreement				5.0	5.0
Adjusted EBITDA per the credit agreement	$105.6	$107.7	$99.2	$92.7	$405.2

Summary of Cash Flows

(In millions)	**Year Ended December 31, 2007**
Net cash provided by (used for):	
Operating activities	$ 96.8
Investing activities	(2,385.0)
Financing activities	2,492.0
Effect of exchange rate on cash	0.3
Net increase in cash and cash equivalents	$ 204.1

14

Table of Contents

KAR Holdings, Inc. was incorporated in the State of Delaware on November 9, 2006. However, the Company had no operations until the consummation of the merger transactions on April 20, 2007. As such, the cash flows of ADESA and IAAI for January 1 through April 19, 2007 are not reflected in the above numbers.

KAR Holdings cash flow initiatives include growing the used vehicle, salvage vehicle and dealer financing businesses internally by relocating/expanding facilities, broadening service offerings and improving operating efficiencies and externally through acquisitions.

Cash flow from operating activities was $96.8 million for the year ended December 31, 2007. Operating cash flow was favorably impacted by non-cash charges for depreciation and amortization, amortization of debt issue costs and other non-cash transactions, as well as a net decrease in working capital.

Net cash used for investing activities was $2,385.0 million for the year ended December 31, 2007 and is almost entirely representative of KAR s purchase of ADESA on April 20, 2007. In addition, $62.7 million has been expended for capital items since the merger as well as $36.6 million for the acquisition of other companies. For a discussion of the Company s capital expenditures, see Capital Expenditures below.

Net cash provided by financing activities was $2,492.0 million for the year ended December 31, 2007. In connection with the merger transactions, KAR Holdings entered into new senior secured credit facilities, including a $1,565.0 million term loan facility. In addition, KAR Holdings issued $600.0 million in fixed rate and floating rate senior notes due 2014 and $425.0 million in fixed rate senior subordinated notes due 2015. The Company also received $710.5 million from the issuance of its common stock, net of costs. A portion of the proceeds from the debt and equity were used to repay existing ADESA and IAAI debt totaling $685.7 million, including premium/consent payments. Payments for debt issue costs of approximately $90.8 million were also paid.

Capital Expenditures

Combined capital expenditures for ADESA and IAAI (excluding acquisitions and other investments) for the year ended December 31, 2007 and the year ended December 31, 2006 totaled $79.4 million and $54.6 million, respectively, and were funded primarily from internally generated funds. The Company continues to invest in its core information technology capabilities and capacity expansion. Capital expenditures are expected to be approximately $94 million for fiscal year 2008. Anticipated expenditures are primarily attributable to ongoing information system maintenance, upkeep and improvements at existing vehicle auction facilities, improvements in information technology systems and infrastructure, and expansion and relocation of existing auction sites that are at capacity. Future capital expenditures could vary substantially based on capital project timing and the initiation of new information systems projects to support the Company s business strategies.

Acquisitions

2007 Acquisitions

In September 2007, ADESA completed the acquisition of certain assets of the used vehicle Tri-State Auto Auction serving the Tri-State New York area. This acquisition complements the Company s geographic presence in the northeast. The auction is positioned on approximately 125 acres and includes seven auction lanes and full-service reconditioning shops providing detail, mechanical and body shop services. The assets purchased included operating equipment, accounts receivable and customer relationships related to the auction. In addition, the Company entered into an operating lease obligation related to the facility through 2017. Initial annual lease payments for the facility are approximately $0.5 million per year. The Company did not assume any other material liabilities or indebtedness in connection with the acquisition. Financial results for this acquisition have been included in the Company s consolidated financial statements since the date of acquisition.

Table of Contents

In October 2007, ADESA acquired all of the issued and outstanding shares of the parent company of Tri-State Auction, Co. Inc., and Sioux Falls Auto Auction, Inc., both North Dakota corporations. Tri-State Auto Auction serves the Fargo, North Dakota area. The auction is comprised of approximately 30 acres and includes six auction lanes and full-service reconditioning shops providing detail, mechanical and body shop services. The Sioux Falls Auto Auction serves the Sioux Falls, South Dakota area. The auction is comprised of approximately 40 acres and includes four auction lanes and full-service reconditioning shops providing detail, mechanical and body shop services. The assets of the auctions included operating equipment, accounts receivable and customer relationships related to the auctions. Liabilities assumed by the Company included operating leases for land and buildings as well as debt. Financial results for this acquisition will be included in the Company s consolidated financial statements from the date of acquisition.

In November 2007, ADESA Canada acquired all of the issued and outstanding shares of Enchere d Auto Transit Inc. (Transit). Transit is a three lane auction located on the south shore of Quebec City and serves the Quebec City region, Eastern Quebec and Northern New Brunswick. The auction is comprised of approximately 30 acres of which about 10 acres are currently being used. The assets of the auction included accounts receivable, land and building, operating equipment and customer relationships related to the auctions. Liabilities assumed by the Company included operating leases for land and buildings as well as debt. Financial results for this acquisition will be included in the Company s consolidated financial statements from the date of acquisition.

The aggregate purchase price for the four previously mentioned ADESA acquisitions was approximately $32.3 million. A preliminary purchase price allocation has been recorded for each acquisition and the purchase price of the acquisitions was allocated to the acquired assets based upon fair market values, including $7.4 million to other intangible assets, representing the fair value of acquired customer relationships and non competes which will be amortized over their expected useful lives of 3 to 15 years. The purchase price allocations resulted in aggregate goodwill of $20.0 million. The goodwill was assigned to the ADESA Auctions reporting segment and is expected to be fully deductible for tax purposes. All debt acquired as a result of these acquisitions was subsequently paid off. Pro forma financial results reflecting these acquisitions were not materially different from those reported.

2008 Acquisitions

In January 2008, IAAI completed the purchase of assets of B&E Auto Auction in Henderson, Nevada which services the Southern Nevada region, including Las Vegas. The site will expand IAAI s national service coverage and provide additional geographic support to clients who already utilize existing IAAI facilities in the surrounding Western states. The purchase agreement includes contingent payments related to the volume of certain vehicles sold subsequent to the purchase date. Financial results for this acquisition will be included in the Company s consolidated financial statements from the date of acquisition.

In February 2008, IAAI purchased the stock of Salvage Disposal Company of Georgia, Verastar, LLC, Auto Disposal of Nashville, Inc., Auto Disposal of Chattanooga, Inc., Auto Disposal of Memphis, Inc., Auto Disposal of Paducah, Inc. and Auto Disposal of Bowling Green, Inc., 11 independently owned Salvage auctions in Georgia, North Carolina, Tennessee, Mississippi and Kentucky. These site acquisitions will expand IAAI s national service coverage and provide additional geographic support to clients who already utilize existing IAAI facilities in the surrounding Southern States. The purchase agreement includes contingent payments related to the volume of certain vehicles sold subsequent to the purchase date. Financial results for these acquisitions will be included in the Company s consolidated financial statements from the date of acquisition.

In February 2008, ADESA completed the purchase of certain assets of Pennsylvania Auto Dealer Exchange (PADE), PADE Financial Services (PFS) and Conewago Partners, LP, an independent used vehicle auction in York, Pennsylvania. This acquisition complements the Company s geographic presence in the northeast. Financial results for this acquisition will be included in the Company s consolidated financial statements from the date of acquisition.

Table of Contents

In February 2008, IAAI completed the purchase of Southern A&S (formerly Southern Auto Storage Pool) in Memphis, Tennessee. IAAI plans to combine the Southern A&S business with the Memphis operation it acquired in the Verastar deal. The combined auctions will be relocated to a new site, which will be shared with ADESA Memphis. The purchase agreement includes contingent payments related to the volume of certain vehicles sold subsequent to the purchase date. Financial results for this acquisition will be included in the Company s consolidated financial statements from the date of acquisition.

The aggregate purchase price for the 14 auctions acquired in 2008 was approximately $114 million. The preliminary purchase price allocations for each auction will occur in the Company s first quarter ending March 31, 2008.

Contractual Obligations

The table below sets forth a summary of the Company s contractual debt and operating lease obligations as of December 31, 2007. Some of the figures included in this table are based on management s estimates and assumptions about these obligations, including their duration, the possibility of renewal and other factors. Because these estimates and assumptions are necessarily subjective, the obligations the Company may actually pay in future periods could vary from those reflected in the table. The following summarizes the Company s contractual cash obligations as of December 31, 2007 *(in millions)*:

	Payments Due by Period				
Contractual Obligations	**Total**	**Less than 1 year**	**1 3 Years**	**4 5 Years**	**More than 5 Years**
Long-term debt					
Term loan B (a)	$ 1,557.2	$ 15.6	$ 31.2	$ 31.2	$ 1,479.2
Floating rate senior notes due 2014 (a)	150.0				150.0
8 $^{3}/4$% senior notes due 2014 (a)	450.0				450.0
10% senior subordinated notes due 2015 (a)	425.0				425.0
Capital lease obligation (b)	34.5				34.5
Interest payments relating to long-term debt (c)	1,211.9	210.8	416.2	411.3	173.6
Interest rate swap (d)	17.9		17.9		
Postretirement benefit payments (e)	0.8	0.1	0.2	0.2	0.3
Operating leases (f)	477.8	50.0	90.9	76.9	260.0
Total contractual cash obligations	$ 4,325.1	$ 276.5	$ 556.4	$ 519.6	$ 2,972.6

(a) The table assumes the long-term debt is held to maturity.
(b) In 2003, ADESA entered into a capital lease for the new Atlanta auction facility in conjunction with the purchase of development revenue bonds.
(c) Interest payments on long-term debt are projected based on the contractual rates of the debt securities. (Note: interest on the capital lease is not included as it is offset by interest received from the related bonds.) Interest rates for the variable rate debt instruments were projected based on information available from lenders and held constant at the December 31, 2007 rates due to their unpredictable nature.
(d) The fair value of the interest rate swap agreement is estimated using pricing models widely used in financial markets and represents the estimated amount the Company would pay to terminate the agreement at December 31, 2007. The $800 million notional amount swap agreement does not mature until June 2009.
(e) Estimated future benefit payments for certain health care and death benefits for the retired employees of Underwriters Salvage Company (USC). IAAI assumed the obligation in connection with the acquisition of the capital stock of USC in 1994.
(f) Operating leases are entered into in the normal course of business. The Company leases some of its auction facilities, as well as other property and equipment under operating leases. Some lease agreements contain options to renew the lease or purchase the leased property. Future operating lease obligations would change if the renewal options were exercised and/or if the Company entered into additional operating lease agreements.

Table of Contents

Off-Balance Sheet Arrangements

AFC sells the majority of its U.S. dollar denominated finance receivables on a revolving basis and without recourse to a wholly owned, bankruptcy remote, consolidated, special purpose subsidiary (AFC Funding Corporation), established for the purpose of purchasing AFC s finance receivables. The securitization agreement allows for the revolving sale by AFC Funding Corporation to a bank conduit facility of up to a maximum of $750 million in undivided interests in certain eligible finance receivables subject to committed liquidity. The agreement expires on April 20, 2012. AFC Funding Corporation had committed liquidity of $600 million at December 31, 2007. Receivables that AFC Funding sells to the bank conduit facility qualify for sales accounting for financial reporting purposes pursuant to SFAS 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities,* and as a result are not reported on the Company s Consolidated Balance Sheet.

At December 31, 2007, AFC managed total finance receivables of $847.9 million, of which $746.1 million had been sold without recourse to AFC Funding Corporation. Undivided interests in finance receivables were sold by AFC Funding Corporation to the bank conduit facility with recourse totaling $522.0 million at December 31, 2007. Finance receivables include $29.4 million classified as held for sale and $225.0 million classified as held for investment at December 31, 2007. Finance receivables classified as held for investment include $91.0 million related to receivables that were sold to the bank conduit facility that were repurchased by AFC at fair market value when they became ineligible under the terms of the collateral agreement with the bank conduit facility. The face amount of these receivables was $99.3 million at December 31, 2007.

AFC s allowance for losses of $7.5 million at December 31, 2007, includes an estimate of losses for finance receivables held for investment. Additionally, accrued liabilities of $4.3 million for the estimated losses for loans sold by the special purpose subsidiary were recorded at December 31, 2007. These loans were sold to a bank conduit facility with recourse to the special purpose subsidiary and will come back on the balance sheet of the special purpose subsidiary at fair market value if they become ineligible under the terms of the collateral arrangement with the bank conduit facility.

Proceeds from the revolving sale of receivables to the bank conduit facility are used to fund new loans to customers. AFC and AFC Funding Corporation must maintain certain financial covenants including, among others, limits on the amount of debt AFC can incur, minimum levels of tangible net worth, and other covenants tied to the performance of the finance receivables portfolio. The securitization agreement also incorporates the financial covenants of the Company s credit facility. At December 31, 2007, the Company was in compliance with the covenants contained in the securitization agreement.

Critical Accounting Estimates

In preparing the financial statements in accordance with generally accepted accounting principles, management must often make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, expenses and related disclosures at the date of the financial statements and during the reporting period. Some of those judgments can be subjective and complex. Consequently, actual results could differ from those estimates.

In addition to the critical accounting estimates, there are other items used in the preparation of the consolidated financial statements that require estimation, but are not deemed critical. Changes in estimates used in these and other items could have a material impact on the Company s financial statements.

KAR Holdings continually evaluates the accounting policies and estimates used to prepare the consolidated financial statements. In cases where management estimates are used, they are based on historical experience, information from third-party professionals, and various other assumptions believed to be reasonable. The following summarizes those accounting policies that are most subject to important estimates and assumptions and are most critical to the reported results of operations and financial condition.

Table of Contents

Uncollectible Receivables and Allowance for Credit Losses and Doubtful Accounts

The Company maintains an allowance for credit losses and doubtful accounts for estimated losses resulting from the inability of customers to make required payments. The allowances for credit losses and doubtful accounts are based on management s evaluation of the receivables portfolio under current economic conditions, the volume of the portfolio, overall portfolio credit quality, review of specific collection matters and such other factors which, in management s judgment, deserve recognition in estimating losses. Specific collection matters can be impacted by the outcome of negotiations, litigation and bankruptcy proceedings.

Due to the nature of the Company s business, substantially all trade receivables are due from vehicle dealers, salvage buyers, institutional customers and insurance companies. The Company generally has possession of vehicles or vehicle titles collateralizing a significant portion of these receivables. At the auction sites, risk is mitigated through a pre-auction registration process that includes verification of identification, bank accounts, dealer license status, acceptable credit history, buying history at other auctions and the written acceptance of all of the auction s policies and procedures.

AFC s allowance for credit losses includes an estimate of losses for finance receivables currently held on the balance sheet of AFC and its subsidiaries. Additionally, an accrued liability is recorded for the estimated losses for loans sold by AFC s subsidiary, AFC Funding Corporation. These loans were sold to a bank conduit facility with recourse to AFC Funding Corporation and will come back on the balance sheet of AFC Funding Corporation at fair market value if they become ineligible under the terms of the collateral arrangement with the bank conduit facility. AFC controls credit risk through credit approvals, credit limits, underwriting and collateral management monitoring procedures, which includes holding vehicle titles where permitted.

Goodwill and Long-Lived Assets

When the Company acquires businesses, the purchase price is allocated to tangible assets and liabilities and identifiable intangible assets acquired. Any residual purchase price is recorded as goodwill. The allocation of the purchase price requires management to make significant estimates in determining the fair values of assets acquired and liabilities assumed, especially with respect to intangible assets. These estimates are based on historical experience and information obtained from the management of the acquired companies. These estimates can include, but are not limited to, the cash flows that an asset is expected to generate in the future, the appropriate weighted-average cost of capital, and the cost savings expected to be derived from acquiring an asset. These estimates are inherently uncertain and unpredictable. In addition, unanticipated events and circumstances may occur which may affect the accuracy or validity of such estimates.

In accordance with SFAS No. 142, *Goodwill and Other Intangible Assets*, the Company assesses goodwill for impairment at least annually and whenever events or circumstances indicate that the carrying amount of the goodwill may be impaired. Important factors that could trigger an impairment review include significant under-performance relative to historical or projected future operating results; significant negative industry or economic trends; and the Company s market valuation relative to its book value. In assessing goodwill, KAR Holdings must make assumptions regarding estimated future cash flows and earnings, changes in the Company s business strategy and economic conditions affecting market valuations related to the fair values of KAR Holdings three reporting units (which consist of the Company s three operating and reportable business segments: ADESA Auctions, IAAI and AFC). If the fair value of a reporting unit is determined to be less than the carrying amount, an impairment charge would be recorded in the period identified. In response to changes in industry and market conditions, KAR Holdings may be required to strategically realign its resources and consider restructuring, disposing of or otherwise exiting businesses, which could result in an impairment of goodwill. To date, no significant changes in events or circumstances have occurred that would indicate the carrying amount of the Company s goodwill has been impaired.

Table of Contents

The Company reviews long-lived assets for possible impairment whenever circumstances indicate that their carrying amount may not be recoverable. If it is determined that the carrying amount of a long-lived asset exceeds the total amount of the estimated undiscounted future cash flows from that asset, the Company would recognize a loss to the extent that the carrying amount exceeds the fair value of the asset. Management judgment is involved in both deciding if testing for recovery is necessary and in estimating undiscounted cash flows. The Company s impairment analysis is based on the current business strategy, expected growth rates and estimated future economic conditions.

Self-Insurance Programs

KAR Holdings self-insures a portion of employee medical benefits under the terms of its employee health insurance program, as well as a portion of its automobile, general liability and workers compensation claims. The Company purchases individual stop-loss insurance coverage that limits the exposure on individual claims. The Company also purchases aggregate stop-loss insurance coverage that limits the total exposure to overall automobile, general liability and workers compensation claims. The cost of the stop-loss insurance is expensed over the contract periods.

KAR Holdings records an accrual for the claims expense related to its employee medical benefits, automobile, general liability and workers compensation claims based upon the expected amount of all such claims. Trends in healthcare costs could have a significant impact on anticipated claims. If actual claims are higher than anticipated, the Company s accrual might be insufficient to cover the claims costs, which would have an adverse impact on the operating results in that period.

Legal Proceedings and Other Loss Contingencies

KAR Holdings is subject to the possibility of various legal proceedings and other loss contingencies, many involving litigation incidental to the business and a variety of environmental laws and regulations. Litigation and other loss contingencies are subject to inherent uncertainties and the outcomes of such matters are often very difficult to predict and generally are resolved over long periods of time. The Company considers the likelihood of loss or the incurrence of a liability, as well as the ability to reasonably estimate the amount of loss, in determining loss contingencies. Estimating probable losses requires the analysis of multiple possible outcomes that often are dependent on the judgment about potential actions by third parties. Contingencies are recorded in the consolidated financial statements, or otherwise disclosed, in accordance with SFAS 5, *Accounting for Contingencies*. The Company accrues for an estimated loss contingency when it is probable that a liability has been incurred and the amount of loss can be reasonably estimated. Management regularly evaluates current information available to determine whether accrual amounts should be adjusted. If the amount of an actual loss is greater than the amount accrued, this could have an adverse impact on the Company s operating results in that period. Legal fees are expensed as incurred.

Income Taxes

All income tax amounts reflect the use of the liability method. Under this method, deferred tax assets and liabilities are determined based on the expected future tax consequences of temporary differences between the carrying amounts of assets and liabilities for financial and income tax reporting purposes.

KAR Holdings operates in multiple tax jurisdictions with different tax rates and must determine the appropriate allocation of income to each of these jurisdictions. In the normal course of business, the Company will undergo scheduled reviews by taxing authorities regarding the amount of taxes due. These reviews include questions regarding the timing and amount of deductions and the allocation of income among various tax jurisdictions. Tax reviews often require an extended period of time to resolve and may result in income tax adjustments if changes to the allocation are required between jurisdictions with different tax rates.

Table of Contents

KAR Holdings records its tax provision based on existing laws, experience with previous settlement agreements, the status of current IRS (or other taxing authority) examinations and management s understanding of how the tax authorities view certain relevant industry and commercial matters. In accordance with FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes*, the Company recognizes the effect of income tax positions only if those positions are more likely than not of being sustained. Recognized income tax positions are measured at the largest amount that is greater than 50% likely of being realized. Changes in recognition or measurement are reflected in the period in which the change in judgment occurs. The Company establishes reserves when it believes that certain positions may not prevail if challenged by a taxing authority. The Company adjusts these reserves in light of changing facts and circumstances.

New Accounting Standards

In September 2006, the FASB issued SFAS 157, *Fair Value Measurements*. The statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. This standard, as issued, is effective for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The FASB issued FASB Staff Position No. FAS 157-b, *Effective Date of FASB Statement No. 157*, which delays the effective date by one year for all nonfinancial assets and nonfinancial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis, at least annually. The Company is currently evaluating the impact the adoption of SFAS 157 will have on the consolidated financial statements.

In February 2007, the FASB issued SFAS 159, *The Fair Value Option for Financial Assets and Financial Liabilities*, which provides companies with an option to report selected financial assets and liabilities at fair value. The objective of SFAS 159 is to reduce both complexity in accounting for financial instruments and the volatility in earnings caused by measuring related assets and liabilities differently. SFAS 159 does not eliminate disclosure requirements of other accounting standards, including fair value measurement disclosures in SFAS 157. This standard is effective as of the beginning of an entity s first fiscal year beginning after November 15, 2007. The Company is currently evaluating the impact the adoption of SFAS 159 will have on the consolidated financial statements.

In December 2007, the FASB issued SFAS 141(R), *Business Combinations*. The statement establishes principles and requirements for recognizing and measuring identifiable assets and goodwill acquired, liabilities assumed and any noncontrolling interest in an acquisition, at their fair value as of the acquisition date. This standard is effective for annual reporting periods beginning after December 15, 2008. The Company is currently evaluating the impact the adoption of SFAS 141(R) will have on the consolidated financial statements.

In December 2007, the FASB issued SFAS 160, *Noncontrolling Interests in Consolidated Financial Statements an Amendment of Accounting Research Bulletin No. 51*. The statement amends Accounting Research Bulletin No. 51 to establish accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. This standard is effective for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years. The Company is currently evaluating the impact the adoption of SFAS 160 will have on the consolidated financial statements.

Table of Contents

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

The financial statements referred to below include the financial statements of KAR Holdings, Inc. for the year ended December 31, 2007. However, KAR Holdings had no operations until its acquisitions of ADESA and IAAI on April 20, 2007. In addition, the historical financial statements of the companies KAR Holdings acquired on April 20, 2007 (ADESA and IAAI) are presented for each of the last two years as well as the period in 2007, prior to the acquisition.

Index to Financial Statements

Table of Contents

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders

KAR Holdings, Inc.:

We have audited the accompanying consolidated balance sheets of KAR Holdings, Inc. and subsidiaries as of December 31, 2007 and 2006, and the related consolidated statements of operations, stockholders equity and cash flows for the year ended December 31, 2007. These consolidated financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of KAR Holdings, Inc. and subsidiaries as of December 31, 2007 and 2006, and the results of their operations and their cash flows for the year ended December 31, 2007, in conformity with U.S. generally accepted accounting principles.

/s/ KPMG LLP

Indianapolis, Indiana

March 26, 2008

Table of Contents

KAR Holdings, Inc.

Consolidated Statement of Operations

For the Year Ended December 31, 2007

(Operations Commenced April 20, 2007)

(In millions)

Operating revenues	
ADESA Auction Services	**$677.7**
IAAI Salvage Services	**330.1**
AFC	**95.0**
Total operating revenues	**1,102.8**
Operating expenses	
Cost of services (exclusive of depreciation and amortization)	**627.4**
Selling, general and administrative	**242.4**
Depreciation and amortization	**126.6**
Total operating expenses	**996.4**
Operating profit	**106.4**
Interest expense	**162.3**
Other income, net	**(7.6)**
Loss before income taxes	**(48.3)**
Income taxes	**(10.0)**
Net loss	**($38.3)**

See accompanying notes to consolidated financial statements

F-3

Table of Contents

KAR Holdings, Inc.

Consolidated Balance Sheets

(Operations Commenced April 20, 2007)

(In millions)

	December 31, 2007	December 31, 2006
Assets		
Current assets		
Cash and cash equivalents	**$ 204.1**	$
Restricted cash	**16.9**	
Trade receivables, net of allowances	**278.3**	
Finance receivables, net of allowances	**246.9**	
Retained interests in finance receivables sold	**71.5**	
Deferred income tax assets	**29.3**	
Other current assets	**54.8**	
Total current assets	**901.8**	
Other assets		
Goodwill	**1,617.6**	
Customer relationships, net of accumulated amortization	**844.4**	
Other intangible assets, net of accumulated amortization	**251.4**	
Unamortized debt issuance costs	**81.6**	
Other assets	**60.8**	
Total other assets	**2,855.8**	
Property and equipment, net of accumulated depreciation	**773.2**	
Total assets	**$ 4,530.8**	$

See accompanying notes to consolidated financial statements

F-4

Table of Contents

KAR Holdings, Inc.

Consolidated Balance Sheets (Continued)

(Operations Commenced April 20, 2007)

(In millions, except share data)

	December 31, 2007	December 31, 2006
Liabilities and Stockholders Equity		
Current liabilities		
Accounts payable	**$ 292.8**	$
Accrued employee benefits and compensation expenses	**54.8**	
Accrued interest	**16.4**	
Other accrued expenses	**80.1**	
Current maturities of long-term debt	**15.6**	
Total current liabilities	**459.7**	
Non-current liabilities		
Long-term debt	**2,601.1**	
Deferred income tax liabilities	**378.1**	
Other liabilities	**78.3**	
Total non-current liabilities	**3,057.5**	
Commitments and contingencies (Note 17)		
Stockholders equity		
Preferred stock, $0.01 par value:		
Authorized shares: 5,000,000		
Issued shares: none		
Common stock, $0.01 par value:		
Authorized shares: 20,000,000		
Issued shares: 10,686,316 (2007)		
100 (2006)	**0.1**	
Additional paid-in capital	**1,027.9**	
Retained earnings (deficit)	**(41.5)**	
Accumulated other comprehensive income	**27.1**	
Total stockholders equity	**1,013.6**	
Total liabilities and stockholders equity	**$ 4,530.8**	$

See accompanying notes to consolidated financial statements

F-5

Table of Contents

KAR Holdings, Inc.

Consolidated Statements of Stockholders Equity

(Operations Commenced April 20, 2007)

(In millions)

	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Retained Earnings (Deficit)	Accumulated Other Comprehensive Income (Loss)	Total
Balance at December 31, 2006		$	$	$	$	$
Issuance of common stock, net of costs	10.7	0.1	739.4			739.5
Contribution of Insurance Auto Auctions, Inc.			272.4			272.4
Contributed capital in the form of exchanged stock options associated with the transaction			8.9			8.9
Comprehensive income:						
Net loss				(38.3)		(38.3)
Other comprehensive income (loss), net of tax:						
Unrealized loss on interest rate swap					(11.3)	(11.3)
Unrealized gain on postretirement benefit obligation					0.2	0.2
Foreign currency translation					38.2	38.2
Comprehensive income				(38.3)	27.1	(11.2)
Stock dividend			3.2	(3.2)		
Capital contributions			3.0			3.0
Stock-based compensation expense			1.0			1.0
Balance at December 31, 2007	**10.7**	**$ 0.1**	**$ 1,027.9**	**($ 41.5)**	**$ 27.1**	**$ 1,013.6**

See accompanying notes to consolidated financial statements

Table of Contents

KAR Holdings, Inc.

Consolidated Statement of Cash Flows

For the Year Ended December 31, 2007

(Operations Commenced April 20, 2007)

(In millions)

Operating activities	
Net loss	**($38.3)**
Adjustments to reconcile net loss to net cash provided by operating activities:	
Depreciation and amortization	**126.6**
Provision for credit losses	**3.2**
Deferred income taxes	**(21.8)**
Amortization of debt issuance costs	**9.2**
Stock-based compensation expense	**6.7**
Unrealized loss on interest rate swap	**(11.3)**
Other non-cash, net	**4.5**
Changes in operating assets and liabilities, net of acquisitions:	
Finance receivables held for sale	**(9.0)**
Retained interests in finance receivables sold	**0.6**
Trade receivables and other assets	**113.6**
Accounts payable and accrued expenses	**(87.2)**
Net cash provided by operating activities	**96.8**
Investing activities	
Net decrease in finance receivables held for investment	**3.8**
Acquisition of ADESA, net of cash acquired	**(2,272.6)**
Acquisition of businesses, net of cash acquired	**(36.6)**
Purchases of property, equipment and computer software	**(62.7)**
Purchase of other intangibles	**(0.1)**
Proceeds from the sale of property, equipment and computer software	**0.1**
Transfer from (to) restricted cash	**(16.9)**
Net cash used by investing activities	**(2,385.0)**
Financing activities	
Net decrease in book overdrafts	**(22.0)**
Repayment of ADESA debt	**(318.0)**
Repayment of IAAI debt	**(367.7)**
Proceeds from long-term debt	**2,590.0**
Payments for debt issuance costs	**(90.8)**
Payments on long-term debt	**(9.8)**
Payments on capital leases	**(0.2)**
Proceeds from issuance of common stock, net of costs	**710.5**
Net cash provided by financing activities	**2,492.0**
Effect of exchange rate changes on cash	**0.3**
Net increase in cash and cash equivalents	**204.1**
Cash and cash equivalents at beginning of period	
Cash and cash equivalents at end of period	**$ 204.1**

Cash paid for interest	**$**	**136.7**
Cash paid for taxes, net of refunds	**$**	**18.1**

See accompanying notes to consolidated financial statements

Table of Contents

KAR Holdings, Inc.

Notes to Consolidated Financial Statements

Note 1 Organization and Other Matters

KAR Holdings, Inc. was organized in the State of Delaware on November 9, 2006. The Company is a holding company organized for the purpose of consummating a merger with ADESA, Inc. and combining Insurance Auto Auctions, Inc. with ADESA. The Company had no operations prior to the merger transactions on April 20, 2007.

Defined Terms

Unless otherwise indicated, the following terms used herein shall have the following meanings:

the Equity Sponsors refers, collectively, to Kelso Investment Associates VII, L.P., GS Capital Partners VI, L.P., ValueAct Capital Master Fund, L.P. and Parthenon Investors II, L.P., which own through their respective affiliates substantially all of KAR Holdings equity;

KAR Holdings or the Company refers to KAR Holdings, Inc., a Delaware corporation that is a wholly owned subsidiary of KAR LLC. KAR Holdings is the parent company of ADESA and IAAI;

KAR LLC refers to KAR Holdings II, LLC, which is owned by affiliates of the Equity Sponsors and management of the Company;

ADESA refers to ADESA, Inc. and its subsidiaries;

AFC refers to Automotive Finance Corporation, an Indiana corporation that is a wholly owned subsidiary of ADESA;

IAAI refers to Insurance Auto Auctions, Inc. and its subsidiaries.

Merger Transactions and Corporate Structure

On December 22, 2006, KAR LLC entered into a definitive merger agreement to acquire ADESA. The merger occurred on April 20, 2007 and as part of the agreement, Insurance Auto Auctions, Inc., a leading provider of automotive salvage auction and claims processing services in the United States, was contributed to KAR LLC. Both ADESA and IAAI became wholly owned subsidiaries of KAR Holdings which is owned by KAR LLC. KAR Holdings is the accounting acquirer, and the assets and liabilities of both ADESA and IAAI were recorded at fair value as of April 20, 2007. See Fair Value of Assets Acquired and Liabilities Assumed below for a further discussion.

The following transactions occurred in connection with the merger:

Approximately 90.8 million shares of ADESA s outstanding common stock converted into the right to receive $27.85 per share in cash;

Approximately 3.4 million outstanding options to purchase shares of ADESA s common stock were cancelled in exchange for payments in cash of $27.85 per underlying share, less the applicable option exercise price, resulting in net proceeds to holders of

$18.6 million;

Approximately 0.3 million outstanding restricted stock and restricted stock units of ADESA vested immediately and were paid out in cash of $27.85 per unit;

Affiliates of the Equity Sponsors and management contributed to KAR Holdings approximately $1.1 billion in equity, consisting of approximately $790.0 million in cash and ADESA, Inc. stock (ADESA, Inc. stock contributed by one of the Equity Sponsors had a fair value of $65.4 million and was recorded at its carryover basis of $32.1 million) and approximately $272.4 million of equity interest in IAAI;

Table of Contents

KAR Holdings, Inc.

Notes to Consolidated Financial Statements (Continued)

KAR Holdings entered into new senior secured credit facilities, comprised of a $1,565.0 million term loan facility and a $300.0 million revolving credit facility. Existing and certain future domestic subsidiaries, subject to certain exceptions, guarantee such credit facilities;

KAR Holdings issued $150.0 million Floating Rate Senior Notes due May 1, 2014, $450.0 million 8 $^{3}/4$% Senior Notes due May 1, 2014 and $425.0 million 10% Senior Subordinated Notes due May 1, 2015.

Use of Proceeds

The net proceeds from the equity sponsors and financings were used to: (a) fund the cash consideration payable to ADESA stockholders, ADESA option holders and ADESA restricted stock and restricted stock unit holders under the merger agreements; (b) repay the outstanding principal and accrued interest under ADESA s existing credit facility and notes as of the closing of the merger; (c) repay the outstanding principal and accrued interest under IAAI s existing credit facility and notes as of the closing of the merger; (d) pay related transaction fees and expenses; and (e) contribute IAAI s equity at fair value.

Fair Value of Assets Acquired and Liabilities Assumed

The merger was recorded in accordance with Statement of Financial Accounting Standards (SFAS) No. 141, *Business Combinations*. The allocation of the $2.8 billion purchase price is preliminary as the receipt and analysis of the final appraisals and valuations from third party valuation experts are pending. The estimates are based on preliminary valuations and information currently available. Management believes the preliminary valuations and estimates are a reasonable basis for the allocation of the purchase price. However, the analysis of the fair value estimates is continuing to be refined in accordance with SFAS 141. As additional information becomes available and as actual results vary from these estimates, the underlying assets or liabilities may need to be adjusted, thereby impacting intangible asset and related amortization estimates, as well as goodwill. The following table summarizes the estimated fair value of the assets acquired and liabilities assumed (in millions):

Current assets	$ 1,060.5
Property, plant and equipment	758.5
Goodwill	1,589.8
Customer relationships	864.9
Other intangible assets	259.8
Other assets	46.5
Total assets	$ 4,580.0
Current liabilities	$ 564.1
Long-term debt	685.7
Deferred income tax liabilities	418.9
Other liabilities	72.3
Total liabilities	$ 1,741.0
Net assets acquired	$ 2,839.0

Business and Nature of Operations

The network of 59 ADESA whole car auctions and 145 IAAI salvage vehicle auctions facilitates the sale of used and salvage vehicles through physical, online or hybrid auctions, which permit Internet buyers to participate in physical auctions. ADESA and IAAI are leading, national providers of wholesale and salvage vehicle auctions

Table of Contents

KAR Holdings, Inc.

Notes to Consolidated Financial Statements (Continued)

and related vehicle redistribution services for the automotive industry in North America. Redistribution services include a variety of activities designed to transfer used and salvage vehicles between sellers and buyers throughout the vehicle life cycle. ADESA and IAAI facilitate the exchange of these vehicles through an auction marketplace, which aligns sellers and buyers. As an agent for customers, the companies generally do not take title to or ownership of the vehicles sold at the auctions. Generally fees are earned from the seller and buyer on each successful auction transaction in addition to fees earned for ancillary services.

ADESA has the second largest used vehicle auction network in North America, based upon the number of used vehicles sold through auctions annually, and also provides services such as inbound and outbound logistics, reconditioning, vehicle inspection and certification, titling, administrative and salvage recovery services. ADESA is able to serve the diverse and multi-faceted needs of its customers through the wide range of services offered at its facilities.

IAAI is the second largest provider of salvage vehicle auctions and related services in North America. The salvage auctions facilitate the redistribution of damaged vehicles that are designated as total losses by insurance companies, recovered stolen vehicles for which an insurance settlement with the vehicle owner has already been made and older model vehicles donated to charity or sold by dealers in salvage auctions. The salvage auction business specializes in providing services such as inbound and outbound logistics, inspections, evaluations, titling and settlement administrative services.

AFC is a leading provider of floorplan financing to independent used vehicle dealers and this financing is provided through 91 loan production offices located throughout North America. Floorplan financing supports independent used vehicle dealers in North America who purchase vehicles from ADESA auctions, independent auctions, auctions affiliated with other auction networks and non-auction purchases.

Note 2 Summary of Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements include the accounts of KAR Holdings and all of its wholly owned subsidiaries. Significant intercompany transactions and balances have been eliminated.

Use of Estimates

The preparation of the consolidated financial statements in conformity with accounting principles generally accepted in the U.S. requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. Actual results could differ from these estimates.

Business Segments

The Company s operations are grouped into three operating segments: ADESA Auctions, IAAI and AFC. The three operating segments also serve as the Company s reportable business segments. Operations are measured through detailed budgeting and monitoring of contributions to consolidated income by each business segment.

Derivative Instruments and Hedging Activity

The Company recognizes all derivative financial instruments in the consolidated financial statements at fair value in accordance with SFAS 133, *Accounting for Derivative Instruments and Hedging Activities*. The Company currently uses an interest rate swap that is designated and qualifies as a cash flow hedge to manage the

KAR Holdings, Inc.

Notes to Consolidated Financial Statements (Continued)

variability of cash flows to be paid due to interest rate movements on its variable rate debt. The Company does not, however, enter into hedging contracts for trading or speculative purposes. The fair value of the interest rate swap agreement is estimated using pricing models widely used in financial markets and represents the estimated amount the Company would receive or pay to terminate the agreement at the reporting date. The fair value of the swap agreement is recorded in Other assets or Other liabilities on the consolidated balance sheet based on the gain or loss position of the contract. Changes in the fair value of the interest rate swap agreement designated as a cash flow hedge are recorded as a component of Accumulated other comprehensive income. Gains and losses on the interest rate swap agreement are subsequently included in earnings as an adjustment to interest expense in the same periods in which the related interest payment being hedged is recognized in earnings. The Company uses the change in variable cash flows method to assess hedge effectiveness in accordance with SFAS 133.

Foreign Currency Translation

Revenues and expenses denominated in foreign currencies are translated into U.S. dollars at average exchange rates in effect during the year. Assets and liabilities of foreign operations are translated using the exchange rates in effect at year end. Foreign currency transaction gains and losses are included in the consolidated statement of operations within Other income, net. Adjustments arising from the translation of net assets located outside the U.S. (gains and losses) are shown as a component of Accumulated other comprehensive income.

Cash Equivalents

All highly liquid investments with an original maturity of three months or less are considered to be cash equivalents. These investments are valued at cost, which approximates fair value.

Restricted Cash

AFC Funding Corporation, a wholly owned, bankruptcy remote, consolidated, special purpose subsidiary of AFC, is required to maintain a cash reserve approximating 1 percent of total sold receivables to the bank conduit facility as security for the receivables sold. AFC also maintains other cash reserves associated with its banking relationships. In addition, ADESA has cash reserves with a bank related to vendor purchases.

Receivables

Trade receivables include the unremitted purchase price of vehicles purchased by third parties at the auctions, fees to be collected from those buyers and amounts for services provided by the Company related to certain consigned vehicles in the Company s possession. These amounts due with respect to the consigned vehicles are generally deducted from the sales proceeds upon the eventual auction or other disposition of the related vehicles.

Finance receivables include floorplan receivables created by financing dealer purchases of vehicles in exchange for a security interest in those vehicles and special purpose loans. Floorplan receivables become due at the earlier of the dealer subsequently selling the vehicle or a predetermined time period (generally 30 to 60 days). Floorplan receivables include (1) eligible receivables that are not yet sold to the bank conduit facility (see Note 6), (2) Canadian floorplan receivables, (3) U.S. floorplan receivables not eligible for the bank conduit facility, and (4) receivables that were sold to the bank conduit facility that come back on the balance sheet of the Company at fair market value if they become ineligible under the terms of the collateral arrangement with the bank conduit facility. Special purpose loans relate to loans that are either line of credit loans or working capital loans that can be either secured or unsecured based on the facts and circumstances of the specific loans.

Table of Contents

KAR Holdings, Inc.

Notes to Consolidated Financial Statements (Continued)

Due to the nature of the Company s business, substantially all trade and finance receivables are due from vehicle dealers, salvage buyers, institutional sellers and insurance companies. The Company has possession of vehicles or vehicle titles collateralizing a significant portion of the trade and finance receivables.

Trade receivables and finance receivables held for investment are reported net of an allowance for doubtful accounts and credit losses. The allowances for doubtful accounts and credit losses are based on management s evaluation of the receivables portfolio under current conditions, the volume of the portfolio, overall portfolio credit quality, review of specific collection issues and such other factors which in management s judgment deserve recognition in estimating losses. Finance receivables held for sale are carried at lower of cost or market. Fair value is based upon estimates of future cash flows including estimates of anticipated credit losses. Estimated losses for receivables sold by AFC Funding Corporation to the bank conduit facility with recourse to AFC Funding Corporation (see Note 5) are recorded as an accrued expense.

Classification of finance receivables in the Consolidated Statement of Cash Flows is dependent on the initial balance sheet classification of the finance receivable. Finance receivables initially classified as held for investment are included as investing activity in the Consolidated Statement of Cash Flows and finance receivables initially classified as held for sale are included as an operating cash flow.

Retained Interests in Finance Receivables Sold

Retained interests in finance receivables sold are classified as trading securities pursuant to SFAS 115, *Accounting for Certain Investments in Debt and Equity Securities*, and carried at estimated fair value with gains and losses recognized in the Consolidated Statement of Operations. Fair value is based upon estimates of future cash flows, using assumptions that market participants would use to value such investments, including estimates of anticipated credit losses over the life of the finance receivables sold. The cash flows were discounted using a market discount rate.

Other Current Assets

Other current assets consist of inventories, taxes receivable, notes receivable and prepaid expenses. The inventories, which consist of vehicles, supplies, and parts are accounted for on the specific identification method, and are stated at the lower of cost or market.

Goodwill

Goodwill represents the excess of cost over fair value of identifiable net assets of businesses acquired. Goodwill will be tested for impairment annually in the second quarter, or more frequently as impairment indicators arise. The goodwill impairment test is a two-step test. Under the first step, the fair value of each reporting unit is compared with its carrying value (including goodwill). If the fair value of the reporting unit is less than its carrying value, an indication of goodwill impairment exists for the reporting unit and the Company must perform step two of the impairment test (measurement). Under step two, an impairment loss is recognized for any excess of the carrying amount of the reporting unit s goodwill over the implied fair value of that goodwill. The implied fair value of goodwill is determined by allocating the fair value of the reporting unit in a manner similar to a purchase price allocation, in accordance with FASB Statement No. 141, *Business Combinations*. The residual fair value after this allocation is the implied fair value of the reporting unit goodwill. Fair value of the reporting unit is determined using a discounted cash flow analysis. If the fair value of the reporting unit exceeds its carrying value, step two does not need to be performed.

Table of Contents

KAR Holdings, Inc.

Notes to Consolidated Financial Statements (Continued)

Customer Relationships and Other Intangible Assets

Customer relationships are amortized over the life determined in the valuation of the particular acquisition. Other intangible assets generally consist of tradenames, computer software and non-compete agreements, and if amortized, are amortized using the straight-line method. Tradenames are not amortized due to their indefinite life. Costs incurred related to software developed or obtained for internal use are capitalized during the application development stage of software development and amortized over their estimated useful lives. The non-compete agreements are amortized over the life of the agreements and are written off upon being fully amortized. The lives of other intangible assets are re-evaluated periodically when facts and circumstances indicate that revised estimates of useful lives may be warranted.

Property and Equipment

Property and equipment are stated at historical cost less accumulated depreciation. Depreciation is computed using the straight-line method at rates intended to depreciate the costs of assets over their estimated useful lives. Upon retirement or sale of property and equipment, the cost of the disposed assets and related accumulated depreciation is removed from the accounts and any resulting gain or loss is credited or charged to selling, general and administrative expenses. Expenditures for normal repairs and maintenance are charged to expense as incurred. Additions and expenditures for improving or rebuilding existing assets that extend the useful life are capitalized. Leasehold improvements made either at the inception of the lease or during the lease term are amortized over the shorter of their economic lives or the lease term including any renewals that are reasonably assured.

Unamortized Debt Issuance Costs

Debt issuance costs reflect the expenditures incurred in conjunction with the merger to issue Term Loan B, the senior notes, the senior subordinated notes and to obtain the bank credit facility. The debt issuance costs are being amortized over their respective lives to interest expense and had a carrying amount of $81.6 million December 31, 2007.

Other Assets

Other assets consist of investments held to maturity, below market leases, deposits, a cost method investment and other long-term assets. Investments at December 31, 2007 included $34.5 million of Fulton County Taxable Economic Development Revenue Bonds purchased in connection with the capital lease for the Atlanta facility that became operational in the fourth quarter of 2003. The bonds will be held to maturity (December 1, 2017) and bear a fixed interest rate of 5 percent.

Long-Lived Assets

ADESA applies SFAS 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*. Management reviews its property and equipment and other intangible assets for impairment whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. The determination includes evaluation of factors such as current market value, future asset utilization, business climate, and future cash flows expected to result from the use of the related assets. If the carrying amount of a long-lived asset exceeds the total amount of the estimated undiscounted future cash flows from that asset, a loss is recognized in the period when it is determined that the carrying amount of the asset may not be recoverable to the extent that the carrying amount exceeds the fair value of the asset. The impairment analysis is based on the Company s current business strategy, expected growth rates and estimated future economic and regulatory conditions.

Table of Contents

KAR Holdings, Inc.

Notes to Consolidated Financial Statements (Continued)

Accounts Payable

Accounts payable include amounts due sellers from the proceeds of the sale of their consigned vehicles less any fees, as well as outstanding checks to sellers and vendors. Book overdrafts, representing outstanding checks in excess of funds on deposit, are recorded in Accounts payable and amounted to $181.2 million at December 31, 2007.

Environmental Liabilities

Accruals for environmental matters are recorded when it is probable that a liability has been incurred and the amount of the liability can be reasonably estimated, based on current law and existing technologies. These accruals are adjusted periodically as assessment and remediation efforts progress, or as additional technical or legal information becomes available. Accruals for environmental liabilities are included in Other accrued expenses (current portion) and Other liabilities (long-term portion) at undiscounted amounts and generally exclude claims for recoveries from insurance or other third parties.

Revenue Recognition

ADESA Auction Services

Revenues and the related costs are recognized when the services are performed. Auction fees from sellers and buyers are recognized upon the sale of the vehicle through the auction process. Most of the vehicles that are sold at auction are consigned to ADESA by the seller and held at ADESA s facilities. ADESA does not take title to these consigned vehicles and recognizes revenue when a service is performed as requested by the owner of the vehicle. ADESA does not record the gross selling price of the consigned vehicles sold at auction as revenue. Instead, ADESA records only its auction fees as revenue because it does not take title to the consigned vehicles, has no influence on the vehicle auction selling price agreed to by the seller and buyer at the auction and the fees that ADESA receives for its services are generally a fixed amount. Revenues from reconditioning, logistics, vehicle inspection and certification, titling, evaluation and salvage recovery services are generally recognized when the services are performed.

IAAI Salvage Services

Revenues (including vehicle sales and fee income) are generally recognized at the date the vehicles are sold at auction. Revenue not recognized at the date the vehicles are sold at auction includes annual buyer registration fees, which are recognized on a straight-line basis and certain buyer-related fees, which are recognized when payment is received.

AFC

AFC s revenue is comprised primarily of securitization income and interest and fee income. As is customary for finance companies, AFC s revenues are reported net of a provision for credit losses. The following table summarizes the primary components of AFC s revenue:

AFC Revenue ***(In millions)***	**For the Period April 20 December 31, 2007**
Securitization income	**$ 49.4**
Interest and fee income	**45.5**
Other revenue	**1.2**
Provision for credit losses	**(1.1)**

	$	**95.0**

Table of Contents

KAR Holdings, Inc.

Notes to Consolidated Financial Statements (Continued)

Securitization income

Securitization income is primarily comprised of the gain on sale of finance receivables sold, but also includes servicing income, discount accretion, and any change in the fair value of the retained interest in finance receivables sold. AFC generally sells its U.S. dollar denominated finance receivables through a revolving private securitization structure. Gains and losses on the sale of receivables are recognized upon transfer to the bank conduit facility.

Interest and fee income

Interest on finance receivables is recognized based on the number of days the vehicle remains financed. AFC ceases recognition of interest on finance receivables when the loans become delinquent, which is generally 31 days past due. Dealers are also charged a fee to floorplan a vehicle (floorplan fee) and extend the terms of the receivable (curtailment fee). AFC fee income including floorplan and curtailment fees is recognized over the life of the finance receivable.

Loan origination costs

Loan origination costs incurred by AFC in originating floorplan receivables are capitalized at the origination of the customer contract. Such costs for receivables retained are amortized over the estimated life of the customer contract. Costs associated with receivables sold are included as a reduction in securitization income.

Income Taxes

The Company will file a consolidated federal income tax return for the period April 20, 2007 through December 31, 2007. The Company files state income tax returns in accordance with the applicable rules of each state. The Company accounts for income taxes under the asset and liability method in accordance with SFAS 109, *Accounting for Income Taxes*. The provision for income taxes includes federal, foreign, state and local income taxes currently payable, as well as deferred taxes. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in years in which those temporary differences are expected to be recovered or settled. If it is more likely than not that some portion or all of a deferred tax asset will not be realized, a valuation allowance is recognized.

In accordance with FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes*, (FIN 48) the Company recognizes the effect of income tax positions only if those positions are more likely than not of being sustained. Recognized income tax positions are measured at the largest amount that is greater than 50% likely of being realized. Changes in recognition or measurement are reflected in the period in which the change in judgment occurs.

Accounting for Stock-Based Compensation

In December 2004, the Financial Accounting Standards Board (FASB) issued SFAS 123(R), *Share-Based Payment*, which replaced SFAS 123 and supersedes APB 25. The statement requires that all stock-based compensation be recognized as expense in the financial statements and that such cost be measured at the fair value of the award at the grant date. An additional requirement of SFAS 123(R) is that estimated forfeitures be considered in determining compensation expense. Estimating forfeitures did not have a material impact on the determination of compensation expense in 2007.

Table of Contents

KAR Holdings, Inc.

Notes to Consolidated Financial Statements (Continued)

SFAS 123(R) requires cash flows resulting from tax deductions from the exercise of stock options in excess of recognized compensation cost (excess tax benefits) to be classified as financing cash flows. This requirement had no impact on KAR Holdings Consolidated Statement of Cash Flows in 2007 as no options were exercised.

New Accounting Standards

In September 2006, the FASB issued SFAS 157, *Fair Value Measurements*. The statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. This standard, as issued, is effective for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The FASB issued FASB Staff Position No. FAS 157-b, *Effective Date of FASB Statement No. 157*, which delays the effective date by one year for all nonfinancial assets and nonfinancial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis, at least annually. The Company is currently evaluating the impact the adoption of SFAS 157 will have on the consolidated financial statements.

In February 2007, the FASB issued SFAS 159, *The Fair Value Option for Financial Assets and Financial Liabilities*, which provides companies with an option to report selected financial assets and liabilities at fair value. The objective of SFAS 159 is to reduce both complexity in accounting for financial instruments and the volatility in earnings caused by measuring related assets and liabilities differently. SFAS 159 does not eliminate disclosure requirements of other accounting standards, including fair value measurement disclosures in SFAS 157. This standard is effective as of the beginning of an entity s first fiscal year beginning after November 15, 2007. The Company is currently evaluating the impact the adoption of SFAS 159 will have on the consolidated financial statements.

In December 2007, the FASB issued SFAS 141(R), *Business Combinations*. The statement establishes principles and requirements for recognizing and measuring identifiable assets and goodwill acquired, liabilities assumed and any noncontrolling interest in an acquisition, at their fair value as of the acquisition date. This standard is effective for annual reporting periods beginning after December 15, 2008. The Company is currently evaluating the impact the adoption of SFAS 141(R) will have on the consolidated financial statements.

In December 2007, the FASB issued SFAS 160, *Noncontrolling Interests in Consolidated Financial Statements an Amendment of Accounting Research Bulletin No. 51*. The statement amends Accounting Research Bulletin No. 51 to establish accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. This standard is effective for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years. The Company is currently evaluating the impact the adoption of SFAS 160 will have on the consolidated financial statements.

Note 3 Acquisitions

2007 Acquisitions

In September 2007, ADESA completed the acquisition of certain assets of the used vehicle Tri-State Auto Auction serving the Tri-State New York area. This acquisition complements the Company s geographic presence in the northeast. The auction is positioned on approximately 125 acres and includes seven auction lanes and full-service reconditioning shops providing detail, mechanical and body shop services. The assets purchased included operating equipment, accounts receivable and customer relationships related to the auction. In addition, the Company entered into an operating lease obligation related to the facility through 2017. Initial annual lease payments for the facility are approximately $0.5 million per year. The Company did not assume any other material liabilities or indebtedness in connection with the acquisition. Financial results for this acquisition have been included in the Company s consolidated financial statements since the date of acquisition.

KAR Holdings, Inc.

Notes to Consolidated Financial Statements (Continued)

In October 2007, ADESA acquired all of the issued and outstanding shares of the parent company of Tri-State Auction, Co. Inc., and Sioux Falls Auto Auction, Inc., both North Dakota corporations. Tri-State Auto Auction serves the Fargo, North Dakota area. The auction is comprised of approximately 30 acres and includes six auction lanes and full-service reconditioning shops providing detail, mechanical and body shop services. The Sioux Falls Auto Auction serves the Sioux Falls, South Dakota area. The auction is comprised of approximately 40 acres and includes four auction lanes and full-service reconditioning shops providing detail, mechanical and body shop services. The assets of the auctions included operating equipment, accounts receivable and customer relationships related to the auctions. Liabilities assumed by the Company included operating leases for land and buildings as well as debt. Financial results for this acquisition will be included in the Company s consolidated financial statements from the date of acquisition.

In November 2007, ADESA Canada acquired all of the issued and outstanding shares of Enchere d Auto Transit Inc. (Transit). Transit is a three lane auction located on the south shore of Quebec City and serves the Quebec City region, Eastern Quebec and Northern New Brunswick. The auction is comprised of approximately 30 acres of which about 10 acres are currently being used. The assets of the auction included accounts receivable, land and building, operating equipment and customer relationships related to the auctions. Liabilities assumed by the Company included operating leases for land and buildings as well as debt. Financial results for this acquisition will be included in the Company s consolidated financial statements from the date of acquisition.

The aggregate purchase price for the four previously mentioned ADESA acquisitions was approximately $32.3 million. A preliminary purchase price allocation has been recorded for each acquisition and the purchase price of the acquisitions was allocated to the acquired assets based upon fair market values, including $7.4 million to other intangible assets, representing the fair value of acquired customer relationships and non competes which will be amortized over their expected useful lives of 3 to 15 years. The purchase price allocations resulted in aggregate goodwill of $20.0 million. The goodwill was assigned to the ADESA Auctions reporting segment and is expected to be fully deductible for tax purposes. All debt acquired as a result of these acquisitions was subsequently paid off. Pro forma financial results reflecting these acquisitions were not materially different from those reported.

2008 Acquisitions

In January 2008, IAAI completed the purchase of assets of B&E Auto Auction in Henderson, Nevada which services the Southern Nevada region, including Las Vegas. The site will expand IAAI s national service coverage and provide additional geographic support to clients who already utilize existing IAAI facilities in the surrounding Western states. The purchase agreement includes contingent payments related to the volume of certain vehicles sold subsequent to the purchase date. Financial results for this acquisition will be included in the Company s consolidated financial statements from the date of acquisition.

In February 2008, IAAI purchased the stock of Salvage Disposal Company of Georgia, Verastar, LLC, Auto Disposal of Nashville, Inc., Auto Disposal of Chattanooga, Inc., Auto Disposal of Memphis, Inc., Auto Disposal of Paducah, Inc. and Auto Disposal of Bowling Green, Inc., 11 independently owned Salvage auctions in Georgia, North Carolina, Tennessee, Mississippi and Kentucky. These site acquisitions will expand IAAI s national service coverage and provide additional geographic support to clients who already utilize existing IAAI facilities in the surrounding Southern States. The purchase agreement includes contingent payments related to the volume of certain vehicles sold subsequent to the purchase date. Financial results for these acquisitions will be included in the Company s consolidated financial statements from the date of acquisition.

Table of Contents

KAR Holdings, Inc.

Notes to Consolidated Financial Statements (Continued)

In February 2008, ADESA completed the purchase of certain assets of Pennsylvania Auto Dealer Exchange (PADE), PADE Financial Services (PFS) and Conewago Partners, LP, an independent used vehicle auction in York, Pennsylvania. This acquisition complements the Company s geographic presence in the northeast. Financial results for this acquisition will be included in the Company s consolidated financial statements from the date of acquisition.

In February 2008, IAAI completed the purchase of Southern A&S (formerly Southern Auto Storage Pool) in Memphis, Tennessee. IAAI plans to combine the Southern A&S business with the Memphis operation it acquired in the Verastar deal. The combined auctions will be relocated to a new site, which will be shared with ADESA Memphis. The purchase agreement includes contingent payments related to the volume of certain vehicles sold subsequent to the purchase date. Financial results for this acquisition will be included in the Company s consolidated financial statements from the date of acquisition.

The aggregate purchase price for the 14 auctions acquired in 2008 was approximately $114 million. The preliminary purchase price allocations for each auction will occur in the Company s first quarter ending March 31, 2008.

Note 4 Stock-Based Compensation Plans

The compensation cost that was charged against income for all stock-based compensation plans was $6.7 million for the period April 20, 2007 through December 31, 2007. The total income tax benefit recognized in the Consolidated Statement of Operations for stock-based compensation agreements was approximately $0.4 million for the period April 20, 2007 through December 31, 2007. The Company did not capitalize any stock-based compensation cost in the year ended December 31, 2007.

IAAI Carryover Stock Plans

Prior to the merger transactions, IAAI was a subsidiary of Axle Holdings, Inc. (Axle Holdings), which in turn was a subsidiary of Axle Holdings II, LLC (LLC). Axle Holdings maintained the Axle Holdings, Inc. Stock Incentive Plan to provide equity incentive benefits to the IAAI employees. Under the Axle Holdings plan, service options and exit options were awarded. The service options vest in three equal annual installments from the grant date based upon service with Axle Holdings and its subsidiaries. The exit options vest upon a change in equity control of the LLC. In connection with the completion of the merger transactions, approximately 0.6 million options (service and exit) to purchase shares of Axle Holdings, Inc. stock were converted into approximately 0.2 million options (service and exit) to purchase shares of KAR Holdings; these converted options have the same terms and conditions as were applicable to the options to purchase shares of Axle Holdings, Inc. The fair value of the exchanged options for which service had been provided approximated $8.9 million and was included as part of the merger price. Compensation cost will be recognized using the straight-line attribution method over the requisite service period for the unvested service options exchanged at the date of the merger. As the ultimate exercisability of the exit options exchanged is contingent upon an event (specifically, a change of control), the compensation expense related to the exchanged exit options will not be recognized until such an event is consummated. The converted options are included in the KAR Holdings, Inc. service option table and exit option table below.

The LLC also maintained two types of profit interests, operating units and value units, which are held by certain designated employees of IAAI. Upon an exit event as defined by the LLC operating agreement, holders of the profit interests will receive a cash distribution from the LLC. The operating units vest in twelve equal quarterly installments from the date of grant based upon service and the value units vest upon a change in equity

KAR Holdings, Inc.

Notes to Consolidated Financial Statements (Continued)

control of the LLC. The number of value units eligible for distribution will be determined based on the strike price and certain performance hurdles based on the Equity Sponsors and other investors achievement of certain multiples on their original indirect equity investment in Axle Holdings subject to an internal rate of return minimum at the time of distribution. A total of 191,152 operating units and 382,304 value units are maintained by the LLC and there were no changes to the terms and conditions of the units as a result of the merger transactions.

The operating units are accounted for as liability awards and as such, compensation expense related to the operating units is recognized using the graded-vesting attribution method and resulted in approximately $4.8 million of expense for the period April 20, 2007 through December 31, 2007. As of December 31, 2007, there was approximately $0.1 million of total unrecognized compensation expense related to nonvested operating units which is expected to be recognized over a weighted average term of 0.4 years.

The Company has not recorded compensation expense related to the value units and none will be recognized on the value units until it becomes probable that an exit event (specifically, a change in control) will occur.

KAR Holdings, Inc. Stock Incentive Plan

The Company adopted the KAR Holdings, Inc. Stock Incentive Plan, the Plan in May 2007. The Plan is intended to provide equity incentive benefits to the Company employees. The maximum number of shares that may be issued pursuant to awards under the Plan is approximately 0.8 million. The Plan provides for the grant of incentive stock options and non-qualified stock options and restricted stock. Awards granted since the adoption of the Plan have been non-qualified stock options.

The Plan provides two types of stock options: service-related options, which will vest in four equal installments from the date of grant based upon the passage of time, and performance-related exit options, which will generally become exercisable upon a change in equity control of KAR LLC. Under the exit options, in addition to the change in equity control requirement, the number of options that vest will be determined based on the strike price and certain performance hurdles based on the Equity Sponsors and other investors achievement of certain multiples on their original indirect equity investment in KAR Holdings subject to an internal rate of return minimum at the time of change in equity control. All vesting criteria are subject to continued employment with KAR LLC or affiliates thereof. Options may be granted under the Plan at an exercise price of not less than the fair market value of a share of KAR Holdings common stock on the date of grant and have a contractual life of ten years. In the event of a change in control, any unvested options shall become fully vested and cashed out. In August 2007, the Company granted approximately 0.2 million service options and 0.5 million exit options, with an exercise price of $100 per share, under the Plan.

The following table summarizes service option activity under the Plan for the year ended December 31, 2007:

Service Options	Number	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value (in millions)
Outstanding at January 1, 2007		$		
Conversion of Axle Options	150,459	43.11		
Granted	162,465	100.00		
Exercised		N/A		
Forfeited	(2,771)	82.48		
Cancelled	(404)	69.70		
Outstanding at December 31, 2007	309,749	$ 72.57	7.9 years	$ 27.9
Exercisable at December 31, 2007	132,502	$ 39.42	5.6 years	$ 16.3

Table of Contents

KAR Holdings, Inc.

Notes to Consolidated Financial Statements (Continued)

The intrinsic value presented in the table above represents the amount by which the market value of the underlying stock exceeds the exercise price of the option at December 31, 2007. The intrinsic value changes whenever the fair value of the Company changes. The market value at December 31, 2007 was developed in consultation with independent valuation specialists. The fair value of all vested and exercisable service options at December 31, 2007 was $21.6 million.

Service options are accounted for as equity awards and, as such, compensation expense is measured based on the fair value of the award at the date of grant and recognized over the four year service period, using the straight-line attribution method. The grant date fair value of the service options granted in August 2007 was $35.70 per share, and was estimated using the Black-Scholes option pricing model and the following assumptions:

Assumptions	
Risk-free interest rate	4.255%
Expected life	4 years
Expected volatility	38.0%
Dividend yield	0%

Risk-free interest rate This is the yield on U.S. Treasury Securities posted at the date of grant having a term equal to the expected life of the option. An increase in the risk-free interest rate will increase compensation expense.

Expected life years This is the period of time over which the options granted are expected to remain outstanding. Options granted by KAR had a maximum term of ten years. An increase in the expected life will increase compensation expense.

Expected volatility Actual changes in the market value of stock are used to calculate the volatility assumption. As KAR Holdings is a new nonpublic entity, the expected volatility used was determined based on an examination of the historical volatility of the stock price of ADESA, the volatility of selected comparable companies and other relevant factors. An increase in the expected volatility will increase compensation expense.

Dividend yield This is the annual rate of dividends per share over the exercise price of the option. An increase in the dividend yield will decrease compensation expense.

The Company recorded compensation expense of $0.5 million related to the service options granted in 2007 and $0.4 million related to the service options converted from Axle Holdings. As of December 31, 2007, there was approximately $5.6 million of total unrecognized compensation expense related to nonvested service options (new and converted) which is expected to be recognized over a weighted average term of 3.4 years. This unrecognized compensation expense only includes the cost of those service options expected to vest, as the Company estimates expected forfeitures in accordance with SFAS 123(R). An increase in estimated forfeitures would decrease compensation expense.

Table of Contents

KAR Holdings, Inc.

Notes to Consolidated Financial Statements (Continued)

The following table summarizes exit option activity under the Plan for the year ended December 31, 2007:

Exit Options	Number	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value (in millions)
Outstanding at January 1, 2007		$		
Conversion of Axle Options	80,023	67.96		
Granted	487,397	100.00		
Exercised		N/A		
Forfeited	(9,934)	79.21		
Cancelled		N/A		
Outstanding at December 31, 2007	557,486	$ 95.74	9.4 years	$ 37.3

The intrinsic value presented in the table above represents the amount by which the market value of the underlying stock exceeds the exercise price of the option at December 31, 2007. The intrinsic value changes whenever the fair value of the Company changes. The market value at December 31, 2007 was developed in consultation with independent valuation specialists.

The weighted average grant date fair value of the exit options granted during the year ended December 31, 2007 was $4.90. As the ultimate exercisability of the exit options is contingent upon an event (specifically, a change in control), the compensation expense related to the exit options will not be recognized until such an event is consummated.

KAR LLC Override Units

KAR LLC owns 100% of the outstanding shares of KAR Holdings. The KAR LLC operating agreement provides for override units in the LLC to be granted and held by certain designated employees of the Company. Upon an exit event as defined by the LLC operating agreement, and at any other time determined by the board, holders of the override units will receive a cash distribution from KAR LLC.

Two types of override units were created by the KAR LLC operating agreement: (1) operating units, which vest in four equal installments commencing on the first anniversary of the grant date based upon service, and (2) value units, which are eligible for distributions upon attaining certain performance hurdles. The number of value units eligible for distributions will be determined based on the strike price and certain performance hurdles based on the Equity Sponsors and other investors achievement of certain multiples on their original indirect equity investment in KAR Holdings subject to an internal rate of return minimum at the time of distribution.

There were approximately 0.1 million operating units awarded and 0.4 million value units awarded to employees of the Company in June 2007 with a strike price equal to $100 for the override units. The following table summarizes the KAR LLC override unit activity for the year ended December 31, 2007:

Override Units:	Operating Units	Value Units
Outstanding at January 1, 2007		
Granted	121,046	363,139
Vested		
Forfeited		

Outstanding at December 31, 2007	121,046	363,139

Table of Contents

KAR Holdings, Inc.

Notes to Consolidated Financial Statements (Continued)

The grant date fair value of the operating units and value units was $36.90 and $45.21, respectively. The fair value of each operating unit was estimated on the date of grant using the Black-Scholes option pricing model. The fair value of each value unit was estimated on the date of grant using a lattice-based valuation model.

The compensation expense of KAR LLC, which is for the benefit of Company employees, will result in a capital contribution from KAR LLC to the Company and compensation expense for the Company. Compensation expense related to the operating units is recognized using the straight-line attribution method and resulted in $1.0 million for the period April 20, 2007 through December 31, 2007. As of December 31, 2007, there was approximately $6.5 million of total unrecognized compensation expense related to nonvested operating units which is expected to be recognized over a weighted average term of 3.5 years.

The Company has not recorded compensation expense related to the value units and none will be recognized until it becomes probable that the performance conditions associated with the value units will be achieved.

Note 5 Allowance for Credit Losses and Doubtful Accounts

The following is a summary of the changes in the allowance for credit losses related to finance receivables held for investment (*in millions*):

	For the Period April 20 December 31, 2007
Allowance for Credit Losses	
Balance at beginning of period	$ 7.3
Provision for credit losses	1.1
Recoveries	0.4
Less charge-offs	(1.5)
Other	0.2
Balance at end of period	$ 7.5

AFC s allowance for credit losses includes estimated losses for finance receivables currently held on the balance sheet of AFC and its subsidiaries. Additionally, an accrued liability of $4.3 million for estimated losses for loans sold by AFC Funding is recorded at December 31, 2007. These loans were sold to a bank conduit facility with recourse to AFC Funding and will come back on the balance sheet of AFC Funding at fair market value if they prove to become ineligible under the terms of the collateral arrangement with the bank conduit facility.

The following is a summary of changes in the allowance for doubtful accounts related to trade receivables (*in millions*):

	For the Period April 20 December 31, 2007
Allowance for Doubtful Accounts	
Balance at beginning of period	$ 5.2
Provision for credit losses	2.1
Less net charge-offs	(1.0)

Balance at end of period	**$**	**6.3**

Table of Contents

KAR Holdings, Inc.

Notes to Consolidated Financial Statements (Continued)

Recoveries of trade receivables were netted with charge-offs, as they were not material. Changes in the Canadian exchange rate did not have a material effect on the allowance for doubtful accounts.

Note 6 Finance Receivables

AFC sells the majority of its U.S. dollar denominated finance receivables on a revolving basis and without recourse to a wholly owned, bankruptcy remote, consolidated, special purpose subsidiary (AFC Funding Corporation), established for the purpose of purchasing AFC s finance receivables. The securitization agreement allows for the revolving sale by AFC Funding Corporation to a bank conduit facility of up to a maximum of $750 million in undivided interests in certain eligible finance receivables subject to committed liquidity. The agreement expires on April 20, 2012. AFC Funding Corporation had committed liquidity of $600 million at December 31, 2007. Receivables that AFC Funding sells to the bank conduit facility qualify for sales accounting for financial reporting purposes pursuant to SFAS 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities,* and as a result are not reported on the Company s Consolidated Balance Sheet.

At December 31, 2007, AFC managed total finance receivables of $847.9 million, of which $746.1 million had been sold without recourse to AFC Funding Corporation. Undivided interests in finance receivables were sold by AFC Funding Corporation to the bank conduit facility with recourse totaling $522.0 million at December 31, 2007. Finance receivables include $29.4 million classified as held for sale and $225.0 million classified as held for investment at December 31, 2007. Finance receivables classified as held for investment include $91.0 million related to receivables that were sold to the bank conduit facility that were repurchased by AFC at fair market value when they became ineligible under the terms of the collateral agreement with the bank conduit facility. The face amount of these receivables was $99.3 million at December 31, 2007.

AFC s allowance for losses of $7.5 million at December 31, 2007, includes an estimate of losses for finance receivables held for investment. Additionally, accrued liabilities of $4.3 million for the estimated losses for loans sold by the special purpose subsidiary were recorded at December 31, 2007. These loans were sold to a bank conduit facility with recourse to the special purpose subsidiary and will come back on the balance sheet of the special purpose subsidiary at fair market value if they become ineligible under the terms of the collateral arrangement with the bank conduit facility.

The outstanding receivables sold, the retained interests in finance receivables sold and a cash reserve equal to 1 percent of total sold receivables serve as security for the receivables that have been sold to the bank conduit facility. After the occurrence of a termination event, as defined in the agreement, the bank conduit facility may, and could, cause the stock of AFC Funding Corporation to be transferred to the bank conduit facility, though as a practical matter the bank conduit facility would look to the liquidation of the receivables under the transaction documents as their primary remedy.

Proceeds from the revolving sale of receivables to the bank conduit facility are used to fund new loans to customers. AFC and AFC Funding Corporation must maintain certain financial covenants including, among others, limits on the amount of debt AFC can incur, minimum levels of tangible net worth, and other covenants tied to the performance of the finance receivables portfolio. The securitization agreement also incorporates the financial covenants of the Company s credit facility. At December 31, 2007, the Company was in compliance with the covenants contained in the securitization agreement.

Table of Contents

KAR Holdings, Inc.

Notes to Consolidated Financial Statements (Continued)

The following illustration presents quantitative information about delinquencies, credit losses less recoveries (net credit losses) and components of securitized financial assets and other related assets managed. For purposes of this illustration, delinquent receivables are defined as receivables 31 days or more past due.

(in millions)	December 31, 2007 Principal Amount of: Receivables	Receivables Delinquent	Net Credit Losses From April 20 December 31, 2007
Floorplan receivables	**$ 234.3**	**$ 10.2**	**$ 0.9**
Special purpose loans	**20.1**		**0.2**
Finance receivables held	**$ 254.4**	**$ 10.2**	**$ 1.1**
Receivables sold	**522.0**		
Retained interests in finance receivables sold	**71.5**		
Total receivables managed	**$ 847.9**		

The net credit losses for receivables sold approximated $15.5 million.

The following table summarizes certain cash flows received from and paid to the special purpose subsidiaries:

	For the Period April 20 December 31, 2007
Proceeds from sales of finance receivables	**$ 3,456.6**
Servicing fees received	**$ 12.1**
Proceeds received on retained interests in finance receivables sold	**$ 87.6**

The Company s retained interests in finance receivables sold, including a nominal interest only strip, amounted to $71.5 million at December 31, 2007. Sensitivities associated with the Company s retained interests were insignificant at all periods presented due to the short-term nature of the asset.

Note 7 Goodwill and Other Intangible Assets

Goodwill represents the excess cost over fair value of identifiable net assets of businesses acquired. At December 31, 2007, there was $1,617.6 million of goodwill recorded on the Company s Consolidated Balance Sheet that was recorded as a result of the merger transactions, post merger acquisitions and contingent consideration related to prior year acquisitions. The analysis of the fair value estimates is continuing to be refined in accordance with SFAS 141. As additional information becomes available and as actual results vary from these preliminary estimates, the underlying assets or liabilities may need to be adjusted, thereby impacting intangible asset and amortization estimates, as well as goodwill. Goodwill has increased since the merger transactions primarily as a result of 2007 acquisitions, additional consideration for 2006 acquisitions, as required by certain purchase agreements, and changes in the Canadian exchange rate.

Table of Contents

KAR Holdings, Inc.

Notes to Consolidated Financial Statements (Continued)

Goodwill consisted of the following at December 31, 2007 (*in millions*):

	Carrying Amount
ADESA Auctions	
Acquisition of ADESA	$ 785.9
Increase for 2007 acquisitions	20.8
	806.7
IAAI	
Contribution of IAAI	445.4
Increase for prior year acquisitions	7.0
	452.4
AFC	
Acquisition of ADESA	358.5
	$ 1,617.6

The gross carrying amount of customer relationships has increased since the date of the merger as a result of changes in the Canadian exchange rate and acquisitions. Customer relationships consisted of the following at December 31, 2007 (*in millions*):

	Useful Lives (in years)	Gross Carrying Amount	Accumulated Amortization	Carrying Value
Customer relationships	11 19	$ 889.3	($ 44.9)	$ 844.4

The gross carrying amount of other intangible assets has increased since the date of the merger as a result of computer software additions and acquisitions. A summary of other intangibles is as follows at December 31, 2007 (*in millions*):

	Useful Lives (in years)	Gross Carrying Amount	Accumulated Amortization	Carrying Value
Tradenames	Indefinite	$ 190.4	$	$ 190.4
Computer software	3 7	61.3	(7.7)	53.6
Covenants not to compete	1 5	15.4	(8.0)	7.4
Total		$ 267.1	($15.7)	$ 251.4

Amortization expense for other intangibles was $60.7 million for the period April 20, 2007 through December 31, 2007. Estimated amortization expense for the next five years is $85.9 million for 2008, $79.1 million for 2009, $77.6 million for 2010, $75.3 million for 2011 and $70.3 million for 2012.

F-25

Table of Contents

KAR Holdings, Inc.

Notes to Consolidated Financial Statements (Continued)

Note 8 Property and Equipment

Property and equipment consisted of the following (*in millions*):

	Useful Lives (in years)	December 31, 2007
Land		$ 330.1
Buildings	3 40	193.1
Land improvements	1 20	99.5
Building and leasehold improvements	1 33	92.5
Furniture, fixtures and equipment	1 10	78.0
Vehicles	1 6	13.3
Construction in progress		32.5
		839.0
Accumulated depreciation		(65.8)
Property and equipment, net		$ 773.2

As discussed in Note 1, in connection with the merger transactions, the property and equipment of the Company was revalued at fair value based on preliminary estimates and assumptions, resulting in adjusted basis, and the elimination of the related accumulated depreciation.

Depreciation expense for the period April 20, 2007 through December 31, 2007 was $65.9 million.

In 2003, ADESA entered into a capital lease for the new Atlanta auction facility in conjunction with the purchase of development revenue bonds. The assets included above under this capital lease are summarized below (*in millions*):

Classes of Property	December 31, 2007
Land	$ 16.8
Buildings	9.6
Land improvements	3.8
Furniture, fixtures and equipment	2.2
	32.4
Accumulated depreciation	(1.4)
Capital lease assets	$